

**Primeline Energy Holdings Inc.**  
(an exploration stage company)

**Interim Consolidated Financial Statements**  
**September 30, 2014**  
**(Unaudited)**

# Primeline Energy Holdings Inc.

(an exploration stage Company)

Consolidated Statement of Financial Position (Unaudited)

As at September 30, 2014 and March 31, 2014

(In Chinese Yuan Renminbi)

|   | Note   | Sep 30, 2014<br>RMB | Mar 31, 2014<br>RMB | Sep 30, 2014<br>CAD\$<br>(note 3.3) |
|---|--------|---------------------|---------------------|-------------------------------------|
| <b>Non-current assets</b>                         |        |                     |                     |                                     |
| Exploration and evaluation assets                 | 7      | 513,109,626         | 462,103,858         | 92,702,733                          |
| Property, plant and equipment                     | 8      | 5,126               | 8,189               | 926                                 |
|   |        | <u>513,114,752</u>  | <u>462,112,047</u>  | <u>92,703,659</u>                   |
| <b>Current assets</b>                             |        |                     |                     |                                     |
| Cash and cash equivalents                         |        | 6,041,339           | 24,648,035          | 1,091,479                           |
| Prepaid expenses and deposit                      |        | 923,057             | 838,097             | 166,767                             |
|   |        | <u>6,964,396</u>    | <u>25,486,132</u>   | <u>1,258,246</u>                    |
| <b>Total assets</b>                               |        | <u>520,079,148</u>  | <u>487,598,179</u>  | <u>93,961,905</u>                   |
| <b>Equity attributable to shareholders</b>        |        |                     |                     |                                     |
| Share capital                                     | 10     | 1,029,572           | 1,028,202           | 186,011                             |
| Reserves  |        | 568,736,219         | 561,351,770         | 102,752,704                         |
| Accumulated deficit                               |        | (109,616,394)       | (108,202,863)       | (19,804,227)                        |
| <b>Total equity</b>                               |        | <u>460,149,397</u>  | <u>454,177,109</u>  | <u>83,134,488</u>                   |
| <b>Non-current liabilities</b>                    |        |                     |                     |                                     |
| Shareholder loan                                  | 13(e)  | 56,631,241          | 19,258,753          | 10,231,480                          |
| Advances from a related party                     | 13(f)  | -                   | 8,355,607           | -                                   |
| Derivative warrant liabilities                    | 9      | 1,689,924           | 3,408,483           | 305,316                             |
|   |        | <u>58,321,165</u>   | <u>31,022,843</u>   | <u>10,536,796</u>                   |
| <b>Current liabilities</b>                        |        |                     |                     |                                     |
| Accounts payable and accrued liabilities          |        | 1,278,984           | 2,395,523           | 231,072                             |
| Cash calls payable                                | 13 (b) | 329,602             | 2,704               | 59,549                              |
|   |        | <u>1,608,586</u>    | <u>2,398,227</u>    | <u>290,621</u>                      |
| <b>Total liabilities</b>                          |        | <u>59,929,751</u>   | <u>33,421,070</u>   | <u>10,827,417</u>                   |
| <b>Total shareholders' equity and liabilities</b> |        | <u>520,079,148</u>  | <u>487,598,179</u>  | <u>93,961,905</u>                   |

Nature of operations and going concern (Note 1)

Approved by the Board of Directors

“*Brian Chan*”

Director

“*Ming Wang*”

Director

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

# Primeline Energy Holdings Inc.

(an exploration stage Company)

Consolidated Statement of Loss and Comprehensive Loss (Unaudited)

For the three months and six months ended September 30, 2014 and September 30, 2013

(In Chinese Yuan Renminbi)

|  | Notes | Three Months Ended |             |             | Six Months Ended |             |             |
|--|-------|--------------------|-------------|-------------|------------------|-------------|-------------|
|  |       | September 30       |             |             | September 30     |             |             |
|  |       | 2014               | 2013        | 2014        | 2014             | 2013        | 2014        |
|  |       |                    |             |             |                  |             |             |
|  |       | RMB                | RMB         | CAD\$       | RMB              | RMB         | CAD\$       |
|  |       |                    |             | (note 3.3)  |                  |             | (note 3.3)  |
| Expenses   |       |                    |             |             |                  |             |             |
| Auditor's remuneration                               |       | (36,605)           | -           | (6,613)     | (36,605)         | -           | (6,613)     |
| Bank charges   |       | (18,850)           | (13,666)    | (3,406)     | (28,181)         | (27,378)    | (5,091)     |
| Business promotion                                   |       | (135,155)          | (143,766)   | (24,418)    | (204,023)        | (270,024)   | (36,861)    |
| Directors remuneration and benefit                   |       | (301,870)          | (381,008)   | (54,538)    | (691,652)        | (795,481)   | (124,960)   |
| Office expenses                                      |       | (17,355)           | (114,732)   | (3,136)     | (24,758)         | (289,482)   | (4,472)     |
| Professional fees                                    |       | (836,558)          | (906,776)   | (151,140)   | (1,106,524)      | (2,114,400) | (199,914)   |
| Salary and benefit                                   |       | (554,662)          | (414,001)   | (100,210)   | (980,404)        | (904,151)   | (177,128)   |
| Travel   |       | (48,714)           | (153,660)   | (8,801)     | (49,216)         | (375,949)   | (8,892)     |
| Operating Loss                                       |       | (1,949,769)        | (2,127,609) | (352,262)   | (3,121,363)      | (4,776,865) | (563,931)   |
| Finance income                                       | 11    | 1,793,531          | 1,111,871   | 324,035     | 1,665,894        | 1,112,446   | 300,974     |
| Exchange gain (loss), net                            |       | 448,297            | (24,112)    | 80,993      | 41,938           | 646,058     | 7,577       |
| Profit(Loss) and comprehensive loss                  |       | 292,059            | (1,039,850) | 52,766      | (1,413,531)      | (3,018,361) | (255,380)   |
| Basic and diluted profit(loss) per share             |       | 0.003              | (0.011)     | 0.001       | (0.013)          | (0.032)     | (0.002)     |
| Weighted average number of common shares outstanding |       | 112,791,018        | 94,041,246  | 112,791,018 | 112,740,198      | 94,041,246  | 112,740,198 |

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

# Primeline Energy Holdings Inc.

(an exploration stage company)

Consolidated Statement of Changes in Equity (Unaudited)

(In Chinese Yuan Renminbi)

|   | Attributable to equity owners of the company |               |                             |                      |                                  |               | Total       |
|---|--|---------------|-----------------------------|----------------------|----------------------------------|---------------|-------------|
|   | Share Capital                                | Share Premium | Contributed Surplus Reserve | Share Option Reserve | Shares Purchase Warrants Reserve | Deficit       |             |
| Balance – April 1, 2013                           | 858,406                                      | 437,506,225   | 5,001,482                   | 64,245,066           | -                                | (103,464,121) | 404,147,058 |
| Debt Conversion                                   | 86,052                                       | 27,762,246    | 1,109,401                   | -                    | -                                | -             | 28,957,699  |
| Share issue costs                                 | -  | (15,291)      | -                           | -                    | -                                | -             | (15,291)    |
| Private placement                                 | 83,744                                       | 23,157,742    | -                           | -                    | -                                | -             | 23,241,486  |
| Share issue costs                                 | -  | (2,958,390)   | -                           | -                    | -                                | -             | (2,958,390) |
| Broker warrant issue costs                        | -  | (1,213,235)   | -                           | -                    | 1,213,235                        | -             | -           |
| Loss and comprehensive loss for the year          | -  | -             | -                           | -                    | -                                | (4,738,742)   | (4,738,742) |
| Discount on shareholder loan                      | -  | -             | 2,621,485                   | -                    | -                                | -             | 2,621,485   |
| Share based payments                              | -  | -             | -                           | 2,921,804            | -                                | -             | 2,921,804   |
| Balance – March 31, 2014                          | 1,028,202                                    | 484,239,297   | 8,732,368                   | 67,166,870           | 1,213,235                        | (108,202,863) | 454,177,109 |
| Warrants exercised                                | 1,370  | 727,310       | -                           | -                    | (263,064)                        | -             | 465,616     |
| Discount on shareholder loan                      | -  | -             | 5,464,982                   | -                    | -                                | -             | 5,464,982   |
| Share based payments                              | -  | -             | -                           | 1,455,221            | -                                | -             | 1,455,221   |
| Loss and comprehensive loss for the year          | -  | -             | -                           | -                    | -                                | (1,413,531)   | (1,413,531) |
| Balance – September 30, 2014                      | 1,029,572                                    | 484,966,607   | 14,197,350                  | 68,622,091           | 950,171                          | (109,616,394) | 460,149,397 |
| Balance – September 30, 2014, in CAD\$ (note 3.3) | 186,011                                      | 87,618,177    | 2,565,013                   | 12,397,848           | 171,666                          | (19,804,227)  | 83,134,488  |

|  | Attributable to equity owners of the company |               |                             |                      |               | Total       |
|--|--|---------------|-----------------------------|----------------------|---------------|-------------|
|  | Share Capital                                | Share Premium | Contributed Surplus Reserve | Share Option Reserve | Deficit       |             |
| Balance – April 1, 2013                    | 858,406                                      | 437,506,225   | 5,001,482                   | 64,245,066           | (103,464,121) | 404,147,058 |
| Loss and comprehensive loss for the period | -  | -             | -                           | -                    | (3,018,361)   | (3,018,361) |
| Discount on shareholder loan               | -  | -             | 2,023,485                   | -                    | -             | 2,023,485   |
| Share based payments                       | -  | -             | -                           | 1,577,619            | -             | 1,577,619   |
| Balance – September 30, 2013               | 858,406                                      | 437,506,225   | 7,024,967                   | 65,822,685           | (106,482,482) | 404,729,801 |

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

# Primeline Energy Holdings Inc.

(an exploration stage company)

Consolidated Statement of Cash Flows (Unaudited)

For three months ended and six months ended September 30, 2014 and September 30, 2013

(in Chinese Yuan Renminbi)

|   | Note  | Three Months Ended<br>September 30 |                    |                             | Six Months Ended<br>September 30 |                    |                             |
|---|-------|------------------------------------|--------------------|-----------------------------|----------------------------------|--------------------|-----------------------------|
|   |       | 2014<br>RMB                        | 2013<br>RMB        | 2104<br>CAD\$<br>(note 3.3) | 2014<br>RMB                      | 2013<br>RMB        | 2014<br>CAD\$<br>(note 3.3) |
| <b>Cash flows from operating activities</b>                                     |       |                                    |                    |                             |                                  |                    |                             |
| Profit(Loss) for the period   |       | 292,059                            | (1,039,850)        | 52,766                      | (1,413,531)                      | (3,018,361)        | (255,380)                   |
| Item not involving cash   |       |                                    |                    |                             |                                  |                    |                             |
| Depreciation  |       | 1,532                              | 1,532              | 277                         | 3,063                            | 3,064              | 553                         |
| Finance income from fair value<br>adjustment of advance from related<br>company |       | -                                  | (1,111,304)        | -                           | -                                | (1,111,304)        | -                           |
| Finance income from fair value<br>adjustment of warrant liability               |       | (1,792,986)                        | -                  | (323,936)                   | (1,664,790)                      | -                  | (300,775)                   |
| Stock-based compensation  | 10    | 389,387                            | 480,729            | 70,350                      | 834,374                          | 1,017,294          | 150,745                     |
| Unrealized foreign exchange (gain)<br>loss                                      |       | (385,656)                          | 5,442              | (69,677)                    | 59,748                           | (775,955)          | 10,794                      |
|   |       | <u>(1,495,664)</u>                 | <u>(1,663,451)</u> | <u>(270,220)</u>            | <u>(2,181,136)</u>               | <u>(3,885,262)</u> | <u>(394,063)</u>            |
| Changes in non-cash working capital items:                                      |       |                                    |                    |                             |                                  |                    |                             |
| Prepaid expenses and deposit  |       | (14,127)                           | 28,994             | (2,552)                     | (84,960)                         | 892,530            | (15,350)                    |
| Accounts payable and accrued<br>liabilities                                     |       | (855,450)                          | (951,262)          | (154,553)                   | (555,453)                        | (976,604)          | (100,353)                   |
|   |       | <u>(869,577)</u>                   | <u>(922,268)</u>   | <u>(157,105)</u>            | <u>(640,413)</u>                 | <u>(84,074)</u>    | <u>(115,703)</u>            |
|   |       | <u>(2,365,241)</u>                 | <u>(2,585,719)</u> | <u>(427,325)</u>            | <u>(2,821,549)</u>               | <u>(3,969,336)</u> | <u>(509,766)</u>            |
| <b>Cash flows from investing activities</b>                                     |       |                                    |                    |                             |                                  |                    |                             |
| Expenditures on exploration and<br>evaluation assets                            | 7     | (3,994,061)                        | (3,009,421)        | (721,601)                   | (48,003,672)                     | (7,443,221)        | (8,672,750)                 |
|   |       | <u>(3,994,061)</u>                 | <u>(3,009,421)</u> | <u>(721,601)</u>            | <u>(48,003,672)</u>              | <u>(7,443,221)</u> | <u>(8,672,750)</u>          |
| <b>Cash flows from financing activities</b>                                     |       |                                    |                    |                             |                                  |                    |                             |
| Gross proceeds of broker warrants<br>exercised                                  |       | -                                  | -                  | -                           | 465,616                          | -                  | 84,122                      |
| Shareholder loan  | 13(e) | 10,271,666                         | 7,369,177          | 1,855,766                   | 41,373,533                       | 11,204,040         | 7,474,893                   |
| Cash call from a related party  | 13(b) | -                                  | 875,790            | -                           | 6,182,133                        | 2,960,120          | 1,116,917                   |
| Cash utilized for a related party   | 13(b) | (1,034,643)                        | (1,444,454)        | (186,927)                   | (15,759,435)                     | (2,618,019)        | (2,847,233)                 |
|   |       | <u>9,237,023</u>                   | <u>6,800,513</u>   | <u>1,668,839</u>            | <u>32,261,847</u>                | <u>11,546,141</u>  | <u>5,828,699</u>            |
| <b>Increase (decrease) in cash and cash<br/>equivalents</b>                     |       | <u>2,877,721</u>                   | <u>1,205,373</u>   | <u>519,913</u>              | <u>(18,563,374)</u>              | <u>133,584</u>     | <u>(3,353,817)</u>          |
| <b>Effect of foreign exchange rate on cash<br/>and cash equivalents</b>         |       | <u>(72,617)</u>                    | <u>44,265</u>      | <u>(13,120)</u>             | <u>(43,322)</u>                  | <u>(25,647)</u>    | <u>(7,827)</u>              |
| <b>Cash and cash equivalents - Beginning<br/>of period</b>                      |       | <u>3,236,235</u>                   | <u>3,897,243</u>   | <u>584,686</u>              | <u>24,648,035</u>                | <u>5,038,944</u>   | <u>4,453,123</u>            |
| <b>Cash and cash equivalents - End of<br/>period</b>                            |       | <u>6,041,339</u>                   | <u>5,146,881</u>   | <u>1,091,479</u>            | <u>6,041,339</u>                 | <u>5,146,881</u>   | <u>1,091,479</u>            |

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

# Primeline Energy Holdings Inc.

(an exploration stage company)

Notes to Consolidated Financial Statements

September 30, 2014

(in Chinese Yuan Renminbi)

## 1. Nature of operations and going concern

Primeline Energy Holdings Inc. (PEHI or the Company) was incorporated under the Companies Law of the Cayman Islands on March 31, 1995. The Company is in the business of exploration and development of offshore oil and gas properties. To date, PEHI has not realized any revenues from its oil and gas properties and is considered to be an exploration stage company.

The Company owns exploration and development rights in the East China Sea pursuant to contracts in relation to Block 25/34 (the Petroleum Contract) and Block 33/07 (the New Contract). The contracts were entered into between China National Offshore Oil Corporation (CNOOC), a Chinese State Oil company, Primeline Energy China Ltd. (PECL), a wholly owned subsidiary of the Company, and Primeline Petroleum Corporation (PPC), a company wholly owned by Mr. Victor Hwang, chairman, director and majority shareholder of the Company. Block 25/34 covering 84.7 sq kms is the development and production area for the LS36-1 gas field for which CNOOC is the Operator with a 51% interest, and PECL and PPC hold 36.75% and 12.25% interests respectively.

Block 33/07 covers an offshore area of 5,877 sq kms enclosing Block 25/34. PECL and PPC are collectively the Contractors. The Contractors are responsible for 100% of the exploration costs and CNOOC has the right to participate in up to 51% of any commercial development. The Contractors' interest is shared 75%/25% by PECL and PPC. Primeline Energy Operations International Ltd (PEOIL), a wholly owned subsidiary of the Company, is the operator for Block 33/07.

These financial statements have been prepared on the basis of accounting principles applicable to a going concern, which assumes that the Company will be able to continue in operation for the foreseeable future and will be able to realize its assets and discharge its liabilities in the normal course of business. Several adverse conditions cast significant doubt upon the validity of this assumption. Consistent with other entities in the exploration stage, the Company has incurred operating losses since inception, has no source of revenue and is unable to self-finance operations. The Company has significant cash requirements to meet its overhead requirements and carry out its exploration activities under the New Contract. The Company's portion of the LS 36-1 development costs is estimated to be approximately RMB 1,400 million (CAD\$249 million) according to the ODP budget. To address the need for LS36-1 development funding, the Company and PPC have jointly entered into a syndicated loan agreement on November 17, 2014. The syndicate consists of China Development Bank ("CDB") and China Export and Import Bank ("EXIM") as joint lead arrangers and Shanghai Pudong Development Bank ("SPDB") as participant and agent bank. The loan will be made available to the Company and PPC on a joint borrower basis and secured on their respective interests in the Development. The loan will be for a total amount of US\$ 274 million of which the Company's share is US\$205.5 million and will be repayable over 9 years. The first drawdown of the loan will be before the end of November 2014 to fund its cash calls in relation to the development operation.

The Company's working capital has been financed by interest free loans from the Chairman and majority shareholder, Mr. Hwang. The Company has continued to explore various possible ways of securing funds for its exploration obligations under the New Contract. In June 2014, Mr. Hwang agreed to provide the Company an interest free loan of US\$ 8,000,000 which will be sufficient to meet the Company's overhead requirement and to carry out its exploration activities under the New Contract for the coming twelve months.

If the going concern assumption were not appropriate for these financial statements then adjustments would be necessary to the carrying value of assets and liabilities, the reported expenses and the statement of financial position classifications used, and such adjustments would be material.

# Primeline Energy Holdings Inc.

(an exploration stage company)

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September 30, 2014

(in Chinese Yuan Renminbi)

On July 1, 2014 the development of its LS36-1 gas field was officially completed and since then CNOOC Limited, as operator, and the downstream buyer, Zhejiang Provincial Gas Development Co. ("Zhejiang Gas"), commenced joint commissioning of the upstream and downstream facilities and trial gas production from the LS36-1 gas field commenced on July 16, 2014.

## 2. Basis of presentation

These consolidated financial statements have been prepared in accordance with International Financial Reporting Standard ("IFRS") issued by the International Accounting Standards Board ("IASB") and Interpretations of the International Financial Report Interpretations Committee ("IFRIC") under the historical cost convention, except for the revaluation of derivative warrant liability. The comparative information has also been prepared on this basis.

The accounting policies applied in these interim consolidated financial statements are based on IFRS effective for the period ended September 30, 2014 as issued and outstanding as of November 24, 2014, the date the Board of Directors approved the statements.

The preparation of the financial statements in conformity with IFRS requires the use of estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Although these estimates are based on management's best knowledge of the amount, event or actions, actual results ultimately may differ from those estimates. Areas where estimates are significant to the interim consolidated financial statements are disclosed in note 6.

## 3. Summary of significant accounting policies

The principal accounting policies applied in the preparation of these consolidated financial statements are set out below. These policies have been consistently applied to all the periods presented.

### 3.1 Consolidation

#### *Subsidiaries*

Subsidiaries are all entities (including special purpose entities) over which the Company has control. The Company controls an entity when the Company is exposed to, or has the rights to variable returns from its involvement with the entity and has the ability to affect those return through its power over the entity. Subsidiaries are fully consolidated from the date on which control is transferred to the Company. They are de-consolidated from the date that control ceases. All subsidiaries, as listed below, have been consolidated into the Company's consolidated financial statements.

# Primeline Energy Holdings Inc.

(an exploration stage company)

Notes to Consolidated Financial Statements

September 30, 2014

(in Chinese Yuan Renminbi)

| <b>Name of subsidiary</b>                         | <b>Place of Incorporation</b> | <b>Paid up issued share capital</b> | <b>Percentage of issued capital held by the Company</b> | <b>Functional currency</b> |
|---|-------------------------------|-------------------------------------|---|----------------------------|
| Primeline Energy China Limited                    | Cayman Islands                | US\$2                               | 100%  | Chinese Yuan Renminbi      |
| Primeline Energy Operations International Limited | Cayman Islands                | US\$2                               | 100%  | Chinese Yuan Renminbi      |

PECL and PEOIL are registered and have been granted business licenses by the Shanghai Administration of Industry and Commerce in China.

Inter-company transactions, balances and unrealised gains on transactions between group companies are eliminated.

### 3.2 Segment reporting

The Company has one operating segment, which is the exploration of oil and gas properties located in the People's Republic of China.

### 3.3 Foreign currency translation

#### *(a) Functional and presentation currency*

Items included in the financial statements of each of the group's entities are measured using the currency of the primary economic environment in which the entity operates (the 'functional currency'). The consolidated financial statements are presented in Chinese Yuan Renminbi ("RMB"), which is also the functional currency of the Company and its subsidiaries.

#### *(b) Transactions and balances*

Foreign currency transactions are translated into the functional currency using the exchange rates prevailing at the dates of the transactions. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation at period – end exchange rates of monetary assets and liabilities denominated in foreign currencies are recognized in the statement of income (loss).

#### *(c) Convenience Translation into Canadian Dollar Amounts*

The Company's functional and presentation currency is RMB. The Canadian dollar amounts provided in the financial statements represent supplementary information solely for the convenience of the reader.

The financial information presented in Canadian dollars has been translated from RMB using a convenience translation at the rate of RMB5.535 to Canadian \$1, which is the exchange rate published in South China Morning Post as of September 30, 2014.

Such presentation is not in accordance with IFRS and should not be construed as a representation that the RMB amounts shown could be readily converted, realized or settled in Canadian dollars at this or at any other rate.



# Primeline Energy Holdings Inc.

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## **3.4 Exploration and evaluation assets (E&E)**

Once the legal right to explore has been acquired, costs directly associated with an exploration project are capitalized as either tangible or intangible exploration and evaluation assets according to the nature of the asset acquired. Such E&E costs may include undeveloped land acquisition, geological, geophysical and seismic, exploratory drilling and completion, testing, decommissioning and directly attributable internal costs. E&E costs are not depleted and are carried forward until technical feasibility and commercial viability of extracting a mineral resource is considered to be determined.

The technical feasibility and commercial viability of an oil and gas resource is considered to be established when all of the following conditions are met - proved and/or probable reserves are determined to exist, the decision to proceed with development has been approved by the Board of Directors, the receipt of regulatory approval to develop the project and the Company has the sufficient funds to complete or participate in the project.

All such carried costs are subject to technical, commercial and management review at least once a year to confirm the continued intent to develop or otherwise extract value from the exploratory activity. When this is no longer the case, the impairment costs are charged to exploration and evaluation expense.

Upon determination that the technical feasibility and commercial viability of an oil and gas resource is established, E&E assets attributed to those reserves are first tested for impairment and then reclassified to oil and gas development and production assets within property, plant and equipment, net of any impairment. Expired land costs are also expensed to exploration and evaluation expense as they occur.

E&E assets are assessed for impairment if facts and circumstances suggest that the carrying amount exceeds the recoverable amount, and upon transfer to property, plant and equipment whereby they are allocated to cash-generating units based on geographical proximity and other factors.

## **3.5 Property, plant and equipment (PP&E)**

Property, plant and equipment may include the costs of oil and gas development and production wells and costs for the associated plant and for general corporate assets. PP&E is recorded at cost less accumulated depletion and depreciation and accumulated impairment losses, net of recovered impairment losses.

Computer and office equipment are depreciated at a straight-line basis at the rate of 30% per annum.

### **3.5.1 Oil and gas development and production assets**

Development and production assets are capitalized on an area-by-area basis and include all costs associated with the development and production of oil and natural gas reserves. These costs may include proved property acquisitions, development drilling (including delineation wells), completion, gathering and infrastructure, decommissioning costs, amounts transferred from E&E assets and directly attributable internal costs.

Expenditures related to renewals or betterments that improve the productive capacity or extend the life of an asset are capitalized. Maintenance and repairs are expensed as incurred.

Any gains or losses from the divestiture of development and production assets are recognized in earnings.

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Accumulated costs are depleted using the unit-of-production method based on estimated proved reserves. Depletion is calculated based on individual components (i.e. fields or combinations thereof and other major components with different useful lives).

### 3.6 Impairment of non-current assets

The carrying amounts of the Company's property, plant and equipment are reviewed at each reporting date for indicators of impairment. If any such indication exists, the recoverable amount of the asset is estimated in order to determine the amount of the impairment, if any. The recoverable amount of an asset is evaluated at the Cash Generating Unit ("CGU") level, which is the smallest identifiable group of assets that generates cash inflows that are largely independent of the cash inflows from other assets or groups of assets. The recoverable amount of a CGU is the greater of its fair value less costs of disposal and its value in use. Fair value is determined as the amount that would be obtained from the sale of the asset in an arm's length transaction between knowledgeable and willing parties, less the 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 assessments of the time value of money and the risks specific to the asset. An impairment loss is recognized in earnings for the period to the extent that the carrying amount of the asset (or CGU) exceeds the recoverable amount.

Impairment losses recognized in prior periods are assessed at each reporting date for any indication that the loss has decreased or no longer exists. An impairment loss is reversed if there has been a change in the estimate used to determine the recoverable amount. An impairment loss is reversed only to the extent that the carrying amount of the asset (or CGU) does not exceed the carrying amount that would have been determined, net of depletion and depreciation, had no impairment loss been recognized for the asset (or CGU). A reversal of an impairment loss is recognized immediately in earnings.

E&E assets are assessed for impairment when they are reclassified to oil and gas properties, or if facts and circumstances suggest that the carrying amount exceeds the recoverable amount.

### 3.7 Asset retirement obligation (ARO)

Provision is made for the present value of the future cost of abandonment of oil and gas wells and related facilities. This provision is recognised when a legal or constructive obligation arises.

The estimated costs, based on engineering cost estimates prevailing at the reporting date, are computed on the basis of the latest assumptions as to the scope and method of abandonment. Provisions are measured at the present value of the expenditures expected to be required to settle the obligation using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the obligation. The corresponding amount is capitalised as part of exploration and evaluation expenditure or oil and gas properties and is amortised on a unit-of-production basis on the same basis as the related asset. Any adjustment arising from the reassessment of the estimated cost of the ARO is capitalized. The charge arising from the accretion of the discount applied to the ARO is treated as a component of finance costs.

Management has determined that, based on the exploration work carried out to date, there is no legal or constructive obligation requiring remediation of the Company's oil and gas property at this time.

### 3.8 Financial assets and liabilities

Financial assets and financial liabilities are recognised on the Company's statement of financial position when the Company becomes party to the contractual provisions of the instrument. Financial assets are de-

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recognised when the contractual rights to the cash flows from the financial asset expire or when the contractual rights to those assets are transferred.

Financial liabilities are de-recognised when the obligation specified in the contract is discharged, cancelled or expired. It is the Company's policy that when there is a change to the contractual terms of a financial liability, the Company will use quantitative criteria to establish if the change in the contractual terms resulted in an extinguishment of the financial liability. The Company will also consider qualitative criteria to assess if the change in the contractual terms resulted in a substantially different revised terms and accordingly will account for the change in the contractual terms as an extinguishment even if the quantitative criteria are not met.

The Company classifies its financial assets as loans and receivables. Loans and receivables and financial liabilities are recognized initially at fair value and subsequently at amortized cost using the effective interest method.

Financial assets and liabilities are classified as current if the assets are realized / liabilities are settled within 12 months. Otherwise, they are presented as non-current.

### **3.9 Cash and cash equivalents**

Cash and cash equivalents comprise cash in hand, deposits held on call with banks and other short-term highly liquid investments with original maturities of three months or less. Cash and cash equivalents have been classified as loans and receivables and are measured at amortized cost using the effective interest rate method.

### **3.10 Trade payables**

Trade payables are obligations to pay for goods or services that have been acquired in the ordinary course of business from suppliers. Trade payables are classified as other financial liabilities and are measured at amortised cost using the effective interest method.

### **3.11 Conversion of debt to equity**

It is the Company's policy that when there is a conversion of debt to equity and the creditor is a shareholder acting in its capacity as such, then the equity issued is recorded at the carrying amount of the financial liability extinguished. No gain or loss arises from the conversion of debt to equity.

### **3.12 Derivative financial instruments**

The Company's derivative instruments are the share purchase warrants issued. During the period, the Company issued warrants as part of a Unit offering. These share purchase warrants were issued with an exercise price in Canadian dollars rather than Chinese Yuan (the functional currency of the Company). Such share purchase warrants are considered to be derivative instruments.

The Company measured the warrant liability at fair value at the date which the warrants were issued. The Company's warrant liability is subsequently revalued by reference to the fair value of the warrants at each reporting date using the Black Scholes model and the exchange rate at the balance sheet date with changes in fair value recorded to the income (loss) statement. Valuation of the warrant liability also requires determining the most appropriate inputs to the valuation model and making assumptions about them. Significant

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assumptions include: expected life of the warrants, volatility, and dividend yield. A change in the valuation model or related inputs would change the reported amount of the components of the instrument.

### 3.13 Share capital

Ordinary shares are classified as equity. Incremental costs directly attributable to the issue of new ordinary shares or options are shown in equity as a deduction, net of tax, from the proceeds.

Share purchase warrants that are issued for underwriting services are initially accounted for under IFRS 2 as equity instruments (their initial fair value would be recognized as a share issue cost). Subsequent to their issuance, share purchase warrants issued for services that can be tracked (are non-transferable) are considered as equity for their entire life. The fair values of such share purchase warrants are not re-measured. Where these share purchase warrants are ultimately exercised, the applicable amounts of share purchase warrants are credited to share capital.

### 3.14 Current and deferred income tax

Tax is recognized in the income statement, except to the extent that it relates to items recognized in other comprehensive income or directly in equity. In this case, the tax is also recognized in other comprehensive income or directly in equity, respectively.

The income tax charge is calculated on the basis of the tax laws enacted or substantively enacted at the balance sheet date in the countries where the Company and its subsidiaries operate and generate taxable income. Management periodically evaluates positions taken in tax returns with respect to situations in which applicable tax regulation is subject to interpretation. It establishes provisions where appropriate on the basis of amounts expected to be paid to the tax authorities. As the Company and its subsidiaries are domiciled in an income tax-exempt jurisdiction and are in a taxable loss position in People's Republic of China (PRC), no income tax charges have been recognized during the period.

Deferred income tax is recognised, using the liability method, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the consolidated financial statements. Deferred income tax is determined using tax rates (and laws) that have been enacted or substantially enacted by the balance sheet date and are expected to apply when the related deferred income tax asset is realised or the deferred income tax liability is settled.

Deferred income tax assets are recognised only to the extent that it is probable that future taxable profit will be available against which the temporary differences can be utilized.

Deferred income tax is provided on temporary differences arising on investments in subsidiaries and associates, except for circumstances where the timing of the reversal of the temporary difference is controlled by the Company and it is probable that the temporary difference will not reverse in the foreseeable future.

Deferred income tax assets and liabilities are offset when there is a legally enforceable right to offset current tax assets against current tax liabilities and when the deferred income taxes assets and liabilities relate to income taxes levied by the same taxation authority on either the same taxable entity or different taxable entities where there is an intention to settle the balances on a net basis.

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## **3.15 Share-based payments**

The Company has a share-based compensation plan, details of which are disclosed in note 10. The Company applies the fair value based method of accounting to recognize the expenses arising from stock options granted to employees and non-employees. The fair value is determined using the Black – Scholes option pricing model, which requires the use of certain assumptions including future stock price volatility and expected life of the instruments.

The total share-based compensation expense is recognised over the vesting period, which is the period over which all of the specified vesting conditions are to be satisfied. At the end of each reporting period, the Company revises its estimates of the number of options that are expected to vest based on the non-market vesting conditions. It recognises the impact of the revision to original estimates, if any, in the income statement of income (loss), with a corresponding adjustment to equity.

When the options are exercised, the Company issues new shares. The proceeds received net of any directly attributable transaction costs are credited to share capital when the options are exercised.

## **3.16 Revenue recognition**

Revenue is measured at the fair value of the consideration received or receivable, and represents amounts receivable for goods supplied, stated net of discounts, returns and value added taxes. The Company recognizes revenue when the amount of revenue can be reliably measured; when it is probable that future economic benefits will flow to the entity; and when specific criteria have been met for each of the Company's activities, as described below. The Company bases its estimate of return on historical results, taking into consideration the type of customer, the type of transaction and the specifics of each arrangement.

Revenues from the sale of petroleum, natural gas and other related products are recorded when title passes to an external party.

## **3.17 Per share amounts**

Basic earnings (loss) per share is computed by dividing the net earnings or loss for the period by the weighted average number of common shares outstanding during the period. Diluted per share amounts reflect the potential dilution that could occur if the Company's stock options and warrants outstanding are exercised into common shares. Diluted shares are calculated using the treasury stock method which assumes that any proceeds received from "in-the-money" stock options would be used to buy back common shares at the average market price for the period. No adjustment is made to the weighted average number of common shares if the result of these calculations is anti-dilutive.

## **3.18 Borrowing costs**

Borrowing costs attributable to the acquisition, construction or production of qualifying assets are added to the cost of those assets, until such time as the assets are substantially ready for their intended use. All other borrowing costs are recognised as finance costs in the statement of comprehensive income (loss) in the period in which they are incurred.

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## 4 Changes in accounting standards

The Company has adopted the following new and revised standards, along with any consequential amendments, effective April 1, 2013. These changes were made in accordance with the applicable transitional provisions:

- a) IFRS 10, 'Consolidated Financial Statements' was issued in May 2011 and will supersede the consolidation requirements in SIC-12 'Consolidation — Special Purpose Entities' and IAS 27 'Consolidated and Separate Financial Statements' effective for annual periods beginning on or after January 1, 2013, with early application permitted. IFRS 10 builds on existing principles by identifying the concept of control as the determining factor in whether an entity should be included within the consolidated financial statements of the parent company. The standard also provides additional guidance to assist in the determination of control where this is difficult to assess. The adoption of the standard has no impact on the Company's interim financial statements.
- b) IFRS 11, 'Joint Arrangements' was issued in May 2011 and will supersede existing IAS 31, 'Joint Ventures' effective for annual period beginning on or after January 1, 2013, with early application permitted. IFRS 11 provides for the accounting of joint arrangements by focusing on the rights and obligations of the arrangement, rather than its legal form (as is currently the case). The adoption of the standard has no impact on the Company's interim financial statements.
- c) IFRS 12, 'Disclosure of Interests in Other Entities' was issued in May 2011 and is a new and comprehensive standard on disclosure requirements for all forms of interests in other entities, including subsidiaries, joint arrangements, associates and unconsolidated structured entities. IFRS 12 is effective for annual periods beginning on or after January 1, 2013, with earlier application permitted. The adoption of the standard has no impact on the Company's interim financial statements.
- d) IFRS 13, 'Fair Value Measurement' was issued in May 2011 and sets out in a single IFRS a framework for measuring fair value. IFRS 13 defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. This definition of fair value emphasizes that fair value is a market-based measurement, not an entity-specific measurement. In addition, IFRS 13 also requires specific disclosures about fair value measurement. IFRS 13 is effective for annual periods beginning on or after January 1, 2013, with earlier application permitted. The adoption of IFRS 13 did not require any adjustment to the valuation technique used by the Company to measure fair value and did not result in any measurement adjustments.
- e) IAS 1, 'Presentation of Financial Statements' was amended in June 2011. This standard requires companies preparing financial statements under IFRS to group items within Other Comprehensive Income (OCI) that may be reclassified to the profit or loss. The amendments also reaffirm existing requirements that items in OCI and profit or loss should be presented as either a single statement or two consecutive statements. The amendments to IAS 1 set out in Presentation of Items of OCI are effective for fiscal years beginning on or after July 1, 2012. This adoption of the standard has no impact on the Company's interim financial statements.

The Company has not early adopted the following standards, amendments and interpretations to existing standards that are not yet effective.

Certain new standards, interpretations, amendments and improvements to existing standards were issued by the IASB or International Financial Reporting Interpretations Committee (IFRIC) that are mandatory for accounting periods beginning after April 1, 2014 or later periods. The standards that are applicable to the Company are as

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follows:

- a) IAS 32, “Financial instruments”: Presentation has been amended to clarify some of the requirements for offsetting financial assets and financial liabilities on the balance sheet. This standard has no impact on the Company.
- b) IAS 36, “Impairment of Assets”, has been amended to address the disclosure of information about the recoverable amount of impaired assets if that amount is based on fair value less costs of disposal. This standard has no impact on the Company.
- c) IFRS 9, Financial Instruments (“IFRS 9”), was published on July 2014 which replaces the guidance in IAS 39. This final version includes requirements on the classification and measurement of financial assets and liabilities; it also includes an expected credit losses model that replaces the incurred loss impairment model used today. The final hedging part of IFRS 9 was issued in November 2013.

The standard is effective for annual periods beginning on or after January 1, 2018, with early application permitted. The Company will be required to adopt this standard.

We are currently assessing the effect of this standard and related amendments on our financial statements.

## 5 Financial risk management

### 5.1 Financial risk factors:

The Company’s financial instruments consist of cash and cash equivalents, accounts payable and accrued liabilities, shareholder loan, cash calls payable and derivative warrant liabilities.

Fair values of assets and liabilities approximate amounts at which these items could be exchanged in transactions between knowledgeable parties. Fair value is based on available public market information or when such information is not available, estimated using present value techniques and assumptions concerning the amount and timing of future cash flows and discount rates which factor in the appropriate credit risk. The calculation of estimated fair value is based on market conditions at the specific point in time and in the respective geographic locations and may not be reflective of future values.

The fair value of the financial assets and current liabilities approximates their carrying value.

The Company’s financial instruments are exposed to certain financial risks, including currency risk, credit risk, liquidity risk and interest rate risk.

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## (a) Currency risk

The Company held financial instruments in different currencies during the period/year ended as follows:

|                                       | Sep 30, 2014     | Mar 31, 2014     |
|---------------------------------------|------------------|------------------|
| Cash and cash equivalents of:         |                  |                  |
| - CAD\$                               | CAD\$104,701     | CAD\$156,625     |
| - US\$                                | US\$285,894      | US\$3,609,762    |
| - GBP                                 | GBP30,080        | GBP72,339        |
| - HK\$                                | HK\$3,580,410    | HK\$629,345      |
| Shareholder loan of US\$              | (US\$10,166,667) | (US\$3,494,871)  |
| Advance from a related party of CAD\$ | -                | (CAD\$1,700,000) |

Based on the above net exposures, and assuming that all other variables remain constant, a 10% depreciation or appreciation of the Renminbi against the Canadian dollar, US dollar, British Pound and Hong Kong dollar, would result in an increase/decrease of the Company's net (loss) income of approximately:

|         | Sep 30, 2014<br>RMB | Mar 31, 2014<br>RMB | Sep 30, 2014<br>CAD\$ |
|---------|---------------------|---------------------|-----------------------|
| - CAD\$ | 57,952              | 866,296             | 10,470                |
| - US\$  | 6,101,377           | 71,290              | 1,102,327             |
| - GBP   | 30,140              | 74,726              | 5,445                 |
| - HK\$  | 284,643             | 50,348              | 51,426                |

## (b) Credit risk

Credit risk is the risk of an unexpected loss if a customer or third party to a financial instrument fails to meet its contractual obligations.

The Company's cash and cash equivalents are held at a large international financial institution in interest bearing accounts. Minimal cash balances are held in Chinese financial institutions.

## (c) Liquidity risk

Liquidity risk is the risk that the Company will not be able to meet its financial obligations as they fall due.

Financing will be required to fund the Company's obligations in relation to the LS36-1 Development and in relation to any future exploration work. On November 17, 2014 PECL and PPC entered into a syndicated project finance facility to fund their respective share of the Development costs with CDB and EXIM as joint lead arrangers and SPDB as participant and agent bank. The syndicate loan is for a total amount of US\$ 274 million (of which the Company's share is US\$ 205.5 million). The loan facility is sufficient to cover all of the obligations of PECL and PPC with respect to the costs of the Development to date.

In addition, in June 2014, Mr. Hwang agreed to provide the Company an interest free loan of US\$



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8,000,000 to meet the Company's overhead requirement and to carry out its exploration activities under the New Contract for the coming twelve months. The Company is actively exploring all possible fund-raising possibilities for the planned exploration drilling program.

Additional information regarding liquidity risk is disclosed in Note 1.

The Company's non-derivative financial liabilities which are amounts due on the shareholder loan are repayable on demand after December 31, 2015.

## *(d) Interest rate risk*

Interest rate risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market interest rates. The Company has minimal interest rate risk.

## **5.2 Capital management**

The Company's objectives when managing capital are to safeguard the Company's ability to continue as a going concern in order to pursue the exploration and development of its petroleum property interests, acquire additional petroleum property interests and to maintain a flexible capital structure which optimizes the costs of capital at an acceptable risk. In the management of capital, the Company includes its cash and cash equivalent balances and components of shareholders' equity.

The Company manages the capital structure and makes adjustments to it in light of changes in economic conditions and the risk characteristics of the underlying assets. To maintain or adjust the capital structure, the Company may attempt to issue new shares, issue debt, acquire or dispose of assets or adjust the amount of cash and cash equivalents and investments.

In order to facilitate the management of its capital requirements, the Company prepares annual expenditure budgets that are updated as necessary depending on various factors, including successful capital deployment and general industry conditions. The annual and updated budgets are approved by the Board of Directors.

At this stage of the Company's development, in order to maximize ongoing development efforts, the Company does not pay out dividends.

Additional information regarding capital management is disclosed in note 1.

## **6 Critical judgments and accounting estimates**

The preparation of interim financial statements in conformity with IFRS requires management to make judgments, estimates and assumptions that affect the reported amounts of assets, liabilities and expenses. Estimates and judgments are regularly evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances. Uncertainty about these assumptions and estimates could result in outcomes that require a material adjustment to the carrying amount of assets or liabilities affected in future periods. Further information on management's judgments, estimates and assumptions and how they impact the various accounting policies are described below and also in the relevant notes to the consolidated financial statements.

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The most significant judgments made by management in applying accounting policies when preparing the Company's interim financial statements are described as follows:

## Exploration and evaluation assets

The Company applies critical judgment in the application of accounting policies as to when technical feasibility and commercial viability of an oil and gas resource is considered to be established (Note 3.4) and has determined that the Company continues to be an exploration company.

## Shareholder loan

Shareholder loans are recorded at fair value on inception in accordance with IAS 39 and carried at amortized cost. The difference between the fair value of these loans and cash received represents a capital contribution which is recorded directly in equity.

The Company follows the guidance of IAS 39 to assess whether a change in the contractual terms of the shareholder loans is substantial enough to represent an extinguishment of the original agreement. This determination requires significant judgment. In making this judgment, the Company, evaluates, among other factors, the quantitative criteria and the qualitative criteria to assess if the change in the contractual terms result in a substantially different revised terms and account for the change in the contractual terms as an extinguishment (Note 3.8).

The Company considers that, when there is a conversion of shareholder loans to equity, the related party is not acting as a creditor of the Company. As such, the equity issued is recorded at the carrying amount of the financial liability extinguished and neither gain nor loss arises (Note 3.11).

## Impairment of exploration and evaluation assets

The Company reviews and evaluates the carrying value of exploration and evaluation assets for impairment when events or changes in circumstances indicate that the carrying amounts of the asset may not be recoverable. The identification of such events or changes and the performance of the assessment require significant judgment. No impairment indicators were noted at the end of the financial year.

## 7 Exploration and evaluation assets

|   | <b>Exploration and<br/>evaluation assets</b> |
|---|--|
|   | RMB  |
| <b>Balance at March 31, 2013</b>                      | 444,002,914                                  |
| Additions   | 18,100,944                                   |
| <b>Balance at March 31, 2014</b>                      | 462,103,858                                  |
| Additions   | 51,005,768                                   |
| <b>Balance at September 30, 2014</b>                  | 513,109,626                                  |
|   | CAD\$  |
| <b>Balance September 30, 2014 in CAD\$ (note 3.3)</b> | 92,702,733                                   |

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The Company and PPC are the Contractors under a petroleum contract dated March 24, 2005 (Petroleum Contract) with CNOOC to explore, develop and produce oil and gas reserves that may exist in an area known as Block 25/34 (the Contract Area) in Lishui and Jiaojiang Basins, East China Sea. PECL and PPC hold 75% and 25% of the Contractors' interest, respectively and PEOIL is appointed as operator for the Contract Area.

The Petroleum Contract became effective on May 1, 2005, and had three periods: exploration, development and production, with a maximum contract term of 30 years. The exploration period was seven years while the production period was 15 years. The exploration period was further subdivided into three exploration phases, which included the first phase of three contract years (the first contract year through the third contract year); the second phase of two contract years (the fourth contract year through the fifth contract year); and the third phase of two contract years (the sixth contract year through the seventh contract year).

Under the Petroleum Contract the Contractors were committed to drilling one exploration well in each of the three exploration phases (plus an additional 200 square kilometers of 3D seismic surveys in phase one)

The Petroleum Contract provided that the Contractors would fund all costs incurred during the exploration period, and CNOOC had the right to participate in up to 51% of any future development and production of oil and/or gas fields in the Contract Area by paying its pro rata share of the development and production costs.

By an Amendment Agreement dated February 18, 2008 between CNOOC, the Company and PPC, the parties agreed that the Petroleum Contract be amended to provide that the exploration period beginning on the date of the commencement of the implementation of the contract shall be divided into three phases and shall consist of 8 years rather than 7 years. The first exploration period was to be for a period of four years from the date of commencement on May 1, 2005, and the second and the third exploration phases shall be for two year periods respectively.

On March 17, 2010, CNOOC, PECL and PPC signed a supplemental development agreement, joint operating agreement and implementation agreement (collectively "Development Agreements") with respect to the development of the LS36-1 gas field. A development and production area of 85 sq km was designated. CNOOC was appointed as operator for the development and production of the LS36-1 gas field and development operations commenced soon after.

From 2010 to 2014, CNOOC, PECL and PPC completed the development of the LS36-1 gas field which has now been on stream since July 2014 to supply gas to Zhijiang Province. Production has averaged 23.3 mmcfpd since early September 2014.

On July 15, 2011, the Company signed a Memorandum of Agreement ("MOA") with CNOOC to further amend the Petroleum Contract. The MOA amended the Petroleum Contract so that no further exploration activity would be carried out under that contract and the Company and PPC relinquished all of the area held under the Petroleum Contract, save for the development area for the LS36-1 gas field. The Petroleum Contract remains in effect in relation to the continuing development and production operations for the LS36-1 gas field.

The MOA further provided that the parties would enter into a new petroleum contract and, on June 15, 2012, the Company and PPC signed the new petroleum contract (the "New Contract") with CNOOC to explore, develop and produce oil and gas reserves that may exist in an area known as Block 33/07 in East China Sea. Block 33/07 covers the same area as that previously held under Block 25/34 but with an additional adjacent area to the east.

The New Contract became effective from November 21, 2012 after ratification by the Ministry of Commerce in the People's Republic of China. The New Contract is held by PECL and PPC in the same proportions in which

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they held the Petroleum Contract being 75%/25% and PEOIL is the operator. The New Contract provides for an exploration period, a development and production period. The exploration period is for 7 consecutive years divided into 3 exploration periods of 3, 2 and 2 years each with a minimum work commitment in the first phase of two wells plus 600 sq kms of 3D seismic surveys. The commitment for each of the second and third phases is one well. PEOIL acts as the operator for the exploration operation, development operation and production operation within this new contract area.

During the year, PEOIL entered into an agreement with China Oilfield Services Ltd (“COSL”) to carry out the acquisition and processing of seismic data on a turnkey basis for part of the Company and PPC’s rolling development and exploration program. Under the Turnkey Contract, COSL gathered the 3D seismic data over 600 sq km. The survey started in March 2014 and completed in May 2014. The processing will take about 4-5 months and will allow the Company and PPC to merge the new data with the existing 3D seismic data for interpretation in Q3 2014. Exploration drilling comprising two commitment wells is planned for 2015 fiscal year.

Any future discoveries in the New Contract area (and any CNOOC self -financed discoveries nearby, if there is spare capacity) will use the production facilities built for the LS36-1 gas field.

## 8 Property, plant and equipment

|                                    | Computer & Office<br>Equipment | Computer &<br>Office Equipment |
|------------------------------------|--------------------------------|--------------------------------|
|                                    | RMB                            | CAD\$<br>(note 3.3)            |
| <b>COST</b>                        |                                |                                |
| At April 1, 2013                   | 20,425                         | 3,690                          |
| Additions                          | -                              | -                              |
| <b>At March 31, 2014</b>           | <b>20,425</b>                  | <b>3,690</b>                   |
| Additions                          | -                              | -                              |
| <b>At September 30, 2014</b>       | <b>20,425</b>                  | <b>3,690</b>                   |
| <b>DEPRECIATION AND IMPAIRMENT</b> |                                |                                |
| At April 1, 2013                   | 6,108                          | 1,104                          |
| Charge for the year                | 6,128                          | 1,107                          |
| <b>At March 31, 2014</b>           | <b>12,236</b>                  | <b>2,211</b>                   |
| Charge for the year                | 3,063                          | 553                            |
| <b>At September 30, 2014</b>       | <b>15,299</b>                  | <b>2,764</b>                   |
| <b>CARRYING VALUES</b>             |                                |                                |
| At April 1, 2013                   | 14,317                         | 2,586                          |
| At March 31, 2014                  | 8,189                          | 1,479                          |
| <b>At September 30, 2014</b>       | <b>5,126</b>                   | <b>926</b>                     |

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## 9 Derivative warrant liability

The Company issued share purchase warrants in connection with the private placement offering completed on December 30, 2013 and January 23, 2014 (see Note 10 (a) (ii)). These warrants are exercisable in Canadian dollars. As the functional and reporting currency of the Company is RMB, share purchase warrants with an exercise price in a different currency are considered a derivative instrument under IAS 32.

The initial fair value on recognition of the share purchase warrants was calculated using the Black-Scholes pricing model, using the assumptions in the following table. Subsequent to their initial recognition, the share purchase warrants liability is re-measured and re-translated each reporting period in accordance with IAS 32.

Tranche 1 on December 30, 2013:

|   | <b>As at September 30, 2014</b> | <b>As at March 31, 2014</b> | <b>At date of issue<br/>December 30, 2013</b> |
|---|---------------------------------|-----------------------------|---|
| Exchange rate at date of fair value (RMB/CAD) | 5.535                           | 5.613                       | 5.705   |
| Stock price                                   | CAD\$0.46                       | CAD\$0.57                   | CAD\$0.63                                     |
| Exercise price                                | CAD\$0.90                       | CAD\$0.90                   | CAD\$0.90                                     |
| Risk free interest rate                       | 1.12%                           | 1.07%                       | 1.09%   |
| Expected dividend yield                       | Nil                             | Nil                         | Nil   |
| Expected stock price volatility               | 77%                             | 70%                         | 83%   |
| Expected warrant life                         | 1.25 years                      | 1.75 years                  | 2 years                                       |

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Tranche 2 on January 23, 2014:

|   | <b>As at September 30, 2014</b> | <b>As at March 31, 2014</b> | <b>At date of issue<br/>January 23, 2014</b> |
|---|---------------------------------|-----------------------------|--|
| Exchange rate at date of fair value (RMB/CAD) | 5.535                           | 5.613                       | 5.55   |
| Stock price                                   | CAD\$0.46                       | CAD\$0.57                   | CAD\$0.53                                    |
| Exercise price                                | CAD\$0.90                       | CAD\$0.90                   | CAD\$0.90                                    |
| Risk free interest rate                       | 1.12%                           | 1.07%                       | 0.97%  |
| Expected dividend yield                       | Nil                             | Nil                         | Nil  |
| Expected stock price volatility               | 73%                             | 74%                         | 73%  |
| Expected warrant life                         | 1.32 years                      | 1.82 years                  | 2 years                                      |

The Company's warrant liability for the period ended September 30, 2014 and year ended March 31, 2014 is set out below:

|   | <b>Warrants Outstanding</b> | <b>Value assigned RMB</b> | <b>Value assigned CAD\$</b> | <b>Average exercise price CAD\$</b> |
|---|-----------------------------|---------------------------|-----------------------------|-------------------------------------|
| Balance – as at March 31, 2013          | -                           | -                         | -                           | -                                   |
| Warrants issued                         | 4,586,250                   | 5,406,242                 | 976,737                     | 0.90                                |
| Fair value re-measurement in the year   | -                           | (1,997,759)               | (360,932)                   | -                                   |
| Balance – as at March 31, 2014          | 4,586,250                   | 3,408,483                 | 615,805                     | 0.90                                |
| Fair value re-measurement in the period | -                           | (1,718,559)               | (310,489)                   | -                                   |
| Balance – as at September 30, 2014      | 4,586,250                   | 1,689,924                 | 305,316                     | 0.90                                |

The share purchase warrants outstanding and exercisable as at September 30, 2014 is set out below:

| <b>Exercise Price CAD\$</b> | <b>Expiry date</b> | <b>Number</b> |
|-----------------------------|--------------------|---------------|
| 0.90                        | December 30, 2015  | 3,826,250     |
| 0.90                        | January 23, 2016   | 760,000       |

# Primeline Energy Holdings Inc.

(an exploration stage company)

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## 10 Share capital

### a) Authorized Share capital

The Company is authorized to issue 500,000,000 ordinary shares with a par value of US\$0.001 each. As at September 30, 2014 the total issued share capital of the Company was 112,791,018 common shares.

|   | Number of shares | Share<br>Capital<br>RMB | Share<br>Premium<br>RMB | Total<br>RMB | Total<br>CAD\$ |
|---|------------------|-------------------------|-------------------------|--------------|----------------|
| Balance as at March 31, 2013  | 94,041,246       | 858,406                 | 437,506,225             | 438,364,631  | 79,198,669     |
| Shareholder loan converted to ordinary shares (Note i)                  | 9,427,272        | 86,052                  | 27,762,246              | 27,848,298   | 5,031,309      |
| Share issue costs in relation to shareholder loan conversion (Note iii) | -                | -                       | (15,291)                | (15,291)     | (2,763)        |
| Gross proceeds from private placement (Note ii)                         | 9,172,500        | 83,744                  | 23,157,742              | 23,241,486   | 4,199,004      |
| Share issue costs incurred in relation to private placement (Note iii)  | -                | -                       | (2,958,390)             | (2,958,390)  | (534,488)      |
| Share issue costs - Broker Warrants (Note iv)                           | -                | -                       | (1,213,235)             | (1,213,235)  | (219,193)      |
| Balance – as at March 31, 2014  | 112,641,018      | 1,028,202               | 484,239,297             | 485,267,499  | 87,672,538     |
| Broker Warrants exercised (Note v)                                      | 150,000          | 1,370                   | 727,310                 | 728,680      | 131,650        |
| Balance – as at September 30, 2014                                      | 112,791,018      | 1,029,572               | 484,966,607             | 485,996,179  | 87,804,188     |

- i) On October 10, 2013, Mr. Victor Hwang, the majority shareholder, director and officer of the Company agreed to convert US\$5,000,000 of the shareholder loans payable to him into 9,427,272 common shares. This transaction was approved by the TSX Venture Exchange (the "TSX-V") on November 7, 2013. The carrying amount of the loan payable to Mr. Hwang on November 7, 2013, immediately prior to the conversion to common shares, was RMB28,957,699 (CAD\$5,231,43). The Company recorded the shares issued to Mr. Hwang at the carrying amount of the financial liability extinguished.
- ii) On December 30, 2013, the Company completed the first tranche of a private placement ("Private Placement") offering led by D&D Securities Inc. (the "Agent") as agent. The Company issued a total of 7,652,500 units ("Units") at a price of CAD\$0.55 per Unit for gross proceeds of CAD\$4,208,875. Each Unit consists of one ordinary share (a "Common Share") and one half of one warrant (a "Warrant"). Each Warrant is exercisable to purchase a further Common Share at a price of CAD\$0.90 per share for period of two years following the closing date of the Private Placement. The Company has the right to accelerate expiry of the Warrants if the volume weighted average closing price of the common shares on the TSX-V exceeds CAD\$1.35 per share for 10 consecutive trading days by giving notice, whereupon the Warrants will expire 30 days from the date of notice. The Company considered the value of the right to accelerate as immaterial. The Common Shares comprised in the Units, the Warrants, and any Common Shares issued on exercise of the Warrants, are subject to a hold period of four months plus one day from the closing date.

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The Company first calculated the fair value of the derivative warrant liabilities (see Note 9) that were issued using the Black Scholes model, and the remaining cash proceeds were allocated between share capital and share premium.

On January 23, 2014, the company closed the second and final tranche of the Private Placement. In this second tranche Primeline issued a total of 1,520,000 Units at a price of CAD\$0.55 per Unit for gross proceeds of CAD\$836,000. Each Unit consists of one Common Share and one half of one Warrant. Each Warrant is exercisable to purchase a further Common Share at a price of CAD\$0.90 per share for 24 months from the closing date. The Company will have the right to accelerate expiry of the Warrants if the volume weighted average closing price of the common shares on the TSX-V exceeds CAD\$1.35 per share for 10 consecutive trading days by giving notice, whereupon the Warrants will expire 30 days from the date of notice. The Company considered the value of the right to accelerate as immaterial. The Common Shares comprised in the Units, the Warrants and any Common Shares issued on exercise of the Warrants and the Broker Warrants, are subject to a hold period of four months plus one day from the closing date.

The Company first calculated the fair value of the derivative warrant liabilities (see Note 9) that were issued using the Black Scholes model, and the remaining cash proceeds were allocated between share capital and share premium.

- iii) In relation to the shareholder loan conversion and Private Placement, the Company incurred share issue costs of RMB2,973,681 (CAD\$537,250) in total as follows:

The Company incurred legal and professional fees of RMB 15,291 (CAD\$2,763) for the shareholder loan conversion.

In connection with the Private Placement, the Company incurred RMB2,958,390 (CAD\$534,488) share issuance costs which are comprised of the Agent's fee of RMB2,005,341 (CAD\$362,302), and legal and professional costs of RMB953,049 (CAD\$172,186).

- iv) The Company issued 733,800 warrants ("Broker Warrants") exercisable to purchase a number of Common Shares equal to 8% of the number of Units sold by the Agent at an exercise price of CAD\$0.55 per share. The Broker Warrants and any Common Shares issued on exercise of the Broker Warrants are subject to a hold period of four months plus one day from the closing date.

The fair value of the Broker Warrants issued is RMB1,213,235 (CAD\$ 219,193). The Company calculated the fair value of the Broker Warrants, using the Black Scholes model.

- v) On June 2, 2014, a member of the Agent's selling group exercised 150,000 Broker Warrants at an exercise price of CAD\$0.55 per share. The Company received gross proceeds of RMB 465,616 (CAD\$84,122). The fair value of the Broker Warrants exercised of RMB 263,064 (CAD\$ 47,527) initially recognized in share purchase warrants reserve was transferred to share premium in Equity as at the date the Broker Warrants were exercised.



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b) Broker Warrants

|   | Warrants<br>outstanding | Value<br>assigned<br>RMB | Value<br>assigned<br>CAD\$ | Average<br>exercise price<br>CAD\$ |
|---|-------------------------|--------------------------|----------------------------|------------------------------------|
| Balance as at March 31, 2013                      | -                       | -                        | -                          | -                                  |
| Broker Warrants issued (see note 10 (a)(iv))      | 733,800                 | 1,213,235                | 219,193                    | 0.55                               |
| Balance as at March 31, 2014                      | 733,800                 | 1,213,235                | 219,193                    | 0.55                               |
| Broker Warrants exercised<br>(see note 10 (a)(v)) | (150,000)               | (263,064)                | (47,527)                   | 0.55                               |
| Balance as at September 30, 2014                  | 583,800                 | 950,171                  | 171,666                    | 0.55                               |

The number of Broker Warrants outstanding and exercisable as at September 30, 2014 is set out below:

| Exercise Price CAD\$ | Expiry date       | Number  |
|----------------------|-------------------|---------|
| 0.55                 | December 30, 2015 | 462,200 |
| 0.55                 | January 23, 2016  | 121,600 |

The fair value of the Broker Warrants granted has been calculated using the Black-Scholes option pricing model, using the following assumptions:

|                                 | Broker Warrants issued<br>on December 30, 2013 | Broker Warrants issued<br>on January 23, 2014 |
|---------------------------------|--|---|
| Risk free interest rate         | 1.09%  | 0.97%   |
| Expected dividend yield         | Nil  | Nil   |
| Expected stock price volatility | 83%  | 73%   |
| Expected warrant life           | 24 Months                                      | 24 Months                                     |

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## c) Share Purchase Options

The Company has a stock option plan (the “Plan”), pursuant to which the directors are authorized to grant options to purchase up to 10% of the issued and outstanding Common Shares from time to time. The options enable the directors, officers, consultants and employees of the Company to acquire Common Shares. The exercise price of a share option is set by the board of directors, subject to TSX-V policy. Options granted under the Plan may have a maximum term of ten years and, subject to any vesting restrictions imposed by the TSX-V, shall vest over such period as is determined by the board of directors at the grant date.

The following table summarizes the stock option activity under the Plan.

|                          | <b>Options<br/>outstanding</b> | <b>Weighted<br/>Average exercise<br/>price<br/>CAD\$</b> | <b>Options<br/>exercisable</b> | <b>Weighted<br/>Average<br/>exercise<br/>price</b> |
|--------------------------|--------------------------------|--|--------------------------------|--|
| As at April 1, 2013      | 5,505,000                      | 0.49   | 1,766,660                      | 0.37   |
| As at March 31, 2014     | 5,505,000                      | 0.49   | 2,400,000                      | 0.36   |
| Additions                | 450,000                        | 0.68   | -                              |  |
| As at September 30, 2014 | 5,955,000                      | 0.51   | 2,400,000                      | 0.36   |

On July 27, 2011, the Company granted 2,100,000 options at an exercise price of CAD\$0.32 per share to directors, officers, employees and consultants, of which 200,000 options have expired and 1,900,000 options will expire on July 27, 2016. Share based payments of RMB Nil (CAD\$ Nil) and RMB Nil (CAD\$ Nil) (2013 – RMB67,570 and RMB34,630) were recognized as Directors remuneration & benefit and Salary & benefit respectively in the consolidated statement of loss and comprehensive loss. Share based payment of RMB Nil (CAD\$ Nil) (2013 – RMB58,277) was capitalized as exploration and evaluation assets.

The share options vested according to the following schedule:

| <b>Vesting date</b> | <b>Number of Share<br/>options</b> |
|---------------------|------------------------------------|
| July 27, 2011       | 700,000                            |
| July 27, 2012       | 700,000                            |
| July 27, 2013       | 700,000                            |

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On July 9, 2012, the Company granted to D&D Securities Inc. options to purchase a total of 500,000 Common Shares at an exercise price of CAD\$0.50 per share in consideration of D&D Securities Inc.'s ongoing services on corporate marketing and investor relations. The options expire on June 25, 2017. Share based payments of RMB nil (2013 – RMB nil) were recognized as business promotion in the consolidated statement of loss and comprehensive loss.

The share options vested according to the following schedule:

| <b>Vesting date</b> | <b>Number of Share options</b> |
|---------------------|--------------------------------|
| July 9, 2012        | 200,000                        |
| September 30, 2012  | 100,000                        |
| December 31, 2012   | 100,000                        |
| March 31, 2013      | 100,000                        |

On September 26, 2012, the Company granted 3,105,000 options at an exercise price of CAD\$0.60 per share to directors, officers, employees and consultants. Such options will expire on September 26, 2017. Share based payments of RMB407,627 (CAD\$73,645), RMB185,285 (CAD\$33,475) and RMB150,081 (CAD\$27,115) (2013 – RMB433,586, RMB228,203 and RMB253,305) were recognized as Directors remuneration and benefit, professional fees and salary & benefit respectively in the consolidated statement of loss and comprehensive loss. Share based payment of RMB407,627 (CAD\$73,645) (2013 – RMB502,048) was capitalized as exploration and evaluation assets.

The share options vest according to the following schedule:

| <b>Vesting date</b>  | <b>Number of Share options</b> |
|--|--------------------------------|
| Upon date of full repayment of the existing shareholder loans                | 1,035,000                      |
| One year after the date of full repayment of the existing shareholder loans  | 1,035,000                      |
| Two years after the date of full repayment of the existing shareholder loans | 1,035,000                      |

On August 11, 2014, the Company granted 450,000 options at an exercise price of CAD\$0.68 per share to an officer. Such options will expire on August 11, 2019. Share based payments of RMB91,381 (CAD\$16,510) (2013 – Nil) were recognized as salary & benefit respectively in the consolidated statement of loss and comprehensive loss. Share based payment of RMB213,220 (CAD\$38,522) (2013 – Nil) was capitalized as exploration and evaluation assets.

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The share options vest according to the following schedule:

| <u>Vesting date</u> | <u>Number of Share options</u> |
|---------------------|--------------------------------|
| November 11, 2014   | 150,000                        |
| November 11, 2015   | 150,000                        |
| November 11, 2016   | 150,000                        |

Stock options outstanding and exercisable are as follows:

| <u>Exercise price</u>    | <u>Number of outstanding options</u> | <u>Weighted average remaining contractual life</u> | <u>Number of exercisable options</u> |
|--------------------------|--------------------------------------|--|--------------------------------------|
| As at March 31, 2014     |                                      |  |                                      |
| CAD\$0.32                | 1,900,000                            | 2.33 years   | 1,900,000                            |
| CAD\$0.50                | 500,000                              | 3.24 years   | 500,000                              |
| CAD\$0.60                | 3,105,000                            | 3.49 years   | -                                    |
| <b>5,505,000</b>         | <b>5,505,000</b>                     | <b>3.07 years</b>                                  | <b>2,400,000</b>                     |
| As at September 30, 2014 |                                      |  |                                      |
| CAD\$0.32                | 1,900,000                            | 1.82 years   | 1,900,000                            |
| CAD\$0.50                | 500,000                              | 2.74 years   | 500,000                              |
| CAD\$0.60                | 3,105,000                            | 2.99 years   | -                                    |
| CAD\$0.68                | 450,000                              | 4.87 years   | -                                    |
|                          | <b>5,955,000</b>                     | <b>2.37 years</b>                                  | <b>2,400,000</b>                     |

As at November 24, 2014, there are 112,791,018 Common Shares, 5,955,000 stock options and 5,170,050 Warrants and Broker Warrants outstanding.

## 11 Finance Income

|  | <u>For the six months ended</u> |              |              |
|--|---------------------------------|--------------|--------------|
|  | Sep 30, 2014                    | Sep 30, 2013 | Sep 30, 2014 |
|  | RMB                             | RMB          | CAD\$        |
| Bank interest income   | 1,104                           | 1,142        | 199          |
| Gain on extinguishment of Related Party's loan under revised loan facility | -                               | 1,111,304    | -            |
| Gain on fair value of re-measurement of warrant liability                  | 1,664,790                       | -            | 300,775      |

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1,665,894

1,112,446

300,974

During the period ended March 31, 2014, the Company issued share purchase warrants in connection with the private placement offering completed on December 30, 2013 and January 23, 2014 (note 10(a)(ii)). Subsequent to initial fair value recognition, the share purchase warrant liability is re-measured at the end of the reporting period (note 9).

## 12 Taxation

The Company is domiciled in an income tax-exempt jurisdiction and carries out its oil exploration activities in the People's Republic of China (PRC); these activities are subject to PRC income tax at a rate of 25%. In accordance with PRC tax regulation, exploration costs incurred by foreign oil and gas enterprises can be deferred and amortized, over a one year or three years period, from commencement of oil/gas production. The Company has nil deferred income tax.

## 13 Transactions with related parties and directors

During the period ended September 30, 2014, the Company paid or accrued the following:

- a) London office rent of RMB198,486 (CAD\$35,860) (2013 – RMB181,528) was paid or accrued to a company beneficially owned by Mr. Victor Hwang, the majority shareholder, director and officer of the Company.
- b) Cash call received from and utilized for PPC, a company owned by Mr. Hwang, the majority shareholder, director and officer of the Company, for its 25% contribution to exploration costs were RMB 6,182,133 (CAD\$1,116,917) (2013 – RMB2,960,120) and RMB15,759,435 (CAD\$2,847,233) (2013 – RMB2,618,019) respectively. The balance is recorded as a cash call payable on the statement of financial position amounting to RMB329,602 (CAD\$59,549) (2013 – RMB480,571).
- c) Fees and benefits paid or accrued to key management personnel of the Company were RMB2,318,581 (CAD\$418,894) (2013 – RMB2,232,124) and share based payment of RMB725,197 (CAD\$131,020) (2013 – RMB668,831) were recognized for the 2,360,000 (2013 – 2,260,000) share options granted to these key management personnel.
- d) Fees and benefits paid or accrued to directors were RMB284,025 (CAD\$50,000) (2013 – RMB294,325) and share based payment of RMB407,627 (CAD\$73,645) (2013 – RMB501,156) were recognized for the 2,100,000 (2013 – 1,750,000) share options granted to the directors.
- e) Shareholder loan of RMB 56,631,241 (CAD\$10,231,480) (2013 – RMB43,682,803) represents interest-free loans with a principal balance of RMB62,779,169 (CAD\$11,342,217) (2013 – RMB48,065,538) due to Mr. Victor Hwang, the majority shareholder, director and officer of the Company.

During the year ended March 31, 2014, Mr. Hwang advanced a loan amount of US\$1,203,846 which is interest free and repayable on demand so that together with the loan balance of US\$ 6,650,000 as at March 31, 2013, the aggregate amount owing to Mr. Hwang was US\$7,853,846 before October 2013. Then on October 10, 2013, the Company signed a debt settlement agreement with Mr. Victor Hwang, under which the 9,427,272 Common Shares were issued to Mr. Hwang in settlement of US\$5,000,000 of the existing debt owed by the Company to Mr. Hwang (CAD\$5,185,000 at the agreed exchange rate of US \$1/CAD\$1.037) at a deemed price of CAD\$0.55 per share. As a result, the amount owing to Mr. Hwang after such debt settlement was US\$ 2,853,846. On October 10, 2013, Mr. Hwang also agreed to extend another US\$5,000,000 loan facility to the Company. As at the date of such agreement, the amount

# Primeline Energy Holdings Inc.

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drawn down was US\$2,853,846 and the amount remaining available for drawdown was US\$ 2,146,153. This loan facility is interest-free and is repayable upon demand after July 31, 2015. As at March 31, 2014, the Company had drawn down a total of US\$3,494,871 from the facility with a remaining available facility of US\$ 1,505,129.

During the period ended September 30, 2014, the Company drew down the remaining US\$1,505,129 of the US\$5,000,000 facility, which is repayable upon demand after July 31, 2015. On July 31, 2014, Mr. Hwang agreed to extend the US\$5,000,000 facility for five months. It is now repayable upon demand after December 31, 2015. On June 30, 2014, Mr. Hwang agreed to advance an additional US\$8,000,000 interest-free loan facility to the Company. This loan is repayable upon demand after December 31, 2015. As at September 30, 2014, the Company has drawn down a total of US\$5,166,667 from the facility with a remaining available facility of US\$2,833,333.

The shareholder loan has been recorded at fair value on inception and carried at amortized cost. The discount on shareholder loan of RMB5,464,982 (CAD\$987,350) (2013 – RMB2,023,485) and the capitalized interest of RMB1,712,982 (CAD\$309,482) (2013 – RMB1,782,892) were calculated using an effective rate of 10% per annum during the six months period ended September 30, 2014.

- f) Advances from a related party of RMB Nil (CAD\$ Nil) (2013 – RMB8,410,046) represent an interest-free balance with a principal amount of RMB Nil (CAD\$Nil) (2013 – RMB10,094,600) from PPC.

The interest-free non-current advance from a related company has been recorded at fair value on inception and carried at amortized cost.

The capitalized interest of RMB1,229,353 (CAD\$222,105) (2013 – RMB414,037) were calculated using an effective rate of 10% per annum.

During this period, the Company funded CAD\$1.7million of PPC's share of the 3D seismic survey costs on behalf of PPC, thus repaying the advance.

These transactions are measured at the exchange amount, which is the amount of the consideration established and agreed by the related party.

## 14 Commitments

- a) Under the New Contract for Block 33/07, the Company has a 7 years exploration period divided into 3 exploration periods of 3, 2 and 2 years each with a minimum work commitment in the first phase of two wells plus 600 sq kms of 3D seismic surveys. The minimum expenditures for such exploration activities are estimated to be RMB 100 million of which the Company's 75% obligation would be a total of RMB75.6 million. Total exploration expenditures up to the end of the reporting period is RMB 60,330,005 (CAD\$10,899,730).
- b) The Company entered into a lease agreement for the rental of PEHI's Shanghai office in the PRC. The lease is for a period of one year from September 1, 2014 to August 31, 2015 with a monthly rental fee of RMB58,450 (CAD\$10,560).
- c) Under an agreement signed between the Company, PPC and CNOOC for the development and production of the LS 36-1 gas field within contract area 25/34 on March 17, 2010 (Implementation Agreement), CNOOC agreed to provide all funding in relation to the development operations until the ODP approval was obtained. CNOOC and the Company subsequently on August 21, 2014 agreed

# Primeline Energy Holdings Inc.

(an exploration stage company)

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that the Company would have another 4 month extension whereby it would have no obligation to fund cash calls nor will it be liable for costs expended by CNOOC for the development until December 20, 2014. With effect from December 20, 2014, the Company will become liable and will have the obligation to fund its share of the development costs according to the Implementation Agreement. This is currently anticipated to be approximately RMB 1,400 million (CAD\$ 240 million) being the Company's 36.75% share of the total development budget for LS36-1 Gas field.

## 15 Fair value measurement

Certain financial assets and liabilities are measured at fair value on a recurring basis and classified in their entirety based on the lowest level of input that is significant to the fair value measurement. Certain non-financial assets and liabilities may also be measured at fair value on a non-recurring basis. There are three levels of the fair value hierarchy that prioritize inputs to valuation techniques used to measure fair value, with Level 1 inputs having the highest priority. The levels and valuation techniques used to value the Company's financial assets and liabilities are described below:

### 1) Level 1- Quoted Prices in Active Markets for Identical Assets

Unadjusted quoted prices in active markets that are accessible at the measurement date for identical, unrestricted assets or liabilities.

The Company does not have any financial assets and liabilities that are included in Level 1 of the fair value hierarchy.

### 2) Level 2 – Significant Other Observable Inputs

Quoted prices in market that are not active, quote prices for similar assets or liabilities in active markets, or inputs that are observable, either directly or indirectly, for substantially the full term of the asset or liability.

Warrant liability is included in Level 2 of the fair value hierarchy as the warrants are valued using a pricing model, which require a variety of inputs, including but not limited to historical stock prices and discount rates.

### 3) Level 3 – Significant Unobservable Inputs

Unobservable (supported by little or no market activity) prices

The Company does not have any financial assets and liabilities that are included in Level 3 of the fair value hierarchy.

|   | As at September 30, 2014 |           |        |                  | March 31, 2014 |           |        |                  |
|---|--------------------------|-----------|--------|------------------|----------------|-----------|--------|------------------|
|   | Level1                   | Level2    | Level3 | Total            | Level1         | Level2    | Level3 | Total            |
| <b>Recurring fair value measurement</b> |                          |           |        |                  |                |           |        |                  |
| Warrant liability                       | -                        | 1,689,924 | -      | <b>1,689,924</b> | -              | 3,408,483 | -      | <b>3,408,483</b> |
|   | -                        | 1,689,924 | -      | <b>1,689,924</b> | -              | 3,408,483 | -      | <b>3,408,483</b> |

# Primeline Energy Holdings Inc.

(an exploration stage company)

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## **16 Subsequent Events**

- a) On October 29, 2014, CNOOC and Zhejiang Gas signed the final Natural Gas Sale Agreement. This supersedes the Gas Sale Agreement-in principle and subsequent Framework and Amendment Agreements signed between 2008 and 2012 and confirms general commercial terms already negotiated including, inter alia, gas quality, take-or-pay principles, base price and annual quantity.
  
- b) On November 17, 2014, the contracts for the project finance facility for the financing of the Company's share of the costs to complete the LS36-1 gas field development ("Development") was signed by the Company, PPC and the financing banks namely China Development Bank, China Export and Import Bank and Shanghai Pudong Development Bank. Following the signing of the documentation, the security arrangements and accounts set up will be implemented with first drawdown expected around the end of November.



**Primeline Energy Holdings Inc. (TSX Venture-PEH) (“the Company”)  
Management Discussion and Analysis for the Quarter Ended September 30, 2014**

**INTRODUCTION**

This Management Discussion and Analysis is dated November 24, 2014 and takes into account information available up to that date and should be read in conjunction with the audited annual consolidated financial statements for the year ended March 31, 2014 and interim consolidated financial statements for the quarter ended September 30, 2014 which are prepared in accordance with International Financial Reporting Standards (“IFRS”). All monetary amounts in this discussion and analysis are expressed in Chinese Yuan Renminbi (“RMB”) unless otherwise noted. Canadian dollar (“C\$”) equivalents are provided for information only. Such presentation in Canadian dollars is not in accordance with IFRS and should not be construed as a representations that the RMB amounts shown could be readily converted, realized or settled in Canadian dollars at the date of these financial statements or any other date. The exchange rate of one Canadian dollar for RMB published in the South China Morning Post on September 30, 2014 was RMB 5.535 to C\$1.00.

**CAUTIONARY NOTE REGARDING FORWARD-LOOKING STATEMENTS**

Some of the following disclosures contain forward-looking statements, which involve inherent risk and uncertainty affecting the business of the Company. These statements relate to the time anticipated for the commencement of the formal commercial gas production from development of the Lishui 36-1 (or “LS36-1”) gas field (“LS36-1 Development” or “Development”), the financing of the Development and the results of exploration of the Company’s other exploration prospects. They are based on assumptions financing for the Company’s exploration obligations under Petroleum Contract 25/34 (as defined below) can be obtained, that the loan drawdown for the facility as agreed with China Development Bank (“CDB”), China Export and Import Bank (“EXIM”) and Shanghai Pudong Development Bank (“SPDB”) (collectively the “Syndicate”) will proceed as planned and that Primeline’s first revenue will be received on time. Actual results may vary from those anticipated. Primeline may not be able to arrange financing for its exploration obligations or such funding may not be sufficient. The loan drawdown may not happen as planned and may be delayed and Primeline’s receipt of first revenue may also be delayed. If so, the Company may be breach its obligations under the Petroleum Contracts. Exploration for oil and gas is subject to the inherent risk that it may not result in a commercial discovery.

**COMPANY AND PROJECT OVERVIEW**

The Company is focused exclusively on upstream oil and gas opportunities in China. The Company owns exploration and development rights in the East China Sea pursuant to two Petroleum Contracts, one in relation to Block 25/34 (“Petroleum Contract 25/34”) and one in relation to Block 33/07 (“Petroleum Contract 33/07”) both entered into between China National Offshore Oil Corporation (“CNOOC”), Primeline Energy China Ltd. (“PECL”), a wholly owned subsidiary of the Company, and Primeline Petroleum Corporation (“PPC”), an affiliated company wholly owned by Mr. Victor Hwang, the Company’s chairman, president and majority shareholder. Petroleum Contract 25/34, dated March 24, 2005 and Petroleum Contract 33/07, dated June 15, 2012, are together referred to as “the Petroleum Contracts”. PECL and PPC act jointly as the “Contractor” under the Petroleum Contracts.

- Block 25/34 covers 84.7 sq km, being the development and production area for the LS36-1 gas field (the ‘Development’) for which CNOOC is the Operator holding a 51% interest with the Company and PPC holding a 36.75% and 12.25% interest respectively.
- Block 33/07 covers an offshore area of 5,877 sq km (1.45 million acres) enclosing Block 25/34 and the Contractor’s interest is shared 75%/25% by the Company and PPC. Another wholly owned subsidiary of the Company, Primeline Energy Operations International Ltd. (PEOIL), is the operator for Block 33/07. The Contractors are responsible for 100% of the exploration costs and CNOOC has the right to participate in up to 51% of any commercial development.

References in this MD&A to ‘Primeline’ refer generally to the Company, PECL, PEOIL and PPC and references to the Company include its subsidiaries PECL and PEOIL.

Primeline and CNOOC are implementing a rolling development and exploration strategy in the Lishui Basin with CNOOC operating the LS36-1 Development and its production under Petroleum Contract 25/34 and Primeline leading the effort on exploration under Petroleum Contract 33/07. The LS36-1 production infrastructure is the first gas production facility in the southern East China Sea and could become a hub for successful exploration and development work in the remainder of the petroliferous Lishui Basin.

At the time of this Management Discussion and Analysis, the LS36-1 Development has been completed, with trial gas production started on July 16, 2014 and running smoothly, thus establishing access to the dynamic local gas market in Eastern China. The confirmation of the gas market and the completion of the production facility significantly enhance the value of LS36-1 gas field’s incremental reserves and prospective resources and any additional resources which may be discovered in the Lishui Gas Play and elsewhere within Block 33/07.

## **QUARTERLY PROGRESS REVIEW**

During this quarter, the LS36-1 Development was finally completed and connected to the provincial grid. Trial gas production and joint commissioning of the upstream and downstream facilities commenced on July 16, 2014. The joint commissioning has now almost been completed, with most of the facilities fully operational and running smoothly. Trial production has progressed well and has reached the designed level for considerable periods of time.

First production is a significant achievement for the Company. At the time of the discovery of the LS36-1 gas field in 1997, the Chinese gas market was in the very early stages of development. Now, some 17 years later, the Chinese gas market is a more mature market with tremendous growth potential. On the exploration side, Primeline has completed the acquisition of an additional 600 sq. km of 3D seismic data and the processing of the data is near completion. The next step is interpretation of this data to prepare for the next exploration drilling programme in the large exploration area in Block 33/07 surrounding the LS36-1 gas field. This future exploration work will be able to use the infrastructure built in the LS36-1 gas field to access the expanding China gas market.

## **DEVELOPMENT AND PRODUCTION OF LS 36-1 GAS FIELD**

During the past 4 years, CNOOC, as the operator, has completed the LS36-1 Development including the production platform, subsea pipeline, development wells, onshore processing terminal and sale gas pipeline.

CNOOC and Zhejiang Gas, the offtaker of the natural gas from LS36-1 gas field, have been working closely during the past year in relation to the coordination of completion of the Development and of the offtaker's infrastructure, the final connection and the arrangements for the commencement of production.

The final connection with Zhejiang Gas's infrastructure was achieved on July 1, 2014. Joint commissioning of the upstream and downstream facilities commenced on July 8, 2014 and trial gas production from the LS36-1 Gas Field commenced on July 16, 2014.

CNOOC and Primeline are working closely with Zhejiang provincial government, Zhejiang Gas Development Co. and Wenzhou Municipality Government and other entities to ensure that final joint commissioning and the initial production phase proceeds smoothly. By the end of the September 2014, LS36-1 gas field had sold over 25.2million cubic meters (mcm) (0.92bcf) of natural gas to Zhejiang Gas. Condensate and light oil production has also commenced. Gas sales averaged 23.3mmcfpd (vs ODP design of 25mmcfpd) from early September to late November 2014.

With trial production proceeding, CNOOC continues to work on the construction of a small jetty next to the terminal to facilitate the transportation of CO<sub>2</sub> and hydrocarbon liquid products by sea. Prior to the completion of this jetty, transportation of such products is by truck only.

During the financial year, CNOOC and Zhejiang Gas were negotiating the terms of the final gas sale contract. The first gas sale agreement in principle was signed in 2008 and a framework agreement for gas sale was signed in 2011, which provided the commercial support for the Development. The terms of the final gas sale contract were finalized in early July and the final gas sale contract was signed on October 29, 2014 in Beijing, replacing the previous framework agreement. It confirmed general commercial terms already negotiated, including gas quality, take or pay principles, base price and annual quantity.

## **EXPLORATION IN BLOCK 33/07**

In the previous quarter, Primeline completed the acquisition of a 600sq km 3D seismic survey in Block 33/07, and data processing commenced in May 2014. During the quarter under review, Primeline continued with 3D seismic processing work. The initial processed data results were sent to Primeline's technical team in early November this year for evaluation and initial interpretation. The interpretation of the total 3D seismic cube is anticipated to take place in the fourth quarter of 2014.

The data from the Survey are intended to provide better definition of the prospects and leads that have previously been identified in the survey area using 2D data, in order to generate drillable prospects. Exploration drilling, comprising two commitment exploration wells, is planned for 2015.

## **DEVELOPMENT FINANCE**

Under the terms of the agreements entered into by the Company, PPC and CNOOC in March 2010, Primeline had no obligation to fund its share of the development costs for the LS36-1 Development until 3 months after ODP approval was obtained. In the meantime, CNOOC had responsibility for all work required to ensure that the Development remained on schedule.

On May 16, 2014, CNOOC notified Primeline that approval of the ODP had been obtained. In order to allow Primeline sufficient time to finalize the financing arrangements, CNOOC agreed that the period allowed for Primeline to arrange for funding of cash calls in relation to the Development should be extended by 4 months to December 16, 2014. A memorandum of agreement was signed to that effect on October 29, 2014.

In May 2010, PECL, PPC and CDB entered into a loan memorandum to confirm the terms on which China Development Bank ("CDB") agreed in principle to provide a loan facility for PECL and PPC, as joint borrower, to fund their respective share of the costs of the Development. PECL, PPC and CDB signed a revised loan memorandum ("Loan Memorandum") on November 2, 2012, which took into account the various changes and progress made in relation to the Development since 2010 and replaced the previous loan memorandum.

Following the approval of the ODP, Primeline worked with CDB to finalise the loan arrangements for Primeline and PPC's share of the Development costs. As a result of changes in the banking environment and CDB internal regulations since the date of the previous credit committee approval it was agreed that CDB would lead and arrange a syndicated project finance facility. EXIM joined the Syndicate as joint lead arranger, and SPDB as participant and agent bank. The loan contract was signed by Primeline, PPC, and the Syndicate and dated as of November 17, 2014.

The facility is made available to Primeline and PPC on a joint borrower basis and secured on their respective interests in the Development. The facility is for a total amount of US\$ 274 million (of which the Company's share is US\$ 205.5 million) and will be repayable over 9 years at an all-in interest rate of 6 month LIBOR+4.7%.

Following the signing of the contract, the security arrangements and account set up will be implemented with the first drawdown expected around the end of November this year.

The loan facility is sufficient to cover all of the obligations of Primeline and PPC with respect to the costs of the Development to date.

Once the loan is drawdown and CNOOC is repaid, Primeline and PPC expect to receive a significant amount of income for their shares of the sales revenue during the trial production period which has been held in CNOOC's account for Primeline and PPC. An announcement will be made when such event happens.

## **GENERAL FINANCIAL OUTLOOK**

As at September 30, 2014, the Company held cash resources of RMB6,041,339 (C\$1,091,479), and loans in principal amount from Victor Hwang, its Chairman, President and majority shareholder of RMB62,779,169 (C\$11,342,217).

The Company and PPC are working to complete the syndicate for the loan with respect to financing their share of the costs of the LS36-1 Development.

The Company anticipates starting to receive significant cash flow once the LS36-1 gas field enters into full commercial production. Such full cash flow is anticipated to commence in October 2014.

The financial statements have been prepared on the basis of accounting principles applicable to a going concern, which assumes that the Company will be able to continue in operation for the foreseeable future and will be able to realize its assets and discharge its liabilities in the normal course of business.

Several adverse conditions cast significant doubt upon the validity of this assumption. Consistent with other entities in the exploration and development stage, the Company has incurred operating losses since inception, has no source of revenue, is unable to self-finance operations, and has significant cash requirements to meet its overhead, to carry out its exploration activities under Petroleum Contract 33/07 and to fund its share of the LS36-1 Development.

The Company's ability to continue as a going concern is dependent upon management's ability to secure additional financing. While management has been successful in obtaining funding in the past, including support from its majority shareholder, there can be no assurance that it will be able to do so in the future.

If the going concern assumption were not appropriate for these financial statements then adjustments would be necessary to the carrying value of assets and liabilities, the reported expenses and the balance sheet classifications used, and such adjustments would be material.

## **FINANCIAL INFORMATION**

### ***Results of Operations***

The Company's results for the quarter ended September 30, 2014 were a gain of RMB292,059 (C\$52,766). Compared to the loss of RMB1,039,850 for the same quarter last year, the difference in the result of RMB1,331,909 (C\$240,634) was mainly due to the decrease of travel expenses of RMB104,946 (C\$18,960), increase of finance income RMB681,660 (C\$123,154) which related to the change in fair value of warrant liabilities and the exchange gain of

RMB448,297 (CAD\$80,993) compared to the exchange loss of RMB24,112 for the same quarter last year due to depreciation of the RMB against the US dollar. The result was partially set off by the increase of salary and benefit of RMB140,661 (C\$25,413) for the quarter.

### ***Liquidity and Capital Resources***

As at September 30, 2014, net current assets of the Company amounted to RMB5,355,810 (C\$967,626), whereas net current assets of RMB23,087,905 were recorded as at March 31, 2014. The decrease in net current assets of RMB17,732,095 (C\$3,203,631) was mainly due to the decrease of cash and cash equivalents of RMB18,606,696 (C\$3,361,643) paid for the exploration costs and the increase of cash call payable to PPC of RMB 326,898 (C\$59,060).

During this quarter, exploration and evaluation assets of RMB5,116,672 (C\$924,421) were incurred and financed mainly by the shareholder's loans. As at September 30, 2014, the total amount of exploration and evaluation assets incurred and capitalized amounted to RMB513,109,626 (C\$92,702,733) (March 31, 2014 – RMB462,103,858) and can be broken down as follows:

|  | <u>Sep 30, 2014</u> | <u>Mar 31, 2014</u> | <u>Sep 30, 2014</u> |
|--|---------------------|---------------------|---------------------|
|  | RMB                 | RMB                 | C\$                 |
| Exploration Drilling Related Services                        |                     |                     |                     |
| Drilling services  | 178,263,638         | 178,263,638         | 32,206,619          |
| Drilling technical supervision and evaluation                | 4,650,259           | 4,650,259           | 840,155             |
| Exploration Geological&Geophysical Surveys& Work             |                     |                     |                     |
| Geological&geophysical survey acquisition& processing        | 100,781,785         | 64,892,882          | 18,208,091          |
| Technical evaluations&management                             | 45,685,339          | 43,713,058          | 8,253,901           |
| Pre-development study  | 32,583,351          | 32,583,351          | 5,886,784           |
| Interests on funding of deferred exploration expenditures    | 30,365,526          | 27,423,969          | 5,486,093           |
| Deferred costs acquired from Primeline Petroleum Corporation | 8,485,080           | 8,485,080           | 1,532,987           |
| Project administration                                       | 30,713,976          | 29,299,370          | 5,549,047           |
| Salaries and benefits  | 53,666,259          | 50,173,660          | 9,695,801           |
| Travel and accommodation                                     | 20,110,711          | 19,475,389          | 3,633,372           |
| Contract signing fee   | 7,803,702           | 3,143,202           | 1,409,883           |
|  | <u>513,109,626</u>  | <u>462,103,858</u>  | <u>92,702,733</u>   |

As at September 30, 2014, the Company had total assets of RMB520,079,148 (C\$93,961,905) (March 31, 2014 – RMB487,598,179) which were financed by net shareholders' equity of RMB460,149,397 (C\$83,134,488) (March 31, 2014 – RMB454,177,109) and shareholder loan of RMB56,631,241 (C\$10,231,480) (March 31, 2014 – RMB19,258,753).

As at September 30, 2014, the Company had net current assets of RMB5,355,810 (C\$967,626) (March 31, 2014 – RMB23,087,905) and had a accumulated deficit of RMB109,616,394 (C\$19,804,227) (March 31, 2014 – RMB108,202,863). The new loan facility of US\$8,000,000 (with a remaining amount available for drawdown of US\$ 2,833,333 as at September 30, 2014) from Mr. Victor Hwang was arranged in June 2014 and will be sufficient to meet the Company's overhead requirement and to carry out its exploration activities under Petroleum

Contract 33/07 for the coming twelve months but not cover the drilling plan in 2015. The Company is actively investigating other funding options to address further financing requirements for the Company's exploration activities. The loan contract to fund Primeline's obligations with respect to the costs of the LS36-1 Development was signed by Primeline, PPC and the Syndicate on November 17, 2014 for a total amount of US\$ 274 million (of which the Company's share is US\$ 205.5 million). The loan facility is sufficient to cover all of the obligations of Primeline and PPC with respect to the costs of the Development to date.

### ***Financial Instruments***

The Company's financial instruments consist of cash and cash equivalents, accounts payable and accrued liabilities, shareholder loan, cash calls payable, advances from a related party and derivative warrant liabilities.

Fair values of assets and liabilities approximate amounts at which these items could be exchanged in transactions between knowledgeable parties. Fair value is based on available public market information or when such information is not available, estimated using present value techniques and assumptions concerning the amount and timing of future cash flows and discount rates which factor in the appropriate credit risk. The calculation of estimated fair value is based on market conditions at the specific point in time and in the respective geographic locations and may not be reflective of future values.

The fair value of the financial assets and current liabilities approximates their carrying value.

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

#### *(a) Currency risk*

The Company held financial instruments in different currencies during the period/year ended as follows:

|                                       | Sep 30, 2014     | Mar 31, 2014     |
|---------------------------------------|------------------|------------------|
| Cash and cash equivalents of:         |                  |                  |
| - CAD\$                               | CAD\$104,701     | CAD\$156,625     |
| - US\$                                | US\$285,894      | US\$3,609,762    |
| - GBP                                 | GBP30,080        | GBP72,339        |
| - HK\$                                | HK\$3,580,410    | HK\$629,345      |
| Shareholder loan of US\$              | (US\$10,166,667) | (US\$3,494,871)  |
| Advance from a related party of CAD\$ | -                | (CAD\$1,700,000) |

Based on the above net exposures, and assuming that all other variables remain constant, a 10% depreciation or appreciation of the Renminbi against the Canadian dollar, US dollar, British Pound and Hong Kong dollar, would result in an increase/decrease of the Company's net (loss) income of approximately:

|         | Sep 30, 2014 | Mar 31, 2014 | Sep 30, 2014 |
|---------|--------------|--------------|--------------|
|         | RMB          | RMB          | CAD\$        |
| - CAD\$ | 57,952       | 866,296      | 10,470       |
| - US\$  | 6,101,377    | 71,290       | 1,102,327    |
| - GBP   | 30,140       | 74,726       | 5,445        |
| - HK\$  | 284,643      | 50,348       | 51,426       |

*(b) Credit risk*

Credit risk is the risk of an unexpected loss if a customer or third party to a financial instrument fails to meet its contractual obligations.

The Company's cash and cash equivalents are held at a large international financial institution in interest bearing accounts. Minimal cash balances are held in Chinese financial institutions.

*(c) Liquidity risk*

Liquidity risk is the risk that the Company will not be able to meet its financial obligations as they fall due.

Financing will be required to fund the Company's obligations in relation to the LS36-1 Development and in relation to any future exploration work. The loan contract to fund the Company's obligations with respect to the Development was signed by PECL, PPC, and the Syndicate on November 17, 2014 for a total amount of US\$ 274 million (of which the Company's share is US\$ 205.5 million). The loan facility is sufficient to cover all of the obligations of PECL and PPC with respect to the costs of the Development to date.

In June 2014, Mr. Hwang agreed to provide the Company an interest free loan of US\$ 8,000,000 to meet the Company's overhead requirement and to carry out its exploration activities under the New Contract for the coming twelve months. The Company is actively exploring all possible fund-raising possibilities for the planned exploration drilling program.

Additional information regarding liquidity risk is disclosed in Note 1.

The Company's non-derivative financial liabilities which are amounts due on the shareholder loan are repayable on demand after December 31, 2015.



(d) *Interest rate risk*

Interest rate risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market interest rates. The Company has minimal interest rate risk.

***Derivative warrant liability***

The Company's derivative instruments are the share purchase warrants issued. The Company issued warrants as part of a Unit offering. These share purchase warrants were issued with an exercise price in Canadian dollars rather than Chinese Yuan (the functional currency of the Company). Such share purchase warrants are considered to be derivative instruments.

The initial fair value on recognition of the share purchase warrants was calculated using the Black-Scholes pricing model, using the assumptions in the following table. Subsequent to their initial recognition, the share purchase warrants liability is re-measured and re-translated each reporting period in accordance with IAS 32.

Tranche 1 on December 30, 2013:

|   | <b>As at September 30, 2014</b> | <b>As at March 31, 2014</b> | <b>At date of issue December 30, 2013</b> |
|---|---------------------------------|-----------------------------|---|
| Exchange rate at date of fair value (RMB/C\$) | 5.535                           | 5.613                       | 5.705                                     |
| Stock price                                   | CAD\$0.46                       | CAD\$0.57                   | CAD\$0.63                                 |
| Exercise price                                | CAD\$0.90                       | CAD\$0.90                   | CAD\$0.90                                 |
| Risk free interest rate                       | 1.12%                           | 1.07%                       | 1.09%                                     |
| Expected dividend yield                       | Nil                             | Nil                         | Nil                                       |
| Expected stock price volatility               | 77%                             | 70%                         | 83%                                       |
| Expected warrant life                         | 1.25 years                      | 1.75 years                  | 2 years                                   |

Tranche 2 on January 23, 2014:

|   | <b>As at September 30, 2014</b> | <b>As at March 31, 2014</b> | <b>At date of issue January 23, 2014</b> |
|---|---------------------------------|-----------------------------|--|
| Exchange rate at date of fair value (RMB/C\$) | 5.535                           | 5.613                       | 5.550                                    |
| Stock price                                   | CAD\$0.46                       | C\$0.57                     | C\$0.53                                  |
| Exercise price                                | CAD\$0.90                       | C\$0.90                     | C\$0.90                                  |
| Risk free interest rate                       | 1.12%                           | 1.07%                       | 0.97%                                    |
| Expected dividend yield                       | Nil                             | Nil                         | Nil                                      |
| Expected stock price volatility               | 73%                             | 74%                         | 73%                                      |
| Expected warrant life                         | 1.32 years                      | 1.82 years                  | 2 years                                  |

The Company's warrant liability for the period ended September 30, 2014 and year ended March 31, 2014 is set out below:

|  | <b>Warrants<br/>Outstanding</b> | <b>Value assigned<br/>RMB</b> | <b>Value assigned<br/>CAD\$</b> | <b>Average exercise<br/>price<br/>CAD\$</b> |
|--|---------------------------------|-------------------------------|---------------------------------|---|
| Balance – as at March 31, 2013             | -                               | -                             | -                               | -   |
| Warrants issued                            | 4,586,250                       | 5,406,242                     | 976,737                         | 0.90  |
| Fair value re-measurement in<br>the year   | -                               | (1,997,759)                   | (360,932)                       | -   |
| Balance – as at March 31, 2014             | 4,586,250                       | 3,408,483                     | 615,805                         | 0.90  |
| Fair value re-measurement in<br>the period | -                               | (1,718,559)                   | (310,489)                       | -   |
| Balance – as at September 30, 2014         | 4,586,250                       | 1,689,924                     | 305,316                         | 0.90  |

The share purchase warrants outstanding and exercisable as at September 30, 2014 is set out below:

| <b>Exercise Price CAD\$</b> | <b>Expiry date</b> | <b>Number</b> |
|-----------------------------|--------------------|---------------|
| 0.90                        | December 30, 2015  | 3,826,250     |
| 0.90                        | January 23, 2016   | 760,000       |

### ***Capital management***

The Company's objectives when managing capital are to safeguard the Company's ability to continue as a going concern in order to pursue the exploration and development of its petroleum property interests, acquire additional petroleum property interests and to maintain a flexible capital structure which optimizes the costs of capital at an acceptable risk. In the management of capital, the Company includes its cash and cash equivalent balances and components of shareholders' equity.

The Company manages the capital structure and makes adjustments to it in light of changes in economic conditions and the risk characteristics of the underlying assets. To maintain or adjust the capital structure, the Company may attempt to issue new shares, issue debt, acquire or dispose of assets or adjust the amount of cash and cash equivalents and investments.

In order to facilitate the management of its capital requirements, the Company prepares annual expenditure budgets that are updated as necessary depending on various factors, including successful capital deployment and general industry conditions. The annual and updated budgets are approved by the Board of Directors.

At this stage of the Company's development, in order to maximize ongoing development efforts, the Company does not pay out dividends.

Additional information regarding capital management is disclosed in note 1 of the interim consolidated financial statements as at September 30, 2014.

***Transactions with related parties and directors***

During the period ended September 30, 2014, the Company paid or accrued the following:

- a) London office rent of RMB198,486 (CAD\$35,860) (2013 – RMB181,528) was paid or accrued to a company beneficially owned by Mr. Victor Hwang, the majority shareholder, director and officer of the Company.
- b) Cash call received from and utilized for PPC, a company owned by Mr. Hwang, the majority shareholder, director and officer of the Company, for its 25% contribution to exploration costs were RMB 6,182,133 (CAD\$1,116,917) (2013 – RMB2,960,120) and RMB15,759,435 (CAD\$2,847,233) (2013 – RMB2,618,019) respectively. The balance is recorded as a cash call payable on the statement of financial position amounting to RMB329,602 (CAD\$59,049) (2013 – RMB480,571).
- c) Key management includes members of the Board, the Chairman, Chief Executive Officer, Chief Financial Officer, Vice President and Consultants. The aggregate total compensation paid or payable to the key management is as follows:

| Key Management  | Position                | Nature of Compensation | September 30, 2014 | September 30, 2013 | September 30, 2014 |
|-----------------|-------------------------|------------------------|--------------------|--------------------|--------------------|
|                 |                         |                        | RMB                | RMB                | CAD\$              |
| Ming Wang       | Chief Executive Officer | Salary                 | 880,156            | 707,028            | 159,017            |
| Andrew Biggs    | Senior Vice President   | Salary                 | 617,785            | 565,552            | 111,614            |
| Alan Soulsby    | Technical Director      | Consulting             | 73,289             | 191,797            | 13,241             |
| Malcolm Barratt | Consultant              | Consulting             | -                  | 10,581             | -                  |
| Yu Jin Shen     | Senior Advisor          | Consulting             | 75,960             | 109,710            | 13,724             |
| Chongxin Zhang  | Senior Advisor          | Salary                 | 81,529             | 143,123            | 14,730             |
| Mark Norman     | GM, China               | Office Salary          | 410,963            | 415,973            | 74,248             |
| Stuart Joyner   | Former CFO              | Salary                 | 178,899            | -                  | 32,321             |
| Ben Cheng       | Former CFO              | Salary                 | -                  | 88,361             | -                  |
| Alan Johnson    | Director                | Board Advisory         | 71,006             | 73,581             | 12,500             |
| Lien Jown Jing  | Director                | Board Advisory         | 71,006             | 73,581             | 12,500             |
| Vincent         | Director                | Board Advisory         | 71,006             | 73,581             | 12,500             |
| Yunshi Cao      | Director                | Board Advisory         | 71,006             | 73,581             | 12,500             |
| Peter Kelty     | Director                | Board Advisory         | 71,006             | 73,581             | 12,500             |
| <b>Total</b>    |                         |                        | <b>2,602,605</b>   | <b>2,526,449</b>   | <b>468,895</b>     |

Share based payment of RMB1,132,824 (CAD\$204,666) (2013 – RMB1,169,987) were recognized for the 4,460,000 (2013 – 4,010,000) share options granted to these key management personnel. These amounts have not been included in the table above and should be considered as additional compensation.

- d) Shareholder loan of RMB 56,631,241 (CAD\$10,231,480) (2013 – RMB43,682,803) represents interest-free loans with a principal balance of RMB62,779,169 (CAD\$11,342,217) (2013 – RMB48,065,538) due to Mr. Victor Hwang, the majority shareholder, director and officer of the Company.

During the year ended March 31, 2014, Mr. Hwang advanced a loan amount of US\$1,203,846 which is interest free and repayable on demand so that together with the loan balance of US\$ 6,650,000 as at March 31, 2013, the aggregate amount owing to Mr. Hwang was US\$7,853,846 before October 2013. Then on October 10, 2013, the Company signed a debt settlement agreement with Mr. Victor Hwang, under which the 9,427,272 Common Shares were issued to Mr. Hwang in settlement of US\$5,000,000 of the existing debt owed by the Company to Mr. Hwang (CAD\$5,185,000 at the agreed exchange rate of US \$1/CAD\$1.037) at a deemed price of CAD\$0.55 per share. As a result, the amount owing to Mr. Hwang after such debt settlement was US\$ 2,853,846. On October 10, 2013, Mr. Hwang also agreed to extend another US\$5,000,000 loan facility to the Company. As at the date of such agreement, the amount drawn down was US\$2,853,846 and the amount remaining available for drawdown was US\$ 2,146,153. This loan facility is interest-free and is repayable upon demand after July 31, 2015. As at March 31, 2014, the Company had drawn down a total of US\$3,494,871 from the facility with a remaining available facility of US\$ 1,505,129.

During the period ended September 30, 2014, the Company drew down the remaining US\$1,505,129 of the US\$5,000,000 facility, which is repayable upon demand after July 31, 2015. On July 31, 2014, Mr. Hwang agreed to extend the US\$5,000,000 facility for five months. It is now repayable upon demand after December 31, 2015. On June 30, 2014, Mr. Hwang agreed to advance an additional US\$8,000,000 interest-free loan facility to the Company. This loan is repayable upon demand after December 31, 2015. As at September 30, 2014, the Company has drawn down a total of US\$5,166,667 from the facility with a remaining available facility of US\$2,833,333.

The shareholder loan has been recorded at fair value on inception and carried at amortized cost. The discount on shareholder loan of RMB5,464,982 (CAD\$987,350) (2013 – RMB2,023,485) and the capitalized interest of RMB1,712,982 (CAD\$309,482) (2013 – RMB1,782,892) were calculated using an effective rate of 10% per annum during the six months period ended September 30, 2014.

- e) Advances from a related party of RMB Nil (CAD\$ Nil) (2013 – RMB8,410,046) represent an interest-free balance with a principal amount of RMB Nil (CAD\$Nil) (2013 – RMB10,094,600) from PPC.

The interest-free non-current advance from a related company has been recorded at fair value on inception and carried at amortized cost.

The capitalized interest of RMB1,229,353 (CAD\$222,105) (2013 – RMB414,037) were calculated using an effective rate of 10% per annum.

During this period, the Company funded CAD\$1.7million of PPC's share of the 3D seismic survey costs on behalf of PPC, thus repaying the advance.

These transactions are measured at the exchange amount, which is the amount of the consideration established and agreed by the related party.

### ***Subsequent Events***

- a) On October 29, 2014, CNOOC and Zhejiang Gas signed the final Natural Gas Sale Agreement. This supersedes the Gas Sale Agreement-in principle and subsequent Framework and Amendment Agreements signed between 2008 and 2012 and confirms general commercial terms already negotiated including, inter alia, gas quality, take-or-pay principles, base price and annual quantity.
- b) On November 17, 2014, the binding documentation for the project finance facility for the financing of its share of the costs to complete the LS36-1 gas field development ("Development") has now been finalised and was signed by Primeline and the financing banks namely China Development Bank ("CDB"), China Export and Import Bank ("EXIM") and Shanghai Pudong Development Bank ("SPDB"). Following the signing of the documentation, the security arrangements and accounts set up will be implemented with first drawdown expected around the end of November.

### ***Change in Accounting Standards***

The Company has adopted the following new and revised standards, along with any consequential amendments, effective April 1, 2013. These changes were made in accordance with the applicable transitional provisions:

- a) IFRS 10, 'Consolidated Financial Statements' was issued in May 2011 and will supersede the consolidation requirements in SIC-12 'Consolidation — Special Purpose Entities' and IAS 27 'Consolidated and Separate Financial Statements' effective for annual periods beginning on or after January 1, 2013, with early application permitted. IFRS 10 builds on existing principles by identifying the concept of control as the determining factor in whether an entity should be included within the consolidated financial statements of the parent company. The standard also provides additional guidance to assist in the determination of control where this is difficult to assess. The adoption of the standard has no impact on the Company's financial statements.
- b) IFRS 11, 'Joint Arrangements' was issued in May 2011 and will supersede existing IAS 31, 'Joint Ventures' effective for annual period beginning on or after January 1, 2013, with early application permitted. IFRS 11 provides for the accounting of joint arrangements by focusing on the rights and obligations of the arrangement, rather than its legal form (as is currently the case). The adoption of the standard has no impact on the Company's financial statements.
- (c) IFRS 12, 'Disclosure of Interests in Other Entities' was issued in May 2011 and is a new and comprehensive standard on disclosure requirements for all forms of interests in other entities, including subsidiaries, joint arrangements, associates and unconsolidated structured entities. IFRS 12 is effective for annual periods beginning on or after January 1, 2013, with earlier

application permitted. The adoption of the standard has no impact on the Company's financial statements.

- (d) IFRS 13, 'Fair Value Measurement' was issued in May 2011 and sets out in a single IFRS a framework for measuring fair value. IFRS 13 defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. This definition of fair value emphasizes that fair value is a market-based measurement, not an entity-specific measurement. In addition, IFRS 13 also requires specific disclosures about fair value measurement. IFRS 13 is effective for annual periods beginning on or after January 1, 2013, with earlier application permitted. The adoption of IFRS 13 did not require any adjustment to the valuation technique used by the Company to measure fair value and did not result in any measurement adjustments.
- (e) IAS 1, 'Presentation of Financial Statements' was amended in June 2011. This standard requires companies preparing financial statements under IFRS to group items within Other Comprehensive Income (OCI) that may be reclassified to the profit or loss. The amendments also reaffirm existing requirements that items in OCI and profit of loss should be presented as either a single statement or two consecutive statements. The amendments to IAS 1 set out in Presentation of Items of OCI are effective for fiscal years beginning on or after July 1, 2012. This adoption of the standard has no impact on the Company's financial statements.

The Company has not early adopted the following standards, amendments and interpretations to existing standards that are not yet effective.

Certain new standards, interpretations, amendments and improvements to existing standards were issued by the IASB or International Financial Reporting Interpretations Committee (IFRIC) that are mandatory for accounting periods beginning after January 1, 2014 or later periods. The standards that are applicable to the Company are as follows:

- (a) IAS 32, "Financial instruments": Presentation has been amended to clarify some of the requirements for offsetting financial assets and financial liabilities on the balance sheet. This standard has no impact on the Company.
- (b) IAS 36, "Impairment of Assets", has been amended to address the disclosure of information about the recoverable amount of impaired assets if that amount is based on fair value less costs of disposal. This standard has no impact on the Company.
- (c) IFRS 9, Financial Instruments ("IFRS 9"), was published on July 2014 which replaces the guidance in IAS 39. This final version includes requirements on the classification and measurement of financial assets and liabilities; it also includes an expected credit losses model that replaces the incurred loss impairment model used today. The final hedging part of IFRS 9 was issued in November 2013.

The standard is effective for annual periods beginning on or after January 1, 2018, with early application permitted. The Company will be required to adopt this standard.

We are currently assessing the effect of this standard and related amendments on our financial statements.

### ***Outstanding Share Data***

On July 27, 2011, the Company granted 2,100,000 options at an exercise price of C\$0.32 per share to directors, officers, employees and consultants, of which 200,000 options expired and 1,900,000 options expire on July 27, 2016.

On July 9, 2012, the Company granted to D&D Securities Inc. an option to purchase a total of 500,000 common shares at an exercise price of C\$0.50 per share. The option expires on June 25, 2017.

On September 26, 2012, the Company granted 3,105,000 options at an exercise price of C\$0.60 per share to directors, officers, employees and consultants. Such options expire on September 26, 2017.

On December 30, 2013, the Company closed the first tranche of the Private Placement led by D&D Securities Inc. (the "Agent") as agent. The Company issued a total of 7,652,500 units ("Units") at a price of C\$0.55 per Unit for gross proceeds of C\$4,208,875. Each Unit consists of one ordinary share (a "Common Share") and one half of one warrant (a "Warrant"). Each Warrant is exercisable to purchase a further Common Share at a price of C\$0.90 per share for 24 months from today. The Company will have the right to accelerate expiry of the Warrants if the volume weighted average closing price of the common shares on the TSX-V exceeds C\$1.35 per share for 10 consecutive trading days by giving notice, whereupon the Warrants will expire 30 days from the date of notice. The Agent was paid a cash commission of 7% of the gross proceeds, and together with members of its selling group issued 612,200 warrants ("Broker Warrants"), equal to 8% of the number of Units sold. Each Broker Warrant is exercisable for 24 months to purchase a Common Share at C\$0.55 per share.

On January 24, 2014, the Company closed the second and final tranche of the Private Placement. In this second tranche Primeline issued a total of 1,520,000 Units at a price of \$0.55 per Unit for gross proceeds of C\$836,000. Each Unit consists of one Common Share and one half of one Warrant. Each Warrant is exercisable to purchase a further Common Share at a price of C\$0.90 per share for 24 months from the closing date. Primeline will have the right to accelerate expiry of the Warrants if the volume weighted average closing price of the common shares on the TSX-V exceeds C\$1.35 per share for 10 consecutive trading days by giving notice, whereupon the Warrants will expire 30 days from the date of notice. The Agent was paid a cash commission of 7% of the gross proceeds and, together with members of its selling group, was issued a number of warrants ("Broker Warrants") equal to 8% of the number of Units sold. Each Broker Warrant was exercisable for 24 months to purchase a Common Share at C\$0.55 per share.

On June 2, 2014, 150,000 of the Broker Warrants were exercised resulting in the issue of 150,000 Common Shares at C\$ 0.55 each and the receipt of C\$ 82,500 by the Company.

On August 11, 2014, the Company granted 450,000 options at an exercise price of CAD\$0.68 per share to an officer. Such options will expire on August 11, 2019.

As at November 28, 2014, there are 112,791,018 Common Shares; 5,955,000 stock options and 5,170,050 Warrants and Broker Warrants outstanding.

### ***Quarter Ended September 30, 2014***

The Company's results for the quarter ended September 30, 2014 was a gain of RMB292,059 (CAD\$52,766), compared to the loss of RMB1,039,850 for the same quarter last year, the difference in the result of RMB1,331,909 (C\$240,634) was mainly due to the decrease of travel expenses of RMB104,946 (C\$18,960), increase of finance income RMB681,660 (C\$123,154) which related to the change in fair value of warrant liabilities and the exchange gain of RMB448,297 (CAD\$80,993) compared to the exchange loss of RMB24,112 for the same quarter last year due to depreciation of the RMB against the US dollar. The result was partially set off by the increase of salary and benefit of RMB140,661 (C\$25,413).

During the quarter exploration expenditures of RMB5,116,672 (C\$924,421) were incurred, which comprised mainly of technical evaluations & management of RMB1,022,117 (C\$184,664), interest on funding of deferred exploration expenditures of RMB1,076,077 (C\$194,413), project administration of RMB856,005 (C\$154,653) and salaries and benefits of RMB1,928,968 (C\$348,504). These amounts were capitalized as exploration and evaluation assets.

### ***Summary Of Quarterly Results ( Unaudited)***

| Quarter Ended     | 2014<br>Sep 30<br>C\$ | 2014<br>Sep 30<br>RMB | 2014<br>Jun 30<br>RMB | 2014<br>Mar 31<br>RMB | 2013<br>Dec 31<br>RMB |
|-------------------|-----------------------|-----------------------|-----------------------|-----------------------|-----------------------|
| Net gain (loss)   | 52,766                | 292,059               | (1,705,590)           | 187,718               | (1,908,099)           |
| Per basic share   | 0.001                 | 0.003                 | (0.015)               | 0.002                 | (0.019)               |
| Per diluted share | 0.001                 | 0.003                 | (0.015)               | 0.002                 | (0.019)               |

| Quarter Ended     | 2013<br>Sep 30<br>RMB | 2013<br>Jun 30<br>RMB | 2013<br>Mar 31<br>RMB | 2012<br>Dec 31<br>RMB |
|-------------------|-----------------------|-----------------------|-----------------------|-----------------------|
| Net (loss) gain   | (1,039,850)           | (1,978,511)           | 508,236               | (2,364,487)           |
| Per basic share   | (0.011)               | (0.021)               | 0.005                 | (0.025)               |
| Per diluted share | (0.011)               | (0.021)               | 0.005                 | (0.025)               |

The net gain for the quarter ended September 30, 2014 of RMB292,059 (C\$52,766) was mainly attributable to the gain recognized from the warrant liabilities' fair value change of RMB1,792,986 (C\$323,936) and the exchange gain of RMB448,297 (CAD\$80,993), and the reducing directors remuneration and benefit of RMB301,870 (C\$54,538), salary and benefit of RMB554,662 (C\$100,210) and professional fees of RMB836,558 (C\$151,140).

The loss for the quarter ended September 30, 2013 of RMB1,039,850 was mainly attributable to professional fees of RMB906,776, salary and benefit of RMB414,001 and directors remuneration and benefit of RMB381,008 and partially set off by finance income of RMB1,111,871.

The Company has a website at [www.primelineenergy.com](http://www.primelineenergy.com) or [www.pehi.com](http://www.pehi.com). The site features information on PEHI, new releases, background information and a technical summary of the project.