ZELAN BERHAD

("ZB" or "the Group")
(Company No: 27676-V)

NOTES TO THE INTERIM FINANCIAL REPORT FOR THE QUARTER ENDED 31 DECEMBER 2013

PART A – Explanatory Notes Pursuant to Malaysian Financial Reporting Standard 134

1. Basis of Preparation

The interim financial information is unaudited and has been prepared in accordance with the requirements of MFRS 134: Interim Financial Reporting and paragraph 9.22 of the Main Market Listing Requirements of Bursa Malaysia Securities Berhad.

The interim financial information should be read in conjunction with the audited financial statements for the financial year ended 31 March 2013. The explanatory notes attached to the interim financial information provide an explanation of events and transactions that are significant to an understanding of the changes in the financial position and performance of the Group since the financial year ended 31 March 2013.

The accounting policies and methods of computation adopted for the interim financial information are consistent with those adopted for the annual audited financial statements for the financial year ended 31 March 2013 except for the adoption of the following new Malaysian Financial Reporting Standards ("MFRS").

<u>MFRSs</u>

MFRS 10	Consolidated Financial Statements
MFRS 11	Joint Arrangements
MFRS 12	Disclosure of Interest in Other Entities
MFRS 13	Fair Value Measurement
MFRS 127	Separate Financial Statements
MFRS 128	Investments in Associates and Joint Ventures
Amendments to MFRS 101	Presentation of Items of Other Comprehensive Income
Amendments to MFRS 7	Financial Instruments: Disclosures

The adoption of the new MFRS and amendments to the existing standards did not result in a significant impact to the interim financial information of the Group.

1. Basis of Preparation (Continued)

MFRS, Amendments to MFRS and IC Interpretation that are applicable to the Group but not yet effective

The Group did not early adopt the following standards that have been issued by the Malaysian Accounting Standards Board as these are effective for the Group's financial statements for the financial period beginning on or after 1 April 2014:

Amendments to MFRS 132	Offsetting Financial Assets and Liabilities (effective from 1 January 2014)
Amendments to MFRS 10, MFRS 12 and MFRS 127	Investment Entities (effective from 1 January 2014)
Amendments to MFRS 136	Recoverable Amount Disclosures for Non-Financial Assets (effective from 1 January 2014)
Amendments to MFRS 139	Novation of Derivatives and Continuation of Hedge Accounting (effective from 1 January 2014)
IC Interpretation 21	Levies (effective from 1 January 2014)
MFRS 9	Financial Instruments: Classifications and Measurement of Financial Assets and Financial Liabilities (effective date from 1 January 2015)

In addition, the interim financial information complies with the International Financial Reporting Standards as issued by the International Accounting Standards Board.

The Group recorded a net profit of RM22.9 million during the third quarter ended 31 December 2013 and a net profit of RM24.5 million for the nine months ended 31 December 2013 and, as of that date, the current liabilities of the Group exceeded its current assets by RM144.2 million.

The Directors have considered the following matters in preparing the interim financial information of the Group on a going concern basis:

Project in Indonesia

In respect of the project in Indonesia which was undertaken by the Group through a Consortium in which the Group is the consortium leader, the owner of the project has issued the taking over certificate ("TOC") for Unit 1 dated 1 February 2012 on 12 December 2012 and the Consortium received partial retention sum of USD11.4 million (approximately RM35 million) on 28 December 2012. Subsequently, on 28 January 2013, the owner issued TOC for Unit 2 dated 1 May 2012 and the retention sum of USD11.5 million (approximately RM35 million) was received on 26 February 2013. On 31 July 2013, the owner issued the Final Acceptance Certificate for Unit 1 dated 15 July 2013, and subsequently on 15 August 2013, the Group received partial retention sum, net of liquidated ascertained damages ("LAD"), of USD9.4 million (approximately RM29.8 million).

1. Basis of Preparation (Continued)

Project in Indonesia (continued)

The Group expects to receive the Final Acceptance Certificate for Unit 2 and the remaining retention sum, net of LAD, of USD9.7 million (approximately RM30.8 million) in the fourth quarter of the financial year ending 31 March 2014.

The Group had, in the previous financial year, recognised LAD receivable from a subcontractor / supplier as a result of its delay in completing its scope of works as set out in the agreement for supply for the above project in Indonesia. The Group is virtually certain that it is entitled to impose and receive the LAD in accordance with the provisions of the said agreement, which is supported by external legal advice.

Project in the Middle East

In respect of the Group's project in Abu Dhabi, United Arab Emirates ("UAE"), on 21 November 2012, the owner of the project in Abu Dhabi, UAE, gave notice to terminate the contract and liquidate the performance bond. On 9 December 2012, the guarantor of the performance bond released the performance bond of AED92.5 million (approximately RM78 million) to the project owner.

The Group has, to date, issued 9 Notices of Intention to Commence Arbitration on 27 December, 31 December 2012, 19 February 2013, 19 August 2013 and 16 December 2013 due to the disputes which include under-certification of progress claims, the validity of the termination of contract, the validity of the liquidation of performance bond, dispute on the rejection of entitlement to extension of time by the owner's engineer, dispute on the engineer's certification of interim claims and the owner's payments, dispute on the insurance claim submission and dispute on the engineer's failure to value and certify the Progress Claim No. 53.

The Group had engaged an independent claim consultant to carry out a review on the Group's claim against the project owner based on the Group's entitlement for an extension of time and other additional payments in connection with the project. The Group had also obtained legal opinions from external solicitors based in Dubai, UAE and Malaysia on 2 February, 14 April and 23 May 2013, respectively. Based on the claims consultant's report and supported by external legal advice, the Group is of the view that it has strong legal grounds to challenge the basis of the notice of termination issued by the project owner and recover the outstanding receivable balance.

The Group recorded a total receivable balance of AED170.8 million (approximately RM151.6 million) due from the project owner as at 31 December 2013, which includes the performance bond drawndown. The expected timing of the receipt of the outstanding balance has been considered in arriving at the carrying value of the receivable.

1. <u>**Basis of Preparation (Continued)**</u>

<u>Project in the Middle East (Continued)</u>

Notwithstanding the above, the Group is currently in the midst of negotiations with the project owner to reach a commercial settlement on the purported wrongful termination of contract and for the Group to proceed with the completion of the project.

The Group will commence the arbitration process in the event the commercial settlement is not reached with the project owner as indicated above.

<u>Cash flows of the Group</u>

As at 31 December 2013, the Group is in a net current liabilities position of RM144.2 million. The financial position of the Group as at 31 December 2013, the ability of the Group to generate positive cash flows, the timeliness of the receipt of retention sums from the project owner in Indonesia and the uncertainty of the outcome of the arbitration of the Group's construction project in Abu Dhabi indicate the existence of a material uncertainty that may cast significant doubt about the ability of the Group to continue as a going concern, and therefore, the Group may be unable to realise the assets and discharge the liabilities in the normal course of business. If the Group ceases to be a going concern, assets are to be stated at their estimated recoverable amounts and provisions are to be made for any further estimated liabilities which might arise.

The Group had successfully restructured one of its existing unsecured term loan amounting to AED107.1 million (approximately RM89 million) in April 2013 which allows the Group to make progressive principal repayments over a period up to March 2014.

Following the approval from the shareholders in September 2013, the Group had disposed of some of its existing available-for-sale financial assets which were pledged as security for the Group's secured term loan. The proceeds from the disposal of these available-for-sale financial assets were used to fully settle the term loan. The Group has also completed its corporate exercise in January 2014, comprising capital restructuring and the issuance of rights shares with warrants. The net proceeds from the issuance of the rights shares of approximately RM40 million and the disposal of the remaining available-for-sale financial assets will be utilised to repay the Group's other existing borrowings when due, meet the cash flow requirements of the projects in progress, working capital and financial covenant requirements, and carry out all other investing and financing activities for the next twelve months from the reporting date.

With the various action plans by the Board as disclosed above, the Directors are of the view that the Group will have sufficient cash flows for the next twelve months from the end of the reporting period to meet the operating and financing cash flow requirements. Accordingly, the interim financial information of the Group is prepared on a going concern basis.

2. **Auditors' Report on Preceding Annual Financial Statements**

The auditors' report on the Group's financial statements for the financial year ended 31 March 2013 was not subject to any qualification.

3. **Seasonal or Cyclical Factors**

The Group's operations were not materially affected by any seasonal or cyclical factors.

4. **Unusual Items**

There was no unusual item affecting assets, liabilities, equity, net income, or cash flows during the quarter under review because of their nature, size, or incidence except for the following:

i) The sale of 51,511,000 of IJM shares during the quarter resulted in the transfer of RM84.0 million from the "Fair Value Reserve" to the statement of comprehensive income as gain on disposal of the available-for-sale financial assets.

ii) On 19 November 2013, the Capital Restructuring (comprising a reduction of RM0.40 of the par value of each existing ordinary share of RM0.50 each in the Company ("Par Value Reduction") and a reduction of the share premium account pursuant to Sections 64 and 60 of the Companies Act, 1965 ('the Act") took effect with the lodgement of the Court Order with the Companies Commission of Malaysia. Following the above, the issued and paid-up share capital and share premium of the Company has been reduced from RM281.6 million and RM124.4 million to RM56.3 million and nil, respectively, with a corresponding reduction in the accumulated losses brought forward.

5. **Changes in Estimates of Amount Reported Previously**

There was no change in estimates of amounts reported in the prior financial period that has a material effect in the current quarter.

6. **Debt and Equity Securities**

There was no issuance, cancellation, repurchase, resale and repayment of debt and equity securities for the current quarter ended 31 December 2013.

7. Dividends Paid

For the current financial period-to-date, no dividend has been paid. For the preceding year's corresponding period, no dividend was paid.

8. Segmental Reporting

Segment analysis for the current quarter is as follows:

	Engineering & construction RM'000	Property & development RM'000	Investment & others RM'000	Total RM'000
Revenue				
Total	74,215	196	4,990	79,402
Inter-segment	(22,728)	-	(4,889)	(27,618)
External	**51,487**	**196**	**101**	**51,784**
Results				
Segment (loss) /profit	(48,969)	169	(2,134)	(50,934)
Interest income	1,398	1	3	1,402
Profit from Islamic deposits	-	-	1	1
Gain on disposal of available-for-sale financial assets	-	-	83,950	83,950
Depreciation	(505)	(37)	(22)	(564)
Loss on fair value of derivative	-	-	(258)	(258)
Finance costs	(5,942)	-	(2,100)	(8,042)
Share of results of associates	(363)	-	-	(363)
(Loss)/profit before taxation	(54,381)	133	79,440	25,192
Tax expense				(2,263)
Profit for the quarter				**22,929**

Analysis by business segments for the financial period to date:

	Engineering & construction RM'000	Property & development RM'000	Investment & others RM'000	Total RM'000
Revenue				
Total	233,727	612	15,483	249,822
Inter-segment	(66,419)	-	(9,302)	(75,721)
External	**167,308**	**612**	**6,181**	**174,101**

8. Segmental Reporting (Continued)

	Engineering & Construction RM'000	Property & development RM'000	Investment & others RM'000	Total RM'000
Results				
Segment (loss)/profit	(40,018)	502	494	(39,022)
Interest income	12,288	2	12	12,302
Profit from islamic deposits	-	-	58	58
Depreciation	(1,623)	(110)	(67)	(1,800)
Loss on fair value of derivative	-	-	(14,597)	(14,597)
Gain on disposal of available-for-sale financial assets	-	-	98,144	98,144
Finance costs	(17,851)	-	(9,709)	(27,560)
Share of results of associates	(649)	-	-	(649)
(Loss) /profit before taxation	(47,853)	394	74,335	26,876
Tax expense				(2,336)
Profit for the period				**24,540**

The Group's segmental report for the corresponding three-month financial quarter and financial period to date ended 31 December 2012 is as follows:

Segment analysis for the corresponding quarter is as follows:

	Engineering & construction RM'000	Property & development RM'000	Investment & others RM'000	Total RM'000
Revenue				
Total	9,788	191	2,835	12,814
Inter-segment	(78)	-	(4)	(82)
External	**9,710**	**191**	**2,831**	**12,732**

8. <u>Segmental Reporting (Continued)</u>

	Engineering & construction RM'000	Property & development RM'000	Investment & others RM'000	Total RM'000
Results				
Segment (loss)/profit	(12,363)	151	194	(12,018)
Interest income	(6,387)	1	26	(6,360)
Depreciation	(482)	(31)	(1)	(514)
Impairment of property, plant and equipment	(6,702)	-	-	(6,702)
Loss on fair value of derivative	-	-	(6,616)	(6,616)
Finance costs	16,272		(4,012)	12,260
Share of results of associates	(844)	-	-	(844)
(Loss)/profit before taxation	(10,506)	121	(10,409)	(20,794)
Tax credit				450
Loss for the quarter				**(20,344)**

Analysis by business segments for the corresponding financial period to date:

	Engineering & construction RM'000	Property & development RM'000	Investment & others RM'000	Total RM'000
Revenue				
Total	38,350	580	10,577	49,507
Inter-segment	(233)	-	(2,079)	(2,312)
External	**38,117**	**580**	**8,498**	**47,195**
Results				
Segment (loss) /profit	(14,030)	572	2,738	(10,720)
Interest income	(4,601)	2	522	(4,077)
Depreciation	(1,546)	(147)	(79)	(1,772)
Impairment of property, plant and equipment	(6,702)	-	-	(6,702)
Gain on fair value of derivative	-	-	25,544	25,544
Gain on disposal of available for sale financial asset	-	-	57	57
Finance costs	2,196	-	(12,014)	(9,818)
Share of results of associates	(1,373)	-	-	(1,373)
(Loss)/profit before taxation	(26,056)	427	16,768	(8,861)
Tax expense				(23,722)
Loss for the period				**(32,583)**

9. Material Events Subsequent to the End of the Reporting Period

There was no material event subsequent to the end of the current quarter under review that has not been reflected in the interim financial report except for the announcements made and disclosed under Note 6 of Part B and as stated below.

(i) Subsequent to the period under review, the Group sold 5,160,000 ordinary shares of RM1.00 each in IJM for a cash consideration of RM29.6 million. The gain on disposal of these shares amounted to approximately RM8.2 million.

10. Changes in Composition of the Group

There was no change in the composition of the Group during the current quarter.

11. Changes in Contingent Liabilities or Contingent Assets

Save and except as disclosed below, there was no change in contingent liabilities or contingent assets since the last quarter.

A subsidiary's branch in Indonesia ("Branch") had on 20 May 2013 and 29 May 2013, received two tax demand letters stating that an amount approximately RM20.3 million is payable as the interest charges on the late payment of the tax charged based on the revised tax assessment issued by the Indonesian Tax Authorities. The Branch, through its tax consultants in Indonesia, has submitted an application to the Indonesian Tax Authorities for the waiver of the interest charges. Pending the outcome of the said application and the abovementioned Judicial Review, management has recorded a provision of RM14.4 million as at 31 March 2013 based on the advice from the external tax consultants, having duly the considered various legal grounds and basis of the aforementioned application and Judicial Review.

The Group has now made a full provision of RM20.3 million of the tax penalty in relation to the Indonesian tax with the additional provision of RM5.9 million made during the quarter. The provision is made following the Group's decision to submit the appeal to the Tax Court for the waiver of the interest charges.

12. Fair Value Measurements

The disclosure of fair value measurements by level of the fair value measurement hierarchy is as follows:

Level 1:
- Quoted prices (unadjusted) in active markets for identical assets or liabilities (Level 1);

12. Fair Value Measurements (Continued)

Level 2:
- Inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (that is, as prices) or indirectly (that is, derived from prices) (Level 2);

Level 3:
- Inputs for the asset or liability that are not based on observable market data (that is, unobservable inputs) (Level 3).

The following table presents the available-for-sale financial assets and the equity collar embedded in the term loan for the Group that are measured at fair value as at 31 December 2013:

	Level 1	Level 2	Level 3	Total
	RM'000	RM'000	RM'000	RM'000
At 31 December 2013				
Available-for-sale financial assets	30,341	-	-	30,341

The movements of the derivative financial liability (Level 3) are as follows:

	31.12.2013
	RM'000
At 1 April 2013	22,037
Loss recognised in the profit or loss	14,597
Unwinding of the derivative financial liability	(36,634)
At 31 December 2013	-

The methods and valuation techniques used for the purpose of measuring fair value are unchanged compared to the last financial year ended 31 March 2013.