

The assessment of the situation of the Company PROCHEM S.A. in 2014 including the assessment of the internal controls and risk management system

The assessment of the Company Prochem S.A. for 2014 was carried out in four aspects:

- results of operations,
- Company's situation,
- functioning of internal control system,
- risk management.

I. THE ASSESSMENT OF THE COMPANY'S RESULTS IN 2014

In the scope of basic activity – sale of engineering and construction services – the Company reached the amount of PLN 128.3 million, that is by 45.4 million more than volume of sales achieved in 2013. The achieved result at the operating level in the amount of PLN 7.5 million was much better than the result achieved in the previous year (PLN 2.4 million). It should be emphasized that this was a good year in the Company's business, in which the Company significantly improved the result compared to the previous year.

The Company's achieved net profit in the amount of PLN 5.0 million is indeed about 25% lower than the net profit achieved in the previous year, but unlike in 2013, its height, first of all was the result of the principal activity of PROCHEM SA.

The results of the Capital Group of Prochem SA, although clearly better than in 2013 (revenues increased by over 25%, and the operating result from the loss in 2013 transformed into a profit of nearly PLN 5.7 million), but subsequent year they are unfortunately burdened with losses the Company Elektromontaż Krakow - in 2014 amounting to about PLN 2.0 million.

The situation in the company, after the change of the Management Board, the introduction of a recovery program and conducting an active marketing policy, is gradually improving.

II. THE SITUATION OF THE COMPANY

After two years of slowdown, growth in GDP in 2014 was accelerated. Growth rate amounted to 3.4%, against 1.8% and 1.7% respectively, in the previous two years.

The role of the stimulator of economic growth took over domestic demand and in particular - investment demand.

In 2014 was reported dynamic revival of investment - the increase was 11.6%. This situation may attest about a gradual reduction of concern about the future condition of the economy, and such signals encourage the companies to take a decision on the start of the investment plans.

It can therefore be concluded that the macroeconomic situation in 2014 was clearly better than in the two previous years, and favored the engineering business, which is basic activity of PROCHEM SA.

The improvement of the macroeconomic situation in connection with the active marketing activities, and the credible position in the area of engineering activities, what was result from the consistent policy of maintaining of high-quality engineering potential, helped in 2014 Company in obtaining of good results and in the creation of the premises for further growth in 2015.

Financial position and liquidity of PROCHEM SA are also stable, what strengthens of its position in business as a honest and credible company.

From all projects being currently in-progress two projects require special supervision, both because of scale, as well as the risks different from standard risks in business. It is a contract executed by PROCHEM in Belarus, and the developer's project for Astrum office center.

The first contract is associated with risk of a political and system nature, but also occurs the risk arising from different administrative and organizational culture.

The current course of this project, despite a series of tensions and protracted procedures, allow to positive assessment of the possibility of its accomplishment in accordance with contractual arrangements.

The second project is own investment project and is implemented jointly with the financial partner.

The size of the project in the first stage is about 22 thousand. m² - a significant scale of the already borne own funds, the credit funds which are launched, but also unfavorable situation on the office space market in Warsaw, creates the necessity of careful supervision of the project and carrying out a current assessments of the risk which is associated with its execution.

In the future, in case of implementation of optimistic scenario, this project can be a source of raising of substantial and available financial resources which will enable to accelerate the development and transformation of the Capital Group.

III. ASSESSMENT OF INTERNAL CONTROL SYSTEM

In the opinion of the Supervisory Board the control system in Prochem SA has not changed in comparison with the previous year.

The comprehensive nature of the system provides timely and accurate disclosure of facts regarding the essential elements of the Company's operations. It enables the Management Board and the Supervisory Board a complete understanding of the financial position, operating results, the state the Company's assets and management efficiency.

Scope of the controls includes above all:

- company's economic activities - principal activity and auxiliary
- financial reporting and accounting settlements,
- compliance of the company's activities with the applicable laws and with the company's internal regulations,
- employment and wages.

The specificity of the activities of PROCHEM SA is associated with the implementation of the complex investment projects for the customers.

Accordingly in the company exist and are used the planning and control systems of implemented projects. These systems monitor the activities in the real time, what is enabling the possible actions in the event of undesirable phenomena. They also allow the monitoring of the feedback inspection of the selected projects when they are completed in order to avoid future mistakes.

The main task of institutional control is to conduct comprehensive checks in the scope of the most important issues for the company, and the collecting and preparing the information on the activities of the organizational units of the company, selected economic problems and other issues that in the given period were regarded by the Board as the most important. Apart from the institutional internal control in the company, there is also the so-called functional control exercised by managers at various levels. Managers have led the supervision over subordinates, which is consisting in checking of the degree of accomplishment of established objectives.

Checks are carried out in all phases of activity in the form of the preliminary control, the current control and the successive. Financial and accounting documents are subjected to the substantive, formal and accounting checking. Information about the correctness substantive, formal and calculating shall be signed in the identifiable way (full name), or shall bear the personal stamp of authorized person and the date of approval of the document.

The Supervisory Board appraises that the control system which was functioning in Prochem SA in 2014 ensures the completeness of recognition of economic operations, correct classification of source documents as well as the correct valuation of existing resources at various stages of registration, and thus assured the correct preparation of the financial statements and allowed the Management Board for the conducting of the business activity of the Company based on verified and complete information.

IV. RISK MANAGEMENT

In Prochem SA does not occur a distinct, and separated organizationally and procedurally system of risk management. Identification and assessment of risk areas are done by the services of the Company which are proper for specific risk. Their duties include also the defining of the actions which are necessary to reduce the risk.

Supervision, but also the key decisions relating to the scale of the exposure to risk are undertaken by the Management Board of the Company.

1. Risk of economic fluctuation

The Company's situation is strongly dependent on the business conditions and it reflects in diversified level of demand for engineering services, and has a permanent character in PROCHEM S.A..

In order to reduce the impact of that risk on the results and the Company's position:

- is carried out monitoring of the macroeconomic situation and the situation in selected industries
- is continued the diversification of activities (execution of works, developer's activity and the maintenance)
- is started the geographical diversification (through expansion of exports)
- is optimized the level of financial reserves.

2. Risk of the occurrence of threats in the performance of contracts

Types of activities conducted in Prochem SA - the preparation and management of investment projects for clients - cause that it is a risk constantly occurring.

For limiting it Prochem SA applies:

- realistic price calculation during the concluding contracts,
- monitoring of the progress in the implementation of contracts and disclosure of threats,
- selection of reliable subcontractors,
- stipulations in contracts limiting the upper level of contractual penalties.

The use of the system's instruments has allowed to avoid the financial consequences during the implementation of the contracts concluded under crisis conditions, including the conditions of strong price competition.

3. Risk of payment unreliability

The instruments limiting this constantly occurring type of risk are:

- monitoring of the financial standing of customers before and during the execution of contracts,
- the use of specialized debt collection procedures,
- optimization of payment structures.

4. Risk of adverse settlement of litigation with PERN

The current course of judicial proceedings indicates a low risk of occurrence of such a situation.

In the opinion of the Supervisory Board both identification of risk factors in 2014, and monitoring them, as well as the system of preventive actions are in Prochem SA at a good level. There is a feedback between the Company's control system and the risk occurring. Company's control system helps to detect and quantify the size of the risk, and this, in turn, helps for more precisely monitoring all areas of increased risk.

Signatures of the Members of the Supervisory Board:

1. Marek Garliński

2. Andrzej Karczykowski

3. Wiesław Kiepel

4. Krzysztof Obłój

5. Steven Tappan