

**ASSESSMENT OF THE SITUATION OF PROCHEM S.A.
IN 2011
INCLUDING EVALUATION OF INTERNAL CONTROL SYSTEM
AND RISK MANAGEMENT SYSTEM**

Evaluation of the company PROCHEM S.A. for the year 2010 will be conducted in four aspects:

- performance,
- situation of the company,
- functioning of the internal control system,
- risk management.

I. EVALUATION OF PERFORMANCE OF THE COMPANY IN THE YEAR 2011

After three years of decline in revenues the Company achieved growth of income from sales in 2011. They amounted to over PLN 127 million and were approximately 80 million higher than the level reached in 2010. Source of this growth were mainly contracts for implementation. Sale of design services remained at a level similar to the previous year.

Operating income amounted to near PLN 1.5 million last year. This income has increased by PLN 2.4 million derived in large part from the sale of shares of ASI Sp. z o.o. As a result net profit of company Prochem S.A. amounted to PLN 3.2 m and was by ca PLN 2.0 m higher than net profit of the previous year.

Revenues of Capital Group of Prochem S.A. amounted to over PLN 178 m and it means an increase of nearly 50 % in comparison with the previous year. These volumes are not fully comparable as in the 1st quarter of 2011 shares of subsidiary ASI were sold which resulted in its exclusion from consolidation. Financial result of Capital Group was also higher as compared with last year, and was in part attributable to the parent entity, nearly PLN 5.0 million.

In 2011 we did not succeed in beginning construction of office development projects in Kraków and Warsaw.

The results of last year should be assessed as moderately satisfactory. Despite marketing activities and flexible pricing policy, backlog of design services could not be filled at the level of economically rewarding and increase in revenue from construction activity does not seem to be permanent on the basis of observations of this year. Last year's increase in investment in the Polish economy by 8.7 % is mainly the result of growth in the area of public and infrastructure investments projects in which Prochem did not participate because of its profile.

II. SITUATION OF THE COMPANY

Results achieved in 2011, although generally positive, did not result in significant change in the situation of the business of the company. Still within the scope of basic activities - engineering activities – company is under the strong influence of conditions on the investment market. This situation in turn is determined by the high level of uncertainty as to possible further process of recovery from the economic crisis.

Forecasts of more or less dramatic economic developments formulated by analysts, particularly in Europe, this uncertainty even increase.

In effect, the vast majority of companies, although often with good financial position still restrain from decisions on the starting meaning investment projects. In turn, these segments of the investment market, in which there was a significant increase last year (infrastructure investment projects) are outside the principal competence area of PROCHEM S.A.

Possibility of further adjustment of the engineering potential of PROCHEMS.A. to a limited – of necessity – scale of operations is exhausting.

Also in the field of complementary activities stagnation still maintains. The start of the preparation of development projects encounters difficulties in obtaining the financing or finding a reliable partner which also would allow to begin the implementation of these undertakings.

Additional factor having an effect on limiting the possibility of better liquidity of the investment (financial means, which could be directed to the development) is the protracted lawsuit with PERN.

Therefore, this year it is required from the company to focus on the financial position and its permanent supervision and to take measures to rebuild financial reserves.

III. ASSESMENT OF INTERNAL CONTROL SYSTEM

In the opinion of the Supervisory Board the control system for the PROCHEM SA didn't change significantly as compared to the last year.

Comprehensive nature of the system provides timely and accurate disclosure of facts concerning the essential elements of company's activity. It allows the Management Board as well as the Supervisory Board to obtain complete understanding of the financial position, operating results, the state of the company's assets, and management efficiency.

Scope of supervision includes above all:

- business activities of the company – basic and auxiliary ,
- financial reporting and accounting for,

- compliance of the company's operations with applicable and internal regulations,
- employment and remuneration.

Specifics of the activities of PROCHEM S.A. is connected with the implementation of complex investment projects for customers.

In connection with the above in the company exist and are applicable planning and control systems for implemented projects. These systems monitor activity in real time allowing for possible action in case of adverse events. They also allow for the monitoring of feedback of the selected projects after their completion aiming at avoiding mistakes in the future.

The main task of institutional control is the conducting comprehensive inspections within the scope of the most important issues for the company as well as collecting and development the information on the activities of organizational units of the company, chosen economic problems and other issues, which in the given period were regarded as most significant by the company's Management Board. In addition to the institutional internal control, there is also so-called functional control in the company exercised by managers of various levels. The managers supervise subordinates, consisting in checking the status of implementation of determined tasks.

Control activities are conducted in all phases of activity in the form of the preliminary checks, the current and the next. Financial and accounting documents are subjected to the substantive, formal and accounting control. Information about the substantive, formal and accounting correctness shall be signed in the identifiable way (full name) or bears the personal stamp of authorized person and the date of approval of the document.

The Supervisory Board judges, that the control system functioning in PROCHEM S.A. in 2011 ensures the completeness of the approach to economic operations, the correct classification of the source documents, as well as proper valuation of resources at various stages of registration, and thus ensures proper of drawing up financial statements and allow the Management Board to conduct company's activity based on a verified and complete information.

IV. RISK MANAGEMENT

In PROCHEM S.A. does not appear distinct, separated organizationally and procedurally risk management system. The Company's service appropriate to the type of the risks are dealing with the identification and evaluation of areas of the risk.

Also define the action necessary to reduce the risk is included in their duties. Management Board conducts supervision but also takes the key decisions on reducing the exposure to the risk.

1. Risk of economic fluctuations

Continued in 2011 weak market linked to global crisis affected the situation of the Company throughout 2011. It showed a low demand for engineering services provided by PROCHEM S.A. and especially in the design and influenced the worsening of business conditions and the possibility of financing of development projects. To reduce this risk the Company:

- keeps the strategy of diversification of activities,
- gets ahead in cutting costs,
- strives for the optimal level of financial reserves.

Depth of the crisis and the conservatism of the financial sector considerably reduced the possibility of using these instruments. The crisis affected all activities appearing in the PROCHEM S.A. and Capital Group, and restrictions in the area of the external financing stopped the possibility of implementations of property projects as well as possibilities of the optimization of financial reserves.

Also further reduction of costs, especially personal, could significantly reduce the ability of PROCHEM S.A. to integrated implementation of more complex projects.

2. Risk of the appearance of threats at execution of contracts

Types of activity lead in PROCHEM S.A. - pre-investment activities and management of investment projects for customers cause that the risk is constantly appearing.

For limiting it PROCHEM S.A. applies:

- realistic price calculation at concluding a contract,
- monitoring of the progress of the execution of contract and revealing threats,
- selection of credible subcontractors,
- contractual clauses limiting contractual penalties as for the ceiling.

In 2011 in spite of applying these system instruments the Company didn't manage to avoid financial consequences at the realization of the contracts concluded in crisis conditions, including those concluded in conditions of the strong price competition.

3. Risk of the payment unreliability

The instruments limiting this constantly appearing kind of risks are:

- monitoring of the standing of customers before and during the process of the execution of contracts,
- applying of special debt collection procedures,
- optimization of structures of the payment.

In the crisis conditions the risk of worsening the liquidity can be of the substantial significance in current year.

4. Risk of disadvantageous settling the litigation with PERN S.A.

The current court course of the dispute shows little risk that such a situation will happen. In the result of the prolonged dispute is the risk of deterioration in the liquidity connected with financial obligations arising from the deposit guarantee.

In the evaluation of the Supervisory Board the identification of risk factors in 2011, and monitoring them, as well as system of precautions are in PROCHEM SA on the good level. A feedback exists in the Company between the control system and appearing risks. The control system is helping to detect and determine size of risks and it helps in turn to control the areas of the increased risk more thoroughly.

Signatures of members of Supervisory Board

1. Andrzej Karczykowski - Chairman _____

2. Marek Garliński _____

3. Krzysztof Obłój _____

4. Dariusz Krajowski - Kukiel _____

5. Adam Parzydeł _____