

The assessment of the situation of the Company PROCHEM S.A. in 2013 including the assessment of the internal control system and risk management system

The appraisal of the Company PROCHEM S.A. for 2013 was carried out in four aspects:

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

I. THE ASSESSMENT OF THE COMPANY'S PERFORMANCE IN 2013

In the scope of basic activity – sale of engineering services and construction services – the Company reached the level of PLN 82.9 million, that is about PLN 1.4 million lower than achieved in 2012. The achieved results at the operating level of PLN 2.4 million, compared to a loss from the previous year (PLN 5.4 million) should be considered Company's back to "normal", i.e. of achieving stable results from the engineering activities. High net profit achieved by the Company in the amount of PLN 6.6 million is more than twice higher than the net profit of the previous year. Its height was primarily determined by sale by PROCHEM S.A. of a significant part of the shares of Elektromontaż Kraków S.A. to PROCHEM Inwestycje.

The results of PROCHEM S.A. Group are not satisfactory. Despite higher by PLN 4 million revenues compared to last year, the Group incurred a loss in the amount of PLN 0.7 million at the operational level. The main source of the result are high losses incurred by Elektromontaż Kraków S.A. from two large contracts in 2013. So far, companies belonging to the Group have contributed to its improved result. Particularly stable and significant influence on the result of the entire Group, had the activities of Elektromontaż Kraków S.A. In order to restore hitherto the company's position in the Group, has been launched recovery program, covering a range of organizational and personnel actions.

II. THE SITUATION OF THE COMPANY

The macroeconomic situation in 2013 was unfavourable to engineering activities, constituting a basic activity of PROCHEM S.A. Distinct slowdown in economic growth and persisting low level of investments were the source of the low demand for services offered by PROCHEM.

Also the persisting uncertainty, especially in the first half of the year, in relation to the further course of the process of recovery from the crisis, restrains companies from making decisions on actuating significant investment projects. Gradually the situation during the year, however, shows certain, slight improvement, raising hopes about the possibility of accelerating of economic growth.

Against the background of the macroeconomic environment, and its however, in total, adversely affecting, in 2013 the situation of PROCHEM was been relatively good. This resulted mainly from the marketing activities, that have been led by the Company actively and consequently, and often in continuous way with selected partners. Another important issue for clients is the technical credibility of the Company, resulting from the policy of maintaining the engineering potential at a level enabling the implementation of significant, technologically complex, multi-discipline investment projects.

The second, more optimistic half of 2013 and the first months of the year show that gradually, the macroeconomic factors will be more conducive to PROCHEM activities.

In addition to general, the expected increase in investment expenditures we have to deal with the process of launching of a large investments in the power sector, as well as with the programming in terms of large projects in the chemical industry or environmental protection.

It seems, therefore, that both the current year and the following years would be characterized by the market conditions which are favourable to PROCHEM S.A.

Launching of development project of office building in Warsaw, and also preparatory works leading to implementation of the project in Krakow, additionally use the engineering potential of the Company.

In the future, these projects can be a source of the significant free financial means, enabling acceleration of the development and reconstruction of the Capital Group.

III. ASSESSMENT OF INTERNAL CONTROL SYSTEM

In the opinion of the Supervisory Board the control system in PROCHEM S.A. 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 Supervisory Board to obtain 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 business activities - basic and supplementary activities,
- financial reporting and accounting settlements,
- compliance of the company's activities with the applicable laws and internal regulations,
- employment and wages.

The specificity of the activities of PROCHEM S.A. is associated with the implementation of 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 adverse phenomena. They also allow the monitoring of the feedback inspection of the selected projects after their completion, in order to avoid future mistakes. The main task of institutional control is to conduct comprehensive checks on 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 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. The managers have led the supervision

over subordinates, which is consisting in checking 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 next. Financial and accounting documents are subjected to the substantive, formal and accounting control. Information about the correctness substantive, formal and accounting shall be signed in the identifiable way (full name), or 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 S.A. in 2013 ensures the completeness of approach to economic operations, correct classification of source documents as well as the correct valuation of existing resources at various stages of registration, and thus has ensured correct preparation of the financial statements and has enabled to the Management Board conducting of business activity of the Company on the basis of verified and complete information.

IV. RISK MANAGEMENT

In PROCHEM S.A. 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 to define the actions which are necessary to reduce the risk. Supervision, but also the key decisions relating to the reduction of the exposure to risk are made by the Management Board of the Company.

1. Risk of economic fluctuation

The Company's situation is strongly dependent on the economic conditions what is reflected in diversified level of demand for engineering services, and has a permanent character in PROCHEM.

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 maintenance)
- is begun 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 S.A. - the preparation and management of investment projects for clients - cause that this is constantly occurring risk.

For limiting it PROCHEM S.A. applies:

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

The use of these system instruments has allowed to avoid the financial consequences of 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. The consequence of the protracted dispute is the deterioration of the liquidity associated with the financial obligations arising from the security deposits.

In the opinion of the Supervisory Board both the identification of risk factors in 2013, and monitoring them, as well as the system of preventive actions are in PROCHEM S.A. at a good level. In the Company there is a feedback between control system and occurring risks. The control system helps to detect and quantify the size of the risk, and this, in turn, helps to more closely monitor all areas of risk.

Signatures of the members of the Supervisory Board:

1. Andrzej Karczykowski - Chairman _____

2. Marek Garliński _____

3. Krzysztof Oblój _____

4. Dariusz Krajowski-Kukiel _____

5. Adam Parzydeł _____