



# **MANAGEMENT BOARD'S REPORT OF ACTIVITIES OF DOM DEVELOPMENT S.A. CAPITAL GROUP IN 2012**

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**APPROVAL BY THE MANAGEMENT BOARD OF THE MANAGEMENT BOARD'S REPORT OF  
ACTIVITIES OF DOM DEVELOPMENT S.A. CAPITAL GROUP IN 2012**

This Management Board's report of activities of Dom Development S.A. Capital Group in 2012 was prepared and approved by the Management Board of the Company on 26 February 2013.

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Jarosław Szanajca,  
President of the Management Board

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Janusz Zalewski,  
Vice President of the Management Board

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Jerzy Ślusarski,  
Vice President of the Management Board

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Janusz Stolarczyk,  
Member of the Management Board

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Terry R. Roydon,  
Member of the Management Board

## INTRODUCTION

The joint stock company Dom Development S.A. (the "Company", "parent company") is the parent company of Dom Development S.A. Capital Group (the "Group"). The Company has been entered into the National Court Register under number 0000031483 maintained by the District Court for the capital city of Warsaw, 12<sup>th</sup> Commercial Division of the National Court Register. The registered office of the Company is in Warsaw (00-078 Warsaw, pl. Piłsudskiego 3).

Dom Development was established in 1995 by a group of international investors, and Polish management staff joined it in November 1996. Participation of the international investors guaranteed implementation of Western European experience and standards as regards housing developments in the market where the Company operates.

As at 31 December 2012 the Company was controlled by Dom Development B.V. with registered office in the Netherlands which held 61.53% of the Company's shares.

## 1. GENERAL INFORMATION ABOUT DOM DEVELOPMENT S.A. CAPITAL GROUP

### 1.1. Group's Structure

The Group's structure and the Company's interest in the share capital of the entities comprising the Group as at 31 December 2012 is presented in the table below:

Entity	Country of registration	% of the share capital held by the parent company	% of the votes held by the parent company	Consolidation method
<b>Subsidiaries</b>				
Dom Development Morskie Oko sp. z o.o., under liquidation	Poland	100%	100%	full consolidation
Dom Development Grunty sp. z o.o.	Poland	46%	100%	full consolidation
<b>The Group has been also engaged in the joint venture:</b>				
Fort Mokotów sp. z o.o., under liquidation	Poland	49%	49%	proportionate consolidation

### 1.2. Activities of the Company and the Group

The main area of activity of the Company and the companies operating within the Group is the construction and sale of residential real estate. All development projects of the Group are conducted directly within the Dom Development organisational structure.

In the twelve-month period ended 31 December 2012:

- the Group did not discontinue any of its activities;
- The Group did not make any material deposits or capital investments within the framework of the Dom Development S.A. Capital Group. All free cash was invested by the companies operating within the Group in short term bank deposits.

### 1.3. Information on core products

The main aim of the Group has always been the construction of affordable flats in the so-called popular segment (mid market). The Group's offer is supplemented with other market segment products.

Currently, the Group's product mix is as follows:

- Multi-family buildings (flats and apartments), which can be divided into the following market segments:
  - *Popular flats (mid-market)* – flats in residential buildings and housing estates are usually located outside of the immediate city centre, normally with at least 200 flats.
  - *Apartments* – apartments in residential buildings or small groups of buildings located in Warsaw's city centre and in popular residential districts (Żoliborz, Mokotów, Śródmieście, Ochota).
  - Flats and apartments are offered in two standards: "turn-key" and unfinished. The unfinished flats/apartments are finished by buyers on their own account. Various finishing options are available for "turn-key" flats/apartments.
  - *Commercial space* – mainly shops constructed by the Company as part of residential buildings. The revenues from the sale of such space account for an insignificant part of the total revenue but they enable the possibility to offer such facilities as shops, which increases the attractiveness of a given project.
- Single-family houses (detached, semi-detached and terraced houses).

In addition to this, the Company's tasks include the management of housing estates constructed under development projects conducted by the Group. Management will be performed only through a limited period of time, i.e. until the final management company is chosen by the common hold associations which take over the managerial duties from the Company.

In 2012, the Group's revenue from the sale of products and services related to real estate management were as follows:

REVENUE STRUCTURE	01.01- -31.12.2012 in thousand PLN	01.01- -31.12.2011 in thousand PLN	Change 2012/2011
Revenue from the sale of flats/apartments, houses and commercial space	838 799	568 082	48%
Revenue from the sale of real estate management services	4 605	1 758	162%
Revenue from other sales	8 009	8 834	(9)%
<b>Total</b>	<b>851 413</b>	<b>578 674</b>	<b>47%</b>

#### 1.4. Information on the markets, customers and sources of supply of production materials

In 2012 the activity of the Group was mainly concentrated in Warsaw and its vicinity. In 2012, the changes in portfolio of housing products offered by the Group continued, i.e. there was a further increase in the share of popular flats in the structure of the planned investment projects. This has already been reflected in both, the sales structure in 2012 and the structure of planned investment projects. The Group have continued its operations in the Wrocław market in 2012. The first project in Wrocław, namely Oaza estate phase I, was completed in December 2012.

##### 1.4.1 Group's sales structure

NUMBER OF PRODUCTS SOLD BY PRODUCT GROUPS	2012	2011	Change
Popular (mid-market) apartments	1 382	1 668	(17)%
High-end apartments (including luxury apartments)	31	60	(48)%
Single-family houses	23	7	229%
<b>Total</b>	<b>1 436</b>	<b>1 735</b>	<b>(17)%</b>

The Group does not depend on any of its customers because the sales are dispersed amongst a large, varied and changing group of buyers of residential and commercial units. The majority of the Group's customers are natural persons.

### 1.4.2 Major contractors

The main costs incurred by the Group in the real estate development activity are the costs of construction services provided by third parties, not related to the Group, under a general contracting system and the purchase costs of land for the investment projects.

As regards the land, despite individual transactions of significant value, the Company does not depend on one supplier.

As regards the construction services, contractors are chosen in internally organised tender procedures. The Group uses the services of various construction companies operating in the Warsaw and Wrocław markets.

The Group's major contractors in 2012, in terms of the value of services purchased in this period, were:

CONTRACTOR	01.01- -31.12.2012 in thousand PLN
UNIBEP S.A.	90 525
HENPOL Sp. z o.o.	88 877
ERBUD S.A.	43 868
KALTER Sp. z o.o.	38 514
Mostostal Warszawa S.A.	24 760
WPBP Nr 2 Wrobis S.A.	23 083
PB Unimax Sp. z o.o.	13 660

The turnover shown above accounts for approximately 73% of the sum spent by the Group on construction and design services in 2012.

## 2. OPERATIONS OF DOM DEVELOPMENT S.A. CAPITAL GROUP

### 2.1. OPERATIONS OF DOM DEVELOPMENT S.A. CAPITAL GROUP IN 2012

In 2012 the Group continued its development activities, being the construction and sale of residential real estates. The construction works have been conducted predominantly in the general contractor system, and the works are contracted to specialized third-party building companies.

There are several development projects that are simultaneously conducted by the Group. The Management Board of the Company regularly reviews and gives its opinion on:

- current projects during their implementation in relation to both, the progress of construction works, and current and anticipated sales revenue,
- the best possible manner in which the plots of land from the land-bank may be used and adjustment of the product offer to best meet the expectations and demand in the market,
- the potential plots of land which may be purchased for further development projects to be carried out in the following years, also in major Polish cities other than Warsaw,
- optimization of financing of the Group's operating activities.

#### 2.1.1 Development projects commenced and completed

In 2012, the following material changes in the portfolio of the Group's real estate development investments under construction took place:

Projects commenced in the period from 1 January 2012 until 31 December 2012:

Project	Standard	Number of apartments
Derby 14, phase 2	Popular	154
Wilno, phase 4	Popular	109
Młyny Królewskie	Popular	294
Saska I, phase 3/1	Popular	159
Wilno, phase 2B	Popular	124
Derby 14, phase 3	Popular	189
Klasyków I, phase 2	Popular	236
Saska I, phase 3/2	Popular	163
Willa na Harfowej	Popular	90
Adria, phase 3	Popular	183



Projects completed in the period from 1 January 2012 until 31 December 2012:

Project	Standard	Number of apartments
Wilno, phase 1 (stage 1A)	Popular	130
Regaty, phase 5	Popular	180
Klasyków I, phase 3	Popular	187
Opera B	Luxury apartments	11
Przy Ratuszu	Popular	465
Saska I, phase 2/1	Popular	190
Wilno, phase 1B	Popular	84
Derby 14, phase 1	Popular	174
Adria, phase 2	Popular	230
Saska I, phase 2/2	Popular	144
Wilno, phase 2 (stage 2A)	Popular	117
Akropol	Popular	366
Oaza, phase 1	Popular	116
Saska I, phase 2/3	Popular	105

### 2.1.2 Current and future development projects

As at 31 December 2012, the projects under development account for 2 123 apartments in total. The new development projects for 7 023 apartments in total are defined and planned by the Group.

### 2.1.3 Agreements significant for the business activity of the Group

Major agreements with the aggregate value exceeding 10% of Company's equity that were concluded with contractors in the financial year

CONTRACTOR	Agreement date	Project name
Unibep S.A.	17-04-2012	Saska I, phase 3

### Other major agreements

The Company entered into a major bond issue agreement in 2012. This and other finance agreements have been described in section 3.4.

### 2.1.4 Agreements with shareholders

Dom Development S.A. Capital Group has no information on any possible agreements between the shareholders concluded in 2012.

### 2.1.5 Cooperation agreements

In 2012, Dom Development S.A. Capital Group did not conclude any significant cooperation agreements with other entities.

### 2.1.6 Transactions with related entities

All transactions made by the Company or its subsidiaries with related entities are based on the arm's length principle.

Transactions with the related entities are presented in note 7.44 to the consolidated financial statements for the period ended 31 December 2012.

### **2.1.7 Litigations**

#### **Proceedings before the courts, arbitration or public administration authority**

As of 31 December 2012 there was no individual proceeding before any court, authority competent for arbitration or public administration body, concerning the liabilities or receivables of the Company or its subsidiary, the value of which would be at least 10% of the Company's shareholders' equity.

As of 31 December 2012 there were not two or more proceedings before any court, authority competent for arbitration or public administration body, concerning the liabilities or receivables, the value of which would be at least 10% of the Company's shareholders' equity.

As of 31 December 2012, the Company was a party to proceedings concerning liabilities and receivables, the total value of which was approx. PLN 12 927 thousand, including the total value of proceedings concerning liabilities at approx. PLN 12 296 thousand and the total value of proceedings concerning receivables at approx. PLN 630 thousand.

The proceedings involving the Company have no significant impact on the Company's activity.

## **2.2. Development of Dom Development S.A. Capital Group, risk factors**

### **2.2.1 Significant risk factors and factors important for development of the Group**

Significant risk factors and threats to the business activity conducted by the Company and by the Group have been presented below.

#### **Macroeconomic factors**

The Group's business activities are significantly affected by global developments, in particular by their impact on the Polish economy. The most important macroeconomic factors for the Group's financial condition and results include: economic growth rate (risk of growth deceleration), unemployment rate (risk of growing unemployment), position of financial institutions (risk of a decrease in trust). The business activities of the Group are affected by the following macroeconomic factors, which have impact on the standing of the Polish economy: GDP, level of investments, household income, interest rates, inflation, unemployment and the condition of the real estate development and construction industries, and the real estate market.

#### **Availability of mortgages**

Stricter lending criteria applied by banks when assessing credit worthiness of their customers led to a situation where many new potential buyers of apartments hit a creditworthiness barrier. The demand for new apartments and houses may be limited as a result of a lack of new lending solutions and difficult access to loans. Restrictive lending has affected the mortgage market by mitigating the positive momentum of reduced interest rates from August 2012.

#### **Foreign exchange risk**

There has been a significant drop in the availability of loans in foreign currencies since the beginning of 2012. Some banks abandoned extending such loans, while others tightened requirements for potential borrowers, and provide foreign currency loans at higher margins than previously.

A great deal of foreign currency loans are mortgages. This brings about the risk of borrower insolvency, and therefore more apartments seized by the banks being put on the market, where a decline in demand of potential buyers who are not able to obtain such loans, is observed.

Foreign currency loans that in the past were taken at exchange rates that were lower than they are at present due to PLN depreciation against EUR or CHF, sometimes exceed the real value of the properties which secure such loans.

### **Concentration of operations in the Warsaw market**

The Group's present and planned activity is concentrated in the Warsaw market. This makes the Group's results highly dependent on the situation in this market. However, it can be assumed that in the long-term this will be the most dynamic residential real estate market in Poland, and the Group already has a well established position and therefore the possibility of further development. The Group has been currently running its first project in the Wrocław market and is preparing to commence the next one. A further expansion of the Company is also considered.

### **Opportunity to purchase land for new projects**

The future success of the Company and the Group is founded on the ability to continually and effectively acquire attractive land for new development projects at the right times and competitive prices. This will allow the generation of satisfying project contributions.

### **Administrative decisions**

The nature of real estate development projects requires a number of licenses, permits and arrangements to be obtained by the Company and the Group at every stage of the investment process. Despite significant caution applied in the project execution schedules there is always a risk of delay in their obtainment, challenges of decisions which have already been issued (also due to appeals with no consequences for appellants) or even failing to obtain them. All these affect the ability to conduct and complete the executed and planned projects.

The fundamental activity adopted by the Group so as to reduce the exposure to market risks is proper assessment of potential and control of current development projects based on investment models and decision-making procedures developed in the Company. The adherence to such procedures is closely monitored by the Management Board of the Company.

There has been a formalised risk management procedure in operation within the Company since 2000. Under this procedure the risk is managed through the identification and assessment of the risk areas for all aspects of the activities, in which the Company and the Group are involved, together with defining activities required to reduce or eliminate such risks (including through the procedures and internal audit system) The risk management procedure is subject to periodic revision and is updated by the Management Board jointly with the key management staff and third party advisers.

#### **2.2.2 Perspectives for the development of the Company's and the Group's business activities**

The housing property market in 2012 was characterized by a large intensity of the negative influences from the economy and the structure of the market. Developers significantly increased the number of projects that began being executed based on the optimistic sentiment after the improvement in the market in 2011, and also due to the entry into force on 29 April 2012 of the Act on the protection of rights of a dwelling unit and house buyer. A surplus of apartments and pessimistic outlook on the Polish economy, and as a consequence the deteriorated situation in the labour market and household earnings together with a tighter conditions for mortgages, made the situation in the property market deteriorate as compared to 2011.

The Rodzina na Swoim (*Family's Own Home*) programme had a significant impact on the sale of apartments in 2012. On the one hand, a progressive reduction in the price thresholds limited the availability of apartments under the programme, and on the other hand, the realization that the program was about to end at the end of 2012 motivated potential beneficiaries to speed up their decisions concerning purchases. Consequently sales may be lower at the beginning of 2013 than in 2012. The Mieszkanie dla Młodych (*Apartment for the Young*) programme as planned to commence at the beginning of 2014 may in turn delay purchase decisions by persons who have the opportunity to take advantage of the government subsidies. This gap between the government support programmes for the purchase of apartments may negatively affect the Polish property market in 2012. However this is not a significant risk for the operations of the company, because the offer of Dom Development S.A. in the majority of cases does not include apartments that qualify for the programmes with government subsidies.

The major objective and task of the Management Board, having considered the rapidly changing situation in the real estate market, was to prepare the Group to face new challenges. The major steps undertaken in this respect included:

- ensuring that adequate sources of finance are available to the Group, both for current and future real estate development projects, with due care from the perspective of the Group and its customers,
- co-operation with banks, and strong assistance to customers in obtaining mortgages for purchase of an apartment,
- adjusting the sales offer to the market demand,
- aligning land purchase outlays to Group's existing and future needs,
- optimizing the way and time the current land bank is used,
- increasing the efficiency and scale of sales support activities,
- maintaining and building upon customer confidence in the Dom Development brand,
- restructuring the organization and employment to the anticipated level of operational activities,
- optimising general administrative expenses.

The above-mentioned measures taken by the Management Board will be continued in 2013. In addition to this, in the next twelve months Dom Development S.A. Capital Group will focus, in particular, on the further increase of sales volume as compared to 2012 and the increase of its share in the Warsaw real estate market. This will be possible due to:

- the well-established position in the Warsaw residential property market,
- the high qualifications and potential of the Group's management,
- the worked out know-how in respect of operational execution of development projects,
- accumulated experience in selling and financing development projects,
- the land bank (for both, ongoing and future projects).
- very good liquidity of the Group.

In the upcoming twelve-month period it is also planned to:

- further focus on the operating activities in the popular flat segment and maintain activities in the remaining product groups within the offered product range,
- concentrate all of the Group's operations in Dom Development S.A. and further reduce the significance of other entities operating within the Group,
- develop operations of the Group outside the Warsaw market (in particular in Wrocław).

### 3. FINANCIAL SITUATION OF THE CAPITAL GROUP, FINANCE MANAGEMENT

#### 3.1. Basic economic and financial figures disclosed in the annual consolidated financial statements of the Group for 2012

##### 3.1.1 Selected data from the consolidated balance sheet

##### Assets

Structure of the Group's assets as at 31 December 2012, and changes as compared to the figures as at the end of 2011.

ASSETS	31.12.2012 in thousand PLN	Share in assets	31.12.2011 in thousand PLN	Change 2012/2011
<b>Total fixed assets</b>	<b>8 236</b>	<b>&lt;1%</b>	<b>7 505</b>	<b>10%</b>
<b>Current assets</b>				
Inventory	1 305 568	74%	1 465 828	(11)%
Trade and other receivables	27 980	2%	49 271	(43)%
Other current assets	7 219	<1%	13 249	(46)%
Cash and cash equivalents and Short-term financial assets	410 687	23%	380 247	8%
<b>Total current assets</b>	<b>1 751 454</b>	<b>&gt;99%</b>	<b>1 908 595</b>	<b>(8)%</b>
<b>Total assets</b>	<b>1 759 690</b>	<b>100%</b>	<b>1 916 100</b>	<b>(8)%</b>

##### Equity and liabilities

Structure of the Group's shareholders' equity and liabilities as at 31 December 2012, and changes as compared to the figures as at the end of 2011.

EQUITY AND LIABILITIES	31.12.2012 in thousand PLN	Share in equity and liabilities	31.12.2011 in thousand PLN	Change 2012/2011
<b>Shareholders' equity</b>				
Share capital	24 715	1%	24 560	<1%
Share premium less treasury shares	233 733	13%	231 535	<1%
Reserve and supplementary capitals, and accumulated unappropriated profit (loss)	634 574	36%	579 611	10%
<b>Total shareholders' equity</b>	<b>893 022</b>	<b>51%</b>	<b>835 706</b>	<b>7%</b>
Non-controlling interests	(621)	<1%	(637)	3%
<b>Total shareholders' equity</b>	<b>892 401</b>	<b>51%</b>	<b>835 069</b>	<b>7%</b>
<b>Liabilities</b>				
Long-term liabilities	452 686	26%	320 593	41%
Total short-term liabilities	414 603	24%	760 438	(46)%
Total liabilities	<b>867 289</b>	<b>49%</b>	<b>1 081 031</b>	<b>(20)%</b>
<b>Total equity and liabilities</b>	<b>1 759 690</b>	<b>100%</b>	<b>1 916 100</b>	<b>(8)%</b>

### 3.1.2 Selected data from the consolidated income statement

Consolidated income statement of the Group for the year ended 31 December 2012 as compared to 2011.

	01.01- -31.12.2012 in thousand PLN	sale %	01.01- -31.12.2011 in thousand PLN	Change 2012/2011
Sales revenue	851 413	100%	578 674	47%
Cost of sales	647 435	76%	388 235	67%
Gross profit on sales	203 978	24%	190 439	7%
Operating profit	113 511	13%	103 181	10%
Profit before tax	113 512	13%	102 812	10%
Net profit	91 233	11%	82 123	11%
Basic earnings per share (in PLN)	3.70	n/d	3.37	10%

### 3.1.3 Selected information from the consolidated cash flow statement

	(in thousand PLN)		Change
	2012	2011	
Cash and cash equivalents – opening balance	380 247	434 691	(13)%
Net cash flow from operating activities	125 625	(40 432)	n/d
Net cash flow from investing activities	(238 163)	(1 099)	n/d
Net cash flows from financing activities	(91 791)	(12 913)	n/d
Cash and cash equivalents – closing balance	175 918	380 247	(54)%

Cash balances amounted to PLN 380 247 thousand at the beginning of 2012 and they amounted to PLN 175 918 thousand at the end of the year. Therefore in the period from 1 January until 31 December 2012 the balance of cash dropped by PLN 204 329 thousand. This results mostly from the presentation of bank deposits with a maturity of over 3 months (the amount of PLN 233 910 thousand) as investment expenditure. The total amount of cash and its equivalents as well as bank deposits with a maturity of over 3 months was PLN 409 828 thousand at the end of the reporting period.

In 2012, the Group recorded a net inflow of cash from the operating activities in the amount of PLN 125 625 thousand. Bearing in mind the size of the Group this is a result of balanced operating activities in 2012 where, in addition to significant revenue from the sale of apartments in new investments and the sale of fully furnished apartments, the Group decided to commence numerous new development projects. At the same time, the Group spent significantly less for the purchase of land for future projects in 2012 as compared to 2011.

In 2012, the Group disclosed a net outflow of cash from investing activities in the amount of PLN 238 163 thousand. This results mostly from the presentation of bank deposits with a maturity of over 3 months in the amount of PLN 233 910 thousand as investment expenditure.

In 2012, the Group recorded a net cash outflow from the financing activities in the amount of PLN 91 791 thousand. The excess of financial outflow over the inflow is mainly due to reduced balance of loans (net cash outflow in the amount of PLN 7 134 thousand) and bonds (net cash outflow in the amount of PLN 50 000 thousand) as well as the payment of dividends by the Company in the amount of PLN 37 006 thousand. On the other hand, the Company received PLN 2 353 thousand for the issue of ordinary shares of the Company as a result of the exercise of share options by participants in the Management Option Programme II.

## 3.2. Forecasts

Both, Dom Development S.A. Capital Group and the parent company did not publish financial forecasts for 2012.

### 3.3. Finance management in the Group

In 2012, the finance management of Dom Development S.A. Capital Group in respect of construction of residential buildings was focused on seeking and structuring sources of external financing for the projects under construction and on maintaining a safe level of liquidity. The Management Board analyses the current and plans the future optimum financing structure on a regular basis in order to achieve planned ratios and financial results, and at the same time, to ensure liquidity and the comprehensive financial security of the Group. In 2012, the activities of the Group generated a positive result at each level of the income statement.

The Management Board is of the opinion that the net assets and financial standing of Dom Development S.A. Capital Group at the end of 2012 demonstrate the strong and stable financial position of the Group. This results from the well established position of the Group in the housing market, appropriate operational experience and potential in place, both in terms of execution of residential development projects, and the sale and financing of these projects. The net assets and financial standing of the Group has been demonstrated by liquidity and debt ratios presented further in this report.

Having considered the situation in the Polish real estate market in recent years, the financial results achieved by the Group in 2012 can be considered good. In 2012, the Group delivered 1 970 apartments (including high-end apartments and single-family houses) to its customers as compared to 1 282 units in 2011. As a result the financial result achieved in 2012 improved as compared to 2011, although the profitability of operating activity is lower than in 2011 (which is demonstrated by the profitability ratios presented below). The Group sold 1 436 apartments (including high-end apartments and single-family houses) which may be considered a good result with the prevailing situation in the residential market.

#### 3.3.1 Profitability ratios

The ratios showing profitability of the business activity pursued by the Group in 2012 have slightly deteriorated as compared to the previous year. It predominantly results from the fact that the average margin generated on the products delivered in 2012 was lower than on the products delivered in 2011. A notably increased number of deliveries in 2012 as compared to 2011 (54%) translated into an increase in the operating profit and net profit.

PROFITABILITY RATIOS	2012	2011
Operating profit margin <i>EBITDA / net sales revenue</i>	13.7%	18.3%
Net profit margin <i>Net profit / net sales revenue</i>	10.7%	14.2%
Return on assets (ROA) <i>Net profit / total assets</i>	5.2%	4.3%
Return on equity (ROE) <i>Net profit / shareholders' equity</i>	10.2%	9.8%

#### 3.3.2 Liquidity ratios

In view of the difficult situation in the market where the Group operates, special attention should be given to the fact of that financial liquidity has been well secured.

All the liquidity ratios significantly increased in 2012 as compared to 2011 and still remain very high. This is due to a number of long-term decisions and actions taken by the Company's Management Board. The improvement in the ratios to a high extent results from the restructuring of short-term and medium-term financing into medium-term and long-term financing. The activities and decisions referred to hereinabove include the management and financing of current investments (including decisions when to commence the construction of individual estates and concerning the product mix offered for sale), the strategy of buying new properties and maintaining suitable employment and related expenses.

The Management Board is of the opinion that the credibility of the Company and the Group in the financial market is high which is reflected by a diversified financing structure and by the willingness of banks and other financial institutions to grant new loans and other forms of long-term financing (bonds) to the Company despite the difficult market situation.

LIQUIDITY RATIOS	2012	2011
Current ratio <i>current assets / short-term liabilities less deferred income</i>	9.86	4.41
Quick ratio <i>current assets less inventory / short-term liabilities less deferred income</i>	2.51	1.02
Cash ratio <i>cash and cash equivalents, and bank deposits with a maturity of over 3 months / short-term liabilities less deferred income</i>	2.31	0.88

### 3.3.3 Leverage ratios

Appropriate operating policy (i.e. proper commencement and pace of projects as well as controlled purchases of land) and financial policy (the financing structure), made values of the presented ratios remain at a safe level for the business activity and they support the Company's and the Group's creditworthiness. All the leverage ratios, in particular net interest bearing debt ratio, were at a lower level at the end of 2012 than at the end of 2011.

The changes to liabilities for loans and bonds are the best position to reflect "net cash flows from financing activities" described in section 3.1.3 of this report.

LEVERAGE RATIOS	2012	2011
Equity ratio (assets/equity) <i>shareholders' equity / total assets</i>	50.7%	43.6%
Debt to equity ratio <i>Total liabilities / shareholders' equity</i>	97.2%	129.5%
Debt ratio <i>total liabilities / total assets</i>	49.3%	56.4%
Interest bearing debt ratio <i>interest bearing liabilities (including accrued interest) / shareholders' equity</i>	48.7%	58.6%
Net interest bearing debt ratio <i>interest bearing liabilities (including accrued interest) less cash and cash equivalents, and bank deposits with a maturity of over 3 month / shareholders' equity</i>	2.7%	13.1%

### 3.4. Information on loans, bonds, borrowings, sureties and guarantees

#### 3.4.1 Borrowings contracted or terminated

As at 31 December 2012 and 31 December 2011 the Group did not have borrowings. The Group did not take or repay any borrowings in 2012 and 2011.

#### 3.4.2 Loans contracted or terminated

On 29 March 2012, the Company and PKO BP S.A. signed Annex No. 1 to the investment loan agreement dated 11 October 2011 under which the loan amount was increased by PLN 50 000 thousand, that is up to PLN 210 000 thousand. The loan is to be entirely repaid in December 2016.

In 2012, the Group prematurely repaid two loans: the last tranche of the loan in the amount of PLN 45 000 thousand provided by PKO BP S.A. due on 31 December 2012 and the investment loan in the amount of PLN 12 100 thousand provided by Bank Millennium S.A. due on 30 June 2012.



Details of the loans contracted by the Group have been presented in note 7.20 to the consolidated financial statements of the Group for 2012.

Moreover, Bank Pocztowy has provided to the Company in 2012 an overdraft facility for the amount of PLN 5 000 thousand with the repayment date on 5 July 2013. This facility was not drawn as at the balance sheet date.

### **Loan agreements terminated in 2012**

No loan facility agreements were terminated in 2012.

### **3.4.3 Bonds**

On 2 February 2012, the Company issued 12 000 unsecured bonds with the nominal value of PLN 10 000 each and the aggregate nominal value of PLN 120 000 thousand. The maturity date for these bonds is 2 February 2017. The issue value equals their nominal value. The interest rate is set at WIBOR 6M plus margin.

It should be emphasized at this point that in the period from 2 February 2012 until 3 April 2012 the Company purchased its bonds for redemption for the aggregate amount of PLN 117 470 thousand and on 28 November 2012 the Company bought out its bonds for the amount of PLN 52 530 thousand.

Details of the obligations issued, redeemed and bought out by the Company have been presented in note 7.25 to the consolidated financial statements of the Group for 2012.

### **3.4.4 Borrowings provided**

The Group did not provide any borrowings in 2012.

### **3.4.5 Sureties provided and received**

The Group did not provide or received any sureties in 2012.

### **3.4.6 Guarantees provided and received**

The guaranties provided in 2012 are presented in the table below.

<b>Guarantee counterparty</b>	<b>Guarantee type</b>	<b>Guarantee amount in thousand PLN</b>
Miasto Stołeczne Warszawa (the Capital City of Warsaw)	Bank guarantee	75
Miasto Stołeczne Warszawa (the Capital City of Warsaw)	Bank guarantee	30

The performance guarantees, warranty bonds and guarantees for payment of liquidated damages during the period of contractual and statutory quality guarantee as received in 2012 are presented in the table below.

Company	Guarantee type	Guarantee amount in thousand PLN
HENPOL SP. Z O.O.	Bank guarantee	7 869
UNIBEP S.A.	Bank guarantee	7 364
MOSTOSTAL WARSZAWA S.A.	Bank guarantee	3 798
DORBUD S.A.	Insurance guarantee	1 974
POLBUD S.A.	Bank guarantee	1 691
ERBUD S.A.	Bank guarantee	1 309
WPBP Nr 2 WROBIS S.A.	Bank guarantee	943
APM Sp. z o.o.	Bank guarantee	796

### 3.5. Use of proceeds from the issue of securities

The Company issued new bonds for the amount of PLN 120 million in 2012. Information concerning the issue are presented in section 2.1.3. The proceeds from the issue of bonds will be used for financing the development of the Company.

In 2012, Dom Development S.A. issued 155 050 ordinary bearer shares. This took place in three series (Ł, M and N). The issues took place as a result of the performance of obligations under Management Option Programme II. The funds in the amount of PLN 2 353 thousand from the issue of Ł, M and N series shares were allocated for current operating activity of the Company. Details of the share issues have been presented in note 7.17 to the consolidated financial statements of the Group for 2012.

### 3.6. Assessment of the possibility to implement investment projects

#### Assessment of the possibility to implement investment projects, including capital investment versus the resources held, with consideration of possible changes in the financing structure of investment activity

Within Dom Development S.A. Capital Group, Dom Development S.A. and its subsidiaries are fully capable of financing the currently executed investment projects. The Group intends to finance the execution of real estate development projects from the shareholders' equity, bank loans and issue of commercial papers. The Management Board attempts to adapt the maturity structure of the bank loans and commercial papers mainly to the duration of individual development projects, with particular consideration given to gradual replenishment of the land bank for future development projects.

Currently, almost all activities of the Dom Development S.A. Capital Group are conducted directly in Dom Development S.A. Nonetheless, the Company does not exclude the possibility of executing the projects through subsidiaries or jointly-controlled entities with the financing (special-purpose loans) for these projects being provided directly by those companies or through Dom Development S.A.

## 4. STATEMENT ON THE APPLICATION OF CORPORATE GOVERNANCE

### Company's corporate governance rules and the location, where the text of corporate governance rules is publicly available

In 2012, Dom Development S.A. followed the corporate governance rules described in the Code of Best Practice for Warsaw Stock Exchange Listed Companies, adopted by the Supervisory Board of the Warsaw Stock Exchange on 4 July 2007 pursuant to Resolution No. 12/1170/2007 of the WSE Supervisory Board (as amended).

The Code of Best Practice for Warsaw Stock Exchange Listed Companies is publicly available on: <http://www.corp-gov.gpw.pl/publications.asp>

Dom Development S.A. has adhered to all of the rules described in the Code of Best Practice for Warsaw Stock Exchange Listed Companies.

### Company's corporate governance rules adopted voluntarily and the location, where the text of such corporate governance rules is publicly available

In 2012, Dom Development S.A. followed the corporate governance rules published in the Code of Best Practice for Customer-Developer Relations drafted by Polski Związek Firm Deweloperskich (*the Polish Union of Developers*).

The Code of Best Practice for Customer-Developer Relations is publicly available on:  
[http://www.pzfd.pl/strona,inicjatywy,kodeks\\_dobrych\\_praktyk.html](http://www.pzfd.pl/strona,inicjatywy,kodeks_dobrych_praktyk.html)

Dom Development S.A. has adhered to all of the rules described in the Code of Best Practice for Customer-Developer Relations.

## 4.1. Share capital, shareholders

### 4.1.1 Shareholders

As at 31 December 2012 Dom Development S.A. as the parent company was controlled by Dom Development B.V. which held 61.53% of the Company's shares.

The table below shows the list of shareholders who have, directly or indirectly through subsidiaries, significant shareholdings as at 31 December 2012:

	Status as at the date of preparing of the financial statements				Change in the period from publication of the financial statements for the year ended 31.12.2011
	Shares	% of capital	Number of votes at the GSM	% of votes at the GSM	Shares
Dom Development B.V.	15 206 172	61.53	15 206 172	61.53	-
Jarosław Szanajca	1 534 050	6.21	1 534 050	6.21	-
Aviva Powszechne Towarzystwo Emerytalne Aviva BZ WBK SA *)	1 313 383	5.31	1 313 383	5.31	no data
Grzegorz Kiępsz	1 280 750	5.18	1 280 750	5.18	-

\*) Shareholding of Aviva Powszechne Towarzystwo Emerytalne (*General Pension Society*) Aviva BZ WBK S.A. has been presented as per the latest notice as of 11.07.2011 received by the Company from Aviva PTE Aviva BZ WBK S.A

#### **4.1.2 Special control rights**

##### **Persons holding any securities with special control rights, and description of these rights**

Pursuant to paragraph 6.2.2 of the Articles of Association of Dom Development S.A., a shareholder holding at least 50.1% of shares in the Company is personally vested with the right to appoint and dismiss half of the members of the Management Board, including the President of the Management Board and the Vice President of the Management Board who is responsible, pursuant to the Management Board bylaws, for the Company's finances. For an odd number of Management Board members, a shareholder who holds at least 50.1% of the shares in the Company is authorised to appoint, accordingly: three (for a 5-person Management Board) and four (for a seven-person Management Board) Management Board members. The above right is exercised by way of serving written statement to the Company on appointment or dismissal of a given Management Board member. The remaining members of the Management Board shall be appointed and dismissed by the Supervisory Board.

Pursuant to paragraph 7.4 of the Articles of Association of Dom Development S.A. a shareholder holding at least 50.1% of shares in the Company is vested with the personal right to appoint and dismiss half of the members of the Supervisory Board, including 1 Vice Chairman thereof. For an odd number of Supervisory Board members, a shareholder holding at least 50.1% shares in the Company is authorised to appoint, accordingly: three (for a 5-person Supervisory Board), four (for a seven-person Supervisory Board) and five (for a nine-person Supervisory Board) Supervisory Board members. The above right is exercised by way of serving written statement to the Company on the appointment or dismissal of a given Supervisory Board member.

On 31 December 2012, Dom Development B.V. with registered office in Rotterdam, the Netherlands was the shareholder who held at least 50.1% of shares in the Company.

#### **4.1.3 Restrictions of right in shares**

##### **Indication of restrictions on voting rights, such as restricted voting rights by persons holding a specific portion or number of votes, and temporary restrictions on voting rights or provisions, according to which, in cooperation with the Company, capital rights attached to securities are separated from possession of securities**

Pledges and beneficial owners of shares of Dom Development S.A. are not entitled to exercise voting rights attached to shares.

##### **Indication of any restrictions on the transfer of ownership title to the issuer's securities**

No other restrictions have been in place in Dom Development S.A. regarding the transfer of ownership title to shares in Dom Development S.A.

#### **4.2. The General Shareholders' Meeting**

##### **The procedure for and major rights of a General Shareholders' Meeting, and description of the rights of shareholders and manner for these rights being exercised, in particular the rules resulting from General Shareholders' Meeting bylaws, if such bylaws were adopted and if the rules in this respect do not directly result from legal regulations**

The General Shareholders' Meeting holds its sessions as Ordinary or Extraordinary General Shareholders' Meetings, and as a governing body of the Company it acts pursuant to the provisions of the Code of Commercial Companies Act dated 15 September 2000 (Journal of Laws No. 94 item 1037, as amended), the Articles of Association of the Company and provisions of unclassified and publicly available General Shareholders' Meeting Bylaws dated 5 September 2006 as amended by

resolution No. 27 by the Extraordinary General Shareholders' Meeting of Dom Development S.A. dated 15 May 2008 and resolution No. 31 by the Extraordinary General Shareholders' Meeting of Dom Development S.A. dated 21 May 2009.

An Ordinary General Shareholders' Meeting is convened by the Management Board. It takes place in Warsaw within 6 months following the end of each financial year. Shareholders are entitled to participate in the General Shareholders Meeting provided that they were shareholders of the Company 16 days before the date of the General Shareholders Meeting (registration date for participation in a general shareholders' meeting). No invitations are required for members of the Company's Management Board and the Supervisory Board to participate in a General Shareholders' Meeting. Other persons, in particular statutory auditors and experts, as invited by the Management Board, may participate in a session or an appropriate part thereof, should their participation be justified by the need to have their opinions on the discussed matters presented to the participants in the General Shareholders' Meeting. A statutory auditor should be present at a session of the General Shareholders' Meeting where Company's financial matters are addressed.

The General Shareholders' Meeting is valid and may adopt resolutions only if shareholders holding at least 50.1% of all votes are represented at the Meeting. Resolutions are adopted by an absolute majority of validly cast votes, unless the Code of Commercial Companies or the Articles of Association of the Company provide otherwise. An electronic system for casting and calculating votes may be used for voting. Pledges and beneficial owners of shares are not entitled to exercise voting rights attached to shares.

A resolution on the removal of certain matters from the agenda of the General Shareholders' Meeting or the abandonment of certain matters included in the agenda or placed on the agenda by a motion of shareholders requires a majority of three-fourths of the votes cast and the express prior consent of all present shareholders who have filed such motion, for it to be valid.

The Chairman puts the agenda to vote, having the attendance list signed and checked. The General Shareholders' Meeting may adopt the suggested agenda without changes, change the order of debate or remove certain matters from the agenda, subject to the provisions of the Articles of Association of the Company. The General Shareholders' Meeting may also put new matters on the agenda and discuss them, however without adopting any resolutions on such matters. The Chairman of the Meeting has no right to remove matters from the agenda or alter the same without the consent of the General Shareholders' Meeting.

Each participant in the General Shareholders' Meeting may speak on matters included in the adopted agenda which are currently brought up for discussion. Each participant of the General Shareholders' Meeting may submit a formal motion. The Chairman gives the floor to a participant willing to lodge a formal motion out of turn. Formal motions are the motions concerning debate and voting procedure.

The General Shareholders' Meeting adopts resolutions on matters included in the agenda by voting. Voting is open and is subject to relevant provisions of the Articles of Association of the Company and the Code of Commercial Companies.

In 2012, the formally convened General Shareholders' Meeting of Dom Development S.A. was held on 23 May 2012 in Warsaw in the registered office of the Company. The General Shareholders' Meeting had been convened upon a motion of the Management Board of the Company, and shareholders of the Company did not file their motions for the General Shareholders' Meeting to be convened.

The course of the General Shareholders' Meeting was in line with the provisions of the Code of Commercial Companies, the Company's Articles of Association, unclassified and publicly available General Shareholders' Meeting Bylaws of Dom Development S.A. and the Code of Best Practice for WSE Listed Companies. The shareholders had the possibility to review the content of draft resolutions included in the agenda, in each case not later than 26 days prior to the planned date of the General Shareholders' Meeting. The Company did not question the correctness of documents submitted by shareholders and their attorneys in support of their right to represent a shareholder when verifying shareholders' IDs being the proof of their entitlement to participate in the General Shareholders' Meeting.

The Chairman of the General Shareholders' Meeting ensured that the session proceeded in an orderly and efficient manner. Sessions of a General Shareholders' Meeting have never been cancelled or discontinued. Members of the Management Board and the Supervisory Board present at the General Shareholders' Meeting readily explained all matters within their competences and as required by the law.

The circumstances for adopting resolutions of the General Shareholders' Meeting enabled for the protection of the rights of minority shareholders, including for voicing reservations and objections against the resolutions. None of the resolutions adopted was appealed against in court.

The Ordinary General Shareholders' Meeting of Dom Development S.A. was held within the time limit set forth in article 395 of the Code of Commercial Companies and Partnerships, and the documentation concerning the financial statements for the financial year 2011 was published on the website of the Company more than 2 months before the date of the Ordinary General Shareholders' Meeting. The resolution by the Ordinary Shareholders Meeting concerning distribution of the profit earned by the Company in 2011 and on payment of the dividend was adopted unanimously.

All resolutions adopted by the General Shareholders' Meeting in 2012 were passed in the best interest of the Company and took into account the rights of other stakeholders. Resolutions adopted by the General Shareholders' Meeting are posted on: <http://inwestor.domdevelopment.pl/informacje-o-spolce/lad-korporacyjny/wza/23-05-2012>

#### **4.3. Principles for the amendment of the articles of association**

Pursuant to article 430 § 1 and art. 415 § 1 of the Code of Commercial Companies and Partnerships, an amendment to the Articles of Association of Dom Development S.A. requires a resolution by the General Shareholders' Meeting adopted by the three-fourths majority of votes and court registration. For a resolution that is to amend the Articles of Association as to benefits of the shareholders or limit the rights granted personally to individual shareholders under art. 354 of the Code of Commercial Companies and Partnerships, the consent of all the shareholders affected by the resolution is required. An amendment to the Articles of Association is to be filed with the court of registration by the Management Board of Dom Development S.A. The General Shareholders' Meeting of Dom Development S.A. may authorize the Supervisory Board to determine a revised and reinstated text for the amended Articles of Association or to make such other editorial changes as defined in the resolution by the General Shareholders' Meeting.

#### **4.4. The Management Board**

##### **4.4.1 Principles for the appointment or dismissal of the Management Board**

##### **Description of the principles for the appointment or dismissal of managing persons and their rights, in particular the right to decide on the issue or repurchase of shares**

In accordance with the Company's Articles of Association, the Management Board of Dom Development S.A. shall comprise of 4 to 8 members, including the President, with a three-year term of office. The Supervisory Board shall determine the number of members of the Management Board. A shareholder who holds at least 50.1% of the shares in the Company is personally vested with the right to appoint and dismiss half of the members of the Management Board, including the President of the Management Board and the Vice President of the Management Board who is responsible, pursuant to the Management Board bylaws for the Company's finances. For an odd number of Management Board members, a shareholder who holds at least 50.1% of the shares in the Company is authorised to appoint, accordingly: three (for a 5-person Management Board) and four (for a seven-person Management Board) Management Board members. The above right is exercised by way of serving written statement to the Company on appointment or dismissal of a given Management Board member. The remaining members of the Management Board shall be appointed and dismissed by the Supervisory Board.

The Management Board represents the Company in and out of court. For statements to be validly made and signed on behalf of the Company, two members of the Management Board are required to act jointly or one member of the Management Board is required to act jointly with a commercial proxy.

Pursuant to paragraph 3.2.8 of the Company's Articles of Association, the Management Board is authorised to increase the Company's share capital by the issue of new shares with an aggregate nominal value of no more than PLN 1 615 825 (in words: one million six hundred and fifteen thousand eight hundred and twenty five) by way of one or several share capital increases within the limits specified above (authorised capital). The Management Board's right to increase share capital and issue new shares within the limits of the authorised capital up to PLN 1 615 825 shall expire 3 years from the

date of the amendment to the Articles of Association made by resolution No. 23 dated 23 May 2012 by the General Shareholders' Meeting being entered in the register of entrepreneurs.

The right to increase the share capital referred to in the foregoing sentence, includes the issue of subscription warrants with subscription rights that expire after the above mentioned period.

Upon the consent of the Supervisory Board, the Management Board may deprive a shareholder of all or a part of its pre-emptive rights in relation to shares issued within the limits of the authorised capital.

A share capital increase by the Management Board within the limits of the authorised capital is conditional upon obtaining a positive opinion in this respect from the Supervisory Board. In other cases, unless otherwise provided by the Code of Commercial Companies, the Management Board may decide on any and all matters related to share capital increases within the limits of the authorised capital.

Pursuant to paragraph 3.2.6. of the Articles of Association of the Company, a purchase of treasury shares by the Company for redemption does not require the consent of the General Shareholders' Meeting (subject to art. 393 item 6 of the Code of Commercial Companies and Partnerships) and only requires the consent of the Supervisory Board.

#### **4.4.2 Composition of the Management Board**

In the period from 1 January until 31 December 2012 the Management Board of the Company was composed of the following five members:

- Jarosław Szanajca, President of the Management Board
- Janusz Zalewski, Vice President of the Management Board
- Jerzy Ślusarski, Vice President of the Management Board
- Janusz Stolarczyk, Member of the Management Board
- Terry R. Roydon, Member of the Management Board.

#### **4.4.3 Principles governing the functioning of the Management Board**

The Company's Management Board acts pursuant to the provisions of the Code of Commercial Companies, the Articles of Association and unclassified and publicly available Management Board Bylaws approved by the Supervisory Board's resolution, and in accordance with the Code of Best Practice for WSE Listed Companies.

The Management Board is an executive body of the Company. It manages the current operations of the Company and represents the same towards third parties. The Management Board decides in all matters concerning the Company not reserved for the General Shareholders' Meeting and/or the Supervisory Board under legal regulations, the Articles of Association of the Company or a resolution of the General Shareholders' Meeting.

For statements to be validly made and signed on behalf of the Company, two members of the Management Board are required to act jointly or one member of the Management Board is required to act jointly with a commercial proxy. Resolutions of the Management Board are adopted by an absolute majority of votes. In case of a voting deadlock, the President of the Management Board has the casting vote.

When defining strategic and current objectives for the Company, the Management Board always acted in the underlying interest of the Company and in line with the legal regulations, and take into account the interests of the shareholders, employees and creditors of the Company.

In order to ensure transparency and efficiency of the management system, the Management Board followed the principles of professional conduct within the limits of reasonable economic risk, and took into consideration a wide range of available information, analyses and opinions.

The amount, form and structure of remuneration for the Members of the Management Board have been determined by the Supervisory Board in line with the applicable remuneration policy and on the basis of clear-cut procedures, and have



corresponded to the scope of their responsibilities and competences and have taken into account the economic performance of the Company. This remuneration has also corresponded to remuneration of Management Boards in comparable companies in the real estate development market.

#### **4.5. The Supervisory Board**

##### **4.5.1 Principles for the appointment or dismissal of the Supervisory Board**

The Supervisory Board shall comprise of 5 to 9 members appointed for a three-year term of office.

The General Shareholders' Meeting shall determine the number of members of the Supervisory Board. In addition to this, the General Shareholders' Meeting shall appoint and dismiss Members of the Supervisory Board, subject to the personal right of a Shareholder holding at least 50.1% of shares to appoint and dismiss half of the Members of the Supervisory Board, including 1 Vice Chairman thereof. For an odd number of Supervisory Board members, a shareholder holding at least 50.1% shares in the Company is authorised to appoint, accordingly: three (for a 5-person Supervisory Board), four (for a seven-person Supervisory Board) and five (for a nine-person Supervisory Board) Supervisory Board members. The above right is exercised by way of serving written statement to the Company on the appointment or dismissal of a given Supervisory Board member.

At least two Members (and their relatives, in particular spouses, descendants or ascendants) of the Supervisory Board appointed by the General Shareholders' Meeting should meet the criteria of the so-called Independent Members, defined in paragraph 7.7 of the Articles of Association of the Company.

##### **4.5.2 Composition of the Supervisory Board**

In the period from 1 January 2011 until 30 March 2012 the Supervisory Board was composed of the following members:

- Grzegorz Kielpsz, Chairman of the Supervisory Board
- Marek Moczulski, Vice Chairman of the Supervisory Board (Independent Member)
- Richard Lewis, Vice Chairman of the Supervisory Board
- Krzysztof Grzyliński, Member of the Supervisory Board (Independent Member)
- Michael Cronk, Member of the Supervisory Board
- Markham Dumas, Member of the Supervisory Board
- Włodzimierz Bogucki, Member of the Supervisory Board (Independent Member)

Mr. Richard Lewis resigned from the position of Member and Chairman of the Supervisory Board on 28 November 2011, with effect on 31 March 2012. The reason for the resignation of Mr. Richard Lewis was his retirement effective on 31 March 2012.

Consequently, Dom Development B.V. with its registered office in Rotterdam appointed Mr. Mark Spiteri as a Member of the Supervisory Board and Mr. Markham Dumas as the Vice Chairman of the Supervisory Board, with effect on 1 April 2012, pursuant to paragraph 7.4 of the Articles of Association of the Company.

In the period from 1 April 2011 until 31 December 2012 the Supervisory Board was composed of the following members:

- Grzegorz Kielpsz, Chairman of the Supervisory Board
- Markham Dumas, Vice Chairman of the Supervisory Board
- Marek Moczulski, Vice Chairman of the Supervisory Board (Independent Member)
- Mark Spiteri, Member of the Supervisory Board
- Michael Cronk, Member of the Supervisory Board
- Włodzimierz Bogucki, Member of the Supervisory Board (Independent Member)
- Krzysztof Grzyliński, Member of the Supervisory Board (Independent Member)



#### 4.5.3 Principles governing the functioning of the Supervisory Board

The Supervisory Board acts pursuant to the provisions of the Code of Commercial Companies, the Articles of Association and unclassified and publicly available Supervisory Board Bylaws, approved by the Supervisory Board's resolution, that set forth its organisation and manner of operation, and in accordance with the Code of Best Practice for WSE Listed Companies.

The Supervisory Board is a permanent supervisory body of the Company for all areas of its operation.

The Supervisory Board adopts resolutions or issues opinions in the matters reserved for the Supervisory Board under the Company's Articles of Association and in the manner as provided for in the Articles of Association or relevant legal regulations.

The Supervisory Board held its meetings regularly. The meetings were attended by the Members of the Management Board. In 2012 the Supervisory Board held 10 sessions including 7 teleconferences. The Management Board provided the Supervisory Board with exhaustive information on all important matters concerning the operations of the Company.

The Supervisory Board complied with the requirement of having among its members at least two independent members in line with the criteria of independence set forth in the Company's Articles of Association.

Resolutions of the Supervisory Board concerning: (i) the consent for the Company or a related entity of the Company to make any considerations on any account whatsoever for the benefit of the Members of the Management Board, (ii) the consent for the Company or a related entity of the Company to conclude a material agreement with a related entity of the Company, a Member of the Supervisory Board or the Management Board, or entities related to such members, (iii) the choice of a statutory auditor for the audit of the Company's financial statements, were all adopted upon the consent of the majority of the independent Members of the Supervisory Board.

The remuneration of the Members of the Supervisory Board was determined in a transparent manner and did not constitute a considerable share in the Company's costs affecting its financial result. The amount of the remuneration was approved by a resolution of the General Shareholders' Meeting and was disclosed in the annual report.

The Supervisory Board presented to the Ordinary General Shareholders' Meeting of the Company which was held on 23 May 2012 an assessment of the Company's situation, to include an assessment of the internal control system and the system of management of substantial risk for the Company, prepared in line with the Code of Best Practice for WSE Listed Companies.

#### 4.5.4 The Supervisory Board Committees

Two committees, the Audit Committee and the Remuneration Committee, were established within the structure of the Supervisory Board.

##### Audit Committee

In the period from 1 January until 31 March 2012 the Audit Committee was composed of the following members:

- Włodzimierz Bogucki, Chairman of the Audit Committee
- Richard Lewis, Member of the Audit Committee
- Marek Moczulski, Member of the Audit Committee

As the mandate of Mr. Richard Lewis, the member of the Supervisory Board of Dom Development S.A. have expired on 31 March 2012, the Supervisory Board appointed Mr. Mark Spiteri as a Member of the Audit Committee (Resolution by the Supervisory Board No. 09/04/2012) on 10 April 2012.

The Audit Committee is a permanent committee at the Supervisory Board. It is composed of at least three members appointed by the Supervisory Board from amongst its members, with at least two members of the Audit Committee being Independent Members of the Supervisory Board within the meaning of paragraph 7.7 of the Articles of Association, and at least one of whom shall have qualifications in accountancy or financial audit.

The duties and competences of the Audit Committee have been set forth in unclassified and publicly available Audit Committee Bylaws approved by the Supervisory Board.

The duties of the Audit Committee include, in particular (i) supervision of the Company's Management Board as regards the Management Board's compliance to relevant laws and other regulations, in particular the Accounting Act dated 29 September 1994, supervision of the preparation of financial information by the Company, in particular in respect of the choice of the accounting policy adopted by the Company, supervision of the application and assessment of the consequences of new legal regulations, supervision of the information on the manner in which estimated items, forecasts etc., are presented in annual reports and supervision of the compliance to recommendations and findings of a statutory auditor appointed by the Supervisory Board, (ii) issuing recommendations to the Company's Supervisory Board concerning the appointment and dismissal of the statutory auditor, (iii) control of independence and objectivity of the statutory auditor, in particular in respect of a possible replacement of the statutory auditor, and their remuneration, (iv) verification of the statutory auditor's work.

In executing its duties, the Audit Committee works with the Supervisory Board, the Management Board, middle management and the external and internal audit unit.

The Vice President of the Management Board responsible for finance, Deputy Financial Director, Financial Controller and representatives of the external and internal audit teams may attend the Audit Committee meetings, if invited. In 2012, the Audit Committee held 8 meetings, including 4 teleconferences.

### **Remuneration Committee**

In the period from 1 January until 31 March 2012 the Remuneration Committee was composed of the following members:

- Marek Moczulski, Chairman of the Remuneration Committee
- Richard Lewis, Member of the Remuneration Committee
- Krzysztof Grzyliński, Member of the Remuneration Committee.

As the mandate of Mr. Richard Lewis, the member of the Supervisory Board of Dom Development S.A. have expired on 31 March 2012, the Supervisory Board appointed Mr. Mark Spiteri as a Member of the Remuneration Committee (Resolution by the Supervisory Board No. 10/04/2012) on 10 April 2012.

The Remuneration Committee is a permanent committee at the Supervisory Board. It is composed of at least three members appointed by the Supervisory Board from amongst its members, with at least two members of the Remuneration Committee being Independent Members of the Supervisory Board within the meaning of paragraph 7.7 of the Articles of Association. The Supervisory Board appoints one member of the Remuneration Committee to the position of the Chairman of the Remuneration Committee. This member serves concurrently as an Independent Member of the Supervisory Board within the meaning of paragraph 7.7 of the Articles of Association. The Supervisory Board may dismiss any Member of the Remuneration Committee at any time.

The duties and competences of the Remuneration Committee have been set forth in unclassified and publicly available Remuneration Committee Bylaws approved by the Supervisory Board

The duties of the Remuneration Committee include, in particular (i) a periodic assessment of the remuneration principles for the members of the Management Board and providing the Supervisory Board with relevant recommendations in this respect, (ii) preparation of suggestions as regards remuneration and additional benefits for individual members of the Management Board, including in particular benefits under a management share option programme (options convertible into shares in the Company's share capital) to be reviewed by the Supervisory Board, (iii) submission of projects concerning the Company's remuneration policy.

The President of the Management Board and the Vice President of the Management Board for finance may attend the Remuneration Committee meetings, if invited. In 2012, the Remuneration Committee held 5 meetings, including 1 teleconference.

#### 4.6. Remuneration for and employment contracts with the members of the Management Board and the Supervisory Board

##### 4.6.1 The amount of remuneration, bonuses and benefits received by individual members of the Management Board and the Supervisory Board

In 2012, the amount of remuneration (including bonuses) paid, accrued or potentially accrued to individual members of the management or supervisory bodies was as follows:

Remuneration and bonuses	In the Company in thousand PLN	In other companies operating within the Group in thousand PLN
<b>The Management Board</b>		
Jarosław Szanajca	1 762	-
Zalewski Janusz	1 264	-
Jerzy Ślusarski	1 143	-
Janusz Stolarczyk	923	-
Terry Roydon	72	-
<b>The Supervisory Board</b>		
Grzegorz Kielpsz	600	-
Richard Lewis	18	-
Mark Spiteri	54	-
Markham Dumas	72	-
Michael Cronk	72	-
Włodzimierz Bogucki	72	-
Marek Moczulski	72	-
Krzysztof Grzyliński	72	-

In 2012, there was no distributions from profit to members of the management or supervisory bodies of the Company, except for the dividend.

##### 4.6.2 Agreements with the members of the Management Board in the event of their resignation or dismissal

**The agreements concluded between the Company and the members of the management which provide for the compensation in the event of their resignation or dismissal from office**

Members of the Company's Management Board: Jarosław Szanajca, Janusz Zalewski, Jerzy Ślusarski and Janusz Stolarczyk are employed by the Company on the basis of employment contracts. Pursuant to the provisions of these employment contracts, an individual Member of the Management Board is entitled to receive remuneration throughout the notice period in the case that their employment is terminated. This has been described in note 7.46 in the Group's consolidated financial statements for 2012.

#### 4.7. Shares held by the members of the Management Board and the Supervisory Board

**Total number and nominal value of all shares in the Company as well as the shares and stocks in the companies operating within the Group held by the members of the management and supervisory bodies of the Company**

The ownership structure of shares and share options in the Company held by the Members of the Management Board and the Supervisory Board as at 31 December 2012 was as follows:

	Shares		Share options	Total
	number	nominal value in thousand PLN	number	number of options and shares
<b>The Management Board</b>				
Jarosław Szanajca	1 534 050	1 534	-	1 534 050
Zalewski Janusz	300 000	300	103 534	403 534
Jerzy Ślusarski	5 363	5	78 634	83 997
Janusz Stolarczyk	105 200	105	49 447	154 647
Terry Roydon	58 500	59	61 767	120 267
<b>The Supervisory Board</b>				
Grzegorz Kielpsz	1 280 750	1 281	-	1 280 750
Markham Dumas	5 000	5	-	5 000
Mark Spiteri	711	1	12 330	13 041

The Members of the Management Board and the Supervisory Board of the Company did not hold any shares in other companies operating within the Group.

#### 4.8. Management Option Programmes

##### 4.8.1 Existing employee share schemes

**Information on the agreements that are known to the Company and that were concluded in the last financial year which may result in future changes in the proportions of shares held by the current shareholders**

Management Option Programmes are in place in the Company. Options for the Company's shares have been granted under these Programmes. The exercise of these options will result in future changes in the proportions of shares held by the current shareholders.

The Management Option Programmes have been described in the consolidated financial statements of the Group for 2012 in note 7.45.

In the twelve-month period ended 31 December 2012 the Company did not grant any new share options.

##### Changes to the Management Option Programmes

On 29 March 2012 the Supervisory Board of the Company adopted a resolution concerning Management Share Option Programme II for 726 000 Shares in Dom Development S.A. (hereinafter "Program II") and Management Share Option Programme III for Senior Executives for 360 000 Shares in Dom Development S.A. (hereinafter "Program III"), pursuant to which the Supervisory Board decided not to grant any options to any person under the programmes concerned.

The Supervisory Board granted 726 000 options under Programme II in the previous years. In the case that any of these options expires, the number of shares attributable to the expired options will not be taken into account by the Supervisory Board and the options will not be granted again.

In the previous years, 120 000 options were granted under Programme III. None of the remaining 240 000 options will be granted by the Supervisory Board. Just like in Programme II, in the case that any of these 120 000 options expires, the number of shares attributable to the expired options will not be taken into account by the Supervisory Board and the options will not be granted again.

Share options granted and exercisable as at respective balance sheet dates, and changes in 2012 and 2011 has been presented in the table below.

<b>SHARE OPTIONS</b>		<b>01.01- 31.12.2012 number/thousan d PLN</b>	<b>01.01- 31.12.2011 number/thousa nd PLN</b>
<b>Unexercised options at the beginning of the period</b>	<b>Number of options</b>	<b>846 000</b>	<b>726 000</b>
	<b>Total exercise price</b>	<b>46 927</b>	<b>46 930</b>
Options granted in the period	Number of options	-	126 000
	Total option exercise value	-	385
Options expired in the period	Number of options	42 277	6 000
	Total option exercise value	2 101	388
Options exercised in the period	Number of options	155 050	-
	Total option exercise value	2 353	-
	Weighted average exercise price per share	-	-
<b>Unexercised options at the end of the period</b>	<b>Number of options</b>	<b>648 673</b>	<b>846 000</b>
	<b>Total exercise price</b>	<b>42 473</b>	<b>46 927</b>
Exercisable options at the beginning of the period	Number of options	490 975	310 800
	Total exercise price	37 968	35 580
Exercisable options at the end of the period	Number of options	534 440	490 975
	<b>Total exercise price</b>	<b>42 100</b>	<b>37 968</b>

#### 4.8.2 Employee share scheme control system

The Management Option Programmes, which are in place in the Company, have been adopted by the Supervisory Board based on the authorisation contained in a resolution issued by the General Shareholders' Meeting.

On 10 August 2006 and 21 May 2009, the Management Board was authorised by the General Shareholders' Meeting to increase the share capital of the Company within the authorised capital and to issue warrants allowing the participants of Management Option Programme II and Programme III to subscribe for shares. The Management Board is then entitled to adopt a resolution concerning the increase of the share capital upon the consent of the Supervisory Board.

#### The Management Option Programme II for 726 000 shares in Dom Development S.A.

Pursuant to Programme II, the Supervisory Board of the Company may adopt a resolution naming the people entitled to participate in the Programme. It is also entitled to set the conditions, which must be met by the participants before they subscribe for shares.

#### The Management Option Programme III for 360 000 shares in Dom Development S.A.

Pursuant to Programme III, the Supervisory Board of the Company may adopt a resolution on granting the options, provided that the General Shareholders' Meeting of the Company decides that the persons named in the resolution(s)

adopted by the Supervisory Board are entitled to take up the shares on the terms and conditions stipulated in Programme III and in resolution(s) regarding the programme adopted by the Supervisory Board. The Supervisory Board is also entitled to set the conditions which must be met by the participants before they subscribe for shares.

As mentioned in section 4.8.1, on 29 March 2012 the Supervisory Board of the Company adopted a resolution that no options are to be granted to any person under the programmes concerned.

#### **4.9. Changes in the basic management principles of the Company**

In 2012 there were no major changes in the basic principles of management. The development of the organisation calls for improvement of the management procedures in both, Dom Development S.A. and other companies operating within the Group.

#### **4.10. Internal control and risk management systems**

##### **Description of the basic features of the internal control and risk management systems in place in the Company for the preparing of standalone and consolidated financial statements**

The Company's Management Board is responsible for the internal control system in the Company and its effectiveness in the preparing of financial statements and periodic reports prepared and published in accordance with the Regulation by the Minister of Finance dated 19 February 2009 on the current and periodic submissions by securities issuers.

The effectiveness of the Company's internal control and risk management systems in financial reporting was ensured through the following means:

##### **The structure and scope of financial reporting applied by the Company**

The medium term plan (covering a period of at least 3 years) is updated on a yearly basis in the Company. In addition to this, a detailed operating and financial budget which implements the assumptions of the medium-term plan are prepared every year. The process is managed by the Management Board and the middle and executive management of the Company is also involved. The budget, which is prepared annually for the following year, is approved by the Company's Management Board.

During any specific year, the Company's Management Board reviews the current financial results versus the adopted budget. The management reporting methodology applied in the Company is used for this purpose. This reporting is based on the accounting policy adopted by the Company (in line with the International Financial Reporting Standards) and takes into account the form and level of detail of financial data presented in the financial statements of the Company and the Group.

Consistent accounting policies are applied by the company for presenting its financial details in the financial statements, periodic financial reports and management reports.

##### **Clear division of duties and competences in the process of preparing financial information**

The financial division headed by the Vice President of the Management Board as the Company's CFO is responsible for the preparing of financial statements, periodic financial reports and current management reports of the Company.

The Company's finance statements are prepared by a team of highly qualified employees from the finance and accounting division, with the assistance of the planning and analysis unit. The entire process is supervised by middle management from the financial division. The financial statements, when ready, are verified by the financial controller (responsible for the accounting department and planning and analysis unit) and then by the Vice President of the Management Board as the Company's CFO, prior to being submitted to the independent statutory auditor.

**Regular assessment of the Company's operations based on its financial reports**

The figures used in the financial statements and periodic reports and in the monthly management and operating reports come from the Company's financial and accounting system. Detailed financial and operating management reports are prepared, having all predefined book-closing procedures completed at the end of each month. These reports, in addition to historical financial data, are supplemented with quantitative operating data and forecasts by the planning and analyses unit. These reports are scrutinized by middle and executive management of individual organizational units of the Company and by the Management Board. As regards closed reporting periods, the Company's financial results are scrutinized versus the budgets and forecasts made in the month preceding the reporting period subject to scrutiny. Taking into consideration the specific nature of the sector, not only individual cost groups are scrutinized but also individual investment projects.

Any identified deviations and errors are clarified and corrected in the Company's books on an ongoing basis, in accordance with the adopted accounting policy.

**Verification of the Company's financial statements by an independent statutory auditor**

Pursuant to the applicable legal regulations, the Company's financial statements are reviewed or audited, respectively, by an independent statutory auditor. This is always a prime and highly qualified statutory auditor.

A so-called Audit Life Cycle has been developed in the Company. This is a cyclical schedule of communication between the Management Board, the statutory auditor and the Audit Committee of the Supervisory Board. The purpose of this schedule is to ensure appropriate interaction between the Audit Committee and the statutory auditor as well as appropriate presentation of the results of the above mentioned review and audit.

**Formalised process for significant assessments that considerably affect the Company's financial statements**

The fundamental activity adopted by the Company so as to reduce the exposure to market risks is proper assessment of potential and control of current development projects based on investment models and decision-making procedures developed in the Company. The adherence to such procedures is closely monitored by the Management Board of the Company.

As implied by the accounting policy adopted by the Company in this respect, detailed budgets for individual development projects that are prepared in accordance with the best practice and experience of the Company constitute the grounds for the calculation of revenue from the sale of products and costs of products sold. The budgets for all construction projects are updated at least once every three months, during the execution of the projects. The update is based on the formalised principles in place in the Company and is scrutinized by the Management Board, in particular by the Vice President of the Management Board as the Company's CFO.

**Risk management process and internal audit**

There has been a formalised risk management procedure in operation within the Company since 2000. Under this procedure the risk is managed through the identification and assessment of the risk areas for all aspects of the activities, in which the Company and the Group are involved, together with defining activities required to reduce or eliminate such risks (including through the procedures and internal audit system) The risk management procedure is subject to periodic revision and is updated by the Management Board jointly with the key management staff and third party advisers.

The internal audit unit that is in place in the Company also participates in the process of risk identification and assessment of the control measures. The schedule of internal audits is created based on the risk assessment made in cooperation with the Management Board under the supervision of the Audit Committee. In addition to scheduled audits, there are verification audits to check implementation of recommendations formulated in the previous audits and non-scheduled audits. The findings of internal audits are reported to the Audit Committee and to experts appointed by this Committee.

#### **4.11. Auditor**

##### **Information on the agreement for the audit and review of the financial statements and the consolidated financial statements concluded with the authorized auditor**

On 31 March 2010, Dom Development S.A. entered into an agreement for the audit of the standalone and consolidated financial statements for 2010, 2011 and 2012, and the review of condensed financial statements and condensed consolidated financial statements for the six-month period ended 30 June 2010, 2011 and 2012, with Ernst & Young Audit Sp. z o.o. (an authorized auditor).

The agreement covers the audit of the financial statements submitted by the Company and the Group for the year ended 31 December 2012 and the review of interim financial statements submitted by the Company and the Group for the six-month period ended 30 June 2012. The total remuneration for the audit of the annual financial statements is PLN 175 thousand and the total remuneration for the review of the interim financial statements is PLN 95 thousand.

Moreover, Ernst & Young Audit Sp. z o.o. provided additional services to the Company in 2012:

- other attestation services for the amount of PLN 40 thousand
- other services for the amount of PLN 4 thousand.

The financial statements of the Company and the Group for the first half of the year 2011 and for the entire year 2011 were, respectively, reviewed and audited by Ernst & Young Audit Sp. z o.o. The total remuneration for the audit of the annual financial statements was PLN 180 thousand and the total remuneration for the review of the interim financial statements was PLN 100 thousand.

Moreover, Ernst & Young Audit Sp. z o.o. provided additional services to the Company for the total amount of PLN 4 thousand, in 2011.