

## **INDEPENDENT AUDITOR'S REPORT ON THE AUDIT OF THE ANNUAL CONSOLIDATED FINANCIAL STATEMENTS**

**To the Shareholders Meeting and Supervisory Board of LC Corp S.A.**

### **The audit report on the annual consolidated financial statements**

We have audited the accompanying annual consolidated financial statements for the year ended 31 December 2017 of LC Corp S.A. Capital Group ('the Capital Group'), for which the dominant company is LC Corp S.A. ('the Company') located in Wrocław at Powstańców Śląskich 2-4, containing the consolidated statement of financial position as at 31 December 2017, the consolidated income statement, the consolidated statement of comprehensive income, the consolidated statement of changes in equity, the consolidated statement of cash flow for the period from 1 January 2017 to 31 December 2017 and other explanatory notes ('the accompanying consolidated financial statements').

#### *Responsibilities of the Company's Management and members of the Supervisory Board for the consolidated financial statements*

The Company's Management is responsible for the preparation and fair presentation of the consolidated financial statements in accordance with International Accounting Standards, International Financial Reporting Standards and related interpretations announced in the form of European Commission decrees and other applicable laws, as well as the Company's Statute. The Company's Management is also responsible for such internal control as determined is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

In accordance with the Accounting Act of 29 September 1994 (the 'Accounting Act'), the Company's Management and the members of the Company's Supervisory Board are required to ensure that the accompanying consolidated financial statements meet the requirements of the Accounting Act.

#### *Auditor's responsibility*

Our objective was to express an opinion on whether the accompanying consolidated financial statements give a true and fair view<sup>1</sup> of the financial position and results of the operations of the Group in accordance with International Accounting Standards, International Financial Reporting Standards and related interpretations announced in the form of European Commission regulations and adopted accounting policies.

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<sup>1</sup> Translation of the following expression in Polish is 'rzetelny i jasny obraz'.

We conducted our audit of the accompanying consolidated financial statements in accordance with:

- Act of 11 May 2017 on Statutory Auditors, Audit Firms and Public Oversight ('Act on Statutory Auditors'),
- National Auditing Standards in the wording of the International Auditing Standards adopted by the resolution no. 2783/52/2015 of the National Council of Statutory Auditors of 10 February 2015 with subsequent amendments,
- Regulation (EU) No. 537/2014 of the European Parliament and of the Council of 16 April 2014 on specific requirements regarding statutory audit of public-interest entities and repealing Commission Decision 2005/909/EC ("Regulation 537/2014").

Those regulations require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance whether the consolidated financial statements are free from material misstatement.

The purpose of the audit is to obtain reasonable assurance as to whether the consolidated financial statements as a whole were prepared based on properly maintained accounting records and are free from material misstatement due to fraud or error, and to issue an independent auditor's report containing our opinion. Reasonable assurance is a high level of assurance, but it is not guarantee that an audit conducted in accordance with the above mentioned standards will always detect material misstatements. Misstatements may arise as a result of fraud or error and are considered material if it can reasonably be expected that individually or in aggregate, they could influence economic decisions of the users taken on the basis of these consolidated financial statements. The risk of not detecting a material misstatement due to fraud is higher than the risk of not recognizing a material misstatement due to an error, as fraud may involve collusion, falsification, deliberate omissions, misleading or circumventing internal control and may affect every area of law and regulation, not just this directly affecting the consolidated financial statements.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the Company's preparation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the presentation of the consolidated financial statements.

The scope of the audit does not include assurance on the future profitability of the audited Group nor effectiveness of conducting business matters of the Group now and in the future by the Company's Management Board.

In accordance with International Auditing Standard 320 section 5 the concept of materiality is applied by the auditor both in planning and performing the audit, and in evaluating the effect of identified misstatements on the audit and of uncorrected misstatements, if any, on the consolidated financial statements and in forming the opinion in the auditor's report. Hence all auditor's assertions and statements contained in the auditor's report, including those on other

information or regulatory requirements, are made with the contemplation of the qualitative and quantitative materiality levels established in accordance with auditing standards and auditor’s professional judgement.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion. The opinion is consistent with the additional report to the audit committee issued on the date of this report.

*Independence*

While conducting our audit, the key certified auditor and the audit firm remained independent of the entities comprising the Group in accordance with the regulations of Act on Statutory Auditors, Regulation 537/2014 and principles of professional ethics adopted by resolutions of the National Council of Statutory Auditors.

Based on our best knowledge and belief, we declare that we have not provided non-audit services, that are prohibited based on article 136 of the Act on Statutory Auditors and article 5, point 1 of Regulation 537/2014, to the Company.

*Appointment of the audit firm*

We were appointed to audit the consolidated financial statements based on the Company’s Supervisory Board resolution dated 7 June 2017. We have been auditing the consolidated financial statements of the Company consecutively since the beginning of the financial year ended 31 December 2009; this is for 9 years.

*Most significant assessed risks*

In the course of our audit we have identified the below described most significant assessed risks of material misstatement (key audit matters), including due to fraud and we designed appropriate audit procedures in response to those risks. Where we considered to be relevant in order to understand the nature of the identified risk and audit procedures performed we have also included key observations arising with respect to those risks.

These matters were addressed in the context of our audit of the accompanying consolidated financial statements as a whole, and in forming our opinion thereon. Therefore we do not provide a separate opinion on these matters.

<i>description of the nature of the risk of material misstatement (key audit matters)</i>	<i>audit procedures in response to the identified risk</i>
Valuation of investment property  Why the matter was determined to be a key audit matter	How the key audit matter was addressed in the audit

<p>As disclosed in note 19 the Group's consolidated financial statements for the year ended 31 December 2017 the value of investment properties amounts to 1,805 million zloty which make up 55% of the total assets. Investment properties comprise mainly two categories: completed investment property measured at fair value and investment property under construction, measured either at cost or at fair value, if certain criteria specified in accounting policies are met.</p> <p>The fair value of the investment property depends to a large extent on Management judgements and estimates such as future rents, occupation, rent-free periods and yields. Inputs used to measure fair value of Group's investment property are categorized into second and third levels of the fair value hierarchy.</p> <p>The valuations are carried out by third party appraisers. The appraisers are engaged by the Management, and perform their work in accordance with applicable valuation and professional standards.</p> <p>In the consolidated financial statements disclosures regarding Investment properties were disclosed in the note 19 Investment Properties.</p>	<p>In the course of the audit we evaluated the valuation of investment properties.</p> <p>We have discussed with Management current market situation and specific properties situation and obtained understanding of the Management's view in that respect.</p> <p>We evaluated the expertise, competency, objectivity and independence of the external appraisers, evaluated data used in respective properties by external appraisers, including estimations used by them. As part of these procedures we compared used yields to market levels.</p> <p>We read the valuation reports for properties and evaluated that the valuation approach was suitable for use in determining the carrying value for the purpose of the financial statements and appropriate in the circumstances. In addition, we carried out substantive audit procedures, on a sample basis, to evaluate the accuracy of the property information provided to the appraisers by the Management.</p> <p>We have performed analytical review and evaluated the reasonableness of fair value movements in correspondence with expectations we built in relation to current market benchmarks and knowledge gained during the audit process.</p> <p>We engaged internal real estate and valuation specialists to assist us in evaluation of the appraisals.</p> <p>We also evaluated the adequacy of the disclosures in the consolidated financial statements.</p>
<p>Inventory valuation</p> <p><i>Why the matter was determined to be a key audit matter</i></p> <p>As disclosed in note 18 and 19 of the Group's consolidated financial statements for the year ended 31 December 2017 the inventory and land classified as long term assets</p>	<p><i>How the key audit matter was addressed in the audit</i></p>

<p>include lands, residential units under constructions and finished goods which make up 32% of the total assets. Upon initial recognition inventory is measured at the lower of cost and net realizable value.</p> <p>The cost of inventory includes, amongst others, land or leasehold rights for land, construction costs, planning and design costs, borrowing costs and professional fees directly attributable to the project and construction overheads and other directly related costs.</p> <p>The Group as at the balance sheet date assessed internally the net realizable value of the inventory and decreased the value when the net realizable value was lower than the cost. The net realizable value calculation is highly dependent on estimates like, amongst others, the estimated sales prices per m<sup>2</sup>, the estimated construction costs and the expected timing of sales of the units. Management assessed possible write-downs on inventory for each project separately, according to the projection of revenues net from cost of sales. As the value of inventory is significant to the financial statements and significant estimates are involved in the assessment of net realizable value, we have concluded that it is key audit matter.</p> <p>In the consolidated financial statements disclosures regarding this matter have been disclosed in the notes 18 and 20.</p>	<p>In the course of the audit we evaluated the inventory valuation with relation to net realizable value.</p> <p>We evaluated the work of management, including the competence, capabilities and, where applicable, objectivity of management's specialists or external specialists with respect to the net realizable value assessment.</p> <p>Additionally, we performed substantive audit procedures by, amongst others, extensively discussions with management of the Company with respect to the net realizable value method applied, the key assumptions used, including comparing these assumptions to similar projects in the market and the actual realized results of the net realizable value calculations on individual projects.</p> <p>With relation to investments for which the commencement of the construction is delayed in time we assessed assumption and estimations made in order to assess the net realizable value, including assessment of parameters used by the Company in its models by comparing key assumptions, including discount rates used in the tests to market levels, performed analysis of projected revenue and cost streams and periods when they appear and assumed margin</p> <p>We performed sensitivity analysis on volatility in key assumptions.</p> <p>We also evaluated the adequacy of the disclosures in the consolidated financial statements.</p>
<p>Revenue recognition</p> <p><i>Why the matter was determined to be a key audit matter</i></p>	<p><i>How the key audit matter was addressed in the audit</i></p>

<p>Revenue arising from the sales of multi-family residential real estate projects, represents the majority of the Company's total revenue. Revenue is recognized by the Company when the significant risks and rewards of ownership of the residential units have been transferred to the buyer and when the revenue can be measured reliably. The risks and rewards are considered as transferred to the buyer when the residential units have been substantially constructed, the occupancy permit for the property has been issued, the apartment has been accepted by the customer (hand-over protocol has been signed between the buyer and the Company) and the full amount resulting from the sale agreement has been paid by the buyer. The remaining risks are considered by the Company's Management as remote. Taking into consideration the significance of revenue recognition to the financial statements, consequently, the proper cutoff of revenues has been identified as a key audit matter.</p> <p>In the consolidated financial statements disclosures regarding this matter have been disclosed in the notes 12.1 Sales revenue.</p>	<p>We obtained an understanding of the sales process and revenue recognition process. Additionally, we performed substantive audit procedures by, amongst others, detailed margin analyses, extensive tests of sales transactions in order to assess the adequacy and completeness of revenue recognition including reconciliation of recognized revenue to source documentation to notarial deeds and bank statements.</p> <p>We have also assessed the adequacy of the related disclosures in the financial statements.</p>
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### *Opinion*

In our opinion, accompanying consolidated financial statements:

- give a true and fair view of the financial position of the Group as at 31 December 2017 and its financial performance for the year from 1 January 2017 to 31 December 2017 in accordance with International Accounting Standards, International Financial Reporting Standards and related interpretations announced in the form of regulations of the European Commission and other applicable laws and the adopted accounting policies,

- are in respect of the form and content in accordance with legal regulations governing the Company and the Company's Statute.

## **Report on other legal and regulatory requirements**

### *Opinion on the Directors' Report*

Our opinion on the consolidated financial statements does not include the Directors' Report.

The Company's Management is responsible for preparation of the Directors' Report in accordance with the Accounting Act and other applicable laws. In addition, the Company's Management and members of the Company's Supervisory Board are required to ensure that the Directors' Report meets the requirements of the Accounting Act.

Our responsibility in accordance with the Act on Statutory Auditors was to issue an opinion on whether the Director's Report was prepared in accordance with relevant laws and that it is consistent with the information contained in the accompanying consolidated financial statements.

Our responsibility was also to make a statement, on whether based on our knowledge about the Company and its environment obtained during the audit of the financial statements we have identified in the Director's Report any material misstatements and to indicate the nature of each of material misstatement.

In our opinion the Directors' Report was prepared in accordance with the relevant regulations and reconciles with the information derived from the accompanying financial statements. Moreover, based on our knowledge of the Company and its environment obtained during the audit of the financial statements, we have not identified material misstatements in the Directors' Report.

### *Opinion on the corporate governance application representation*

The Company's Management and members of the Company's Supervisory Board are responsible for preparation of the representation on application of corporate governance in accordance with the applicable laws.

In connection with the conducted audit of the consolidated financial statements, our responsibility in accordance with the Act on Statutory Auditors was to issue an opinion on whether the issuer, obliged to present a representation on application of corporate governance, constituting a separate part of the Director's Report, included in the representation information required by applicable laws and whether the related information is in accordance with applicable regulations and with the information included in the accompanying consolidated financial statements.

In our opinion, in the representation on application of corporate governance, the Company has included information stipulated in paragraph 91, section 5, point 4, letter a, b, g, j, k and l of the Regulation of the Minister of Finance of 19 February 2009 on current and periodic information provided by issuers of securities and conditions of deeming information required by the regulations of a non-member country equal ('Regulation') Information stipulated in paragraph 91, section 5, point 4 letter c-f, h and i of the Regulation included in the representation on

application of corporate governance is in accordance with applicable laws and information included in the accompanying consolidated financial statements.

Warszawa, 20 March 2018

Key Certified Auditor

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*Łukasz Wojciechowski*  
certified auditor  
No. 12273

on behalf of  
Ernst & Young Audyt Polska spółka  
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