LPP SA Capital Group

CONSOLIDATED ANNUAL REPORT FOR 2016

Including:

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II. Selected financial data of LPP SA Capital Group for 2015-2016
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GDANSK, APRIL 2017

I. Letter from the President of the Management Board to the Shareholders

Dear Shareholders,

For LPP, the last year was a year of further development, with our revenues at a record-breaking level exceeding PLN 6 billion and over 1,700 stores operating in 18 countries on three continents.

Furthermore, 2016 was a year full of changes involving many aspects of the Group's operations. We are convinced that they were necessary to facilitate further development of LPP and effectively compete on the worldwide fast-fashion market. These changes have brought a lot of fresh energy and optimism to our company, therefore, we hold the view that their positive effects will be evident in 2017 and in the years to come.

In 2016, we focused on RESERVED, our flagship brand. Following the client's needs, we have implemented numerous changes relating to the improvement of a product itself (specifically in terms of trends, aesthetics and the quality of workmanship) and changes in logistics (store categorization and changes in stock replenishment) and more efficient management (reinforcement of product departments, employment of foreign designers, the opening of a new RESERVED design office in Warsaw). We have also changed the clearance sales and inventory management policies.

With due consideration of public opinion on the protection of animal rights and our clients' expectations in this regard and in recognition of challenges concerning the alleviation of environmental impact of our operations, we have concluded an official memorandum with the "Open Cages" organisation, as part of which we have joined an international initiative called Fur-Free Retailer and, starting with the AW collection for 2016/17, we will give up natural fur in all our brands.

At present, in Poland and worldwide, consumers are changing their purchase habits for technology-based reasons. Following these changes on the clothing market, we have also increased e-commerce investments, thus gaining an approx. 120% y/y increase in revenues generated through this channel (from PLN 79 million in 2015 to PLN 173 million in 2016). Consequently, at the end of 2016, we had online stores of our five brands not only in Poland but also in Germany, the Czech Republic, Slovakia, Hungary and Romania. In 2016, online sales constituted 3% of total sales of the entire LPP Capital Group, compared to 1.5% in 2015. Our goals in this area for 2017 are no less ambitious as we are working on the opening of online stores in Russia, Ukraine, in the Baltic States and Great Britain. We are focusing on the further improvement of e-commerce functionality i.e. easier store navigation, better product display, adjustment to mobile devices and improved delivery logistics. We plan that, by 2020, online sales will constitute 7-8% of the Group's sales.

However, not all our plans could be accomplished. Last year, we introduced our new Tallinder brand (falling within the premium segment), yet, due to its sales results substantially diverging from what was assumed, we have decided to close it and focus on our leading RESERVED brand.

In consequence, in 2016, our retail store space increased by 77 thousand sq.m., to reach 921 thousand sq.m., i.e. by 9%. Poland remains our largest market, and we have emphasised our strong leading position by opening in June thousandth store in our country. Although the revenues of the LPP Group have increased by approx. 17% y/y in 2016, our net profit was 50% lower y/y, reaching PLN 175 million net. That result has been affected by several factors, namely, pressure from competitors, higher price reductions for missed collections, disadvantageous foreign currency trends and the clearance sales of inventories from the last three years. Despite those drawbacks, in 2016, we continued our dividend disbursement policy. At the same time, we succeeded to reduce the level of inventories and inventories per sq.m. and generate a record-breaking level of operating cash flows. Consequently, our net debt has decreased to a very safe level of 0.3 compared to EBITDA generated.

Our goals for 2017 are aspiring as they involve the improvement of trade margins, further dynamic e-commerce development and a 12% y/y increase in retail store space. At the end of 2017, RESERVED stores should be operating in 22 countries following the opening of four new markets i.e. Serbia, Belarus, Kazakhstan and Great Britain, where, in September 2017, a RESERVED flagship store will be opened at the most prestigious street in Europe, namely the Oxford Street.

Marek Piechocki
President of the Management Board of LPP SA

II. Selected financial data for 2015 – 2016

1. Selected consolidated financial data of LPP SA Group

Selected consolidated financial data	2016 01.01.2016- 31.12.2016	2015 01.01.2015- 31.12.2015	2016 01.01.2016- 31.12.2016	2015 01.01.2015- 31.12.2015
	in thousand PLN		in thousand EUR	
Revenues	6 019 046	5 130 353	1 375 562	1 225 949
Operating profit (loss)	226 421	502 689	51 745	120 123
Pre-tax profit (loss)	194 078	414 368	44 354	99 017
Net profit (loss)	174 775	351 320	39 942	83 951
Profit (loss) per ordinary share (in PLN/EUR))	96.19	193.87	21.98	46.33
Net cash flows from operating activities	718 176	253 888	164 128	60 669
Net cash flows from investing activities	-181 354	-415 526	-41 446	-99 294
Net cash flows from financing activities	-393 849	201 162	-90 008	48 070
Total net cash flows	142 973	39 524	32 674	9 445

Selected consolidated financial data	2016 01.01.2016- 31.12.2016	2015 01.01.2015- 31.12.2015	2016 01.01.2016- 31.12.2016	2015 01.01.2015- 31.12.2015
	in thousand PLN		in thousand EUR	
Total assets	3 677 932	3 565 169	831 359	836 600
Long-term liabilities	267 254	344 083	60 410	80 742
Short-term liabilities	1 275 947	1 331 347	288 415	312 413
Equity	2 134 731	1 889 739	482 534	443 445
Share capital	3 679	3 662	832	859
Weighted average number of ordinary shares	1 816 932	1 812 145	1 816 932	1 812 145
Book value per share (in PLN/EUR)	1 174.91	1 042.82	265.58	244.71
Declared or paid dividend per share (in PLN/EUR)	33.00	32.00	7.46	7.51

Profit per shares is calculated as a quotient of net profit and a weighted average of the number of shares. The book value per share has been calculated as a quotient of the equity capital and a weighted average of the number of shares.

III. Consolidated financial statements of LPP SA Capital Group for the financial year ended 31 December 2016

Consolidated annual report of LPP SA Capital Group for 2016, in PLN '000

1. Consolidated statement of financial position of the LPP SA Group

Statement of the financial position	Notes	Balance at the end 31.12.2016	31.12.2015
ASSETS			
Non-current assets		1 838 664	1 796 996
1. Fixed assets	14.1	1 291 338	1 258 751
2. Intangible assets	14.3	43 511	37 342
3. Goodwill	14.4	209 598	209 598
4. Trademark	14.3	77 508	77 508
5. Investments in subsidiaries	14.5	136	136
6. Investments in other entities	14.6	0	1 626
7. Receivables and loans	14.7	6 180	5 914
8. Deferred tax assets	14.20	143 657	139 194
9. Pre-payments	14.17	66 736	66 927
Current assets		1 839 268	1 768 173
1. Inventory	14.8	1 164 135	1 319 735
2. Trade receivables	14.9	165 389	115 086
3. Receivables from income tax	14.9	75 274	47 017
4. Other receivables	14.9	31 034	35 210
5. Loans	14.7	91	128
6. Pre-payments	14.17	37 592	26 550
7. Cash and cash equivalents	14.10	365 753	224 447
TOTAL assets		**3 677 932**	**3 565 169**

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Statement of the financial position	Notes	Balance at the end: 31.12.2016	31.12.2015
EQUITY AND LIABILITIES			
Equity		2 134 731	1 889 739
1. Share capital	14.12	3 679	3 662
2. Treasury shares		-43 318	-43 306
3. Share premium	14.12	251 393	235 074
4. Other reserves	14.12	1 608 298	1 323 736
5. Foreign currency translation reserve		-114 928	-228 757
6. Retained earnings			
- profit (loss) from previous years		254 832	248 010
- net profit (loss) for the current period		174 775	351 320
Long-term liabilities		267 254	344 083
1. Bank loans and borrowing	14.7	195 033	284 253
2. Provisions for employee benefits	14.13	2 711	2 179
3. Deferred tax liabilities	14.20	3 890	7 085
4. Accruals	14.17	65 575	50 566
5. Other long-term liabilities		45	0
Short-term liabilities		1 275 947	1 331 347
1. Trade and other liabilities	14.16	881 064	721 394
2. Income tax liabilities	14.16	7 449	3 042
3. Bank loans and borrowing	14.7	315 111	561 074
4. Other provisions	14.13	33 607	17 774
5. Special funds	14.10	0	227
6. Accruals	14.17	38 716	27 836
TOTAL equity and liabilities		**3 677 932**	**3 565 169**

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2. Consolidated income statement of LPP SA Capital Group

Consolidated income statement	Notes	01.01.2016-31.12.2016	01.01.2015-31.12.2015
Continuing operations			
Revenue	14.18	6 019 046	5 130 353
Cost of goods sold		3 085 236	2 387 524
Gross profit (loss) on sales		**2 933 810**	**2 742 829**
Other operating income	14.18	39 424	24 231
Selling costs	14.19	2 405 007	2 012 420
General costs	14.19	203 799	179 247
Other operating costs	14.19	138 007	72 704
Operating profit (loss)		**226 421**	**502 689**
Financial income	14.18	1 307	1 981
Financial costs	14.19	33 650	90 302
Pre-tax profit (loss)		**194 078**	**414 368**
Income tax	14.20	19 303	63 048
Net profit (loss)		**174 775**	**351 320**
Net profit (loss) attributable to:			
Shareholders of the parent company		174 775	351 320
Minority interest		0	0
Other comprehensive income			
Currency translation on foreign operations		113 829	-44 381
Total comprehensive income		**288 604**	**306 939**

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3. Consolidated statement of changes in equity of LPP SA Group

Statement of changes in the equity	Share capital	Treasury shares	*Share premium*	Other reserves	Foreign currency translation reserve	Profit (loss) from previous years	Profit (loss) for the current period	Minority capital	TOTAL Equity
Balance as at 1 January 2015	**3 662**	**-43 288**	**235 074**	**1 092 205**	**-184 376**	**531 906**	**0**	**3 231**	**1 638 414**
- correction of errors from previous years									
Balance as at 1 January 2015 after adjustments	**3 662**	**-43 288**	**235 074**	**1 092 205**	**-184 376**	**531 906**	**0**	**3 231**	**1 638 414**
Treasury share purchases		-18							-18
Distribution of profit for 2014				225 908		-283 896			-57 988
Share-based payments				2 392					2 392
Contribution by minority shareholders				3 231				-3 231	0
Transactions with owners	0	-18	0	231 531	0	-283 896	0	-3 231	-55 614
Net profit for 2015							351 320		351 320
Currency translation on foreign operations					-44 381				-44 381
Balance as at 31 December 2015	**3 662**	**-43 306**	**235 074**	**1 323 736**	**-228 757**	**248 010**	**351 320**	**0**	**1 889 739**
Balance as at 1 January 2016	**3 662**	**-43 306**	**235 074**	**1 323 736**	**-228 757**	**599 330**	**0**	**0**	**1 889 739**
- correction of errors from previous years									
Balance as at 1 January 2016 after adjustments	**3 662**	**-43 306**	**235 074**	**1 323 736**	**-228 757**	**599 330**	**0**	**0**	**1 889 739**
Treasury share purchases		-12							-12
Distribution of profit for 2015				284 562		-344 498			-59 936
Purchase of shares	17		16 319						16 336
Transactions with owners	17	-12	16 319	284 562	0	-344 498	0	0	-43 612
Net profit for 2016							174 775		174 775
Currency translation on foreign operations					113 829				113 829
Balance as at 31 December 2016	**3 679**	**-43 318**	**251 393**	**1 608 298**	**-114 928**	**254 832**	**174 775**	**0**	**2 134 731**

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4. Consolidated cash flow statement of LPP SA Group

Cash flow statement	01.01.2016-31.12.2016	01.01.2015-31.12.2015
A. Cash flows from operating activities - indirect method		
I. Pre-tax profit (loss)	194 078	414 368
II. Total adjustments	524 098	-160 480
1. Amortisation and depreciation	267 381	223 555
2. Foreign exchange gains (losses)	-5 679	-15 392
3. Interest and dividends	22 253	18 338
4. Profit (loss) on investing activities	20 661	18 219
5. Income tax paid	-59 239	-127 987
6. Change in provisions	15 806	-1 331
7. Change in inventories	211 737	-381 692
8. Change in receivables	-35 769	6 530
9. Change in short-term liabilities, excluding loans and borrowing	79 976	151 812
10. Change in prepayments and accruals	-5 927	-45 370
11. Other adjustments	12 898	-7 162
III. Net cash flows from operating activities	718 176	253 888
B. Cash flows from investing activities		
I. Inflows	90 530	75 353
1. Disposal of intangible and fixed assets	90 255	74 358
2. From financial assets, including:	275	995
a) in related parties	130	182
- dividend and share in profit	130	182
b) in other entities	145	813
- sales of financial assets - foreign bonds	0	0
- interest	8	510
- repayment of loans	137	303
3. Other investing inflows		
II. Outflows	271 884	490 879
1. Purchase of intangible and fixed assets	271 831	490 627
2. For financial assets, including:	53	252
a) in related parties	0	0
- purchase of shares		
b) in other entities	53	252
- loans granted	53	252
- purchase of financial assets		
3. Other investing outflows		
III. Net cash flows from investing activities	-181 354	-415 526

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C. Cash flows from financing activities		
I. Inflows	16 336	364 819
1. Proceeds from issuance of shares	16 336	
2. Loans and borrowings	0	364 819
3. Debt securities issued		
4. Other inflows from financing activities		
II. Outflows	410 185	163 657
1. Cost of maintenance of treasury shares	12	18
2. Dividends and other payments to owners	59 936	57 989
3. Repayment of loans and borrowings	328 683	87 111
4. Payment of liabilities arising from financial leases	0	0
5. Interest	21 554	18 539
6. Other outflows from financing activities		
III. Net cash flows from financing activities	-393 849	201 162
D. Total net cash flows	**142 973**	**39 524**
E. Balance sheet change in cash, including:	**141 306**	**40 918**
- change in cash due to foreign exchange differences	-1 667	-4 934
F. Opening balance of cash	**223 053**	**183 529**
G. Closing balance of cash, including:	**366 026**	**223 053**
- of limited disposability	0	227

Notes to the consolidated financial statements of LPP SA Capital Group for 2016

INTRODUCTION

1. Overview

Name and registered office of the parent company of the LPP Capital Group:

LPP SPÓŁKA AKCYJNA
with its registered office in Gdańsk, Poland
ul. Łąkowa 39/44
postcode: 80-769

Core business:

- wholesale of clothing, classified in item 51.42 Z of the Polish Classification of Economic Activities (PKD) as "wholesale of clothing and footwear",
- retail sales of clothing, classified in item 52.42 Z as "retail sale of clothing"

Competent District Court

The Company is registered in the District Court for Gdańsk – Północ in Gdańsk, 7th Commercial Division of the National Court Register, under number KRS 0000000778.

Place of business

The Group runs its business in the following countries:

- Poland,
- Estonia,
- Czech Republic,
- Lithuania,
- Latvia,
- Hungary,
- Russia,
- Ukraine,
- Romania,
- Bulgaria,
- Slovakia,
- Cyprus,
- United Arab Emirates
- Germany
- Croatia
- Great Britain
- Serbia

Sector according to the classification of the Warsaw Stock Exchange

Shares in the parent company, LPP SA, are listed on the main market of the Warsaw Stock Exchange and classified in the sector of "trade".

2. Composition of the Management Board and the Supervisory Board of the Issuer

Members of the Management Board:

- Marek Piechocki – President of the Management Board
- Przemysław Lutkiewicz – Vice-President of the Management Board
- Jacek Kujawa - Vice-President of the Management Board
- Sławomir Łoboda- Vice-President of the Management Board

In the period from January 2016 until the date of approval of the financial statements, there were the following changes in the composition of the Management Board of LPP SA:

- Piotr Dyka - Vice-President of the Management Board – resigned on 17 March 2016
- Hubert Komorowski – Vice-President of the Management Board – resigned on 6 September 2016

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Members of the Supervisory Board:
- Jerzy Lubianiec – Chairman of the Supervisory Board
- Krzysztof Olszewski – member of the Supervisory Board
- Wojciech Olejniczak - member of the Supervisory Board
- Maciej Matusiak - member of the Supervisory Board
- Dariusz Pachla - member of the Supervisory Board

3. Characteristics of the LPP SA Capital Group

The LPP SA Capital Group (Capital Group, Group) consists of:
- LPP SA – as the parent company,
- 4 domestic subsidiaries,
- 19 foreign subsidiaries.

LPP SA has no parent company.

The list of companies forming the Capital Group is presented below.

No	Company name	Registered office	Date of taking control
1.	LPP Retail Sp. z o.o.	Gdańsk, Poland	26.09.2001
2.	DP&SL Sp. z o.o.	Gdańsk, Poland	26.09.2001
3.	IL&DL Sp. z o.o.	Gdańsk, Poland	26.09.2001
4.	AMUR Sp. z o.o.	Gdańsk, Poland	09.05.2003
5.	LPP Estonia OU	Tallinn, Estonia	29.04.2002
6.	LPP Czech Republic SRO	Prague, the Czech Republic	16.09.2002
7.	LPP Hungary KFT	Budapest, Hungary	18.10.2002
8.	LPP Latvia LTD	Riga, Latvia	30.09.2002
9.	LPP Lithuania UAB	Vilnius, Lithuania	27.01.2003
10.	LPP Ukraina AT	Peremyshliany, Ukraine	23.07.2003
11.	RE Trading OOO	Moscow, Russia	12.02.2004
12.	LPP Romania Fashion SRL	Bucharest, Romania	12.08.2007
13.	LPP Bulgaria LTD	Sofia, Bulgaria	14.08.2008
14.	LPP Slovakia SRO	Bańska Bystrzyca, Slovakia	30.10.2008
15.	LPP Fashion Bulgaria LTD	Sofia, Bulgaria	26.08.2011
16.	Gothals LTD	Nicosia, Cyprus	22.07.2011
17.	LPP Croatia DOO	Zagreb, Croatia	22.01.2014
18.	Reserved GmbH	Hamburg, Germany	03.03.2014
19.	IPMS Management Services FZE	Ras Al Khaimah, UAE	15.07.2015
20.	LPP Reserved UK LTD	Altrincham, UK	15.10.2015
21.	LLC Re Development	Moscow, Russia	22.04.2016
22.	LLC Re Street	Moscow, Russia	02.09.2016
23.	LPP Reserved doo Beograd	Belgrade, Serbia	26.12.2016

In December 2016, the company P&L Marketing & Advertising Agency S.A.L was incorporated in Lebanon. As at 31 December 2016, the said company was not a subsidiary and it was not a member of the LPP SA Capital Group.
At present, a procedure is being conducted for registering an increase of the said company's share capital, with a majority of the shares to be subscribed to following the said increase by Gothals LTD, a subsidiary of LPP SA. Therefore, P&L Marketing & Advertising Agency S.A.L in Lebanon will become a member of the LPP SA Capital Group. The said company will be engaged in supervising franchise stores in the Middle East and in the marketing activity in that region.

LPP SA is a direct parent company of its subsidiaries, holding almost a 100% stake in their capital and in the total number of votes.

The consolidated financial statements of the Group for the period from 1 January to 31 December 2016 comprise separate results of LPP SA and the results of the above-mentioned foreign subsidiaries, except for LPP Reserved doo Beograd due to the fact that it commenced no activity, as well as the results of the following domestic subsidiaries:

- LPP Retail Sp. z o.o.
- DP&SL Sp. z o.o.
- IL&DL Sp. z o.o.
- AMUR Sp. z o.o.

Polish subsidiaries of LPP SA were not consolidated as their financial data is immaterial. This is consistent with the Accounting Policy adopted by the Group.
Under the Policy, a subsidiary or associate is not consolidated if the amounts reported in the financial statements of that entity are insignificant compared to the financial statements of the parent company. In particular, the balance sheet total, net revenues from sales of goods and services and from financial operations of the entity which, for the financial period, are lower than 10% of balance sheet total and revenues of the parent company are regarded as insignificant. Furthermore, the total amount of revenues and balance sheet totals of non-consolidated entities may not exceed that level, yet determined in respect of corresponding amounts of the consolidated financial statements, based on the assumption that their scope includes all subsidiaries, without any exclusions.
The share in the consolidated results of all non-consolidated Polish subsidiaries is as follows:

- in the Capital Group's balance sheet total – 0.02%
- in the Group's sales revenue and finance revenue – 0.16%

The fact that the financial statements of these companies are not consolidated has no negative impact on the true and fair view of the Capital Group's property and financial standing as well as its financial result.

LPP SA is a company involved in the design and distribution of clothing in Poland and the countries of Central, Eastern and Western Europe, in the Balkans as well as in the countries of the Middle East. The Group companies being consolidated are involved in the distribution of goods under the RESERVED, Cropp, House, MOHITO and SiNSAY brands outside Poland. Further development of the TALLINDER brand was suspended by way of decision made by the Management Board of LPP SA.
Clothing is basically the only product sold by the Group companies. Footwear, bags and clothing accessories are sold as products supplementing the basic offer of the Capital Group companies.
Clothing designs are made in the design office located in the registered office of LPP SA in Gdańsk and in design offices in Cracow and Warsaw, and then transferred to the purchasing department which orders the production of specific models, cooperating in this respect with manufacturing plants in Poland and abroad. Production in China is distributed through the Company's trading office in Shanghai, while the Company's trading office in Dhaka is responsible for coordinating and supervising production in Bangladesh.
A major task of the office in Bangladesh is the regular auditing of manufacturing plants in terms of adequate working conditions and respect for human rights.

The Capital Group also generates insignificant revenues from sale of services, mainly know-how services related to the management of brand stores by Polish contractors and the lease of transport vehicles.
The additional business activity of the LPP Capital Group involves the management of the rights to RESERVED, Cropp, House, MOHITO and SiNSAY trademarks, including their protection, activities aimed at increasing their value, granting licenses for use, etc. Gothals Limited in Cyprus and IPMS in UAE were established for that purpose.
Four domestic subsidiaries are engaged in the lease of real properties where the stores of Cropp, RESERVED, House and MOHITO are operated.

4. Basis for the preparation of the financial statements and information on changes in the applied accounting policies

Pursuant to the Accounting Act of 29 September 1994 (consolidated text: Journal of Laws of 2016, item 1047), as of 1 January 2005, the LPP Capital Group presents its consolidated financial statements based on International Financial Reporting Standards (IFRS) and related interpretations, published as European Commission Regulations. In matters not covered by IFRS, the provisions of the Accounting Act apply respectively. Financial statements covering periods starting before 1 January 2005 were prepared based on the Accounting Act and its implementing provisions.

The report contains the Group's consolidated financial statements and separate financial statements of LPP SA. The Report was drawn up in accordance with IFRS.
This consolidated financial statements were drawn up in PLN '000.
Two departments are responsible for the preparation of financial statements: accounting and finance, headed by the Chief Accountant and the Chief Financial Officer. Before submitting financial statements to an independent statutory auditor, the Chief Financial Officer, responsible for the financial reporting process on behalf of the Management Board, verifies them in terms of completeness and correct recognition of all economic events.

In the current reporting period, there was a change in respect of presenting cash for employee benefits.
From January 2016, cash for employee benefits was excluded from data presented in the Consolidated Financial Statements as funds not owned by the LPP SA Capital Group.
As at 31 December 2015, cash for employee benefits totalled PLN 227 thousand.
If new rules had been applied, the Cash item on the asset side and the Employee Benefits item on the liability side in the Consolidated Financial Statements drawn up as at 31 December 2015 would have been adjusted by the amount of PLN 227 thousand.
Comparative data has not been changed due to its minor impact on the Consolidated Financial Statements of the LPP SA Capital Group.

In 2016, there was also a change in the assessment of revaluation write-downs for goods due to a change in the goods management policy.
The Group has two regular sales seasons: (1) March – June for the SS collection, and (2) September – December for the AW collection. The regular sales period is followed by the clearance sales period.
Before changing the goods management policy, after the end of the regular sales, the Capital Group conducted in stores, at the same time, clearance sales of the goods from both the current and previous collection which had been once again brought to stores from a warehouse for the clearance sales period.
The date of commencing clearance sales stemmed from the Issuer's decision made based on the market situation and the volume of stock held and could be different for each of the brands. Most often, the clearance sales period lasted 2 months and its end date resulted from an earlier adopted date for introducing a new collection to stores.
The level of prices of goods being sold off was determined based on the minimum level of the sales margin in a given month.
Unsold goods from the collection being sold off were returned once again to a warehouse where, subsequently, they were divided into two types of goods i.e. goods for outlet stores and goods for another clearance sales. The quantity of warehoused unsold goods depended on the outcome of the clearance sales in stores.

According to the new goods management policy introduced in the LPP SA Group from the second half of 2016, the date of commencing clearance sales complies with a clearance sales time-schedule and is the same for all brands. The end of clearance sales is strictly related to, and dependent on, the achieved targeted level of selling off the old collection, which is monitored daily. The prices of goods being sold off are changed as needed until an expected clearance sales target is reached. This means that the Capital Group does not set a targeted margin level in the clearance sales period. New collections are introduced to stores as needed and regardless of the process in the clearance sales of the preceding collection. Goods unsold during clearance sales are removed to the warehouse and, subsequently, transferred to outlet stores or to an external recipient. The major purpose of clearance sales will be to regain cash invested in the stock, at a lowest logistic cost i.e. without unnecessary packing, transporting and storing of goods from old collections.
Due to a low commercial value of goods unsold during clearance sales, after the said period, these goods will not be reintroduced to stores to avoid any adverse impact on the brands' image.
The Group will make revaluation write-downs for goods being sold off and older goods depending on their designation:
- goods designated for outlet stores will be sold at a positive margin, which means that there will no write-down,
- for goods not designated for outlet stores, there will be a write-down of 60% of their value. The value of the write-down stems from the pricelist of an external recipient.
Differences in write-downs made for goods from old collections before and after introduction of the new goods management policy are as follows:

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Write-down at the end of the period Stock – season	Previous methodology Write-down	New methodology (from December 2016) Write-down*
AW Current (AW 0)	0%	60%**
SS Current (SS 0)	0%	60%
AW -1	0%	60%
SS -1	10%	60%
AW-2	30%	60%
SS -2	30%	60%
AW -3	100%	not applicable ***
SS -3	100%	not applicable ***
Older	100%	not applicable ***

*) a write-down for goods which will not be introduced to outlet stores; no write-down for goods for outlet stores
**) a write-down applied to the amount of the goods' estimated value remaining after clearance sales
***) the Company should not have goods introduced earlier than two seasons ago

The new goods management model was introduced by LPP SA from the second half of 2016, while the new rule for making revaluation write-downs was applied for the first time to the goods' value as at 31 December 2016. There were no retrospective recalculations made due to the fact that the change in assessing revaluation write-downs stems from the current operating change regarding the clearance sales of older collections.

5. Declaration of compliance with IFRS

The presented consolidated financial statements cover the period between 1 January 2016 and 31 December 2016. Comparable data are presented for the period between 1 January 2015 and 31 December 2015.

These financial statements were drawn up in line with the International Financial Reporting Standards (IFRS) approved by the European Union, covering standards and interpretations approved by the International Accounting Standards Board and the IFRS Interpretations Committee.

Amendments to accounting standards or interpretations, being in force and applied by the Company since 2016

New or updated standards and interpretations valid from 1 January 2016 are given in the table below.
In the Group's opinion, amendments to accounting standards, given below, have no major impact on the accounting policy applied so far.

Standard/interpretation	Effective date	Description of amendments to the standard/interpretation
Amendment to IAS 19 "Employee Benefits"	Annual periods beginning on or after 1 February 2015 Amendments approved by the European Commission *	Amendments consist in clarifying in detail the rules of conduct in cases where employees make payments to cover the costs of a plan involving specific benefits.
Amendments to IFRS 2, IFRS 3, IFRS 8, IAS 16, IAS 24, IAS 38	Annual periods beginning on or after 1 February 2015 Amendments approved by the European Commission **	Minor amendments to standards, implemented as part of their annual amendments (2010 – 2012 cycle): • IFRS 2: The Board has provided detailed clarifications by amending or introducing new definitions of the following terms: market conditions, service conditions, vesting conditions, performance conditions. • IFRS 3: The Board has provided detailed clarifications for the rules of valuation of a conditional payment after the acquisition date to make them compliant with other standards (first of all with IFRS 9 / IAS 39 and IAS 37)

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		• IFRS 8: The Board imposed on entities combining operating segments the requirement of additional disclosures concerning such combined segments as well as economic features based on which they have been combined • IFRS 8: following its amendment, the standard provides that the requirement to disclose the reconciliation of the sum of segment assets with assets disclosed in the balance sheet is obligatory only when asset values are disclosed by segments • IAS 16 and IAS 38: The Board has implemented an adjustment for the rule governing the calculation of an amount gross and accumulated depreciation of a fixed asset (intangible asset) when applying the revaluation model • IAS 24: The definition of related party has been expanded by entities providing key management personnel services. Relevant disclosures have also been added.
Amendment to IFRS 11 "Joint Arrangements"	Annual periods beginning on or after 1 January 2016 Amendments approved by the European Commission	According to this amendment, an entity acquiring interests in a joint operation constituting a business (venture) will be required, for the purpose of recognition of assets and liabilities of a joint operation, to apply the rules provided for in IFRS 3 i.e., among others, to evaluate assets and liabilities at fair value and determine the goodwill.
Amendments to IAS 16 "Property, Plant and Equipment" and IAS 38 "Intangible Assets"	Annual periods beginning on or after 1 January 2016 Amendments approved by the European Commission	According to this amendment, the fixed asset depreciation method based on proceeds earned from the use of an asset is impermissible. With respect to intangible assets, the application of such method has been limited.
Amendments to IAS 16 "Property, Plant and Equipment" and IAS 41 "Agriculture"	Annual periods beginning on or after 1 January 2016 Amendments approved by the European Commission	According to this amendment, bearer plants (such as grape vines, fruit trees) will be excluded from the scope of IAS 41, to be included within the scope of IAS 16 as fixed assets produced at the entity's own effort. Due to the said amendment, it will not be necessary to valuate these plants at fair value as at each balance sheet date, as previously required under IAS 41.
Amendment to IAS 27 "Separate Financial Statements"	Annual periods beginning on or after 1 January 2016 Amendments approved by the European Commission	According to this amendment, in separate financial statements, interests in a subsidiary, joint venture or associate may be valued applying also the equity method. So far, under IAS 27, the valuation could be made solely based on the acquisition price or in accordance with IFRS 9 / IAS 39.
Amendments to IFRS 5, 7, IAS 19, 34	Annual periods beginning on or after 1 January 2016 Amendments approved by the European Commission	Minor amendments to standards, implemented as part of their annual amendments (2012 – 2014 cycle): • IFRS 5: according to this amendment, if the company has changed designation of assets from assets for direct sale to assets to be distributed to owners, or from assets to be distributed to owners to assets for sale, then it is a continuation of an original plan, and adjustments made are not reversed. • IFRS 7: the amendment to this standard specifies in detail that the requirements applicable since 2013 in respect of disclosure of information on items shown in net amounts do not apply to condensed interim financial statements unless this is information to be disclosed under the general principles of IAS 34.

		• IFRS 7: this amendment introduces a new instruction which makes it possible to assess whether there is a continuing involvement in transferred assets. If an entity has transferred assets, yet it has concluded a servicing contract in which a fee depends on amounts of, and deadlines for, repayment of the transferred financial asset, it means that the entity has a continuing involvement in that financial asset. • IAS 19: this standard makes it possible to apply, to cash flows being discounted, interest rates applicable to treasury securities if the market for securities of commercial entities is shallow. According to this amendment to the said standard, the market depth should be assessed from the perspective of the currency of those securities, and not their country. • IAS 34: according to this standard, certain information required under IAS 34 for condensed interim financial statements may be presented in other documents attached to such condensed interim financial statements, such as a statement of operations. If information is provided in attached documents, then, in such condensed interim financial statements, an explicit reference should be made to places where such documents have been disclosed. Additional documents must be available for users on the same terms and conditions and within the same time-frame as the condensed interim financial statements. Otherwise the condensed interim financial statements will be considered incomplete.
Amendments to IAS 1 “Presentation of Financial Statements”	Annual periods beginning on or after 1 January 2016 Amendments approved by the European Commission	As part of a larger project aimed at increasing transparency and avoiding excessive disclosures in financial statements, the IAS Board has published numerous amendments to IAS 1. These amendments cover the following issues: • the Board brings attention to the fact that disclosure in financial statements of too much irrelevant information renders such financial statements unreadable and is incompliant with the principle of materiality, • items in the statement of profit or loss and OCI, required according to this standard, and items in the statement of financial position may be disaggregated, • there are requirements added in respect of additional subtotals presented in the statement of profit or loss and OCI and in the statement of financial position, • entities have flexibility as to the order in which they present the notes to financial statements, yet, in that scope, they are required to ensure comprehensiveness and comparability.
Amendments to IFRS 10 “Consolidated Financial Statements”, IFRS 12 “Disclosure of Interests in Other Entities” and IAS 28 “Investments in Associates and Joint Ventures”	Annual periods beginning on or after 1 January 2016 Amendments approved by the European Commission	The IAS Board added further exemptions from the consolidation requirement or the requirement to apply the equity method with reference to investment entities: • if an intermediate holding company is a subsidiary of an investment entity which recognises its investments at fair value according to IAS39 / IFRS 9, then such intermediate holding company is exempted

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		from preparing consolidated financial statements, • if an investor is a subsidiary of an investment entity which recognizes its investments at fair value according to IAS 39 / IFRS 9, then such investor is exempt from applying the equity method to disclose its investments in jointly controlled entities or associates, • an investment entity is required to consolidate subsidiaries providing ancillary services; however, if such subsidiary is itself an investment entity, then it is not consolidated.

** - the effective date set by the IAS Board is 1 July 2014; the European Commission adopted, as the mandatory effective date, periods beginning on or after 1 February 2015, with earlier application being possible*
*** - the effective date set by the IAS Board is 1 July 2014; the European Commission adopted, as the mandatory effective date, periods beginning on or after 1 February 2015, with earlier application being possible*
**** - effective date set by the IAS Board*

Application of a standard or interpretation before the effective date

In these financial statements, no standard or interpretation was voluntarily applied before the effective date.

Published standards and interpretations which did not enter into force as at 1 January 2016

The Capital Group intends to implement these regulations within the time-frames provided for in the standards or interpretations.

The Group estimates that the standards given below will have no material impact on the accounting policy applied so far.

Standard/interpretation	Effective date	Description of amendments to the standard/interpretation
New IFRS 9 "Financial Instruments"	Annual periods beginning on or after 1 January 2018 The standard approved by the European Commission	A new standard for the valuation and recognition of financial instruments is to replace the current IAS 39. Changes introduced by the accounting standard for financial instruments mainly include: • other categories of financial assets, on which the valuation method of assets depends; the categorising of assets is made depending on the business model relating to a given asset • new principles for hedge accounting, reflecting risk management to a greater extent, • new model for the impairment of financial assets value based on expected losses and causing the need for faster recognition of costs in the financial result.
New IFRS 14 "Regulatory Deferral Accounts"	Annual periods beginning on or after 1 January 2016 * NOTE! This standard will never be approved by the European Commission and will never be applied in the EU.	The new standard applies only to entities that switch to IFRS and operate in industries in which the state regulates prices charged, such as gas, electricity or water supplies. The standard permits the continuation of the accounting policy for the recognition of revenue from such activities, applied before the transition to IFRS, both in the first report prepared in accordance with IFRS, as well as later.

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Standard/interpretation	Effective date	Description of amendments to the standard/interpretation
Amendment to IFRS 10 “Consolidated Financial Statements” and IAS 28 “Investments in Associates and Joint Ventures”	No effective date – voluntary application The approval procedure suspended by the European Commission	The current principles governing the settlement of the loss of control over a subsidiary provided for the recognition of profit or loss at the moment. In turn, the equity method principles stated that the result of transactions with entities valued using the equity method are recognised only to the extent of the other shareholders' interests in those entities. In a situation where the parent company sells or makes an in-kind contribution in the form of interests in a subsidiary to an entity valued using the equity method in such a way that it loses control over it, the above-cited regulations would collide. The amendment to IFRS 10 and IAS 28 eliminates this collision as follows: ▪ if the entity over which control was lost is an enterprise (business entity), the result on the transaction is recognised in full, ▪ if the entity over which control was lost is not a business, the result is recognised only to the extent of other investors' interests.
Amendments to IAS 12 “Income Taxes”	Annual periods beginning on or after 1 January 2017 Amendments not approved by the European Commission	The IAS Board has provided detailed clarifications for the following principles: • recognition of deferred tax assets for unrealised losses, • calculation of future taxable profits required to recognise deferred tax assets.
Amendment to IAS 7 “Statement of Cash Flows”	Annual periods beginning on or after 1 January 2017 Amendments not approved by the European Commission	The amended standard requires entities to disclose information which will enable users of financial statements to assess changes in the entity’s indebtedness (i.e. changes in loans and credit facilities taken out).
Amendment to IFRS 15 “Revenue from Contracts with Customers”	Annual periods beginning on or after 1 January 2018 Amendments not approved by the European Commission	In order to prevent incoherent application of the new standard, the IAS Board clarified in detail the principles governing the following issues: • identification of liability (it has been clarified how to apply the concept of a “separate“ good or service) • identification of the relation “principal versus agent” • transfer of a licence at a point in time or over time Furthermore, interim provisions have been simplified additionally.
Amendment to IFRS 2 “Share-based Payment”	Annual periods beginning on or after 1 January 2018 Amendments not approved by the European Commission	The IAS Board has regulated three issues: • the manner of recognition in the measurement of cash-settled payments of conditions other than vesting conditions • classification of share-based payments if the entity has withholding tax obligations against employees • modification to the terms and conditions of a share-based payment that changes the classification of the transaction from cash-settled to equity-settled.

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Standard/interpretation	Effective date	Description of amendments to the standard/interpretation
Amendment to IFRS 4 "Insurance Contracts"	At the time of application of IFRS 9 Amendments not approved by the European Commission	Due to the entry into force in 2019 of a new standard for financial instruments (IFRS 9), the IAS Board has implemented interim rules (until entry into force of the new standard relating to insurance) for applying new accounting principles for instruments in the insurers' financial statements. Otherwise their results would be exposed to considerable volatility. Two alternative approaches have been proposed: • adjustment of volatility caused by IFRS 9 for certain assets by making a separate item in the statements of operations and OCI • exemption from applying IFRS 9 until entry into force of the new standard relating to insurance (or 2021)
Amendments to IFRS 1, IFRS 12, IAS 28	Annual periods beginning on or after 1 January 2018 (IFRS 1 and IAS 28) Annual periods beginning on or after 1 January 2017 (IFRS 12) Amendments not approved by the European Commission	Minor amendments to standards, implemented as part of their annual amendments (2014 – 2016 cycle): • IFRS 1: there have been removed certain short-term exemptions which were applied at the time of the transition to IFRS due to the fact that they concerned periods which have already elapsed, and they could not be applied. • IFRS 12: it was clarified in detail that disclosures concerning interests in other entities, required under the said standard, apply also in cases where such interests are classified as designated for sale according to IFRS 5. • IAS28: it was clarified in detail that in situation where IAS 28 permits the valuation of investments using the equity method or at fair value (by organisations managing high-risk capital, mutual funds etc. or interests in investment entities), the said choice may be made for each investment separately.
Amendment to IAS 40 "Investment Property"	Annual periods beginning on or after 1 January 2018 Amendments not approved by the European Commission	This amendment specifies in detail the rules based on which real property is transferred to, or from, the category of investment property from, or to, the category of fixed assets or inventory. First of all, a change in classification occurs when the manner of using a property is changed, and such change must be evidenced. According to the explicit wording of the said standard, a change in the management's intentions, alone, is insufficient. The amendment to the standard should be applied to all changes in using a property, which will occur after entry into force of the said amendment to the standard, and to all investment properties held as at the date of the said amendment's entry in force.

** - effective date set by the IAS Board*

The Group estimates that the following new standards will, or may have, a material impact on the accounting policy applied so far.

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Standard and its description	Effective date	Estimated impact
IFRS 16 "Leases" The new standard regulating lease agreements (including rental and land lease agreements) provides a new definition of lease. Significant changes apply to lessees: for each lease agreement, the standard requires recognising "the right to use the asset" and the corresponding financial liability. The right to use the asset is then amortised, while the liability is measured at amortised cost. Simplification has been provided for short-term agreements (up to 12 months) and assets of low value. The accounting treatment of leases for lessors is similar to the principles set out in the current IAS 17.	Annual periods beginning on or after 1 January 2019 The standard not approved by the European Commission	The new IFRS will have a material impact in the accounting principles applied in the Company. Due to the amended definition of lease, all agreements qualified as lease will be shown in the balance sheet, and the Company's result will be affected by the amortisation of the "right to use the asset". The above applies, among others, to lease agreements for commercial space.
New IFRIC 22 "Foreign Currency Transactions and Advance Consideration"	Annual periods beginning on or after 1 January 2018 The interpretation not approved by the European Commission	The said interpretation determines what exchange rate should be applied to the sale or purchase in other currency, which is preceded by the receipt of an advance consideration in such currency. According to the new interpretation, the advance consideration should be recognised as at its payment date based on the exchange rate applicable for that date. Next, at the time of recognition, in the profit and loss account, of revenue earned in a foreign currency or a cost or a purchased asset, they should be recognized based on the exchange rate applicable on the date of recognition of the advance consideration, and not based on the exchange rate applicable on the date on which such revenue or asset was recognised.
New IFRS 15 "Revenue from Contracts with Customers" The new standard will replace current IAS 11 and IAS 18, providing one consistent revenue recognition model. The new 5-step model will make the recognition of revenue dependent on gaining control over the good or service by the customer. In addition, the standard introduces additional requirements for disclosure of information and guidance on several specific issues. The new standard may change the moment, and amounts, of recognised revenues in enterprises operating in many industries. NOTE!!! The IAS Board postponed the date of the standard's entry into force from 2017 to 2018.	Annual periods beginning on or after 1 January 2018 The standard approved by the European Commission	The said standard may have a minor impact on the accounting principles applied by the Company. The said amendment may relate to new disclosures in financial statements.

The Group is currently in the process of assessing the impact of amendments to the said standards on its financial statement.

6. Going concern

The consolidated financial statements for 2016, the financial statements of the Parent Company and the statements of subsidiaries, serving as the basis for the consolidated financial statements, have been drawn up based on the assumption that the Group remains a going concern in the foreseeable future and that its business is not restricted to a considerable extent.
Based on the information available as at the date of the financial statements, the going concern assumption adopted in these financial statements is fully justified.

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7. Date of approval of the financial statements for publication

These financial statements were approved for publication by the Management Board of the Parent Company of LPP Capital Group on 6 April 2017.

8. Events after the balance sheet date

As per IAS 10, events after the balance sheet date include all events that occurred between the balance sheet date and the date on which the financial statements were approved for publication.
The Management Board is authorised to adjust the financial statements after their publication.

On 20 January 2017, LPP SA received from the Tax Audit Office (*Urząd Kontroli Skarbowej*) in Gdańsk the analysis of evidence material, being the outcome of the tax audit carried out by the said Office since 2015 in respect of the reliability of declared tax bases and the correctness of calculation and payment of CIT for 2012.
At the same time, LPP SA informs that, due to a tax audit procedure carried out since 2015 by the Tax Audit Office in Gdańsk (further referred to as "TAO"), of which the Issuer informed in preceding quarterly reports, on 20 January 2017, the Company received the analysis of evidence material collected during the audit procedure covering the reliability of declared tax bases and correctness of calculation and payment of CIT for 2012.
The maximum amount of tax with interest, which could be potentially charged to the Company if the TAO issues a decision based on the findings adopted by the TAO in the said analysis, is approx. PLN 22 million.
On 6 February 2017, the Issuer filed a letter with the TAO, in which the Issuer presented its standpoint on the analysis of evidence material, made by the TAO.
The audit procedure has not been completed yet.

9. Methods of measurement of assets and liabilities and determination of the financial result, adopted in the consolidated financial statements

Tangible fixed assets (property, plant and equipment)
Tangible fixed assets are initially carried at the purchase price, increased by all costs directly related to the purchase and necessary to adapt the asset to the working condition for its intended use. Costs incurred after the date when the fixed asset was put into use, including costs of maintenance and repairs, are charged into the statement of financial result and other comprehensive income as they are incurred.

As at the balance sheet date, PP&E are measured at cost less depreciation and impairment losses.
Depreciation is made by the Capital Group on the straight-line basis. Fixed assets are depreciated over their pre-determined expected useful life. This period is revised annually.

Depreciation rates applied in the Capital Group for specific groups of fixed assets are as follows:

Asset group	Depreciation rate
Buildings, premises, civil engineering works, including:	2.5-50%
Outlays in the premises not owned by the Issuer	14.28%
Devices and machinery	2.5-50%
Transportation means	10-25%
Other fixed assets including:	10-40%
Furniture	20%

The value of fixed assets is also periodically tested for impairment, if any, resulting from any events or changes in the business environment or within the Group, which could cause an impairment of these assets below their current book value.
When fixing the rates of depreciation for individual PP&E, the Group determines whether there are any components of such an asset, the purchase price of which is important as compared the purchase price of the entire asset, and whether the usability period for these components is different from the usability period for the remaining part of the asset.

For accounting purposes, based on the materiality principle, threshold amounts were adopted, being equal to tax threshold amounts, permitting one-off depreciation of a fixed asset or non-inclusion of an asset as part of fixed assets.

Under the accounting policy adopted by the Capital Group, the straight-line depreciation of low-price assets may be applied in justified cases by way of the Management Board's decision if all the following circumstances occur simultaneously:

- substantial quantities of fixed assets are purchased in a single transaction, and their unit price does not exceed the threshold amount, yet their total value is material,
- these assets form a set of uniform and/or interconnected fixed assets, and their purchase is related to the execution of a major investment venture, to be operated at least over the period of normative depreciation specified for this particular group of fixed assets in tax regulations,
- these assets are high-quality and high-reliability fixed assets.

Fixed assets in progress – as at the balance sheet date, they are carried in the total amount of costs directly related to their acquisition or production, less impairment write-downs.
A given item of PP&E may be removed from the statement of financial position after its sale or when no economic benefits of the asset's further use are expected. Profits or losses arising from the sale, liquidation or cessation of the use of fixed assets are specified as a difference between sales revenue and their net value and are recognised in the result in other operating revenues or expenses.

Leased assets
Finance lease agreements under which substantially all risks and benefits arising from the possession of a leased object are transferred to the Group are recognised in the assets and liabilities as at the lease commencement date. The value of assets and liabilities is determined as at the lease commencement date based on the lower of the following values: fair value of the fixed asset being the leased object or the current value of the minimum lease fees.
The minimum lease fees are divided into financial costs and the reduction in the balance of unpaid lease-based liability in a way facilitating the obtaining of a fixed interest rate for the unpaid liability balance. Conditional lease fees are recognized in the costs of the period in which they were incurred.
Fixed assets used under finance lease agreements are depreciated according to the same rules as those applied to the own assets of the Capital Group. However, in the situation where there is no satisfactory assurance that the leaseholder will obtain the ownership title before the end of the lease term, a given asset is depreciated for a shorter of two periods, i.e. the lease term or the usage period.

In the event where the lease agreement has been qualified, in accounting terms, pursuant to IAS 17, as financial lease agreement, yet, in taxation terms, according to the Corporate Income Tax Act, it has been qualified as operating lease agreement, then, in order to determine the correct amount of tax deductible costs, the following rules are applied. Depreciation write-offs made by the user do not constitute tax deductible costs for tax purposes. Tax deductible costs are only lease fees paid as determined in the agreement, recognized as the cost of the period they refer to.

Lease agreements under which the lessor retains substantially all risks and benefits resulting from the ownership of the leased object are qualified as operating lease agreements.
Operating lease fees are recognized as costs by means of the straight-line method for the lease term unless another systematic method better reflects the way in which the Group's benefits are spread in time.

Intangible assets
Intangible assets include trademarks, patents and licenses, computer software, development costs and other intangible assets meeting the recognition criteria provided for in IAS 38.

As at the balance sheet date, intangible assets are disclosed by their purchase price or their manufacturing cost, less depreciation and impairment write-downs. Intangible assets with a determined useful life are depreciated on the straight-line basis for the period of their economic usability. Useful lives of specific intangible assets are verified annually.

The applied depreciation rates for specific groups of intangible assets are as follows.

Asset group	Depreciation rate
Costs of completed development works	20%
Acquired concessions, patents, licences and similar assets	10-50%

Intangible assets with unspecified useful lives are not depreciated but they are tested for impairment annually. The House trademark is an intangible asset an unspecified useful life, owned by the Capital Group.

The Group's companies carry out development projects related to the design and construction of model showrooms.
Outlays directly associated with development works are recognised as intangible assets only if they meet the following criteria:

- an intangible asset may be completed from a technical point of view to make it available for use or sale,
- the Group intends to complete the asset and either use or sell it,
- the Group is able to use or sell the intangible asset,
- the intangible asset will bring economic benefits and the Group may evidence such benefit by, among others, the existence of a market or usability of such asset for the purposes of the Group,
- the Group has technical, financial and other resources available as required for completing development works to sell or use the asset,
- outlays made during development works may be reliably evaluated and attributed to a given intangible asset.

Outlays made for development works carried out as part of a given venture are transferred to a subsequent period if one may consider that they will be recovered in the future. Future benefits are assessed based on the principles provided for in IAS 36.
Upon initial recognition of outlays for development works, the historical cost model is applied, according to which assets are recognised at their purchase prices or their manufacturing cost less accumulated depreciation and accumulated impairment write-downs. Completed development works are depreciated applying the straight-line method over an expected benefit-gaining period lasting five years.

Software maintenance costs incurred in subsequent periods are recognised as the cost of the period at the time they are incurred.

Borrowing costs
According to IAS 23 “Borrowing Costs”, all costs that may be allocated to adjusted assets are capitalised. Adjusted assets are those requiring a considerable period for preparing them for intended use. The Capital Group has made an assumption that a considerable period is a period of 1 year. Thus, any borrowing costs are capitalised, provided that the a given asset would be adjusted for a period of 1 year or longer. All other minor costs of assets adjusted for less than a year are recognised directly in profit or loss.
Borrowing costs may comprise, first of all, the following:

- interest on overdrafts and interest on short- and long-term loans and borrowings;
- differences in exchange rates in connection with loans and credits extended in foreign currencies.

Borrowing costs are capitalised as of the date of making outlays for an adjusted asset, the incurring of borrowing costs and carrying out activities necessary to prepare assets for their intended use. The Capital Group ceases to capitalise borrowing costs when an adjusted asset is delivered for use.

Goodwill
Goodwill is initially recognised pursuant to IFRS 3.
This value is calculated as a difference between the two values:

- the sum of a consideration for the control, non-controlling interests and fair value of blocks of shares held in the acquired entity before the acquisition date, and
- the fair value of the entity’s identifiable acquired net assets.

The excess of the sum calculated as given above over the fair value of the entity’s identifiable acquired net assets is recognised in the assets of the consolidated statement of the financial position as goodwill. Goodwill represents a payment made by the acquiring company expecting future economic benefits from assets which may not be identified individually or recognised separately.

As at the reporting date, goodwill is measured at the cost of purchase less accumulated impairment write-downs made so far and deductions for the disposal of part of shares to which it was previously assigned. Impairment write-downs up to the value assigned to a cash-generating unit (unit group) are not reversible.
Goodwill is reviewed for impairment before the end of the reporting period in which the merger occurred, and then in each subsequent annual reporting period. If there are any prerequisites for impairment, the impairment test is carried out before the end of each reporting period in which such prerequisites occurred.

Until 1 January 2010, for settling mergers, the Capital Group applied the acquisition method as described in the previous version of IFRS 3.

Investments in subsidiaries
The Group owns shares in Polish subsidiaries only.
Shares in subsidiaries are measured at their acquisition prices less impairment write-downs.
The acquisition price comprises the amount due to the selling party less deductible VAT, as well as costs directly related to the purchase and adjusting an asset to make it available for use or for its introduction to trading.
In the event of impairment, an impairment write-down is charged to financial expenses. If a reason for the impairment write-down ceases to exist, the original value of the investment is restored by transferring the reversed amount to income from financial operations. Goodwill may be reinstated in full or in part.

Investments in other entities
This item presents only shares in entities not affiliated with LPP SA.
It is measured at acquisition prices less impairment write-downs.

In the event of impairment, an impairment write-down is charged to financial expenses. If a reason for the impairment write-down ceases to exist, the original value of the investment is restored by transferring the reversed amount to income from financial operations. Goodwill may be reinstated in full or in part.

Financial instruments
Each contract establishing a financial asset for one party and, at the same time, a financial liability or capital instrument for the other party is a financial instrument.

A financial asset or liability is recognised in the statement of financial position if the Group becomes a party to that instrument. Standardised purchase and sale transactions involving financial assets and liabilities are recognised as at the transaction date.

A financial asset is derecognised from the statement of financial position when rights to economic benefits and risks arising from the contract have been exercised or executed, have expired or the Group has waived them.
The Group derecognises a financial liability from the statement of financial position upon its expiry, that is when the obligation specified in the contract has been discharged, cancelled or expired.

As at the acquisition date, the Capital Group values financial assets and liabilities at fair value i.e. most often at fair value of a payment made (in the case of an asset) or a payment received (in the case of a liability).

As at the balance sheet date, financial assets and liabilities are valued in line with the principles specified below.

Financial assets
For the purposes of valuation upon initial recognition, financial assets other than hedging derivatives are classified by the Capital Group as being divided into:
- loans and receivables,
- financial assets measured at fair value through profit or loss,
- investments held to maturity, and
- financial assets available for sale.

These categories define the principles for valuation as at the balance sheet date and the recognition of profits and losses from the measurement in profit or loss or other comprehensive income. Profits and losses recognised in the financial result are presented as financial revenues or costs, except for revaluation write-downs of trade receivables, disclosed as other operating expenses.

All financial assets, except for those measured at fair value through profit or loss, are assessed as at each balance sheet date due to existence of prerequisites for value impairment.

Any prerequisites for value impairment are reviewed for each category of financial assets separately, as given below.

Loans and receivables

Loans extended and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted on an active market. Loans and receivables are measured at depreciated cost based on the effective interest rate method. The valuation of short-term receivables may also be based on the amount expected to be paid as the effect of discounting would be immaterial. They are recognised as current assets if their maturities do not exceed 12 months from the balance sheet date. Loans extended and receivables with maturities exceeding 12 months from the balance sheet date are recognised as fixed assets.

Financial assets classified as loans and receivables are presented in the statement of the financial position as:

- long-term assets in item “Loans and receivables”, and
- short-term assets in items “Loans”, “Trade receivables”, “Other receivables” and “Cash and cash equivalents”.

Revaluation write-downs of receivables are made based on their type:

- disputable receivables (amounts claimed in pending court proceedings and amounts due from debtors put into liquidation or bankruptcy) – write-downs in the total amount receivable,
- other receivables – write-downs made based on a case-by-case review and assessment of the situation and the risk of a potential loss.

Financial assets measured at fair value through profit and loss

Financial assets measured at fair value through profit and loss include assets classified as designated for trading or, upon initial recognition, for valuation at fair value through profit and loss, due to the fulfilment of the criteria set forth in IAS 39.

This category comprises all derivatives presented in the statement of financial position as a separate item and units in investment funds.

Units in investment funds are recognised in item "Other financial assets".

Instruments in this category are measured at fair value, and the measurement results are recognised in profit or loss.

As at the balance sheet date, the Group has no such investments.

Financial assets held to maturity

Financial assets held to maturity are non-derivative financial assets with fixed or determinable payments and with fixed maturity, which the Group intends, and is able, to hold to maturity, except for assets classified as loans and receivables.

In this category, the Capital Group recognises bonds and other debt securities held to maturity, presented in the statement of financial position as “Other securities”.

Financial assets held to maturity are measured at amortised cost, applying the effective interest rate method. If there is any evidence for possible impairment of investments held to maturity, assets are measured at current value of estimated future cash flows. Changes in the balance sheet value, including impairment write-downs, are recognised in profit or loss.

As at the balance sheet date, the Group does not have such investments.

Financial assets available for sale

Assets available for sale are non-derivative financial assets designated as available for sale or not classified in any of the above-mentioned categories of financial assets.

In this category, the Capital Group recognises listed bonds not held to maturity and shares in companies other than subsidiaries or associates.

In the statement of financial position, these assets are disclosed under “Other securities” and “Investments in other entities”.

Shares in unlisted companies are valued at their acquisition price less accumulated impairment write-downs as their fair value may not be reliably assessed. Impairment write-downs are recognised in profit or loss.

All other financial assets available for sale are measured at fair value.

Profits and losses on valuation are recognised as other comprehensive income and accumulated in revaluation capital from financial assets available for sale, except for impairment write-downs which are recognised in profit or loss. Profit or loss comprises also interest which would be recognised at the valuation of these financial assets at amortised cost based on the effective interest rate method.

Financial liabilities

Financial liabilities other than hedging derivatives are recognised under the following items of the statement of financial position:

- loans and borrowings,
- other financial liabilities,
- trade payables and other liabilities

Upon initial recognition, financial liabilities are valued at amortised cost based on an effective interest rate, except for financial liabilities designated for trading or indicated as measured at fair value through profit or loss (derivatives other than hedging instruments). Short-term trade payables are measured based on the amount payable due to immaterial discount effects.

Accruals and prepayments

In item "Accruals and prepayments", in the assets column of the statement of financial position, the Capital Group presents prepaid expenses relating to future reporting periods, including, first of all, rents.
In item "Accruals and prepayments", in the liabilities column of the said statement, income of future periods and profit/loss on the sale of fit out in stores are presented.
Fit-out resale results from the conclusion of a lease agreement, being a form of reimbursement of costs incurred to adjust the showroom to conduct sales. According to SIC 15, this kind of bonus should be deferred, on the straight-line basis, during the term of the agreement, by adjusting lease payments.

Inventories

As at the balance sheet date, inventories are valued at their acquisition prices not exceeding their net selling prices.
Inventories include:

- trading commodities,
- materials (fabrics and sewing accessories) purchased and delivered for processing to external contractors,
- IT consumables related to the operation, maintenance and development of a computer network,
- advertising materials.

Trading commodities in local warehouses are recorded by quantity and value and measured as follows:

- imported goods – at cost, including purchase prices, costs of foreign and domestic transport to the first unloading point in Poland, as well as customs duties; to convert amounts denominated in a foreign currency, the following exchange rate is applied:
- the one specified in a customs document,
- the one applicable on the day preceding the issuance of a purchase invoice for direct deliveries to Russia,
- goods purchased in Poland – at cost; purchase-related costs are charged directly into operating costs when incurred, as their value is immaterial.

Trading goods sold from RESERVED, Cropp, House, MOHITO and SiNSAY collections are valued at weighed average prices.
For trading commodities from other collections, the FIFO method is employed.

Trading commodities in bonded warehouses are valued at cost, including their purchase prices as well as the costs of foreign and domestic transport to the first unloading point in Poland.
The value of goods delivered from bonded warehouses (moved to local warehouses or sold directly abroad) is measured based on the detailed identification of goods for individual lots delivered to bonded warehouses.

Trading goods in transit are measured at their purchase prices plus the costs of foreign and domestic transport, known as at the date of the statement of financial position. As regards imported goods in transit, they are subject to the selling exchange rate published by Raiffeisen Bank Polska SA as at the balance sheet date.

Inventories with trading and useful value impaired are written down and charged to other operating costs.

Cash and cash equivalents

Cash and cash equivalents comprise cash at hand and in the bank, demand deposits and short-term highly liquid investments (up to 3 months).
The balance of cash and cash equivalents, shown in the cash flow statement, is adjusted for exchange rate differences from the balance sheet valuation of cash in foreign currency.

Equity capital
The stated capital is presented at the nominal value of issued shares, in accordance with the Articles of Association of the Parent Company and the entry in the National Court Register.

Shares in the Parent Company, acquired and retained by the Parent Company, are deducted from the equity capital. Treasury shares are valued at their purchase prices.
A share premium account is formed from the surplus of a share issue price over the share nominal value, less issue costs.

Other capital includes:
- spare capital,
- reserve capital,
- capital from the settlement of business combinations, and
- capital component of convertible bonds.

The value of spare capital comprises:
- profits from previous years, qualified by virtue of decisions of the General Meetings of Shareholders,
- amounts of share-based payments, awarded to specific persons under an incentive scheme.

Capital from the settlement of business combinations was created as a result of goodwill revaluation after the acquisition of Artman SA.

The retained earning present results from previous years and the profit or loss for the current year.

Share-based payments
The Group has implemented incentive plans under which options convertible into shares in the Parent Company are granted to key management personnel.

The value of remuneration for work of management staff is determined indirectly by reference to the fair value of equity instruments granted. The fair value of options is measured at grant date, whereas the non-market vesting conditions (achieving the desired level of profit or loss) are not taken into account when estimating the fair value of stock options.
Remuneration costs with a corresponding increase in equity are recognised based on the best available estimates of the number of options which will be vested in a given period. When determining the number of options to be vested, the non-market vesting conditions are given consideration.
The Group makes adjustments to these estimates if, according to subsequent information, the number of options granted is different from previous estimates. Estimate adjustments in respect of the number of options granted are recognised in profit or loss for the current period - no adjustments are made to previous periods.

Once the options convertible into shares are exercised, the amount of capital from valuation of options granted is transferred to the capital from the sale of shares above their nominal value, less share issue costs.

Provisions for employee benefits
Provisions for future retirement benefits are estimated by the Company independently, applying a method involving the duration of work, gender and the value of the current remuneration. It has been assumed that the discount for provisions for retirement benefits corresponds to the expected rate of increase in remunerations and is shown in the non-current part of the statement.
In the reporting period, there were no actuarial gains or losses.

Other provisions
The Company establishes provisions when it has a duty (under the provisions of law or by virtue of custom) arising from past events and when it is probable that the exercise of the said duty will affect economic benefits, and that the amount of such liability may be reliably estimated.
As at the balance sheet date, the Company created the following other provisions:
- for holiday leaves not taken i.e. for future payment of liabilities owed to employees and arising from their day-to-day work,
- for unpaid remuneration the value of which incorporates also bonuses for a current year, to be paid in the next reporting period,
- for future costs related to the liquidation of Tallinder stores, calculated in the amount of cost incurred so far for services of this type,

■ for liquidated damages, if any, related to early termination of lease agreements in respect of the Tallinder brand, estimated in accordance with relevant provisions of lease agreements.

Revenues

Sales revenues are recognised at fair value of payments received or receivable and represent receivables for products, goods and services delivered as part of regular business activity, net of discounts and VAT. Revenues are recognised in the amount of probable economic benefits obtained by the Group and related to a given transaction, provided that this amount may be reliably estimated.

Revenues from the sale of goods are recognised when the significant risks of, and benefits from, the ownership title to such goods have been transferred to the buyer.

Taking into consideration customers' claims and product returns, revenues from the sale of goods are adjusted based on the adjustment of the estimated cost of such returns. Based on historical data, a percentage ratio of product return against sales volume is estimated. For these estimates, it has been assumed that products purchased in a given quarter are returned in the next quarter. The value of this ratio against prime costs and revenues is defined quarterly.

State subsidies are recognised in books so that the subsidy revenue is recognised as commensurate to its costs.

The Capital Group adopted adequate methods for presenting subsidies in its financial statements:

- ■ asset grants – initially as a separate item in "Deferred income" and, subsequently, systematically presented as revenue over the usable life of an asset;
- ■ revenue grants – in item "Other operating/financial revenues".

Interest revenues are recognised successively as they accrue, up to the net carrying amount of the financial asset.

Income tax (including deferred income tax)

Mandatory reductions of profit or loss comprise current and deferred income tax which was not recognised in other comprehensive income or directly in equity.

Current tax is calculated on the basis of the taxable result in a given financial year. Tax gains (losses) are different from book gross gains (losses) since taxable revenues and tax deductible expenses are transferred temporarily to other periods, while permanently non-taxable items of revenues and expenses are eliminated. Tax due is calculated based on tax rates applicable in a given financial year.

Deferred tax is calculated applying the balance sheet method as tax to be paid or returned in the future based on differences between the balance sheet values of assets and liabilities, and the corresponding tax values applied to determine the tax base.

Provision for deferred tax is made for all positive taxable temporary differences, while the asset under the deferred tax is recognised up to the extent that the recognised negative temporary differences may be likely deducted from future tax profits.

Transactions in foreign currencies

The functional and presentation currency of LPP Capital Group is Polish zloty (PLN), which is also the functional currency of the Parent Company.

As at the transaction date, assets and liabilities denominated in foreign currencies are carried in functional currency at the following exchange rates, respectively:

- ■ purchase or selling rate applied by the Parent Company's bank – in the case of purchase or sale of foreign currencies and payment of receivables or liabilities (applicable to accounts in PLN)
- ■ purchase rate applied by the Parent Company's bank - in case of foreign currency deposits made onto a currency account,
- ■ determined by the FIFO method - in case of foreign currency disbursements from a currency account,
- ■ average rate determined for a given currency by the central bank of a given country on the last working day preceding the day of issuing a foreign or domestic invoice - in cases other than import or export (transit) of goods
- ■ resulting from a customs document issued in relation to depositing goods at a bonded warehouse - in case of entering goods and liabilities in accounting records at the time of depositing goods at a bonded warehouse,

- selling rate applied by the Parent Company's bank as at the balance sheet day - in case of measurement of goods in transit and related import liabilities, in the event where no goods were deposited at a bonded warehouse as at the balance sheet day

The following items denominated in foreign currencies are measured as at the balance sheet date:
- monetary items:
  - assets – at the purchase rate applied by the Parent Company's bank as at that date (USD – 4.1761, EUR – 4.4210, RON – 0.9732, RUB – 0.0670, CZK – 0.1625, HUF 100 – 1.4194, BGN – 2.2589, HRK – 0.5838, BDT 100 – 5.3585, GBP 1 – 4.9115),
  - liabilities – at the selling rate applied by the Parent Company's bank as at that date (USD – 4.1826, EUR – 4.4270, RON – 0.9767, RUB – 0.0690, CZK – 0.1650, HUF 100 – 1.4254, BGN – 2.2649, HRK – 0.5868, BDT 100 – 5.3585, GBP 1 – 5.4035).
- non-monetary items – at the historical exchange rate as at the transaction date.

Earnings per share
Net earnings per share for each period are calculated by dividing net profit for a given period by the weighted average number of shares in LPP SA in the said period. As at the balance sheet date, the Capital Group examines whether, in a given period, there were any factors causing dilution of the earning/loss per share. Information on profit per share and diluted profit per share is presented in note 14.21.

Hyperinflation
According to IAS 29 “Financial Reporting in Hyperinflationary Economies”, entities running their business in a hyperinflationary economy should restate items of their share capital by applying the general inflation rate. Results of such restatement should be disclosed as negative amounts in item “Retained earnings” in the statement of financial position. This restatement is made to reflect the impact of hyperinflation on profit or loss in a given reporting period. It is assumed that, in Poland, a hyperinflationary economy was from 1989 to 1996. However, in the opinion of the Management Board, there may be doubts whether the disclosure of this hyperinflationary restatement in the statement of financial position as an accumulated loss brought forward from previous years is justified, taking into account that it refers to events which occurred before 1996, and the corresponding profits had been distributed before these financial statements were drawn up. In addition, it is not clear whether such disclosure, if any, of the hyperinflationary restatement has any effects under provisions of the Commercial Companies Code, relating to e.g. the amount of dividend to be disbursed, the amount of advance payments towards dividends, or the conditions requiring the adoption of a resolution on the entity's remaining a going concern. Therefore, the Management Board is of the opinion that the direct disclosure of this restatement in the statement of financial position drawn up as at 31 December 2016 could be misleading for the users of these financial statements, and, therefore, the Management Board presented relevant amounts, ratios and conversion methods related to the hyperinflationary restatement, in note 14.12 to the financial statements.

The financial statements of the LPP Capital Group are drawn up based on the historical cost method.

Operating segments
The scope of financial information in the segment activity reporting within the Group is determined based on the requirements of IFRS 8.
A division into geographical segments has been adopted by the Group as the main reporting arrangement, which is due to its business activity being conducted in different geographical areas.
Two segments were specified:
- business within the European Union
- business in other countries

The division into geographical segments was based on the criterion of location of the Group's assets.
Segment assets (liabilities) are operating assets (liabilities) used by the segment in its operations, which are directly attributable or allocated to a given segment based on rational prerequisites.

The segment result is determined at the level of operating profit.
Revenues, profit or loss, assets and liabilities of segments are determined before exclusion of transactions between segments, and after elimination within a segment.

10. Financial risk management

The Group is exposed to numerous risks associated with financial instruments. The Group's financial assets and liabilities, divided into categories, are presented in note 14.7. Risks affecting the Capital Group include:
- credit risk
- liquidity risk, and
- market risk including currency risk and interest rate risk.

In the operations of the LPP Capital Group, main financial instruments are, first of all, bank loans (note 14.7). Their main objective is to provide financing for the Capital Group's operations. Moreover, the Group has other financial instruments established in the course of its business operations. Those mainly include cash and deposits (note 14.10), receivables, other financial assets and trade payables (notes 14.9, 14.7 and 14.16). According to IFRS 7, an analysis has been made to review risks related to financial instruments, affecting the Capital Group.

a) Credit risk
The maximum credit risk is reflected by the balance sheet value of trade receivables, loans and guarantees granted.

Balance sheet values of the above-mentioned financial assets are given in the table below.

Items	2016	2015
Loans	195	269
Trade receivables	165 389	115 086
Cash and cash equivalents	365 753	224 447
Contingent liabilities under guarantees granted	189 904	177 953
Total	**721 241**	**517 755**

Concentration of credit risk related to trade receivables is presented in the table below.

Customer	Share of receivables (%) in total receivables
Network 360 LTD	18.14%
Customers with dues not exceeding 5% of total receivables	81.86%
Total gross trade receivables	**100.0%**

Classification of gross trade receivables by overdue period as at 31.12.2016 and 31.12.2015 is given in the table below.

in PLN '000	2016	2015
Not overdue	166 422	108 632
Overdue up to one year	11 077	16 560
Overdue for over one year	3 223	2 658
Total	**180 722**	**127 850**

Receivables outstanding for over one year and up to one year were partly written down.
No hedging instruments for the above financial risks and no hedge accounting are applied by the Capital Group.

b) Liquidity risk
The Group's objective is to maintain a balance between continuity and flexibility of funding by using funding sources such as overdrafts or investment bank credits.

Compared to the previous year, credit exposure of the Group decreased significantly due to quicker repayment of an investment credit designated for purchasing Artman shares. At the same time, the Company has taken out no new investment credits.

A detailed description of the financial position of the Group in terms of extended loans is presented in note 14.7.

As at the balance sheet date, the Group's financial liabilities fell within the following maturity ranges.

As at 31.12.2016	Short-term	Long-term
Credits in credit account	66 027	195 033
Overdrafts	249 084	
Total	**315 111**	**195 033**

As at 31.12.2015	Short-term	Long-term
Credits in credit account	101 494	284 253
Overdrafts	459 580	
Total	**561 074**	**284 253**

Liquidity risk must also include trade liabilities.

Classification of gross trade liabilities by overdue period as at 31.12.2016 and 31.12.2015 is presented in the table below.

in PLN '000	2016	2015
Not overdue	680 042	578 860
Overdue up to one year	38 818	10 984
Overdue for over one year	535	-
Total	**719 395**	**589 844**

The increase in the value of trade liabilities stems, first of all, from the increase in the volume of the Group's operations, from the increase of the USD/PLN exchange rate compared to the preceding year and prolongation of payment terms for suppliers of goods.

c) Currency risk
The basic settlement currency for a majority of transactions involving commercial goods purchases is USD. A small portion of such settlements is made in EUR.
The majority of sales earnings is obtained in PLN.

Apart from the currency risk related to the settlement currency applied for purchasing commercial goods, there is also a risk associated with the fact that commercial space rents are settled in EUR.

The Group's financial assets and liabilities denominated in two major foreign currencies and converted into PLN at the closing exchange rate applicable on the balance sheet date are as follows.

As at 31.12.2016	Values denominated in foreign currency		Value after conversion
	USD	EUR	
Cash	33 586	45 624	79 210
Trade receivables	6 139	949	7 088
Trade payables	439 454	30 236	469 690
Bank credits	5	-	5

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Exchange rate risk

+/- 5%

Balance sheet items	Value	Effect on profit/loss	Effect on profit/loss
Financial assets			
Cash	79 210	-3 960	3 960
Trade receivables	7 088	-354	354
Effect on financial assets before taxation		**-4 314**	**4 314**
Income tax (19%)		820	-820
Effect on financial assets after taxation		**-3 494**	**3 494**
Financial liabilities			
Trade payables	469 690	23 484	-23 484
Bank credits	5	0	0
Effect on financial liabilities before taxation		**23 484**	**-23 484**
Income tax (19%)		-4 462	4 462
Effect on financial liabilities after taxation		**19 022**	**-19 022**
Total		***15 528***	***-15 528***

As at 31 December 2016, net profit of the LPP Capital Group would have been higher by PLN 15 528 thousand if the Polish zloty had strengthened by 5% against foreign currencies (mainly USD), and the remaining factors did not change. This is due to a greater effect of measurement of liabilities denominated in a foreign currency on foreign receivables. The weakening of the Polish zloty by 5% vs. foreign currencies as at 31 December 2016 would have had the same effect in terms of quantity, but the opposite effect in terms of sign, on the currencies applied in the Group.

d) interest rate risk

The interest rate risk is related to the continuous use by the Capital Group of debt financing based on a variable value of Wibor, Libor and Euribor rates. Bank credits with variable interest rate involve the cash flow risk. The Management Board of the Parent Company holds the view that a change in interest rates, if any, will have no major impact on the results earned by the Group.

The tables below present the analysis of impact of interest rate changes and exchange rate changes on profit or loss and the equity capital. This analysis covers the financial items of the statement of the Group's financial position as at the balance sheet date.

Interest rate risk

+/- 75 basis points of the interest rate

Balance sheet items	Value	Effect on profit/loss	Effect on profit/loss
Financial assets			
Cash	365 753	2 743	-2 743
Loans	166	1	-1
Effect on financial assets before taxation		**2 744**	**-2 744**
Income tax (19%)		-521	521
Effect on financial assets after taxation		**2 223**	**-2 223**
Financial liabilities			
Bank credits	510 144	-3 826	3 826
Effect on financial liabilities before taxation		**-3 826**	**3 826**
Income tax (19%)		727	-727
Effect on financial liabilities after taxation		**-3 099**	***3 099***
Total		***-876***	***876***

As at 31 December 2016, the Group's net profit would have been lower by PLN 876 thousand if the interest rates in PLN, EUR and USD had been higher by 75 basis points, assuming that all the remaining parameters remain unchanged. This result is due to a higher balance of credits compared with cash and loans granted.

11. Capital management

The Group manages its capital in order to ensure both the Capital Group's ability to continue its operations and the expected rate of return for shareholders and other parties interested in the Group's financial standing.
The Group reviews indicators assessing its standing, which are presented and described in detail in the Management Board's report on the operations of the Capital Group.

12. Critical accounting estimates and judgements

Estimates affecting values disclosed in the financial statements refer to:
- estimated economic useful life of property, plant and equipment,
- residual value of property, plant and equipment as well as intangible assets,
- percentage of returns of goods sold in the reporting period, made in the next reporting period,
- revaluation write-downs,
- discount rate, the estimated increase in salaries as well as actuarial assumptions made to calculate provisions for retirement benefits,
- future tax results taken into account when calculating deferred income tax assets,
- assumptions made for reviewing trademark and goodwill impairment.

The methodology employed for determining estimated values is based on the best knowledge of the Management Board of the Parent Company and is in line with the requirements of IFRS.

The Company's tax settlements are subject to tax audit. Due to the fact that, in case of numerous transactions, the interpretation of tax laws may differ from that applied by the Management Board in the utmost good faith, amounts disclosed in financial statements may be changed at a later time upon final determination of their values by authorities authorised to carry out tax audits. Similar changes may affect, depending on future interpretations of tax authorities, the possibilities of employing tax benefits disclosed in financial statements in the form of deferred income tax assets.

Methods for determining estimated values are applied on a continuous basis versus the previous reporting period.

The following estimated values remained the same as in the previous period:
- discount rate, the estimated increase in salaries and actuarial assumptions made to calculate the amount of provisions for retirement benefits,
- future tax results taken into account when calculating deferred income tax assets.

The following estimated amounts were changed (in line with the methodology employed):
- the estimated economic useful life of property, plant and equipment – applicable to outlays in third-party facilities (determination of a new depreciation period after modernisation),
- sales adjustment ratio related to returns of goods, made in the next reporting period,
- assumptions made for reviewing trademark and goodwill impairment.

In the reporting period, revaluation write-downs were made for fixed and intangible assets, and provisions were estimated for future liquidation costs arising from the closing of stores following the decision of the Management Board of LPP SA to abandon further development of the TALLINDER brand.
The liquidation of the TALLINDER brand does not satisfy the criteria for being qualified as discontinued operations since the sales of the brand products will be continued in Q1 2017.

Due to the above-mentioned decision, as at 31 December 2016, revaluation write-downs were made in respect of the following:
- value of fixed assets calculated at the level of non-depreciated expenditures, in the amount of PLN 14 914 thousand
- value of intangible assets determined at the level of non-depreciated values of development works, copyright and computer software, in the amount of PLN 2 820 thousand

Additionally, LPP SA created the following two provisions:
■ for future liquidation and disassembly costs related to the vacating of stores, in the amount of PLN 1 226 thousand
■ for liquidated damages, if any, related to early termination of lease agreements, in the amount of PLN 1 198 thousand

Detailed changes in revaluation write-downs are presented below, in notes to specific items of assets.

13. Principles of consolidation

The consolidated financial statements of the Capital Group were drawn up based on financial statements of all its major subsidiaries, yet employing the same methods of valuation and the same principles of financial statements preparation as the Parent Company.
The consolidated financial statements of the Capital Group comprise relevant data stemming from the statements of the Parent Company and those of foreign subsidiaries, denominated in the local currency of their respective countries and converted into PLN based on the following principles:
■ specific items of assets and liabilities presented in the statement of financial position (with the exception of shareholders' equity) are converted at the average exchange rate published by the National Bank of Poland for this particular currency as at the balance sheet date;
■ specific items in the statement of financial result and other comprehensive income are converted at the exchange rate calculated as an arithmetic average of average exchange rates published by the National Bank of Poland for this particular currency on the last day of each month during the financial year;
■ specific items in the cash flow statement are converted at the exchange rate calculated as an arithmetic average of average exchange rates published by the National Bank of Poland for this particular currency on the last day of each month during the financial year;
■ shareholders' equity is converted as at the date when the control was taken over by the Parent Company, at the average exchange rate published by the National Bank of Poland for that date.

Equity includes the following separate items:

- ■ stated capital,
- ■ other equity,
- ■ treasury shares,
- ■ profit (loss) from previous years,
- ■ net financial result,
- ■ foreign exchange differences, including, in particular, foreign exchange differences resulting from different methods of conversion into PLN of the net financial result and the balance sheet, and
- ■ minority interests.

The method of full consolidation was applied.
The following adjustments and exclusions were recognised upon consolidation:

- ■ stake in shareholders' equity of subsidiaries, held by the Parent Company – not consolidated,
- ■ inter-company receivables and payables – not consolidated,
- ■ revenues and costs related to inter-company sale and purchase transactions in the Capital Group – not consolidated,
- ■ dividends paid – not consolidated,
- ■ profits and losses on inter-company transactions within the Capital Group, recognised in the carrying value of assets such as inventories and fixed assets – not consolidated,
- ■ interest on loans granted by the Parent Company to its subsidiaries - excluded from financial revenues and costs,
- ■ adjustments of the Capital Group's financial result, related to deferred income tax on account of interest on loans granted within the Group and foreign exchange differences accruing as at the balance sheet date.

Management Board of LPP SA:

Marek Piechocki – President of the Management Board ....

Przemysław Lutkiewicz – Vice-President of the Management Board ……………………………………………..

Jacek Kujawa – Vice President of the Management Board ………………………………………………

Sławomir Łoboda – Vice-President of the Management Board ....

Gdańsk, 6 April 2017

ADDITIONAL NOTES

14. Additional notes

14.1. Property, plant and equipment

In the reporting period, the Capital Group made impairment write-downs of PP&E in the amount of PLN 17 065 thousand (2015: PLN 146 thousand).
A significant increase in impairment write-downs was caused by the decision of the Management Board of LPP SA to abandon further development of the Tallinder brand (CR 46/2016).
The value of impairment write-downs of PP&E was calculated at the level of non-depreciated expenditures incurred for building Tallinder stores, which, as at 31 December 2016, amounted to PLN 14 914 thousand. The impairment write-down was made in that amount.

Compensations related to PP&E, received by the Group in 2016, amounted to PLN 119 thousand (2015: PLN 796 thousand) and were related mainly to vehicle-related damage.

As at the balance sheet date, the Group had limitations in the disposal of the real property in Pruszcz Gdański and Gdańsk due to an investment credit facility. A detailed description is provided in note 14.7.

As at 31 December 2016, the value of contractual liability to purchase PP&E was PLN 32 235 thousand (2015: PLN 21 271 thousand).
As of the balance sheet date, there were neither fixed assets designated for sale nor any discontinued operations in the Group.

The Group has no information on the fair value of second-hand tangible assets and does not disclose data in that respect.

Depreciation of PP&E is presented in a spreadsheet version of the profit and loss account, together with other expenses, in the following items:
- cost of sales - 2016: PLN 237 015 thousand (2015: PLN 198 959 thousand),
- general costs – 2016: PLN 20 610 thousand (2015: PLN 17 540 thousand).

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Changes in fixed assets (by type) in the period from 1.01.2016 to 31.12.2016

	Land	Buildings, facilities, civil engineering structures	Plant and machinery	Transportation means	Other fixed assets	Fixed assets in progress	Fixed assets, total
Opening balance gross value of fixed assets	42 814	1 221 195	334 086	9 088	443 952	25 495	2 076 630
- foreign exchange differences	0	49 036	8 498	278	26 009	962	84 783
- increase	0	164 541	42 762	1 686	96 002	251 714	556 705
- decrease	0	53 151	9 931	1 591	19 275	255 328	339 276
Closing balance gross value of fixed assets	**42 814**	**1 381 621**	**375 415**	**9 461**	**546 688**	**22 843**	**2 378 842**
Opening balance accumulated depreciation (amortisation)	0	470 275	141 144	6 160	196 959	0	814 538
- depreciation	0	126 981	45 298	1 073	84 273	0	257 625
- foreign exchange differences	0	27 752	5 589	233	17 720	0	51 294
- decrease	0	31 523	9 278	1 193	13 656	0	55 650
Closing balance accumulated depreciation (amortisation)	**0**	**593 485**	**182 753**	**6 273**	**285 296**	**0**	**1 067 807**
Opening balance impairment write-offs	0	3 183	10	0	148	0	3 341
- increase	0	12 173	576	0	4 512	0	17 261
- decrease	0	703	11	0	191	0	905
Closing balance impairment write-offs	**0**	**14 653**	**575**	**0**	**4 469**	**0**	**19 697**
Total closing balance net value of fixed assets	**42 814**	**773 483**	**192 087**	**3 188**	**256 923**	**22 843**	**1 291 338**

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Changes in fixed assets (by type) in the period from 1.01.2015 to 31.12.2015

	Land	Buildings, facilities, civil engineering structures	Plant and machinery	Transportation means	Other fixed assets	Fixed assets in progress	Fixed assets, total
Opening balance gross value of fixed assets	31 163	1 030 941	215 613	10 294	353 109	90 151	1 731 271
- foreign exchange differences	0	-26 191	-2 614	-326	-14 733	-720	-44 584
- increase	11 651	273 734	133 838	571	120 472	423 300	963 566
- decrease	0	57 289	12 751	1 451	14 896	487 236	573 623
Closing balance gross value of fixed assets	**42 814**	**1 221 195**	**334 086**	**9 088**	**443 952**	**25 495**	**2 076 630**
Opening balance accumulated depreciation (amortisation)	0	412 391	120 673	5 882	148 913	0	687 859
- depreciation	0	111 227	34 561	1 578	69 133	0	216 499
- foreign exchange differences	0	-10 619	-1 932	-180	-7 947	0	-20 678
- decrease	0	42 724	12 158	1 120	13 140	0	69 142
Closing balance accumulated depreciation (amortisation)	**0**	**470 275**	**141 144**	**6 160**	**196 959**	**0**	**814 538**
Opening balance impairment write-offs	0	4 385	21	0	169	0	4 575
- increase	0	146	0	0	0	0	146
- decrease	0	1 348	11	0	21	0	1 380
Closing balance impairment write-offs	**0**	**3 183**	**10**	**0**	**148**	**0**	**3 341**
Total closing balance net value of fixed assets	**42 814**	**747 737**	**192 932**	**2 928**	**246 845**	**25 495**	**1 258 751**

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Impairment write-downs - items in the profit and loss account - 2016	Amount
- increase – "Revaluation of non-financial assets"	17 065
- reversal – "Other operating revenues"	905

Impairment write-downs - items in the profit and loss account - 2015	Amount
- increase – "Revaluation of non-financial assets"	146
- reversal – "Other operating revenues"	538

14.2. Leased assets

The Capital Group uses PP&E under long-term lease agreements which, in accordance with IAS 17, are treated as operating leases. These agreements relate to transport vehicles only.

Outstanding future minimum lease payments as at 31.12.2016 were as follows:

Item	Minimum payments
For 1 year	1 246
Between 1 and 5 years	1 330
Over 5 years	0
Total minimum lease payments	2 580

In 2016, in the consolidated profit or loss, the Group recognised operating lease payments in the amount of PLN 1 870 thousand.
This amount comprises the minimum lease payments only.
As at 31 December 2016, there were no contingent fees or sublease payments in the Group.
The basis for determining the minimum lease payments is a monthly lease instalment.
The lessee has the right to terminate a lease agreement with a 30-days' notice. Agreements do not contain any limitations relating, for example, to dividends, additional debt or additional leasing agreements.

14.3. Intangible assets

Intangible assets used by the Capital Group include trademarks, patents and licenses, computer software, internally generated development works and other intangible assets.

The Group made outlays for development works related to the design and construction of model showrooms for RESERVED, House, Cropp, SiNSAY and TALLINDER brands. These outlays were recognized as an increase in intangible assets. As at 31 December 2016, the balance sheet value of such outlays is PLN 5 125 thousand.

Due to the decision of the Management Board to abandon further development of the TALLINDER brand, LPP SA made, in 2016, impairment write-downs of intangible assets for the amount of PLN 2 820 thousand.
The value of impairment write-downs of intangible assets was calculated in the amount of non-depreciated values of development works, copyright and computer software related to the TALLINDER brand.

The most important intangible asset is the House trademark, which was presented in the statement of financial position under a separate item of fixed assets as "Trademark". As at 31 December 2016, its carrying value amounted to PLN 77 508 thousand (2015: PLN 77 508 thousand). The useful life of the said asset is unspecified.

In the current reporting period, the Group reviewed the said asset for impairment, and it was demonstrated that there was no need for a write-down in that respect.

The detailed analysis is as follows:

The recoverable amount of cash-generating units to which a value was assigned was determined on the basis of their value in use, applying the method of licensing fees.

Detailed assumptions for the estimates are as follows:

House trademark – valued by the royalty relief method, based on the determination of the charges that would have to be paid by an external company for the privilege of using the brand. This fee is usually determined as a percentage of revenues:

- the estimate is based on sales generated by clothing under the House brand, which amounted to PLN 778 million in 2016 and was higher by 163.70% as compared to the turnover for 12 months (November 2007-October 2008), adopted for the initial balance sheet valuation,
- license fee at the rate of 3% of turnover was adopted,
- capitalisation rate adopted for the valuation applying the CAPM method (the forecast period is not defined here because it is based on the perpetual rent model) amounted to 9.57% and consisted of several elements:
  - risk-free rate – 2.95%, equal to the profitability of 52-week treasury bills
  - annual inflation rate – -0.90%
  - risk premium – 7.50%

These assumptions are based on profitability parameters of 52-week treasury bills as at the balance sheet date and a published expected inflation rate. They were included in the valuation carried out according to the model drawn up by an expert, who determined the value of the House trademark. This value was initially comprised in the statement of financial position (thus, the assumptions are consistent with external sources of information).

Upon review, it was established that the trademark's value exceeds the carrying value of these intangible assets as at the balance sheet date, and, therefore, there was no need to make any impairment write-downs.

The Group draws up a statement of financial result and other comprehensive income in the spreadsheet format. Consequently, amortisation of intangible assets is recognised in the following items:

- costs of sales in the amount of PLN 2 829 thousand (2015: 2 024 thousand),
- general administrative expenses in the amount of PLN 6 927 thousand (2015: 5 032 thousand).

As at 31 December 2016, the Group was under no contractual obligation to acquire any intangible assets.

Changes in intangible assets in 2016 and in a comparable period are specified in tables below.

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Changes in intangible assets in the period from 1.01.2016 to 31.12.2016

	Costs of completed development works	Acquired concessions, patents, licenses and similar assets, including:		Intangible assets in progress	Total
		Total	Computer software		
Opening balance gross value of intangible assets	11 163	72 182	68 650	3 919	87 264
- foreign exchange differences	0	483	483	5	488
- increase	1 420	8 179	8 179	18 730	28 329
- decrease	0	794	786	9 636	10 430
Closing balance gross value of intangible assets	**12 583**	**80 050**	**76 526**	**13 018**	**105 651**
Opening balance accumulated depreciation (amortisation)	3 200	46 722	44 726	0	49 922
- foreign exchange differences	0	425	425	0	425
- depreciation	2 225	7 531	7 211	0	9 756
- decrease	0	783	778	0	783
Closing balance accumulated depreciation (amortisation)	**5 425**	**53 895**	**51 584**	**0**	**59 320**
Opening balance impairment write-offs	0	0	0	0	0
- increase	2 033	787	514	0	2 820
Closing balance impairment write-offs	**2 033**	**787**	**514**	**0**	**2 820**
Total closing balance net value of intangible assets	**5 125**	**25 368**	**24 428**	**13 018**	**43 511**

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Changes in intangible assets in the period from 01.01.2015 to 31.12.2015

	Costs of completed development works	Acquired concessions, patents, licenses and similar assets, including:		Intangible assets in progress	Total
		Total	Computer software		
Opening balance gross value of intangible assets	4 755	60 621	57 579	6 463	71 839
- foreign exchange differences	0	-269	-269	0	-269
- increase	6 408	11 893	11 403	15 503	33 804
- decrease	0	63	63	18 047	18 110
Closing balance gross value of intangible assets	**11 163**	**72 182**	**68 650**	**3 919**	**87 264**
Opening balance accumulated depreciation (amortisation)	1 902	41 186	39 222	0	43 088
- foreign exchange differences	0	-209	-209	0	-209
- planned amortisation write-offs	1 298	5 758	5 726	0	7 056
- decrease	0	13	13	0	13
Closing balance accumulated depreciation (amortisation)	**3 200**	**46 722**	**44 726**	**0**	**49 922**
Total closing balance net value of intangible assets	**7 963**	**25 460**	**23 924**	**3 919**	**37 342**

14.4. Goodwill

In 2016, the goodwill presented in the statement of financial position did not change as compared to the previous year.

It was created as a result of the following two transactions:
- merger of LPP SA and Artman SA in July 2009, for the amount of PLN 183 203 thousand;
- acquisition of UAB House Plius upon merger of LPP SA and Artman SA, for the amount of PLN 406 thousand,
- purchase of the shares in Koba AS with its registered office in Slovakia in April 2014, for the amount of PLN 25 989 thousand.

As at 31 December 2016, the goodwill did not change and amounted to PLN 209 598 thousand.

Pursuant to IAS 36 and the accounting policy, as at 31 December 2016, the goodwill of Artman was reviewed for impairment, with the carrying value of PLN 183 203 thousand, and the goodwill of Koba was reviewed for impairment, with the carrying value of PLN 25 989 thousand.

The recoverable amount of cash-generating units, to which the goodwill was assigned, was determined on the basis of their value in use based on the discounted cash flow method (DCF).

The detailed assumptions for the estimates are as follows:

Goodwill of Artman – estimated applying the DCF method for cash flows generated by House stores acquired from Artman in 2008 (through the acquisition of Artman shares). The valuation was based on the following assumptions:

- the period covering estimated cash flows for 15 years (2017-2031), excluding the residual value,
- annual forecasts of revenues and costs in 2016 (as per the company's budget) and in subsequent years are growing at a rate similar to the inflation rate,

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- forecasts of revenues and costs for the operating retail shops acquired together with ARTMAN (32 own and 16 franchise retail shops)
- annual sales in tested retail shops – approx. 4% higher in 2017 compared to 2016, and a sales increase by approx. 4% in subsequent years
- operating costs in tested retail shops – approx. 1% higher in 2017 compared to 2016, and an increase by approx. 1% in subsequent years
- the costs of the House sales department, the House production implementation department and marketing costs of the House brand – increasing year on year by 2.0% and assigned to the tested retail shops in proportion to the number of shops acquired (and still operating) at the time of the merger to all House retail shops
- discount rate in the forecast period is variable and calculated on the basis of WACC. The WACC rate is 10.08% in 2016 and remains at that level until 2031.

The parameters adopted above are consistent with past experience (for the expenses and sales assumptions) and information deriving from external sources for other figures.

Goodwill of Koba – estimated applying the DCF method for cash flows generated by RESERVED and Cropp stores acquired from Koba in 2014 (through the acquisition of Koba shares). The valuation was based on the following assumptions:

- the period covering estimated cash flows for 15 years (2017-2031), excluding the residual value,
- annual forecasts of revenues and costs in 2016 (as per the company's budget) and in subsequent years are growing at a rate similar to the inflation rate,
- forecasts of revenues and costs for the operating retail shops acquired together with Koba (32 own retail shops)
- annual sales in tested retail shops – approx. 0.5% higher in 2017 compared to 2016, and a sales increase by approx. 0.5% in subsequent years
- operating costs in tested retail shops – approx. 2% smaller in 2017 compared to 2016, and a decrease by approx. 2% in subsequent years
- discount rate in the forecast period is variable and calculated on the basis of WACC. The WACC rate is 10.08% in 2016 and remains at that level until 2031.

Upon review, it was established that the goodwill exceeds the carrying value of such intangible assets as at the balance sheet date and, therefore, there is no need to make any impairment write-downs.
The table below presents changes in goodwill reviewed for impairment.

Gross value	31.12.2016	31.12.2015
Opening balance	209 192	209 192
Increases	0	0
Reductions	0	0
Closing balance	209 192	209 192

Impairment write-offs	31.12.2016	31.12.2015
Opening balance	0	0
Closing balance	0	0

Net value	31.12.2016	31.12.2015
Opening balance	209 192	209 192
Closing balance	209 192	209 192

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14.5. Investments in subsidiaries

The item "Shares in subsidiaries" in the statement of financial position of the Capital Group comprises only shares in non-consolidated domestic companies.
The value of the shares as at the balance sheet date amounts to PLN 136 thousand (2015: PLN 136 thousand).

Shares in subsidiaries are measured at cost less impairment write-downs. Results of the analysis carried out as at the balance sheet date showed no need for impairment write-downs for that group of assets held by the Capital Group.
In the opinion of the Management Board of the Parent Company, the financial data of non-consolidated subsidiaries are irrelevant for the consolidated financial statements. In 2016, the total value of assets of non-consolidated subsidiaries constituted 0.02% of the Group's assets, and the total value of revenues from sales of these companies constituted 0.19% of the Group's revenues.

14.6. Investments in other entities

This item comprises shares in companies outside the LPP SA Capital Group.
As at 31 December 2015, the value of those investments was PLN 1 626 thousand.

This value was established in 2013, when, by virtue of the resolution of the Cypriot government, adopted to rescue the financial situation of the country, cash held by Group on bank accounts kept by the Bank of Cyprus was converted into series A shares of the same bank.

In 2016, the Capital Group sold all shares held and, as at the balance sheet date in 2016, the value of investments in other entities was null.

14.7. Financial assets and liabilities

14.7.1. Categories of financial assets and liabilities

The value of financial assets presented in the consolidated statement of financial position relates to the following categories of financial instruments defined in IAS 39:
1. loans and receivables (L&R)
2. financial assets measured at fair value through profit or loss (AFV)
3. financial assets available for sale (AAS)

As at 31.12.2016

Fixed assets	**L&R**	**In addition to IAS 39**
Loans and receivables	5 914	
Current assets	**L&R**	**In addition to IAS39**
Trade receivables	165 389	
Other receivables		106 308
Loans	91	
Cash and cash equivalents	365 753	

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As at 31.12.2015

Fixed assets	L&R	In addition to IAS 39
Loans and receivables	5 914	
Current assets	L&R	In addition to IAS 39
Trade receivables	115 086	
Other receivables		82 227
Loans	128	
Cash and cash equivalents	224 447	

The value of financial liabilities presented in the consolidated statement of financial position refers only to one of the categories of financial instruments specified in IAS 39 as financial liabilities measured at amortised cost (LAC).

As at 31.12.2016

Long-term liabilities	LAC	In addition to IAS 39
Loans and borrowings	195 033	
Short-term liabilities	LAC	In addition to IAS 39
Trade payables	719 395	
Other liabilities	0	161 669
Loans and borrowings	315 111	

As at 31.12.2015

Long-term liabilities	LAC	In addition to IAS 39
Loans and borrowings	284 253	
Short-term liabilities	LAC	In addition to IAS 39
Trade payables	587 200	
Other liabilities	0	137 236
Loans and borrowings	561 074	

14.7.2. Loan and receivables

For the purposes of presentation in the consolidated statement of financial position, the Capital Group distinguishes the loans and receivables category (IFRS 7.6).
In the long-term part, loans and receivables are presented as one item in the statement of financial position.
In the short-term part, pursuant to IAS 1, the Group presents trade receivables and other receivables separately.
Items in the statement of financial position of the LPP Capital Group, covering loans and receivables, are given in the table below.

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	31.12.2016	31.12.2015
Fixed assets:		
Receivables	6 076	5 773
Loans	104	141
Long-term loans and receivables	**6 180**	**5 914**
Current assets		
Trade and other receivables	271 697	197 313
Loans	91	128
Short-term loans and receivables	**271 788**	**197 441**
Loans and receivables, including:	**277 968**	**203 355**
Receivables (note 14.9)	277 773	203 086
Loans (note 14.7.2)	195	269

Loans granted are measured at depreciated cost, applying the effective interest rate method. Due to the absence of an active market, it was assumed that the carrying value of loans is equal to their fair value.

As at 31 December 2016, loans granted in PLN, with the carrying amount of PLN 166 thousand (2015: PLN 226 thousand), were charged with a fixed interest rate of 6%. The maturity dates for loans in PLN fall between 2017 and 2020.

The Group also granted foreign currency loans in HUF. As at 31 December 2016, the carrying value of foreign currency loans was PLN 29 thousand (2015: PLN 43 thousand). In accordance with Hungarian laws, employees' loans are interest-fee, being extended for a period of four to seven years.

At the end of the balance sheet period, they are reviewed for impairment.
Results of the analysis carried out as at the balance sheet date showed no need to perform impairment write-downs of loans of the LPP Capital Group.

A change in the net carrying value of loans is as follows.

Gross value	31.12.2016	31.12.2015
Opening balance	269	337
Loans granted during the period	53	252
Calculation of interest	12	21
Repayment of loans and interest	137	336
Impairment write-downs	-4	5
Exchange rate differences	-2	0
Closing balance	195	269

Disclosures of cash and cash equivalents are presented in note 14.10.

14.7.3. Bank loans and borrowings and other debt instruments

The Capital Group does not recognise any credit or loan instruments in financial liabilities chosen for valuation at fair value through profit or loss. All loans and other debt instruments are measured at depreciated cost applying the effective interest rate method.

As at 31 December 2016, the debt arising from loans was as follows.

Bank	Use of bank loans as at 31 December 2016		Bank loan costs	Maturity date
	in PLN '000	currency in '000		
PKO BP SA	139 982		wibor 1 m + bank's margin	31.12.2022
PKO BP SA	76 262		wibor 1 m + bank's margin	04.08.2020
PKO BP SA	232		wibor 1 m + bank's margin	23.06.2017
Pekao SA	44 816		wibor 1 m + bank's margin	30.09.2020
Pekao SA	153 617		wibor 1 m + bank's margin	30.06.2017
Citibank Bank Handlowy	25 536		wibor 1 m + bank's margin	11.01.2018
Raiffeisen Bank Polska SA	3 806		wibor 1 m + bank's margin	30.11.2017
BGŻ BNP Paribas Bank Polska SA	65 893	USD 5	libor 1m +bank's margin	30.01.2017
Total	**510 144**			

Bank loans amounting to PLN 510 144 thousand included:
- long-term loans in the amount of PLN 195 033 thousand,
- short-term loans in the amount of PLN 315 111 thousand (including PLN 66 027 thousand as part of long-term investment loans to be repaid within 12 months after the balance sheet date)

As at 31 December 2015, the debt arising from bank loans was as follows.

Bank	Use of bank loans at 31 December 2015		Bank loan costs	Maturity date
	in PLN '000	currency in '000		
PKO BP SA	169 696		wibor 1 m + bank's margin	31.12.2022
PKO BP SA	83 397		wibor 1 m + bank's margin	31.12.2017
PKO BP SA	75 945		wibor 1 m + bank's margin	04.08.2020
PKO BP SA	37 415		wibor 1 m + bank's margin	23.06.2017
Pekao SA	56 709		wibor 1 m + bank's margin	30.09.2020
Pekao SA	134 788	USD 2 067	libor 1m + bank's margin	30.06.2016
Citibank Bank Handlowy	206 447		wibor 1 m + bank's margin	10.01.2017
BGŻ BNP Paribas Bank Polska SA	1 927		wibor 1 m + bank's margin	30.01.2017
Raiffeisen Bank Polska SA	78 590		wibor 1 m + bank's margin	30.09.2016
Unicredit Bulbank AD	413	EUR 100	euribor 1 m + bank's margin	31.05.2016
Total	**845 327**			

Bank loans amounting to PLN 845 327 thousand included:
- long-term loans in the amount of PLN 284 253 thousand,
- short-term loans in the amount of PLN 561 074 thousand (including PLN 101 494 thousand as part of long-term investment loans to be repaid within 12 months after the balance sheet date)

Long-term loans outstanding as at 31 December 2016 were as follows:
- PLN 105 489 thousand – investment loan designated for the construction of a logistics centre in Pruszcz Gdański,
- PLN 55 728 thousand - investment loan designated for financing the development of the sales network,
- PLN 33 816 thousand - investment loan designated for the modernisation of the registered office of LPP SA.

Detailed information on bank loans and multi-purpose credit lines is given below.

Bank	Type of loan /credit line	Loan amount and currency in '000	currency	Security
PKO BP SA	Multi-purpose and multi-currency credit line	280 000	PLN	2 blank promissory note, current account and currency account deductions clause
PKO BP SA	Investment loan	200 578	PLN	ordinary and capped mortgage, assignment of receivables under insurance policy, blank promissory note, current account deductions clause
PKO BP SA	Investment loan	100 000	PLN	contractual mortgage, assignment of receivables under insurance policy, blank promissory note
Pekao SA	Multi-purpose and multi-currency credit line	330 000	PLN	blank promissory note, power of attorney in respect of accounts
Pekao SA	Investment loan	60 000	PLN	contractual mortgage, assignment of receivables under insurance policy, blank promissory note, power of attorney in respect of bank accounts held in Pekao SA
BGŻ BNP Paribas Bank Polska SA	Multi-purpose and multi-currency credit line	330 000	PLN	blank promissory note
Raiffeisen Bank Polska SA	Multi-purpose and multi-currency credit line	280 000	PLN	blank promissory note, power of attorney in respect of accounts
Citibank Bank Handlowy	Multi-purpose and multi-currency credit line	244 000	PLN	blank promissory note
Citibank Bank Handlowy	Revolving line for opening letters of credit	50 700	PLN	blank promissory note
Citibank Bank Handlowy	Revolving line for stand-by letters of credit	40 000	PLN	blank promissory note
HSBC	Letters of credit line	15 000	USD	blank promissory note, power of attorney in respect of accounts
HSBC	Revolving line for bank guarantees	5 000	GBP	power of attorney in respect of accounts

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In the reporting period, as regards bank loans taken out, the Group companies were neither in default with payments nor breached the terms and conditions of contract.

14.7.4. Other information on financial instruments

Fair values, carrying values as at the balance sheet date and comparable data of specific financial instruments are given in the table below.

2016

Assets*	Fair value	Carrying amount
Trade and other receivables	271 697	271 697
Cash and cash equivalents	365 753	365 753
Total	**637 450**	**637 450**
Liabilities	**Fair value**	**Carrying amount**
Bank loans and borrowings	510 144	510 144
Trade and other liabilities	888 513	888 513
Total	**1 398 657**	**1 398 657**

2015

Assets*	Fair value	Carrying amount
Trade and other receivables	203 086	203 086
Cash and cash equivalents	224 447	224 447
Total	**427 533**	**427 533**
Liabilities	**Fair value**	**Carrying amount**
Bank loans and borrowings	845 327	845 327
Trade and other liabilities	724 436	724 436
Total	**1 569 763**	**1 569 763**

***** as reliable pricing is not possible, the table does not comprise unquoted equity instruments valued at purchase price for which there is no active market.

Fair value is defined as an amount for which, on arm's length basis, a given asset could be exchanged or a liability could be settled, between well-informed, interested and unrelated parties. As regards financial instruments for which there is an active market, their fair value is determined based on parameters deriving from the active market (sales and purchase prices). As regards financial instruments for which there is no active market, their fair value is determined on the basis of valuation techniques, where model input data is variables deriving from active markets (exchange rates, interest rates).

In the Group's opinion, the carrying value of financial assets and liabilities is close to the fair value.

14.8. Inventories

The most important item in the Capital Group's inventories is trading commodities. The structure of inventories as at the balance sheet date is given in the table below.

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Inventories	31.12.2016	31.12.2015
Materials	8 068	14 399
Goods	1 156 067	1 305 336
Total	**1 164 135**	**1 319 735**

The value of inventories disclosed in the statement of financial position was reduced by a revaluation write-down.
Changes in the value of inventory revaluation write-down in the reporting period and a comparative period are given in the table below.

Inventory revaluation write-down	31.12.2016	31.12.2015
Opening balance	22 689	18 420
Inventory write-downs included as cost in the period	47 082	9 863
Reversed write-downs in the period	11 933	3 709
Exchange rate differences	27	-1 885
Closing balance	57 865	22 689

In the reporting period, revaluation write-downs significantly increased compared to the preceding year. The reason for this situation was the decision of the Management Board of LPP SA to change valuation of revaluation write-downs in the LPP SA Group. A detailed description of the new methodology is provided for in point 4 of this report.

As at 31 December 2016, the value of inventories, recognised as cost in the reporting period, amounted to PLN 3 198 249 thousand.

14.9. Receivables

Trade and other receivables recognised by the Capital Group as loans and receivables (note 14.7) are as follows.

Long-term receivables in the carrying amount of PLN 6 076 thousand (2015: PLN 5 773 thousand) comprise only security deposits paid.

Detailed information on the structure of the Capital Group's short-term receivables is given in the table below.

Short-term receivables	31.12.2016	31.12.2015
Trade receivables	180 722	127 850
Revaluation write-downs of trade receivables	15 333	12 764
Net trade receivables	**165 389**	**115 086**
Other receivables beyond IAS 39	106 887	82 659
Revaluation write-downs of other receivables	579	432
Other receivables beyond IAS 39	**106 308**	**82 227**
Total short-term receivables	**271 697**	**197 313**

Changes in inventory revaluation write-downs in the reporting period and in a comparative period are given in the table below.

Receivables revaluation write-down	31.12.2016	31.12.2015
Opening balance	13 196	12 787
Revaluation write-downs made in the period	4 789	1 511
Reversed revaluation write-downs in the period	2 446	1 054
Exchange rate differences	373	-48
Closing balance	15 912	13 196

14.10. Cash

Cash	31.12.2016	31.12.2015
Cash at hand and in bank	297 973	222 170
Other cash	67 780	2 277
Total	**365 753**	**224 447**

"Other cash" includes short-term deposits. These deposits are established for various periods from one day to one month, depending on current needs, and are charged with interest based on agreed interest rates.

The currency structure of cash is given in the table below.

Cash - currency structure	31.12.2016	31.12.2015
In the Polish currency	71 780	45 547
In foreign currencies (by currency)	293 973	178 900
- USD	34 573	24 724
- RMB	1 868	369
- EUR	92 178	73 767
- HRK	8 738	1 736
- CZK	21 414	13 827
- UAH	6 405	7 462
- BDT	336	169
- HUF	5 098	5 864
- RUB	87 320	19 116
- BGN	10 151	8 314
- RON	25 526	23 552
- GBP	366	0
Total (in PLN '000)	**365 753**	**224 447**

As at 31 December 2016, the Group had unemployed loans in the amount of PLN 794 719 thousand.
In the period from 1 January 2016 to 31 December 2016, the Capital Group made non-cash settlements with its customers (by setting off liabilities and receivables) in a total amount of PLN 36 379 thousand.

For the purpose of preparing the cash flow statement, the Capital Group classifies cash in the manner adopted for presenting financial position. The difference in the value of cash shown in the statement of financial position and the cash flow statement is affected by the following.

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	31.12.2016	31.12.2015
Cash and cash equivalents in the statement of financial position	365 753	224 447
Adjustments:		
Exchange differences from balance sheet valuation of cash in foreign currency	273	-1 394
Cash and cash equivalents recognised in CF	**366 026**	**223 053**

14.11. Discontinued operations

In 2016, the Group had no discontinued operations.

14.12. Equity capital

Stated capital

The Group's stated capital is equal to the share capital of the parent company.
As at 31 December 2016, the stated capital amounted to PLN 3 678 582. It was divided into 1 839 291 shares of a nominal value of PLN 2 per share.

The table below shows a total number of shares divided into separate issues.

Series/issue	Type of share	Type of privilege	Type of limitation on rights attached to shares	Number of shares	Value of the issue
A	bearer	ordinary	none	100	200
B	registered	preferred	none	350 000	700 000
C	bearer	ordinary	none	400 000	800 000
D	bearer	ordinary	none	350 000	700 000
E	bearer	ordinary	none	56 700	113 400
F	bearer	ordinary	none	56 700	113 400
G	bearer	ordinary	none	300 000	600 000
H	bearer	ordinary	none	190 000	380 000
I	bearer	ordinary	none	6 777	13 554
J	bearer	ordinary	none	40 000	80 000
K	bearer	ordinary	none	80 846	161 692
L	bearer	ordinary	none	8 168	16 336
Total number of shares				**1 839 291**	

All issued shares are paid up in full.
In the reporting period, LPP SA paid dividends to its shareholders. Part of the profit earned in 2015, in the amount of PLN 59 935 557, was allocated to dividends, which corresponded to PLN 33.00 per eligible share. The amount of PLN 48 385 557 was allocated to ordinary shares, and PLN 11 550 000 – to preferred shares.
Registered shares held by Marek Piechocki, Jerzy Lubianiec and Forum 64 Closed-End Investment Fund and Forum 65 Closed-End Investment Fund, in a total number of 350 000, are preferred in terms of voting rights at the General Meeting of Shareholders. Each registered share gives 5 votes.

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As at 31 December 2016, the ownership structure of the share capital of LPP SA is as follows.

Shareholder	Number of shares held	Share in the share capital	Number of votes at the GM	Share in the total number of votes at the GM	Nominal value of shares
Marek Piechocki	175 497	9.5%	875 493	27.2%	350 994
Jerzy Lubianiec	174 999	9.5%	874 995	27.2%	349 998
Forum TFI SA*	200 730	10.9%	200 738	6.2%	401 460
Treasury stock	18 978	1.0%	0**	0.0%	37 956
Other shareholders	1 269 087	69.0%	1 269 087	39.4%	2 538 174
Total	**1 839 291**	**100.0%**	**3 220 313**	**100.0%**	**3 678 582**

*Forum TFI SA manages the funds of Forum 64 Closed-End Investment Fund (entity affiliated with Mr Jerzy Lubianiec, shareholder of LPP SA) and Forum 65 Closed-End Investment Fund (entity affiliated with Mr Marek Piechocki, shareholder of LPP SA).
The Funds managed by Forum TFI SA hold directly 195 050 shares in LPP SA and indirectly 5 680 shares in LPP SA.
** LPP SA may not exercise voting rights at the GM, attached to 18 978 shares, as these are treasury shares of LPP SA.

In the reporting period, there were the following changes in the ownership structure of the share capital of LPP SA, of which the Company informed on 8 January 2016 in CR 02/2016, on 21 October 2016 in CR 50/2016 and on 27 December 2016 in CR 60/2016.

The share capital of LPP SA was increased due to the exercise of the rights to convert 8 168 subscription warrants of the A series to ordinary bearer shares of the L series (CR 02/2016, CR 50/2016).

FORUM 64 Closed-End Investment Fund, managed by FORUM TFI, acquired from its subsidiary i.e. Hoja SCSp with its registered office in Luxemburg 51 338 book-entry shares and 1 registered share, that is, in total, 51 339 shares in the Company.
FORUM 65 Closed-End Investment Fund, managed by FORUM TFI, acquired from its subsidiary i.e. Quarter SCSp with its registered office in Luxemburg 143 710 book-entry shares and 1 registered share, that is, in total,143 711 shares in the Company (CR 60/2016).

Share premium
The separated value of the spare capital, resulting from the surplus at the sale of shares beyond their nominal value, with the carrying value of PLN 251 393 thousand.

Other capital
The value of other capital results from the sum of spare capital, reserve capital, capital from settling the merger transaction and the equity component of convertible bonds.

The values of specific types of capital are given in the table below.

Type of capital	31 December 2016	31 December 2015
Spare capital	1 579 875	1 302 963
Reserve capital	17 543	9 893
Capital from settling the merger transaction	-1 410	-1 410
Capital component of convertible bonds	12 290	12 290
Total	**1 608 298**	**1 323 736**

The spare capital, presented under equity as at 31 December 2016, was created mainly from net profit brought forward from previous years and following the measurement of share-based payments.
Part of the spare capital created under statutory law, by virtue of Article 396 of the Commercial Companies Code, may be appropriated in the future only to cover a loss (if any).

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The structure of the spare capital is as follows.

Type of spare capital	31 December 2016	31 December 2015
Created under statutory law based on the write-off from profit or loss	1 335	1 335
Created according to the Articles of Association based on write-off from profit or loss	1 544 819	1 267 907
Created from share-based payments	33 721	33 721
Total	**1 579 875**	**1 302 963**

Company's equity in the hyperinflation period

Equity conversion in the hyperinflation period was based on the following data:
1. 18 December 1989 - establishment of the company and contribution of share capital in the amount of (after denomination) PLN 200
2. 4 May 1995 - acquisition of the company by Marek Piechocki and Jerzy Lubianiec
3. 12 April 1995 - registration of the increase of the stated capital up to PLN 700 thousand
4. 24 October 1995 - adoption of the resolution on the increase of the stated capital to PLN 1 500 thousand
5. 4 January 1996 – adoption of the resolution on the increase of the stated capital to PLN 2 200 thousand

Year	Opening balance equity	Increases	Inflation	Days	Inflation rate	Capital after conversion
1990	0.2		585.8%	365	6.858	1.4
1991	1.4		70.3%	365	1.703	2.3
1992	2.3		43.0%	365	1.430	3.3
1993	3.3		35.3%	365	1.353	4.5
1994	4.5		32.2%	365	1.322	5.9
1 January 1995	5.9		27.8%	365	1.278	7.6
12 April 1995		700	27.8%	263	1.200	840
24 October 1995		800	27.8%	68	1.052	841
TOTAL 1995						1 689
1 January 1996	1 916[1)]		19.9%	365	1.199	2 298
4 January 1996		1 400[2)]	19.9%	362	1.197	1 676
Total 1996						3 974

[1)] equity at the end of 1995 + retained result for 1995
[2)] capital increase + aggio

As at 31 December 1996 (excluding profit for the financial year), the equity amounted to PLN 3 127 thousand. The difference resulting from equity revaluation was PLN 847 thousand.

14.13. Provisions

As at the balance sheet date, the Capital Group has the following categories of provisions in its liabilities in the statement of financial position:
- long-term – provisions for employee benefits, in the amount of PLN 2 711 thousand
- short-term – other provisions in the amount of PLN 33 607 thousand

Provisions and changes in the reporting period are listed in the table below.

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	Provision for retirement and other benefits	Provision for unpaid remuneration	Provision for unused holiday leave	Provision for other costs
As at 1 January 2016	2 179	4 337	13 437	0
- provisions made	2 711	10 531	17 955	5 121
- provisions reversed	2 179	4 337	13 437	0
As at 31 December 2016	2 711	10 531	17 955	5 121

In the reporting period, the provision for unpaid remuneration increased substantially due to the estimation of a bonus for the second half of 2016, to be disbursed in Q1 2017.
Additionally, LPP SA made two provisions based on the decision of the Management Board to abandon further development of the Tallinder brand (CR 46/2016). At the end of 2016, the value of those provisions was PLN 2 423 thousand, and they were as follows:

- provision for future liquidation and disassembly costs related to the vacating of stores, in the amount of PLN 1 226 thousand
- provision for liquidated damages, if any, related to early termination of lease agreements, in the amount of PLN 1 198 thousand.

14.14. Contingent liabilities

In 2016, the LPP SA Capital Group companies used bank guarantees to secure payment of rent for leased retail premises in which brand stores are located.
As at 31 December 2016, the total value of bank guarantees issued upon request and at the responsibility of LPP SA amounted to PLN 261 218 thousand, of which:

- guarantees issued to secure agreements concluded by LPP SA amounted to PLN 77 927 thousand,
- guarantees issued to secure agreements concluded by consolidated associates amounted to PLN 181 262 thousand,
- guarantees issued to secure agreements concluded by non-consolidated associates amounted to PLN 1 720 thousand,
- guarantees issued to secure warehouse space lease agreements concluded by LPP SA amounted to PLN 309 thousand.

In 2016, the Company also received guarantees as a collateral for payments from a contracting party. The value of guarantees received is PLN 21 908 thousand.

In the reporting period, the value of guarantees granted by the Parent Company amounted to PLN 109 948 thousand as at 31 December 2016, and it increased as compared to 31 December 2015 by PLN 4 374 thousand.

In the opinion of the Management Board, any outflow of funds disclosed under off-balance sheet/contingent liabilities is very unlikely. The majority of these liabilities are related to guarantees securing payment of rent by entities of the LPP SA Capital Group.

14.15. Future liabilities under lease agreements

The LPP SA Capital Group is party to lease agreements for retail premises in which RESERVED, Cropp, House, MOHITO, SiNSAY and Tallinder brand stores are located.

The value of rents charged to costs of the period amounts to PLN 873 585 thousand**.** This amount comprises both the minimum and contingent rents, depending on the amount of turnover achieved.

Total future minimum payments under lease agreements, estimated as at 31 December 2016, are as follows:

- payables maturing within 12 months after the balance sheet date: PLN 873 646 thousand
- payables with a maturity date between 12 months and 5 years from the balance sheet date: PLN 2 536 618 thousand
- payables maturing within more than 5 years from the balance sheet date: PLN 1 453 483 thousand

The provisions of fixed-term lease agreements providing for the said payments are standard ones. Apart from the minimum rent, these agreements usually provide for additional contingent rent if a specific level of revenues in a given store is exceeded, given as percentage value of such revenues. The agreements contain also adjustment clauses under which the value of rent is matched with statistical price indices. Some of them contain provisions permitting prolongation of a lease agreement for a subsequent period, leaving a decision in that respect to the lessee. As these agreements involve premises located mainly in large shopping centres, they do not provide for the option of purchasing the leased premises.

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14.16. Trade and other liabilities

Short-term liabilities	31.12.2016	31.12.2015
Trade payables	719 395	589 844
Other financial liabilities	0	0
Financial liabilities according to IAS 39	**719 395**	**589 844**
Payables due under taxes and other benefits	154 904	130 598
Other non-financial liabilities	14 214	3 994
Non-financial liabilities beyond IAS 39	**169 118**	**134 592**
Total short-term liabilities	**888 513**	**724 436**

The increase of approx. 20% in the value of trade liabilities as compared to the preceding year stems, first of all, from the increase in the volume of the Group's operations, from the increase of the USD/PLN exchange rate and prolongation of payment terms for suppliers of goods.

14.17. Accruals and prepayments

Prepayments - assets	31.12.2016	31.12.2015
Long-term		
Commissions for intermediaries	60 055	66 406
Loss on sale of investments	5 806	0
Software supervision	733	449
Other	142	72
Total long-term prepayments	**66 736**	**66 927**
Short-term		
Rent	18 740	16 657
Commissions for intermediaries	6 474	3 026
Insurance	3 830	1 852
Licence fees, subscription fees, Internet domains	3 391	2 589
Loss on sale of investments	2 224	0
Software supervision	1 172	585
Power supply costs	412	427
Other	1 349	1 414
Total short-term prepayments	**37 592**	**26 550**

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Accruals - liabilities	31.12.2016	31.12.2015
Long-term		
Profit on sales of investments	53 870	35 242
Subsidies for lease agreements	11 705	15 324
Sale of marketing services	0	515
Total long-term accruals	**65 575**	**50 566**
Short-term		
Sales based on gift cards and vouchers	16 586	13 897
Profit on sales of investments	14 609	7 466
Returns of products sold domestically	4 566	3 911
Sale of marketing services	527	531
Subsidies for lease agreements	2 428	2 031
Total short-term accruals	**38 716**	**27 836**

Prepayments on assets increased, first of all, due to the increase in the volume of the Group's operations and, consequently, due to the increase in running costs and those settled over time.
In the reporting period, accruals also increased due to the increase in the sale of investments in third-party facilities, with profit or loss on such sale settled over time.

14.18. Revenues

Sale revenues	01.01.2016-31.12.2016	01.01.2015-31.12.2015
Net revenues from sales of services	21 602	23 833
Net revenues from sales of goods and materials	5 997 444	5 106 520
Total sales revenues	**6 019 046**	**5 130 353**

The revenues from the sales of services are generated only by the parent company, that is:
- sale of services provided to franchisees operating Polish brand stores: know-how, marketing and telecommunications services;
- sale of services covering support for operation of retail stores to foreign franchisees;
- lease by LPP SA of own means of transportation, sublease of real property, design services.

Other operating income	01.01.2016-31.12.2016	01.01.2015-31.12.2015
Profit from the disposal of non-financial fixed assets	0	805
Subsidies	398	451
Other operating income, including:	39 026	22 975
- reversal of write-downs of fixed assets	837	538
- reversal of write-downs of receivables	1 218	474
- reversal of write-downs of inventories	11 933	3 709
Total operating income	**39 424**	**24 231**

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Financial revenue	01.01.2016-31.12.2016	01.01.2015-31.12.2015
Interest, including:	854	1 794
- on deposits	547	5
- on loans and receivables	307	1 786
- on bonds	0	3
Dividends	176	182
Profit from the disposal of investments	4	0
Other, including:	273	5
- disposal of liabilities	272	5
Total financial revenue	**1 307**	**1 981**

14.19. Costs

Costs by type	01.01.2016-31.12.2016	01.01.2015-31.12.2015
Depreciation	267 381	223 555
Consumption of materials and energy	152 051	137 275
Outsourced services	1 581 650	1 374 997
Taxes and fees	20 709	16 308
Remuneration	388 993	284 173
Social insurance and other benefits, including:	76 367	61 695
- retirement contribution	10 349	7 785
Other expenses by type	120 860	96 650
Total expenses by type	**2 608 011**	**2 194 653**

Reconciliation of expenses by nature and function is given in the table below:

	01.01.2016-31.12.2016	01.01.2015-31.12.2015
Expenses by type	2 608 011	2 194 653
Change in products	795	792
Value of costs of sales and general administrative expenses	**2 608 806**	**2 195 445**

Other operating expenses	01.01.2016-31.12.2016	01.01.2015-31.12.2015
Loss on disposal of non-financial assets	838	0
Revaluation of non-financial assets, including:	71 684	11 374
- fixed assets	16 993	146
- intangible assets	2 820	0
- inventories	47 082	9 863
- receivables	4 789	1 365
Other, including:	65 485	61 330
- losses on current and fixed assets	59 571	52 711
Total operating expenses	**138 007**	**72 704**

In the reporting period, as compared to the preceding year, revaluation write-downs of inventories and fixed assets increased substantially. That is caused by the decision of the Management Board of LPP SA to change the valuation of revaluation write-downs in the LPP SA Group and to abandon further development of the TALLINDER brand. A detailed description of the new methodology adopted for valuating revaluation write-downs of inventories is provided in point 4 of this report.

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Financial expenses	01.01.2016-31.12.2016	01.01.2015-31.12.2015
Interest, including:	22 596	19 061
- on bank loans	22 442	19 061
Revaluation of investments	167	731
- shares	167	731
Other, including:	10 887	70 510
- commissions on bank loans	3 626	1 914
- balance of foreign exchange differences	7 261	68 596
Total financial expenses	**33 650**	**90 302**

14.20. Income tax

The major elements of the Group's income tax for 2016 and for a comparative period are given in the table below.

Income tax	2016	2015
Current income tax	26 596	56 053
Deferred income tax	-7 293	6 995
Total income tax	**19 303**	**63 048**

The reconciliation of income tax calculation disclosed in the consolidated statement of financial result and other comprehensive income for 2016 and 2015 is given in the table below.

Income tax	2016	2015
Gross profit/loss of the Group before consolidation adjustments	497 570	605 362
Adjustment of permanently tax-exempt expenses and revenues	-336 995	-288 472
Gross profit/loss of the Group after adjustment	160 575	316 890
Income tax at the average rate*	38 173	64 535
Tax consolidation adjustments	-17 390	-263
Tax reliefs	- 1 480	-1 224
Income tax	**19 303**	**63 048**

*2015 – 20.36%; 2016 – 23.77%

Income tax is calculated based on the following rates:
- LPP SA – 19%,
- Re Trading OOO (Russia) – 20%,
- LPP Deutschland GmbH – 32%,
- LPP Lithuania UAB (Lithuania) – 15%,
- LPP Latvia LTD (Latvia) – 15%,
- LPP Ukraina AT – 18%
- LPP Hungary KFT (Hungary) – 10%
- LPP Estonia OU – 20%
- LPP Czech Republic SRO (Czech Republic)– 19%
- LPP Bulgaria LTD – 10%
- LPP Slovakia SRO– 22%

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- LPP Romania Fashion SRL (Romania) – 16%
- LPP Croatia DOO – 20%
- Gothals LTD (Cyprus) – 12.5%

The amount of deferred income tax assets and liabilities, recognised in the statement of financial position, results from items and values given in the table below.

Deferred income tax assets	31.12.2016	31.12.2015
Depreciation of fixed assets	23 045	12 592
Depreciation of trademarks	96 224	101 569
Revaluation of trade receivables	249	398
Revaluation of inventories	1 539	2 240
Margin on goods unsold outside the Group	5 948	12 039
Margin on the sale of investments	10 349	5 907
Tax loss	0	433
Remuneration and surcharges	3 014	1 648
Estimated returns of goods	1 086	865
Estimated expenses	1 107	1 163
Other	1 096	340
Total	**143 657**	**139 194**

Deferred income tax liabilities	31.12.2016	31.12.2015
Depreciation of intangible assets	3 653	4 940
Estimate of rent costs	0	1 077
Outstanding damages	160	131
Accrued interest on bank loans and borrowings	77	239
Adjustments received in the following year	0	692
Other	0	6
Total	**3 890**	**7 085**

Deferred income tax shown in the statement of financial result and other comprehensive income for the period from January to December 2016 and 2015 results from the following items:

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Deferred income tax assets	31.12.2016	31.12.2015
Depreciation of fixed assets	10 453	1 032
Depreciation of trademarks	-5 345	-5 346
Revaluation of trade receivables	-149	-344
Revaluation of inventories	-701	809
Margin on goods unsold outside the Group	-6 091	1 650
Margin on the sale of investments	4 442	5 907
Tax loss	-433	-8 865
Remuneration and surcharges	1 366	188
Estimated returns of goods	221	78
Estimated expenses	-56	0
Other temporary differences	756	555
Foreign exchange differences from translation	-360	-231
Total	**4 103**	**-4 567**

Deferred income tax liability	31.12.2016	31.12.2015
Accelerated tax depreciation	-1 287	546
Estimate of rent costs	-1 077	1 077
Outstanding damages	29	-2
Accrued interest on bank loans	-162	188
Adjustments received in the following year	-692	692
Other	-6	-73
Foreign exchange differences from translation	5	0
Total	**-3 190**	**2 428**

14.21. Earnings per share and diluted earnings per share

The earnings per share (EPS) ratio is calculated by dividing net profit allocated to the parent company's shareholders by the weighted average number of ordinary shares in a given period.
While calculating both basic and diluted profit (loss) per share, LPP SA applies, in the numerator, the amount of profit (loss) allocated to shareholders of the parent company i.e. there is no dilutive effect impacting the amount of profit (loss).
While calculating diluted earnings per share, the denominator accounts for a dilutive effect of stock options convertible into shares.
The EPS calculation is given below.

	01.01.2016-31.12.2016	01.01.2015-31.12.2015
Number of shares in the denominator in the formula		
Weighted average number of ordinary shares	1 816 932	1 812 145
Dilutive effect of stock options convertible into shares	8 093	15 388
Diluted weighted average number of ordinary shares	1 825 025	1 827 533
Earnings per share		
Net profit (loss) for the current period	174 775	351 320
Profit (loss) per share	96.19	193.87
Diluted profit (loss) per share	95.77	192.24

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14.22. Transactions with associates

The following companies have been recognised as the Group's associates:
- foreign and Polish companies controlled by the Group companies having direct shareholdings in such companies,
- key management personnel of LPP SA Capital Group and their close family members,
- entities controlled or significantly influenced by key management personnel or their close family members

14.22.1. Transactions with key management personnel

The Group's key management personnel includes members of the Management Board and the Supervisory Board of the Parent Company.

The Management Board members received remuneration for their functions served both in LPP SA and in its subsidiary IPMS.

The value of short-term benefits of members of the Management Board of the Parent Company, received between 1 January and 31 December 2016, amounted to PLN 2 995 thousand.
Remunerations shown separately for each person being a member of key management personnel were as follows.

Name and surname	Position	Remuneration for 2016
Marek Piechocki	President of the Management Board	PLN 765 thousand
Przemysław Lutkiewicz	Vice-President of the Management Board	PLN 548 thousand
Piotr Dyka*	Vice-President of the Management Board	PLN 191 thousand
Hubert Komorowski**	Vice-President of the Management Board	PLN 471 thousand
Jacek Kujawa	Vice-President of the Management Board	PLN 510 thousand
Sławomir Łoboda	Vice-President of the Management Board	PLN 510 thousand

*Piotr Dyka, Vice-President of the Management Board, resigned from his position of member of the Management Board of LPP SA on 17 March 2016. The remuneration shown covers the period of his sitting on the Company's board.
**Hubert Komorowski, Vice-President of the Management Board, resigned from his position of member of the Management Board of LPP SA on 6 September 2016. The remuneration shown covers the period of his sitting on the Company's board.

The value of short-term benefits of members of the Supervisory Board of the Parent Company, received between 1 January and 31 December 2016, amounted to PLN 184 thousand.
Remunerations shown separately for each person being a member of the Supervisory Board were as follows.

Name and surname	Position	Remuneration for 2016
Jerzy Lubianiec	Chairman of the Supervisory Board	PLN 80 thousand
Maciej Matusiak	Member of the Supervisory Board	PLN 20 thousand
Wojciech Olejniczak	Member of the Supervisory Board	PLN 20 thousand
Krzysztof Olszewski	Member of the Supervisory Board	PLN 20 thousand
Dariusz Pachla	Member of the Supervisory Board	PLN 44 thousand

For members of the Management Board of LPP SA as at 31 December 2016, provisions accrued for retirement allowances in the amount of PLN 18 thousand (2015: PLN 23 thousand) and for unused holiday leaves in the amount of PLN 149 thousand (2015: PLN 136 thousand).

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14.22.2. Transactions with associates

No.	Associates	Liabilities as at 31.12.2016	Receivables as at 31.12.2016	Revenues in 2016	Expenses in 2016
1.	Polish subsidiaries	94	1	14	9 742
Total		**94**	**1**	**14**	**9 742**

No.	Associates	Liabilities as at 31.12.2015	Receivables as at 31.12.2015	Revenues in 2015	Expenses in 2015
1.	Polish subsidiaries	0	8	14	9 885
Total		**0**	**8**	**14**	**9 885**

The figures given in the table reflect only transactions between LPP SA and non-consolidated Polish subsidiaries, and they are presented from the parent company's perspective.
Data presented as liabilities of LPP SA are receivables in associates, while expenses are revenues of given companies.
All transactions with associates were concluded on arm's length basis.

Revenue from domestic companies is earned from the lease of office space for the purposes of their operation. Expenses related to the domestic subsidiaries involve the lease of real properties where Cropp and RESERVED, MOHITO and House stores are operated.

Payment terms agreed for subsidiaries are between 45 and 120 days.

14.22.3. Transactions with associates through key management personnel

In 2016, LPP SA entered into transactions with BBK SA, controlled by members of key management personnel. These transactions mainly involved the lease of retail space in “Wars&Sawa” commercial centre, with a minor involvement of the sale of trading commodities.

No.	Associates	Liabilities as at 31.12.2016	Receivables as at 31.12.2016	Revenues in 2016	Expenses in 2016
1.	BBK SA	0	4	586	0
Total		**0**	**4**	**586**	**0**

14.23. Operational segments

Financial results and other information on geographical segments for the period from 1 January 2016 to 31 December 2016 and for a comparative period are given in the tables below.

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2016

	EU Member States	Other countries	Consolidation adjustments	Values not attributed to segments	Total
External sales	4 865 748	1 153 298	0	0	6 019 046
Inter-segment sales	649 505	636	(650 141)	0	-
Other operating income	35 560	3 864	0	0	39 424
Total revenue	**5 550 813**	**1 157 798**	**(650 141)**	**0**	**6 058 470**
Total operating expenses, including	5 023 983	1 148 161	(681 901)	203 799	5 694 042
Costs of inter-segment sales	560 400	636	(561 036)	0	-
Other operating expenses	78 038	59 131	0	838	138 007
Segment result	**448 792**	**(50 130)**	**31 760**	**(204 637)**	**226 421**
Financial revenue					1 307
Financial expenses					22 650
Profit before taxation					**194 078**
Income tax					19 303
Net profit					**174 775**

	EU Member States	Other countries	Consolidation adjustments	Values not attributed to segments	Total
Segment assets	3 006 100	592 318	(64 338)	0	3 534 080
Unallocated assets across the group	0	0	0	143 852	143 852
Consolidated total assets	**3 006 100**	**592 318**	**(64 338)**	**143 852**	**3 677 932**
Segment liabilities	964 314	102 223	(37 370)	0	1 029 167
Unallocated liabilities across the group	0	0	0	514 034	514 034
Consolidated total liabilities	**964 314**	**102 223**	**(37 370)**	**514 034**	**1 543 201**

Other disclosures	EU Member States	Other countries
Segment capital expenditures	212 887	58 943
Segment depreciation	216 212	51 169
Impairment write-downs	31 627	40 224
Reversal of impairment write-downs	11 545	2 443
Other non-cash expenses	48 058	19 427

Consolidated annual report of LPP SA Capital Group for 2015, in PLN '000

2015

	EU Member States	Other countries	Consolidation adjustments	Values not attributed to segments	Total
External sales	4 105 749	1 024 604	0	0	5 130 353
Inter-segment sales	655 459	0	(655 459)	0	-
Other operating income	17 684	5 742	0	805	24 231
Total revenue	**4 778 892**	**1 030 346**	**(655 459)**	**805**	**5 154 584**
Total operating expenses, including	4 106 038	891 743	(597 837)	179 247	4 579 191
Costs of inter-segment sales	480 055	0	(480 055)	0	-
Other operating expenses	49 668	23 036	0	0	72 704
Segment result	**623 186**	**115 567**	**(57 622)**	**(178 442)**	**502 689**
Financial revenue					1 981
Financial expenses					90 302
Profit before taxation					**414 368**
Income tax					63 048
Net profit					**351 320**

	EU Member States	Other countries	Consolidation adjustments	Values not attributed to segments	Total
Segment assets	3 122 773	500 028	(197 095)	0	3 425 706
Unallocated assets across the group	0	0	0	139 463	139 463
Consolidated total assets	**3 122 773**	**500 028**	**(197 095**	**139 463**	**3 565 169**
Segment liabilities	787 101	174 903	(138 986)	0	823 018
Unallocated liabilities across the group	0	0	0	852 412	852 412
Consolidated total liabilities	**787 101**	**174 903**	**(138 986)**	**852 412**	**1 675 430**

Other disclosures	EU Member States	Other countries
Segment capital expenditures	409 210	40 905
Segment depreciation	175 424	48 131
Impairment write-downs	8 230	3 875
Reversal of impairment write-downs	4 523	198
Other non-cash expenses	42 210	19 120

*Impairment write-downs of assets by segments, shown in the statement of financial result and other comprehensive income, include:

- revaluation write-downs of receivables;
- revaluation write-downs of inventories;
- revaluation write-downs of assets.

Impairment write-downs and their reversal were due to the occurrence or cessation of grounds for overdue receivables and the occurrence of bad debts.

Management Board of LPP SA:

Marek Piechocki – President of the Management Board ....

Przemysław Lutkiewicz – Vice-President of the Management Board …..…………………………………..

Jacek Kujawa – Vice President of the Management Board ……..…………………………………

Sławomir Łoboda – Vice-President of the Management Board …………………………………………

Gdańsk, 6 April 2017

IV. Management Board Report on the operations of the LPP SA Capital Group (including a declaration of corporate governance) for 2016

(with due consideration of disclosure requirements for the Report on the operations of the Parent Company in the said period)

1. Introduction

This Report of the Management Board on the operations of the LPP SA Capital Group for 2016 incorporates information the scope of which has been set forth in §§ 91 - 92 of the Regulation of the Minister of Finance, dated 19 February 2009, on current and interim information provided by issuers of securities […] (the Regulation).
Under § 83 subparagraph 7 of the Regulation, this report comprises also disclosures required for the Report on the operations of the Parent Company, referred to in § 91 subparagraph 1 point 4 of the Regulation.
The consolidated annual report, comprising consolidated financial statements and this report on the operations, was drawn up under § 91 and § 92 in connection with § 82 subparagraph 1 point 3 and § 82 subparagraph 2 of the Regulation.
The rules for drawing up annual financial statements have been provided for in subsequent notes to these statements.

2. Operating information

2.1. Composition of the LPP SA Capital Group

The LPP SA Capital Group is composed of 5 Polish companies (including the parent company) and 19 foreign companies.

The consolidated financial statements of the LPP SA Capital Group, covering the period between 1 January and 31 December 2016, include separate results of LPP SA and the results of foreign subsidiaries listed below:

- LPP Estonia OU
- LPP Czech Republic SRO
- LPP Hungary KFT
- LPP Latvia LTD
- LPP Lithuania UAB
- LPP Ukraina AT
- Re Trading OOO
- LPP Romania Fashion SRL
- LPP Bulgaria EOOD
- LPP Slovakia SRO
- LPP Fashion Bulgaria EOOD
- Gothals LTD
- LPP Croatia DOO
- LPP Deutschland GMBH
- IPMS Management Services FZE
- LPP Reserved UK LTD
- LLC Re Development
- LLC Re Street

The consolidated financial statements of the Capital Group for the period between 1 and 31 December 2016 does not comprise the consolidation of LPP Reserved DOO Beograd, a subsidiary with its registered office in Serbia, as this company does not conduct any operating activity yet. The financial statements of the Capital Group neither incorporate the consolidation of Polish subsidiaries of LPP SA due to the irrelevance of data. This is compliant with the Accounting Policy adopted by the Group.

2.2. Information on the basic operations of the LPP Capital Group

LPP SA, as a parent company, is involved in the design and distribution of clothing in Poland and the countries of Central, Western and Eastern Europe, in the Balkans and in the Middle East. The Group companies being consolidated are involved in the distribution of goods under the RESERVED, Cropp, House, MOHITO and SiNSAY brands outside Poland.

Clothing is the basic commodity sold by the LPP SA Capital Group companies. Footwear, bags and clothing accessories are sold as products supplementing the basic offer of the Capital Group companies.
Designs of clothing are prepared in the LPP design offices located in Gdańsk (in the registered office of the Parent Company), Cracow and Warsaw, and then transferred to the purchasing department which orders the

production of specific models, cooperating in this respect with manufacturing plants in Poland and abroad (in, among others, China and Bangladesh).
Production in China is distributed through the Company's trading office in Shanghai, while the Company's trading office in Dhaka is responsible for coordinating and supervising production in Bangladesh.
A major task of the office in Bangladesh is the regular auditing of manufacturing plants in terms of adequate working conditions and respect for human rights.
The Capital Group also generates revenues from the sale of services (these are, in total, revenues of the parent company, covering mainly services relating to know-how on the operation of brand stores by domestic contracting parties and the lease of transportation means).
An additional object of business in the Group is the management of the RESERVED, Cropp, House, MOHITO and SiNSAY trademarks, including their protection, activities aimed at increasing their value, the granting of licences for use etc. Gothals Limited in Cyprus and IPMS in UAE were established for that purpose.
Four domestic subsidiaries are engaged in the lease of real properties where the stores of Cropp, RESERVED, House and MOHITO are operated.

Source of revenues	2015		2016		Change
	in PLN '000	Share in sales volume %	in PLN '000	Share in sales volume %	%
Sales of trading commodities	5 106 520	99,5%	5 997 444	99,6%	17,4%
Sales of services	23 833	0,5%	21 602	0,4%	-9,4%
Total	**5 130 353**	**100,0%**	**6 019 046**	**100,0%**	**17,3%**

The main distribution channels guaranteeing the development of the Capital Group are chains of RESERVED, Cropp, House, MOHITO, SiNSAY and Tallinder stores and on-line stores of each of the above-listed brands. Individual customers are the recipients of products both in regular and online stores.

2.3. Information in supply sources and sales markets

The majority of companies manufacturing goods for the LPP SA Capital Group have their registered offices in China. Purchases made in 2016 in that country amounted for approx. 55.8%, and in other Asian countries – for approx. 31,5%. Furthermore, the Capital Group purchased goods from Turkish (approx. 8.9%) and Polish manufacturers (approx. 1.5%).
The value of purchases made from a single manufacturer did not exceed 10% of sales.
The Capital Group concluded framework agreements setting forth cooperation terms and conditions. Specific goods are manufactured for the LPP SA Capital Group under detailed agreements concluded for the purpose of executing specific deliveries.

Region	%
China	55,8%
Far East (Bangladesh, India)	31.5%
Turkey	8.9%
Poland	1.5%
Other	2.3%
Total	**100.0%**

Recipients of the goods of LPP SA are located in Poland and abroad (subsidiaries and non-affiliated entities). LPP SA sold goods in 26.1% on foreign markets, with 96.5% of goods being sold to subsidiaries building the chains of RESERVED, Cropp, House, MOHITO, SiNSAY stores in their area and are supplied with trading commodities by LPP SA. A share of one of the recipients affiliated with LPP SA exceeded 10% of the Company's sales in 2016. That company was Re Trading OOO, a Russian subsidiary. The sale to that company amounted to PLN 542 million, which accounted for 11.4% of revenues of LPP SA.
The share of other recipients did not exceed 10% of sales of LPP SA.
Export sales to entities not belonging to the LPP SA Capital Group in 2016 was PLN 43 669 thousand, which constituted 0.9% of revenues of LPP SA.

The Company's major non-affiliated exports customers are companies from Russia, Belarus and the Middle East.

Presented below are the main directions in LPP exports sales.

Country	2015		2016	
	exports amount in PLN '000	share in exports in %	exports amount in PLN '000	share in exports in %
Belarus	3 122	7.8%	2 379	5.4%
Egypt	5 802	14.6%	6 475	14.8%
Russia	6 809	17.1%	7 474	17.1%
Qatar	6 506	16.3%	10 902	25.0%
Kuwait	7 130	17.9%	4 948	11.3%
United Arab Emirates	2 680	6.7%	3 897	8.9%
Saudi Arabia	4 527	11.4%	4 695	10.8%
Other	1 597	4.0%	2 899	6.6%
Total	**39 850**	**100.0%**	**43 669**	**100.0%**

Revenues from the sales of products, goods and materials, disclosed in the consolidated financial statements, have been earned by individual companies of the Capital Group in the following amounts (excluding intra-group sales):

Company name	Country	Sales revenues between 01.01.2015 and 31.12.2015	Sales revenues between 01.01.2016 and 31.12.2016
LPP SA	Poland	3 250 263	3 542 891
LPP Estonia OU	Estonia	78 036	88 896
LPP Latvia LTD	Latvia	66 158	73 902
LPP Czech Republic SRO	Czech Republic	224 117	278 735
LPP Hungary KFT.	Hungary	48 110	76 349
LPP Lithuania UAB	Lithuania	77 451	93 622
LPP Ukraina AT	Ukraine	188 363	225 547
Re Trading OOO	Russia	836 242	1 043 698
LPP Romania Fashion SRL	Romania	56 410	111 015
GMBH Reserved	Germany	93 933	193 553
LPP Croatia DOO	Croatia	32 515	60 448
LPP Bulgaria LTD	Bulgaria	44 905	58 296
LPP Slovakia SRO	Slovakia	133 846	172 095
Total:		**5 130 348**	**6 019 046**

* total revenues of 2 companies in Russia (Re Trading OOO and Re Street LLC)
** total revenues of 2 companies in Bulgaria (LPP Bulgaria LTD and LPP Fashion Bulgaria EOOD)

2.4. Information on agreements material for the Issuer's business

In 2016, the Capital Group entered into the following material agreements:

- 188 lease agreements (including annexes prolonging the agreements) with retail space distributors in shopping centres. These agreements cover the premises in which RESERVED, Cropp, House, MOHITO and SiNSAY, and Tallinder clothing is sold.
- Bank loan agreements and annexes to existing loan agreements. Detailed information on these agreements has been made public and published in current reports (CR 03/2016, CR 04/2016, CR 35/2016, CR 36/2016, CR 37/2016, CR 39/2016, CR 48/2016, CR 53/2016). A list of bank loan agreements is presented in notes to the financial statements (point 14.7.3).
- Agreement on insurance guarantees for payment of customs liabilities

■ Insurance contract – a comprehensive insurance policy covering all property of the LPP SA Capital Group, including real property, goods, plant and equipment.
Apart from those agreements, in 2016, the LLP Capital Group companies concluded no material cooperation agreements.
The Group has no knowledge on agreements concluded between Shareholders, affecting its operations.

2.5. Transactions with associates

All transactions entered into by the issuer with associates in the reporting period were concluded on arm's length basis.
Detailed information on transactions with associates is given in note 14.22. to the consolidated financial statements for 2016.

3. Description of financial position

3.1. Basic economic and financial figures of the LPP Capital Group

The basic tasks carried out by the Capital Group in 2016 are as follows:

1) sales revenues of LPP SA Capital Group amounted to PLN 6 019 million and were higher by 17.3% than those achieved in 2015,
2) in 2016, the Capital Group generated net profit of approx. PLN 175 million. This is by 50.0% less than in 2015 (approx. PLN 351 million).
3) the total selling area in brand stores increased by approx. 77 thousand sq.m. (i.e. approx. 9.2%). At the end of 2016, the total retail selling area in the entire LPP SA Capital Group amounted to approx. 920.8 thousand sq. m, including approx. 424.2 thousand sq.m. outside Poland.

Chain	2015		2016		Change in area
	Area (thousand m2)	Number of stores	Area (thousand m2)	Number of stores	%
RESERVED	461.3	449	509.1	461	10.4%
Cropp	114.5	372	120.4	379	5.2%
House	99.7	319	105.7	330	6.0%
MOHITO	94.5	280	99.1	290	4.9%
SiNSAY	59.7	170	69.8	198	16.9%
Tallinder	-	-	4.1	9	-
Outlet	13.8	37	12.6	36	-8.7%
Total	**843.5**	**1 627**	**920.7**	**1 703**	**9.2%**

4) Results generated by the LPP SA Capital Group in 2016 depended primarily on the performance of five retail sales networks: RESERVED, Cropp, House, MOHITO and SiNSAY, with the majority of revenues and profits being generated by RESERVED stores. However, the highest revenue growth rate was recorded by SiNSAY and MOHITO.

Presented below are basic economic and financial figures and their changes in comparison with the previous year.

Distribution channel	2015 in PLN '000	2015 Share in sales volume %	2016 in PLN '000	2016 Share in sales volume %	Change %
RESERVED brand stores	2 433 755	47.4%	2 692 885	44.7%	10.6%
Exports*	39 850	0.8%	43 669	0.7%	9.6%
Cropp brand stores	789 853	15.4%	914 873	15.2%	15.8%
House brand stores	673 179	13.1%	767 149	12.7%	14.0%
MOHITO brand stores	586 498	11.4%	736 789	12.2%	25.6%
SiNSAY brand stores	328 866	6.4%	460 869	7.7%	40.1%
Tallinder brand stores	-	-	12 116	0.2%	-
Other	278 352	5.4%	390 696	6.5%	40.4%
Total	**5 130 353**	**100.0%**	**6 019 046**	**100.0%**	**17.3%**

* Exports to entities not affiliated with LPP SA

5) In 2016, the LPP SA Capital Group earned PLN 173 million from online sales, which was 2.9% of the Group’s sales. Approx. 86.0% of online sales were generated in Poland.

Online sales in PLN '000 000			
2013	2014	2015	2016
26.7	64.8	79.3	173.1

Online sales in PLN '000 000				
Q1 2016	Q2 2016	IQ3 2016	Q4 2016	Total
27.4	41.2	31.6	73.0	173.1

Presented below are basic economic and financial figures and their changes in comparison with the previous year.

Item	2015 (in PLN ‘000)	2016 (in PLN ‘000)	Change %
Revenues	5 130 353	6 019 046	17.3%
Gross profit (loss) on sales	2 742 829	2 933 810	7.0%
Profit from sales	551 162	325 004	-41.0%
Operating profit	502 689	226 421	-55.0%
Pre-tax profit	414 368	194 078	-53.2%
Net profit	351 320	174 775	-50.3%
Equity	1 889 739	2 134 731	13.0%
Liabilities and provisions for liabilities:	1 675 430	1 543 201	-7.9%
Long-term liabilities	344 116	267 254	-22.3%
Short-term liabilities:	1 331 314	1 275 947	-4.2%
- bank loans	561 074	315 111	-43.8%
- trade liabilities	721 394	881 064	22.1%
Non-current assets	1 796 996	1 838 664	2.3%
Current assets	1 768 173	1 839 268	4.0%
Inventories	1 319 735	1 164 135	-11.8%
Short-term receivables	197 313	271 697	37.7%
Trade receivables	115 086	165 389	43.7%

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3.2. Assets and liabilities

Assets of the LPP SA Capital Group

The assets of the LPP SA Capital Group comprise two major components: (1) fixed assets being store fixtures and equipment, in the amount of PN 1 839 million, and (2) inventories of trading commodities in the amount of PLN 1 164 million as t the end of 2016. The value of fixed assets will increase along with development of the sales network and the increase in the number of stores. The volume of inventories depends on the size of retail space and increases as subsequent stores are being opened. At the same time, the company is working in diminishing its financial engagement in inventories by reducing store replenishment and, simultaneously, by accelerating goods rotation which should translate into an increased efficiency of operations.

Liabilities of the LPP SA Capital Group

The LPP SA Capital Group pursues a conservative liabilities management policy aimed at maintaining a safe financing structure i.e. maintaining an over 50% share of equity capital in liabilities (at the end of 2016, the share of equity capital in liabilities was 58%, with equity capital amounting to PLN 2 135 million).The LPP SA Capital Group finances its operations also with liabilities owed to suppliers (aiming at prolonging a liabilities turnover cycle) and employing investment and current bank loans. At the end of 2016, the balance of bank loans was PLN 510 million and was lower by PLN 335 million compared to the balance as at the end of the preceding year.

3.3. Monetary position

The LPP SA Capital Group applies a centralised liquidity management model: the parent company (LPP SA) purchases goods and distributes them to subsidiaries and, next, subsidiaries pay the parent company for those goods in a local currency. LPP SA is vested with decision-making capacities in terms of the flow of receivables, foreign currency exchange and the incurring of financial liabilities. The basic goal of the Finance Department of LPP SA is the safeguarding of liquidity, solvency and bank debt management. At the end of 2016, the LPP SA Capital Group held almost PLN 366 million in cash, with the balance of bank loans in the amount of PLN 510 million, which means that a net debt was PLN 144 million and was lower by PLN 477 million than a year ago. At the same time, the net debt / EBITDA ratio, determining financial safety, was reduced to 0.3 (from 0.9 a year ago). The aim is to maintain the net debt / EBITDA ratio at a level below 1.0.

3.4. Profitability ratios

Profitability ratios presented in the table have been calculated as follows:

a) gross profit margin – gross profit on sales divided by revenues from sales of goods and services;
b) operating profit margin – operating profit divided by revenues from sales of goods and services;
c) net profit margin – net profit divided by revenues from sales of goods and services,
d) Return on Assets – net profit divided by average assets during the financial year;
e) Return on Equity – net profit divided by average equity during the financial year.

Volume	2015 %	2016 %	Change p.p.
Gross profit margin on sales	53.5%	48.7%	-4.7%
Operating profit margin	9.8%	3.8%	-6.0%
Net profit margin	6.8%	2.9%	-3.9%
Return on assets	10.8%	4.8%	-6.0%
Return on equity	19.9%	8.7%	-11.2%

3.5. Liquidity ratios

Liquidity ratios were calculated as follows:

a) current ratio – current assets divided by the carrying amount of short-term liabilities;
b) quick ratio – current assets less inventory divided by the carrying amount of short-term liabilities;

Consolidated annual report of LPP SA Capital Group for 2015, in PLN '000

c) inventory turnover ratio (days in inventory) – average inventory divided by costs of goods and products sold and multiplied by the number of days in a given period;
d) receivables turnover ratio (days in receivables) – average trade receivables divided by revenues from sales and multiplied by the number of days in a given period;
e) trade liabilities turnover ratio (days) – average trade liabilities divided by costs of goods and products sold and multiplied by the number of days in a given period.

Volume	2015	2016	Change %
Current liquidity ratio	1.3	1.4	7.7%
Quick liquidity ratio	0.3	0.5	66.7%
Inventory turnover (days)	176	147	-16.5%
Receivables turnover (days)	10	9	-10.0%
Trade payables turnover (days)	102	95	-6.9%

3.6. Asset Management Ratios

The ratios were calculated as follows:
a) fixed assets to equity ratio – shareholders' equity divided by fixed assets;
b) total debt – long- and short-term payables divided by the balance sheet total (including provisions for liabilities);
c) short-term debt ratio – short-term debt divided by the balance sheet total;
d) long-term debt ratio – long-term debt divided by the balance sheet total.

Volume	2015 %	2016 %	Change p.p.
Fixed assets to equity ratio	105.2%	116.1%	10.9%
Total debt ratio	47.0%	42.0%	-5.0%
Short-term debt ratio	37.3%	34.7%	-2.7%
Long-term debt ratio	9.7%	7.3%	-2.4%

3.7. Basic economic and financial figures of the Parent Company LPP SA

The basic tasks carried out by LPP in 2016 are as follows:

1) sales revenues of LPP SA amounted to PLN 4 741 million and were higher by 9.3% than those achieved in 2015,
2) in 2016, LPP SA generated net profit of approx. PLN 280 million. This is by 18.7% less than in 2015 (approx. PLN 344 million),
3) the retail selling area in brand stores increased by approx. 32 thousand sq.m. (i.e. approx. 6.8%). At the end of 2016, the total retail selling area of LPP SA amounted to approx. 496.6 thousand sq. m.

Chain	2015		2016		Change in area
	Area (thousand m2)	Number of stores	Area (thousand m2)	Number of stores	%
RESERVED	232.5	237	248.7	236	7.0%
Cropp	63.0	217	65.3	219	3.7%
House	62.2	208	64.9	212	4.3%
MOHITO	52.1	164	53.4	166	2.5%
SiNSAY	43.5	127	48.6	142	11.7%
Tallinder	-	-	4.1	9	-
Outlet	11.6	33	11.6	33	0.0%
Total	**464.9**	**986**	**496.6**	**1017**	6.8%

1) Results generated by the LPP SA in 2016 depended primarily on the performance of five retail sales networks: RESERVED, Cropp, House, MOHITO and SiNSAY, with a majority of revenues and profits generated by RESERVED stores. However, the highest revenue growth rate was recorded by SiNSAY and MOHITO.

Distribution channel	2015		2016		Change
	Area (thousand m2)	Share in sales volume %	Area (thousand m2)	Share in sales volume %	%
RESERVED brand stores	1 421 468	32.8%	1 407 005	29.7%	-1.0%
Exports*	1 124 963	25.9%	1 239 630	26.1%	10.2%
Cropp brand stores	467 834	10.8%	497 362	10.5%	6.3%
House brand stores	469 735	10.8%	517 280	10.9%	10.1%
MOHITO brand stores	353 524	8.2%	405 467	8.6%	14.7%
SiNSAY brand stores	261 967	6.0%	346 088	7.3%	32.1%
Tallinder brand stores	-	-	12 116	0.3%	-
Other	236 262	5.4%	328 045	6.9%	38.8%
Total	**4 335 753**	**100.0%**	**4 740 877**	**100.0%**	**9.3%**

* Exports to affiliated entities (subsidiaries of LPP SA) and non-affiliated entities

1) In 2016, LPP SA generated PLN 149 million from online sales, which was 3.1% of the sales of LPP SA.

Online sales in PLN '000 000			
2013	2014	2015	2016
26.7	64.2	75.8	149.3

Online sales in PLN '000 000				
Q1 2016	Q2 2016	Q3 2016	Q4 2016	Total
25.2	38.3	28.3	57.5	149.3

Presented below are basic economic and financial figures and their changes in comparison with the previous year.

Item	2015 (in PLN '000)	2016 (in PLN '000)	Change %
Revenues	4 335 753	4 740 877	9.3%
Gross profit (loss) on sales	1 813 038	1 769 372	-2.4%
Profit from sales	272 880	23 193	-91.5%
Operating profit	248 455	5 662	-97.7%
Pre-tax profit	381 908	297 634	-22.1%
Net profit	344 347	280 071	-18.7%
Equity	1 856 386	2 092 846	12.7%
Liabilities and provisions for liabilities:	1 564 439	1 401 123	-10.4%
Long-term liabilities	317 752	244 476	-23.1%
Short-term liabilities:	1 246 687	1 156 647	-7.2%
- bank loans	560 661	315 111	-43.8%
- trade liabilities	654 814	792 684	21.1%
Non-current assets	1 865 472	2 095 664	12.3%
Current assets	1 555 353	1 398 305	-10.1%
Inventories	954 211	832 586	-12.7%
Short-term receivables	470 529	387 756	-17.6%
Trade receivables	417 435	294 500	-29.5%

The increase by 9.3% in sales revenues was achieved by increasing sales in all retail chains.
A gross margin reached 37.3% and was lower by 4.5 percentage points that last year.
The profit on sales fell by 2.4%.
The operating profit amounted to PLN 5 662 thousand (decrease by 97.7% compared to 2015), and the operating profit margin amounted to 0.1% (last year, it was, respectively, PLN 248 455 thousand and 5.7%).
The profit on business operations was lower compared to the previous year by 22.1% and amounted to PLN 297 634 thousand.
The net profit generated in 2016 amounted to PLN 280 071 thousand and was lower compared to the previous year (PLN 344 347 thousand) by 18.7%. The resulting net profit margin amounted to 5.9% (in 2015, profitability was 7.9%).
The equity capital of LPP SA increased by 12.7% in 2016. It was mainly due to the transfer of profit to equity.
Long-term liabilities decreased by 23.1%, while short-term liabilities decreased by 7.2% compared to 2015.

3.8. Assessment of factors and extraordinary events affecting the financial result

In 2016, unusual factors affecting profit or loss on the operations of the LPP SA Capital Group was recognition by the Company of provisions and write-downs for the closing of Tallinder, in the total amount of PLN 24.6 million, and the transaction involving the sale to an external entity of old collection inventories of a value of PLN 138 million for PLN 26 million, which was an effect of the new goods management policy.

3.9. Financial agreements

3.9.1. Loans and borrowings taken out

Information on bank loans taken out as at 31 December 2016 and their maturity dates is given in additional notes to the financial statements (point 14.7.3).
In 2016, the LPP SA Capital Group made no borrowings.

3.9.2. Loans extended

Information on loans extended by the LPP SA Capital Group is given in additional notes to the financial statements (point 14.7.2).

3.9.3. Guarantees and bank guarantees granted and received

Guarantees
In the reporting period, the LPP SA Capital Group granted the following guarantees within the Group:

Description	Amount in PLN '000
Promissory note guarantee issued to Orlen for a single business entity	22
Guarantee for Amur Sp. z o.o.	7 678
Guarantee for BBK SA	894
Guarantee for DP and SL Sp. z o.o.	1 358
Guarantee for Re Trading OOO	19 634
Guarantee for LPP Estonia OU	770
Guarantee for LPP Romania Fashion SRL	2 082
Guarantee for LPP Ukraina AT	5 023
Guarantee for LPP Czech Republic SRO	26 669
Guarantee for Reserved GmbH	14 004
Guarantee for LPP Latvia LTD	2 989
Guarantee for LPP Bulgaria LTD	2 570
Guarantee for LPP Slovakia SRO	8 582
Guarantee for LPP Lithuania UAB	829
Guarantee for LPP Hungary KFT	4 207
Guarantee for LPP Croatia DOO	12 636

In 2016, the LPP SA Capital Group was not granted any guarantees, and only LPP SA granted guarantees to its subsidiaries).
No guarantees were granted by subsidiaries. Subsidiaries received the above-mentioned guarantees from the parent company only.

Bank guarantees
In 2016, the LPP SA Capital Group used bank guarantees to secure payment of rent for the leased premises in which brand stores, offices and a warehouse are located. The Capital Group applied for banking guarantees to secure lease agreements in which the Company is lessee, and to secure lease agreements in which entities affiliated with the Company are lessees.
As at 31 December 2016, the total value of bank guarantees issued upon request and at the responsibility of LPP SA amounted to PLN 261 218 thousand, of which:
- guarantees issued to secure agreements concluded by LPP SA amounted to PLN 77 927 thousand,
- guarantees issued to secure agreements concluded by consolidated associates amounted to PLN 181 262 thousand,
- guarantees issued to secure agreements concluded by non-consolidated associates amounted to PLN 1 720 thousand,
- guarantees issued to secure warehouse space lease agreements concluded by LPP SA amounted to PLN 309 thousand**.**

In 2016, the Company also received guarantees as a collateral for payments from a contracting party. As at 31 December 2016, the value of guarantees received was PLN 21 908 thousand.

Apart from the above-mentioned guarantees and bank guarantees, the companies of the LPP SA Capital Group have no major off-balance sheet items.

3.10. Issue of securities

In Q1 and Q4 2016, part of subscription warrants of the A series was converted to shares of the L series in the share capital of LPP SA.
As a result of the exchange, the Company issued, in total, 8 168 bearer shares of the L series. Following the said issue, the Issuer's share capital amounts to PLN 3 678 582 and is divided into 350 000 registered shares and 1 489 291 bearer shares. Consequently, the total number of votes at the general meeting is 3 220 313 (the Company has also 18 978 treasury shares based on which voting rights may not be exercised, therefore, the said votes were not included in the total number of votes at the General Meeting of Shareholders).
The new shares of the L series constitute 0.4% of the Issuer's share capital and give 0.3% of the total number of votes at the General Meeting of Shareholders.
The shares of the L series were dematerialised, admitted to trading and, subsequently, introduced to trading on the stock exchange in February 2016 and in 2017, as informed by the Company in the following reports: CR 9/2016, CR 10/2016, CR 5/2017 and CR 08/2017.

3.11. Financial result forecast

No financial result forecasts were published.

3.12. Financial asset management

The LPP SA Capital Group fulfils all relevant obligations against the State and contracting parties on an on-going basis. The basic business model consisting in retail sales allows to receive immediate payments for goods sold. Proceeds generated and bank loan agreements concluded safeguard in full the fulfilment of liabilities incurred.

3.13. Information on financial instruments

3.13.1. Description of financial risk, including price change risk and credit risk, risk of serious disruption of cash flows and financial liquidity loss, to which the entity is exposed

In line with the International Accountancy Standards on the detailed principles for the recognition, valuation, disclosure and presentation of financial instruments, the following financial instruments were identified by the LPP SA Capital Group:
- borrowings granted,
- bank loans taken out,
- bank deposits.

The Group also identified embedded derivatives related to:
- retail space lease agreements for brand stores, with rent calculated based on foreign exchange rates
- liabilities denominated in foreign currencies, connected with the purchase of trading commodities abroad
- receivables in foreign currencies, relating to the sales of trading commodities to foreign contracting parties.

Embedded derivatives are not measured and shown in the balance sheet, which is compliant with IAS on the detailed principles for the recognition, valuation, disclosure and presentation of financial instruments.

3.13.2. Description of goals set, and methods of financial risk management adopted, by the entity

- Financial liquidity risk – the business model adopted by the Issuer (sale of goods for cash to an end-purchaser) guarantees that the Company will generate, on a constant basis, day-to-day cash proceeds, and that the Company will not be dependent on single large recipients. Liquidity management consists in goods management and the determination of adequate prices and margins and in the strict auditing of costs and expenses. The Company's liquidity is audited by way of day-to-day monitoring of the balance of bank accounts, the creation of cash flow forecasts for monthly periods and the planning of cash flows between subsidiaries and LPP SA.

■ Creditworthiness risk – a priority of the Management Board of LPP SA in the finance area is the earning by the Company of profit in an amount enabling the daily handling of credit liabilities and ensuring funds for the Issuer's further development. LPP SA makes endeavours to maintain borrower's creditworthiness at a high level – by paying, on a day-to-day basis, all its liabilities, by increasing sales and optimising costs, and by adequate future planning to recognize beforehand any upcoming hazards. Financial ratios, including a debt ratio, are monitored.
■ Risk in guarantees granted – guarantees granted by LPP involve the lease of retail space or the operations of subsidiaries, in which LPP SA holds 100% shares and controls their business. Consequently, the risk in guarantees granted is reduced to the minimum.
■ Investment risk – the Company invests in ventures falling within the scope of its competencies, which increases success probability; the only major investments are as follows:
- development of the chains of own retail stores,
- development of foreign sales networks,
- expansion of the Logistics Centre,
- acquisition in the years 2008-2009 of Artman SA from Cracow, operating in the same business sector.
At the same time, LPP SA avoids investments in other business sectors and investments in financial instruments on a capital market.
■ ■ Interest rate risk – bank loans taken out by LPP are charged with variable interest rate depending on changes in market interest rates. According to the Management Board, based on the analysis of changes in interest rates in previous periods, any potential increase of this parameter, determining the costs of bank loans taken out, may not substantially affect profit or loss.
■ Credit risk – the basic settlement currency for a majority of transactions involving the purchase of trading commodities is USD. A minor part of settlements in that respect is made in EUR. The majority of sales proceeds is earned in PLN.
Apart from the currency risk involved in the settlement currency applied for purchasing trading commodities, there is also a risk related to the settlement of rents under retail space lease agreements in EUR.

The LPP SA Capital Group does not apply any risk-hedging instruments within the above-mentioned scope.

3.14. Investments

3.14.1. Capital investments

Apart from engagement in subsidiaries and investments made in other entities to the extent provided for in notes 14.5 and 14.6 to the consolidated financial statements of the LPP SA Capital Group, the Issuer has no capital investments.

3.14.2. Capital expenditure

In 2016, capital expenditure (CAPEX) amounted to PLN 271 million i.e. by 81% less than in 2015. The reasons for the decrease was a lower volume of newly opened retail space, better use of fit-outs, completion of the investments in the logistics centre and the company's registered office and the prolongation of payment terms for construction suppliers by Q1 2017.

3.14.3. Assessment of the possibility of carrying out investment plans and methods for their financing

Investment plans will be carried out with funds held and bank loans taken out.

4. Operating strategy, development perspectives as well as risks and threats

4.1. External and internal factors substantially affecting the Issuer's development

The basic tasks of the LPP SA Capital Group, the implementation of which will determine its future position, is as follows:
a) expansion into new markets in Western Europe, the Balkans, the Middle East, Belarus and Kazakhstan,
b) building brand strength for RESERVED, Cropp, House, MOHITO and SiNSAY,

c) developing online sale,
c) increasing business profitability and effectiveness.

The achievement of the Issuer's strategic tasks and goals will depend on numerous internal and external factors (representing both opportunities and threats).

4.1.1. Internal factors

Market strategy of the LPP SA Capital Group

The Capital Group is focused on the designing and distribution of clothing as well as on building its brand by outsourcing many activities. The LPP SA Capital Group does not have its own manufacturing capacities, which facilitates significant reduction of fixed costs. The entire clothing production is outsourced to contracting parties mainly from the Far East. Consequently, all Group's investments are aimed at increasing its commercial potential, maintaining a competitive advantage on the market, creating own distribution network, building a positive image of the Capital Group on the clothing market and gaining consumers that are loyal to the Capital Group and its products. Apart from investments in the chain of regular stores, LPP SA invests also in e-commerce development, opening online stores in subsequent countries and increasing the functionality of online sales.

The development strategy for RESERVED, the leading brand, envisages taking actions to maintain the brand's renowned position in customers' eyes, leaving it still in the segment of mass clothing retailers.

Market position of the LPP SA Capital Group

The volume of sales revenues generated by the LPP SA Capital Group reflects its high position on the domestic clothing market, with its market share of approx. 13%.
At the end of 2016, the LPP Capital Group had a network of 1 703 stores in Poland and abroad, selling products of all brands, with total retail space of approx. 920.7 thousand sq.m.
As planned for 2017, new stores will be opened and, therefore, the total retail space will increase by approx. 12**%.**

Logistics

The Capital Group has a chain of stores in Poland and abroad, to which it supplies goods every couple of days, dispatching them from the Logistics Centre in Pruszcz Gdański or from ancillary warehouses. The maintenance of continuity and timeliness of deliveries is essential for the operation of the Issuer's business.
The applied logistic model consisting in the use of specialised technology in the company's own logistics centre, while outsourcing the transport of goods from suppliers to the logistics centre and from the logistics centre to brand stores to specialised transportation companies, facilitates a more effective implementation of processes in this area.
Ambitious plans for the development of the sales network of LPP SA and its subsidiaries in the coming years necessitate the need to increase efficiency of the logistics centre. In 2015, having constructed new facilities, we completed the expansion of the existing logistics centre. The implemented technological solutions will facilitate supporting LPP SA and its subsidiaries in their needs until approx. 2020.

Development of online sales

Adapting to the prevailing trend related to the increasing popularity of online shopping, the LPP SA Capital Group has been dynamically developing its sales through this channel. Initially, the Company launched online stores for all its brands in Poland, and, subsequently, it started launching online stores abroad.
At the end of 2016, online stores of the Issuer's five brands, i.e. RESERVED, Cropp, House, MOHITO and SiNSAY, were available in six countries.
As planned for 2017, online stores will be launched on six new markets: Great Britain, Lithuania, Latvia, Estonia, Ukraine and Russia.

Key personnel

The employment of qualified and engaged staff guarantees that a company will have an adequate market offer and an adequate customer approach and that it will be successful on the market. However, there is also a risk that a company will be made excessively dependent on several key persons or a specialised group of employees with unique skills in a given branch.
As regards LPP SA, the Company's key personnel comprise its Management Board (by virtue of their experience, market expertise and branch-specific knowledge) as well as clothing design specialists, graphic designers and purchase specialists.
The retention of key personnel is to be achieved by way of an incentive plan developed by LPP SA and by investing in employees by offering professional training, talent acquisition and development of skills, setting career paths and facilitating promotion within LPP structures.
To minimise somehow the risk, described above, in 2016, the Company opened a new design office in Warsaw, thus procuring additional creative employees who had been earlier discouraged by a prospective change of their place of residence, considering the location of the Company's registered office.

Measures aimed at maintaining low levels of costs, increasing profitability and market share through global sales growth

To ensure the Company's efficiency and productivity at a high level, measures have been taken to reduce incurred costs - keeping them at a relatively low level is one of the main objectives of the LPP SA Capital Group. The size of the LPP SA Capital Group and its development facilitates the application of economies of scale. However, considering business costs, in 2016, there was an increase in labour costs in each country in which LPP SA operates.
The Group pursues a strategy aimed at increasing profitability while expanding retail space by building new stores, and, where the forecasts are highly satisfactory, by building stores with a larger floor area.

Company's renown

The Company may be exposed to the risk of loss of renown due to assigning work to suppliers from the third world countries and inadequate use of copyright of third parties, for example when using photos during the manufacturing process without licences purchased.
LPP SA minimises the said risk by:
- joining Accord on Fire and Building Safety in Bangladesh,
- creating an internal unit within the Company's structure, dedicated to the auditing of working conditions and safety in suppliers' plants,
- changing the model of cooperation with independent agents, consisting in the placing of orders for products with certified suppliers only,
- creation of internal procedures for purchases of photographs and graphic licences.

4.1.2. External factors

Macroeconomic factors - the pace of economic growth in Poland and in countries where the stores of the LPP SA Capital Group are operated

The economic situation in countries in which the LPP SA Capital Group sales its products and the situation in countries in which plants manufacturing goods for the Issuer as located is of major importance for the company's standing. The economic increase or decrease in countries in which the company's stores are operated translates proportionately into an increase or decrease in the sales of goods. The economic increase or decrease in countries in which goods are manufactured may translate into an increase or decrease in manufacturing costs.
The Company aims at minimising the said risk as follows:
- sale of goods on numerous markets – risk diversification into many countries with a diversified macroeconomic situation, sale of goods under several brands to distribute risk onto several age groups,
- purchase of goods by ordering their manufacturing with many manufacturers in several countries, including mainly countries with lower manufacturing costs (China, India, Bangladesh), through long-term cooperation with selected suppliers, which facilitates negotiating advantageous prices of goods.

LPP SA increases its presence on all markets in which the stores of the Capital Group are already operated and opens new online stores. At present, the most important issue is to start business in the countries of Western Europe, where LPP SA intends to build awareness of the RESERVED brand. The building of a global brand will give the Company the possibility of further expansion and sales increase. Apart from own stores, LPP SA supports the development of franchise stores; currently such business endeavours are supported in the countries of the Middle East, in Belarus and Kazakhstan.

Currency exchange rates

The basic settlement currency in most transactions involving purchases of trading commodities is USD. A minor part of settlements in this respect is made in EUR.
The majority of sales proceeds is generated in PLN. The instability of the exchange rate of the Polish zloty vs. USD and EUR is a risk which increases along with acceleration of changes in foreign exchange rates (PLN/USD).
In addition to foreign exchange risk involved in the settlement currency used for purchasing trading commodities, there is also a risk associated with the fact of settling retail space rents in EUR. Large fluctuations of the Russian rouble and the Ukrainian hryvnia also have a significant impact on profit or loss.

Information on foreign exchange risk is presented in Note 11.

Changes in fashion influencing the attractiveness of products offered

The key success factor for a clothing company is sensing changes in fashion trends and offering the range of goods meeting current consumer preferences.
The LPP SA Capital Group pays great attention specifically to fashion. Analysing the continuously changing trends, the design department adapts them to meet consumer needs to continue offering desirable products at very good price-quality ratio. To fulfil their tasks, the designers participate in trade fairs around the world, have knowledge of professional literature and information on issues related to fashion, available on the Internet. Since there is a strong correlation between the clothing industry and fashion trend changes, the Capital Group, observing customers' changing preferences, introduces every year new groups of products, aiming to anticipate market needs.
LPP clothing designs are developed by several teams of designers, and their work is organised so as to minimise the influence of a single designer over entire collections.
The Company brings special attention to those issues, being aware of their enormous impact on the results of its operations.

Competitors

As barriers to the clothing market entry are limited, competitiveness may increase. At the same time, on the Polish and European clothing markets, there are many entities operating, including world leaders in this business sector.
LPP SA analyses the activity of its competitors. It monitors their financial result, development of their sales networks and their product and price offer.
The Company focuses on competing with other entities by offering high-quality products at affordable prices and a diversified product offer, with special emphasis on the trendiness of collections offered.

Legal changes and law amendments

Considering the specific features of the Polish legal system, an important risk for the dynamics and development of the Company's business may be law amendments or changes in construing the provisions of law, in particular, in respect of commercial and tax laws and laws governing financial markets. The introduction of retail sales tax and the prospective implementation of a ban for Sunday trade may have an adverse impact on the operations of the LPP Capital Group.

4.2. Perspectives for the development of the economic activity of the LPP SA Capital Group

The long-term development strategy of the LPP SA Capital Group assumes the strengthening of its current position on the markets where it is already operating, the expansion into new geographic areas such as Western

Europe, the Balkans and the Middle East and increasing online sales. The sales network is to be expanded simultaneously with activities aimed at increasing operating efficiency in each area.

5. Corporate information and declaration on corporate governance

5.1. Application of corporate governance principles

The Management Board of the Issuer declares that, in 2016, the Company applied corporate governance principles attached as Enclosure to the Resolution No 26/1413/2015 of the GPW Supervisory Board, dated 13 October 201, titled "Best Practice for GPW Listed Companies 2016" (Corporate Governance Principles), published in a website dedicated to good practice for companies listed on the stock exchange Giełda Papierów Wartościowych w Warszawie SA, operated by Giełda Papierów Wartościowych w Warszawie SA at website address: https://www.gpw.pl/lad_korporacyjny_na_gpw.

The Management Board of LPP SA declares that the Company and its governing bodies applied in 2016 recommendations and detailed principles provided for in the new Collection of Good Practice for GPW Listed Companies 2016, except for:

■ Recommendation IV.R.2 – conducting of a general meeting using electronic communication means (real-life broadcast of the general meeting, real-time bilateral communication, exercise of the right to vote during a general meeting either in person or through a plenipotentiary.

<u>The Company does not apply the said recommendation.</u>

The above-mentioned recommendation is not applied by the Company as its implementation would involve a technical risk. The giving to shareholders of an option to communicate in the course of the general meeting without being present at the meeting, using electronic communication means, involves both technical and legal hazards for the proper and efficient conduct of the general meeting. In particular, the above brings about a real risk of technical interference preventing continuous bilateral communication with shareholders present in venues other that the meeting room. Therefore, the Company may not guarantee the reliability of technical infrastructure.

At the same time, in the Company's opinion, the currently applicable rules for participation in general meetings facilitate the proper and effective exercise of rights attached to shares and sufficiently secure the interests of all shareholders.

Furthermore, the Company has not been informed of any expectations of shareholders in respect of conducting the general meeting using electronic communication means.

■ Recommendation VI.R.1 – the remuneration of members of the company's governing bodies and key managers should follow the approved remuneration policy.

<u>The Company does not apply the said recommendation.</u>

The Company has not implemented any remuneration policy. However, LPP SA does not exclude future application of the said rule.

■ Recommendation VI.R.2 – the remuneration policy should be closely tied to the company's strategy, its short- and long-term goals, long-term interests and results, taking into account solutions necessary to avoid discrimination on whatever grounds.

<u>The Company does not apply the said recommendation.</u>

The Company has not implemented any remuneration policy. However, LPP SA does not exclude future application of the said rule.

■ Detailed principle I.Z.1.20 – Display on a corporate website of an audio or video recording of a general meeting.

<u>The Company does not apply the said principle.</u>

The Company does not plan to make an audio or video recording of a general meeting and display it on its website. In the Company's opinion, the manner of which general meetings have been documented so far ensures transparency of the Company's operations and safeguards the rights of all shareholders.

In particular, the Company makes available the wording of resolutions adopted, in the form of current reports and website publications.

Additionally, detailed data on voting results and objections, if any, raised against adopted resolutions are made available in the same form. Consequently, investors may obtain the knowledge of the material parts of, and matters discussed at, a general meeting.

However, the Company does not exclude future application of the said rule.

■ Detailed principle IV.Z.2. – companies should ensure publicly available real-time broadcasts of general meetings.
The Company does not apply the said principle.
The Company does not plan to provide real-time broadcasts of general meetings. In the Company's opinion, the manner of which general meetings have been documented so far ensures transparency of the Company's operations and safeguards the rights of all shareholders.
In particular, the Company makes available the wording of resolutions adopted, in the form of current reports and website publications.
Additionally, detailed data on voting results and objections, if any, raised against adopted resolutions are made available in the same form. Consequently, investors may obtain the knowledge of the material parts of, and matters discussed at, a general meeting.
However, the Company does not exclude future application of the said principle.

■ Detailed principle VI.Z.4. – publishing, in the report on the operations, of a report on the remuneration policy.
The Company does not apply the said principle.
The Company will not publish a report on its remuneration policy due to the fact that no such policy has been implemented. However, LPP SA does not exclude future application of the said rule.

5.2. Description of the main features of the Company's internal control systems and risk management in relation to the process of preparing financial statements and consolidated financial statements

LPP SA has adapted to its needs and characteristics a well-functioning internal control system, which provides:
■ completeness of invoiced revenues,
■ appropriate cost control,
■ efficient use of resources and assets,
■ accuracy and reliability of financial information included in financial statements and periodic reports,
■ adequate protection of sensitive information and prevention of uncontrolled outflow of information from the company,
■ effective and prompt identification of irregularities,
■ identification of significant risks and appropriate responding to such risk.

Elements of the internal control system within LPP SA include:
■ control activities taken at all levels and in all units of the Company, based on procedures (permits, authorizations, verifications, reconciliation, review of operational activities, distribution of duties) ensuring compliance with guidelines of the Company's Management Board and, at the same time, enabling to identify and take the necessary actions to minimise errors and risks for the Company,
■ Workflow Guide - proper records and documentation circulation control system (to ensure compliance of the account records with accounting evidence),
■ suitably qualified personnel carrying out inspections,
■ division of duties excluding a possibility that one employee performs an action associated with execution and documentation of a business transaction from beginning to end,
■ inventory manual, specifying the rules for the use, storage and inventory of assets,
■ principles for balance sheet amortisation of intangible and tangible fixed assets,
■ information system - the Company's accounting books are kept with the help of computerised Integrated Enterprise Management System AWEK at the Company's headquarters, which provides credibility, reliability and accuracy of the processed information. Access to AWEK information resources is limited to authorised personnel, only for performance of their duties,
■ accounting policy, taking into account the principles of the International Accounting Standards and International Financial Reporting Standards (IAS/IFRS) and related interpretations published in the form of executive regulations of the European Commission,
■ electronic system for document processing (invoices, elements of employee documentation, commissions to purchase equipment, payment orders, etc.).

The audit of financial statements, carried out by an independent statutory auditor, is an essential element of internal audit in the process of preparing the Company's financial statements, both individual and consolidated. The statutory auditor is appointed by the Supervisory Board of LPP Company. The tasks of the independent auditor include reviewing semi-annual and annual statements and controlling accuracy of their preparation and compliance with accounting rules.

Consolidated annual report of LPP SA Capital Group for 2015, in PLN '000

Two departments are responsible for the preparation of financial statements: accounting and finance, headed by the Chief Accountant and the Chief Financial Officer. Before submitting financial statements to the independent statutory auditor, the Chief Financial Officer, responsible for the financial reporting process on behalf of the Management Board, verifies them for completeness and correctness of all economic events.

Semi-annual reviews of the strategy and implementation of business plans are carried out in LPP SA. This is due to cycles occurring in the clothing trade. After closing the first half of the year, senior and middle management, with the participation of the finance department, review the Company's financial results. Operating results of the Company, individual business units or even individual stores are analysed each month. Internal control and closely related risk management in relation to financial reporting processes are the subject of current interest of the Company's managing authorities. LPP SA performs an analysis of business risk factors related to the company operations. An important role in this respect is also played by the managerial personnel responsible for monitoring activities of their departments, including identification and assessment of risks associated with the process of preparation of financial statements in an accurate, reliable manner and in compliance with the law.

5.3. Shares and shareholders

5.3.1. Shareholding structure

The structure of shareholdings in LPP SA as at 31 December 2016.

Shareholder	Number of shares held	Share in the share capital	Number of votes at the GM	Share in the number of votes at the GM	Nominal value of shares
Marek Piechocki	175 497	9.5%	875 493	27.2%	350 994
Jerzy Lubianiec	174 999	9.5%	874 995	27.2%	349 998
Forum TFI SA*	200 730	10.9%	200 738	6.2%	401 460
Treasury shares	18 978	1.0%	0**	0.0%	37 956
Other shareholders	1 269 087	69.0%	1 269 087	39.4%	2 538 174
Total	**1 839 291**	**100.0%**	**3 220 313**	**100.0%**	**3 678 582**

*Forum TFI SA manages the funds of Forum 64 Closed-End Investment Fund (entity affiliated with Mr Jerzy Lubianiec, shareholder of LPP SA) and Forum 65 Closed-End Investment Fund (entity affiliated with Mr Marek Piechocki, shareholder of LPP SA).
The Funds managed by Forum TFI SA hold directly 195 050 shares in LPP SA and indirectly 5 680 shares in LPP SA.
** LPP SA may not exercise voting rights at the GM, attached to 18 978 shares, as these are treasury shares of LPP SA.

5.3.2. Shares held by key management and supervisory officers

As at 31 December 2016, key management and supervisory officers held the following shareholdings in the Company:

Shareholder	Number of shares held	Number of votes at the GM
Marek Piechocki – President of the Management Board	175 497	875 493
Jacek Kujawa – Vice-President of the Management Board	153	153
Przemysław Lutkiewicz - Vice-President of the Management Board	10	10
Sławomir Łoboda - Vice-President of the Management Board	102	102
Jerzy Lubianiec – Chairman of the Supervisory Board	174 999	874 995
Dariusz Pachla – Member of the Supervisory Board	500	500

Additionally, the Issuer's key management officers hold rights to subscribe to 13 132 shares of the L series due to the possibility of converting subscription warrants of the A series to shares in LPP SA.
Key management and supervisory officers hold no shares in any associates.

5.3.3. Information on agreements which may give grounds in the future for changes in proportions of shareholdings of current shareholders

In the reporting period, an incentive plan implemented in 2011 for key management officers of the Parent Company for the years 2011-2014 was applied.
As part of the said plan, the Company issued 21 300 subscription warrants which were subscribed to by eligible persons, of which 8 168 warrants were converted into shares of the L series (CR 02/2016, RB 50/2016).
If all remaining subscription warrants, which were subscribed to, were converted into shares, then the total number of shares would be 1 852 423, and the number of votes at the General Meeting of Shareholders of LPP SA would amount to 3 233 445.

The Company has not implemented any employee share control system.

Subject to the above-mentioned information, the Company has no knowledge on any agreements which could give grounds in the future for any changes in proportions of shareholdings of current shareholders and bondholders.

5.3.4. Treasury shares

In 2016, the LPP SA Capital Group purchased no treasury shares.

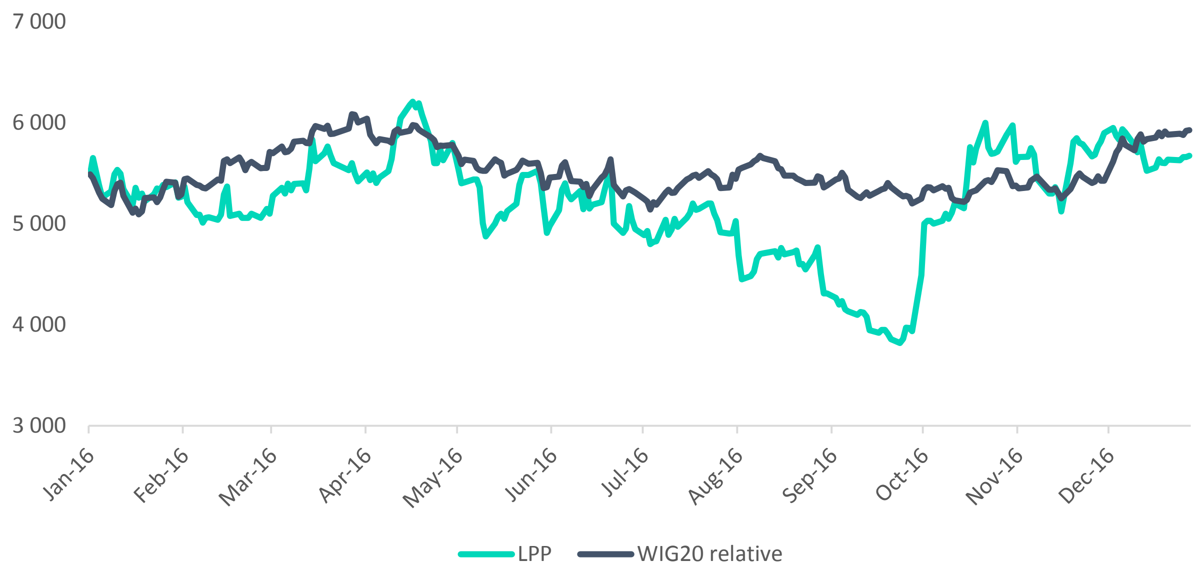
5.3.5. Share quotations

The shares in LPP SA have been quoted on the main market of the Warsaw Stock Exchange (WSE) since 2001.
On the debut date, the price of the Company's shares was PLN 48.00. The lowest value of the Company's shares in the history of listings was recorded by LPP SA on 18 May 2001: PLN 47.00, and the highest value was recorded on 4 September 2014: PLN 10 100.00.
In 2016, the prices of LPP SA shares were between PLN 3 820.00 and 6 162.44 (at closing prices). The share quotation during the last session (at closing prices) in 2015 was PLN 5 512.51, and a year later the price amounted to PLN 5 673.60.
Net earnings per ordinary share were PLN 96.19 at the end of 2016, and a year before - PLN 193.87.

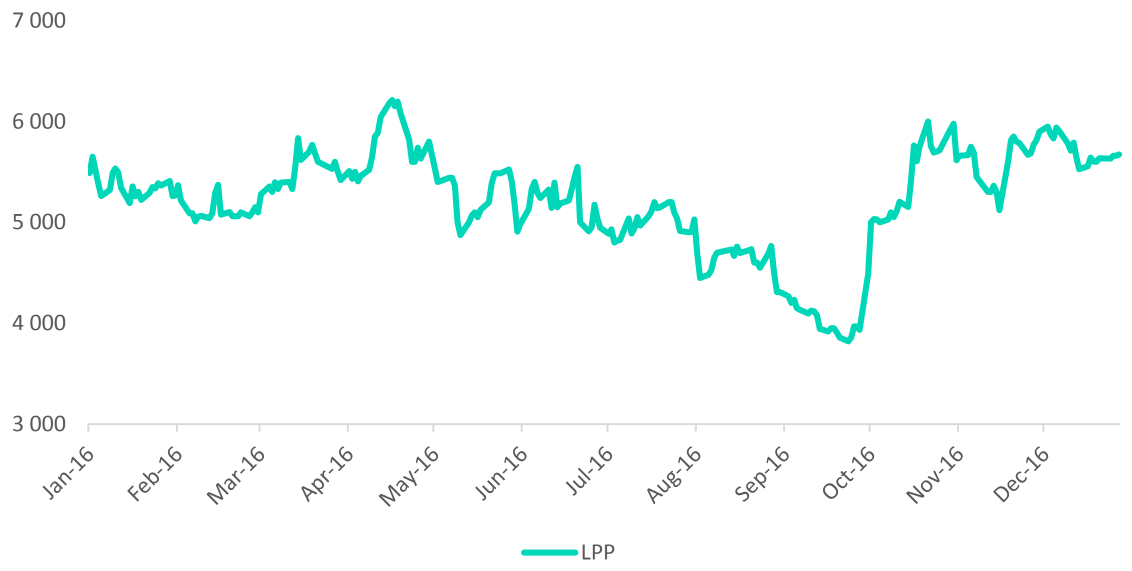
As at 31 December 2016, shares in LPP SA were constituents of the following stock exchange indices:

1. WIG-Poland – a national index comprising only shares in Polish companies listed on the main market of the WSE, which meet basic criteria for being index constituents. The share of LPP SA in WIG-Poland was 2.6%.
2. WIG20 – an index calculated on the basis of the value of the portfolio of 20 largest and most liquid companies from the main market of the WSE. LPP SA has been a constituent of the said index since 2014, with its share amounting to 4.1%.
3. WIG30 – index comprising 30 largest and most liquid companies listed on the main market of the WSE. The share of LPP SA in WIG30 is 3.8%
4. WIG-Clothes – a sub-sector index including WIG constituents which simultaneously belong to the "clothes and cosmetics" sector. As at 31 December 2016, the said index was not published yet. At present, the share of LPP in WIG-Clothes is 54.5%,
5. MSCI Poland Index – an index including over 20 key companies listed at the WSE. LPP SA has been a constituent of the said index since 2014.

The price of LPP SA shares as compared to WIG20 in 2016



The price of LPP SA shares in 2016



5.3.6. Share-related limitations and shareholders with special control rights

The shareholders with shareholdings conferring the right to more than 15% at the General Meeting exercise their voting right up to 15% of votes, regardless of the number of votes arising from the shares held. Two shareholders, who have managed the company for many years, Mr. Jerzy Lubianiec and Mr. Marek Piechocki, hold each directly 174 999 shares of the B series and indirectly 1 share of the B series, preferred in terms of voting rights, with a single share giving right to 5 votes at the General Meeting of Shareholders. In addition, shares of the said shareholders are not covered by the statutory limitation described above, limiting voting rights only up to 15% of votes at the General Meeting of Shareholders regardless of the number of shares held. The above-mentioned provisions of the Articles of Association give the dominant position to the two shareholders indicated above.

Subject to the information given above, there are no other securities giving any special control rights.

Limitations on transferring the ownership title to securities apply to registered shares.

The sale or pledging of registered shares requires approval of the Company. Permits for selling or pledging shares are granted by the Supervisory Board in writing, otherwise being null and void, within 14 days from the date of application. If the Company refuses to give the permit, it should designate another buyer and define the date and place of payment of the price within 30 days. If, within the above-mentioned time-frame, the Company does not indicate another buyer, shares may be sold without any limitations.

5.4. Governing bodies

5.4.1. Management Board of LPP SA

Composition

Composition of the Management Board as at 31 December 2016:
- Marek Piechocki – President of the Management Board
- Przemysław Lutkiewicz - Vice-President of the Management Board
- Jacek Kujawa- Vice-President of the Management Board
- Sławomir Łoboda - Vice-President of the Management Board

At the same time, in 2016, there were changes in the composition of the Management Board, consisting in the resignation by Mr Piotr Dyka from his position as Member of the Management Board of LPP SA (CR 12/2016) and the resignation by Mr Hubert Komorowski from his position as Member of the Management Board of LPP (CR 45/2016).

The scope of competence of, and working rules for, the Management Board of LPP SA are set forth in the following documents:
- LPP SA Articles of Association (available on the Company's website)
- Management Board By-Laws (available on the Company's website)
- Commercial Companies Code

Rules for appointing and dismissing key management officers and the scope of competence of the Management Board
The Management Board consists of two to six members, including the President, and from one to five Vice-Presidents. The number of members is determined by the Supervisory Board.
Members of the Management Board are appointed for a term of five years and dismissed by the Supervisory Board.
The scope of competence of, and working rules for, the Management Board of LPP SA are set forth in the following documents:
- LPP SA Articles of Association (available on the Company's website)
- Management Board By-Laws (available on the Company's website)
- Commercial Companies Code

The Management Board is responsible for any and all matters not falling within the scope of competence of other governing bodies of LPP SA.
The Management Board is not entitled to make decisions on the issue or buy-out of shares.

Agreements with key management officers, providing for a compensation
No agreements were concluded with key management officers, which would provide for a compensation in case of their resignation or dismissal from their position otherwise than on solid grounds or if they are recalled or dismissed as a result of the issuer's merger by acquisition.

Remuneration of key management officers

Values of all remunerations of key management and supervision officers are given in point 15.22.1 of the Notes.

5.4.2. Supervisory Board of LPP SA

Composition

The composition of the Supervisory Board as at 31 December 2016 was as follows:
- Jerzy Lubianiec - Chairman of the Supervisory Board
- Krzysztof Olszewski - member of the Supervisory Board

- Wojciech Olejniczak - member of the Supervisory Board
- Maciej Matusiak - member of the Supervisory Board
- Dariusz Pachla - member of the Supervisory Board

During the financial year, there were no changes in the composition of the Supervisory Board.

The scope of competence of, and working rules for, the Supervisory Board of LPP SA are set forth in the following documents:
- LPP SA Articles of Association (available on the Company's website)
- By-Laws of the Supervisory Board (available on the Company's website)
- Commercial Companies Code

Supervisory Board Committees
In the financial year 2016, and by the date of publishing this report, no special-task committees were appointed within the Supervisory Board. Due to the fact that the Supervisory Board is composed of five persons, the tasks of the Audit Committee, specified in the Statutory Auditors Act […], are carried out by the entire Supervisory Board collectively.
The statutory tasks in that respect, comprise, in particular, the following:
1) monitoring of the financial reporting process;
2) monitoring of the effectiveness of internal audit systems, internal audit and risk management;
3) monitoring of performance of financial auditing activities;
4) monitoring of the independence of a statutory auditor and the entity authorised to audit financial statements, including in cases of the provision of services, referred to in Article 48 paragraph 2 of the Statutory Auditors Act (…), such as the services covering the keeping of accounting books and tax records as well as tax advisory services.
Furthermore, when performing the tasks of the Audit Committee, the Supervisory Board reviews written information from the entity authorised to audit financial statements on material issues relating to financial auditing activities, including, in particular, significant irregularities in the entity's internal audit system versus the financial reporting process, threats relating to the independence of the entity authorized to audit financial statements and activities performed in order to limit any such threats.
If the number of members of the Supervisory Board is increased to exceed 5 members, then an audit committee will be appointed within the Board, as provided for in the Company's Articles of Association.

5.5. Mode of action of the General Meeting, its powers, the description of shareholders' rights and the way of their exercise

Convention of the General Meeting of Shareholders
1) The General Meeting of Shareholders may be convened in an ordinary or extraordinary mode.
2) The General Meeting of Shareholders is held in Gdańsk, Warsaw or Sopot, at the place designated by the Management Board.
3) The Annual General Meeting is held within six months after the end of a financial year.
4) The Extraordinary General Meeting is convened by the Management Board on its own initiative, at the request of the Supervisory Board and at the written request of shareholders representing one twentieth of the equity capital.
5) The fact of convening the General Meeting, stating the date (day, hour) and place, is announced by the Management Board on the Company's website, in the manner provided for conveying current information and in accordance with the provisions on public offering, as well as terms and conditions for introducing financial instruments to an organised trading system, and on public limited companies.

Scope of competence of the General Meeting
1) Examining and approving financial statements and reports of the Management Board on the activity of LPP SA for the previous year.
2) Taking all decisions relating to claims for damages suffered during the establishment of LPP SA or its management or supervision.
3) Adopting a resolution on the distribution of profits or covering losses.
4) Discharging the LPP SA Board members from the fulfilment of their duties.
5) Adopting a resolution on the issue of bonds, including convertible bonds.
6) Amending the Articles of Association.
7) Adopting resolutions on a merger, conversion of LPP SA, its dissolution and liquidation.
8) Adopting resolutions on the sale and lease of the company and establishing beneficial ownership.

9) Examining and deciding on proposals submitted by the Supervisory Board.
10) Deciding on other matters falling within the scope of competence of the General Meeting in the Commercial Companies Code and the provisions of the Company's Articles of Association.

Sessions of General Meeting of Shareholders

1) General Meeting is opened by the Chairman of the Supervisory Board or a person authorised by him, who then holds the elections for Chairperson of the General Meeting.
2) The person opening the General Meeting provides for an immediate election for Chairperson of the General Meeting, who directs the works of the GM and ensures efficient and proper conduct of the session.
3) The General Meeting adopts resolutions only on items put on the agenda.
4) Draft resolutions proposed for adoption by the General Meeting and other relevant issues are presented to the shareholders together with a justification and the opinion of the Supervisory Board.
5) The course of the General Meeting is recorded by a notary public.

Voting

1) Voting at the General Meeting is open. Secret voting takes place at the election of governing bodies and at requests to dismiss the Company's governing bodies or liquidators or to make them accountable, as well as in case of personal matters. In addition, secret voting is held at the request of any shareholder or their representative.
2) The General Meeting may choose a three-person ballot counting committee, whose duties include ensuring the proper conduct of each voting, supervising computer service (in the case of voting with the use of electronic technology) as well as reviewing and announcing the results.
3) Each share entitles to one vote at the General Meeting. In the case of a series B preferred share, one share entitles to five votes at the GM.
4) The Chairperson announces voting results, which are then recorded in the minutes of the session.

5.6. Description of rules for amending the Issuer's articles of association

Any amendment to the Articles of Association requires a resolution of the General Meeting.

6. Supplementary information

6.1. Proceedings before a court or a competent arbitration authority

Neither LPP SA nor any of its subsidiaries is a party to any proceedings before a court, a competent arbitration authority or a public administration body, involving liabilities or receivables of a single or total value exceeding 10% of the equity of LPP SA.

At the same time, LPP SA informs that, due to a tax audit procedure carried out since 2015 by the Tax Audit Office in Gdańsk (further referred to as “TAO”), of which the Issuer informed in preceding quarterly reports, on 20 January 2017, the Company received the analysis of evidence material collected during the audit procedure covering the reliability of declared tax bases and correctness of calculation and payment of CIT for 2012.
In the current report of 20 January 2017 (CR 04/2017), the Company informed of the maximum amount of tax with interest, which could be potentially charged to the Company if the TAO issued a decision based on the findings adopted by the TAO in the said analysis.
On 6 February 2017, the Issuer filed a letter with the TAO, in which the Issuer presented its standpoint on the analysis of evidence material, made by the TAO.
The Company’s Management Board holds the view that LPP SA has correctly settled its income tax and that there are no prerequisites under which the TAO could issue a decision charging the Company with an additional tax liability for 2012.
The audit procedure has not been completed yet due to the continuing works of the TAO, aimed at determining the facts of the case.

6.2. Information on key achievements in research & development

In the reporting period, the LPP SA Capital Group conducted research and development works related to the design and construction of model RESERVED, House, SiNSAY and Tallinder brand stores.

6.3. Information on the policy in the field of business sponsorship, charity or any other similar policy

Due to the nature of our business, since 1996, we have donated our brand clothing for charitable purposes. Annually, aid in this form is provided to almost one hundred and twenty non-governmental organisations (associations and foundations) in Poland. In the years 1996-2016, as part of this aid, LPP SA donated over PLN 18 million net.

As one of the largest employers in Pomerania, LPP SA is actively supporting the local community. In just the past few years, together with its Partners, the Issuer has implemented numerous social projects. On the initiative of people employed in LPP SA, a corporate volunteering programme is run, within which actions are taken for the benefit of people and organisations in need of support.

To date, the company focused mainly on aid for the sick, children and the youth at risk of social exclusion, investing its funds in projects that counteract the above:

■ Since 2010, in December, in the company's registered office, the LPP employees' action "Santas' Time" is carried out: employees collect funds and then, with financial support of the company, prepare Christmas gifts for a selected local organisation (for the last few years, it was Caritas Gdańsk). So far, more than 550 people in need from Gdańsk and Cracow have benefited from our support. Thanks to the engagement of our employees, in 2016, the “Santas’ Time” was completed with a record-breaking figure, and we gave donations, either in goods or in cash, of a value exceeding PLN 100 thousand.

■ For many years, LPP SA has been also co-operating with the Gdańsk Hospice Foundation. Our cooperation started over 10 years ago. Apart from encouraging customers to transfer 1% of their income tax for the organisation and donating clothes and gift cards to our stores that go to dozens of hospice establishments, the Issuer has been supporting the Foundation also financially. The financial assistance provided to the Foundation in 2013-2016 amounted to over PLN 140 thousand. In 2016, LPP SA became a partner of the Orphans Fund, having donated funds for scholarships for 42 children supported by that Fund.

■ In September 2016, LPP SA informed of having joined the Fur-Free Retailer programme. The collections of all 6 brands, starting from AW 2016, will be totally fur-free. It means that there will never be natural fur in any form, including accessories and winter jacket trims. The Company has signed a relevant memorandum with the Open Cages Organisation. The decision of LPP SA has been highly welcomed by clients, non-governmental organisations and other interested parties.

■ In 2016, LPP SA signed an agreement for the preparation and organisation of a joint programme for employment activation of beneficiaries of the Social Innovations Foundation. The beneficiaries of the Foundation will gain their first professional experience through training sessions, by getting prepared for the requirements of the labour market and, ultimately, by being employed in the Issuer’s sales network.

In 2016, a separate position was established in the Company, namely CSR Coordinator, in Corporate Communication and Sustained Development Department. The duties of the CSR Coordinator cover, among others, the implementation and execution of the CSR strategy, preparation for non-financial reporting and the implementation of a policy for performing sponsorship and charity activities, which currently has no form of document.

6.4. Information on the entity authorised to audit financial statements

On 30 June 2014, LPP SA concluded with Grant Thornton Frąckowiak Sp. z o.o. Sp. K. an agreement for the audit of the annual financial statements of the Company and the LPP SA Capital Group for the years 2014, 2015 and 2016, and a review of interim financial statements of the Company and the LPP SA Capital Group for the above-mentioned years.
The fee of the entity authorised to audit and review the financial statements for the financial and for the previous year amounted to:

1) auditing the financial statements for the period from 1 January 2016 to 31 December 2016, giving opinion on it and preparing the audit report - PLN 60 thousand plus VAT.
2) auditing the Capital Group's consolidated financial statements for the period from 1 January 2016 to 31 December 2016, giving opinion on it and preparing the audit report - PLN 30 thousand plus VAT.

3) auditing the interim financial statements for the period from 1 January 2016 to 30 June 2016 and preparing the audit report - PLN 30 thousand.
4) auditing the consolidated interim financial statements for the period from 1 January 2016 to 30 June 2016 and preparing the audit report - PLN 20 thousand plus VAT.
5) auditing the financial statements for the period from 1 January 2015 to 31 December 2015, giving opinion on it and preparing the audit report - PLN 60 thousand plus VAT.
6) auditing the Capital Group's consolidated financial statements for the period from 1 January 2015 to 31 December 2015, giving opinion on it and preparing the audit report - PLN 30 thousand plus VAT.
7) auditing the interim financial statements for the period from 1 January 2015 to 30 June 2015 and preparing the audit report - PLN 30 thousand plus VAT.
8) auditing the consolidated interim financial statements for the period from 1 January 2015 to 30 June 2015 and preparing the audit report - PLN 20 thousand plus VAT.

Additionally, in 2015, Grant Thornton Frąckowiak Sp. z o.o Sp. K. provided other services for which it received a fee of PLN 383 thousand plus VAT.

Management Board of LPP SA:

Marek Piechocki – President of the Management Board ....

Przemysław Lutkiewicz – Vice President of the Management Board …..…………………………………………..

Jacek Kujawa – Vice President of the Management Board ………………………………………………

Sławomir Łoboda – Vice President of the Management Board ....

Gdańsk, 6 April 2017

V. Statements of the Management Board of LPP SA

STATEMENT OF THE MANAGEMENT BOARD

In line with the Regulation by the Minister of Finance dated 19 February 2009 on current and interim information provided by issuers of securities, the Management Board of LPP SA hereby declares that:

- to the best of the Board's knowledge, the annual consolidated financial statements for the financial year 2016 and comparative data have been prepared in line with accounting principles currently in effect and present a true and fair view of the assets, the financial standing and the financial result of the LPP SA Capital Group and LPP SA in the periods presented, and that the report of the Management Board on the operations of the LPP SA Capital Group in 2016 presents a true and fair view of the development, achievements and the standing of the LPP SA Capital Group and LPP SA, including an accurate description of risks and threats,

- the entity authorised to audit financial statements, which conducted the audit of the annual consolidated financial statements of the LPP SA Capital Group and the separate financial statements of LPP SA, was appointed in line with applicable legal provisions currently in effect. This entity and statutory auditors, who performed the audits, satisfied all requirements to prepare an impartial and independent report on the audited annual financial statements, pursuant to the applicable provisions of law and professional standards.

Management Board of LPP SA:

Marek Piechocki – President of the Management Board ....

Przemysław Lutkiewicz – Vice President of the Management Board ……………………………………………..

Jacek Kujawa – Vice President of the Management Board ………………………………………………

Sławomir Łoboda – Vice President of the Management Board ....

Gdańsk, 6 April 2017