

## **2016 ANNUAL ACTIVITY REPORT OF THE CODERE, S.A. AUDIT COMMITTEE**

### **1.- INTRODUCTION**

We are pleased to present the 2016 Annual Activity Report of the Codere, S.A. Audit Committee. Article 14.2.g of the Regulations of the Board of Directors of Codere S.A. states that this committee must draw up a brief report describing the activities carried out by the Committee within the year.

Additionally, the Code of Good Governance of Listed Companies, provides in Recommendation No. 6:

*"Listed companies shall develop the reports listed below, either mandatory or voluntary, and publish them on their website in time for the holding of the annual general meeting, although their distribution is not mandatory:*

- a) Report on auditor independence.*
- b) Reports on the functioning of the audit committee, and the appointments and remuneration committee.*
- c) Report of the audit committee on related party transactions.*
- d) Report on the corporate social responsibility policy".*

This Annual Report of the Audit Committee of Codere S.A. for the year 2016 has been approved by the Committee at its meeting held on January 12th 2017. The Audit Committee shall recommend to the Board of Directors that this Annual Report be made available to the Company shareholders for the next Ordinary General Meeting of Shareholders.

In application of the best principles of transparency in corporate governance, since the 2015 the Annual Activity Report of the Audit Committee of Codere, S.A. has been made available to shareholders simultaneously with the convening of the Annual General Meeting, and can be consulted on the corporate website and by requesting the free delivery of a copy.

### **2. MEETINGS AND COMPOSITION OF THE AUDIT COMMITTEE.**

During 2016, the Audit Committee held a total of 15 meetings.

During 2016, as a result of successful restructuring undertaken by the Company, the composition of the Board of Directors of Codere, S.A. was modified, reducing the number of its members to 9. This change in the composition of the Board was reflected in the Audit Committee, producing a change in all the members thereof.

Accordingly, until 28 April 2016, the composition of the Committee was as follows:

Mr. Joseph Zappala	Independent	Chair
Mr. Juan Junquera Temprano	Independent	Member
Mr. Eugenio Vela Sastre	Other external director	Member
Mr. Juan José Zornoza Pérez	Other external director	Member
Mr. José Ramón Romero Rodríguez	Nominee	Member

The new Board of Directors of Codere, S.A. met on 5 May 2016, and among other matters, agreed to modify the composition of the Audit Committee. Since then the composition has not been modified and since the date of issuance of this report, the composition is as follows:

Mr. Matthew Turner	Independent	Chair
Mr. Norman Sorensen Valdez	Independent	Member
Mr. Timothy Lavelle	Nominee	Member

According to art. 13.5 of the Regulations of the Board, Director Mr. Manuel Martínez-Fidalgo Vázquez also attends the meetings as an observer, with a right to speak but not to vote.

The composition of the Committee meets the requirements of current legislation and with the provisions of Article 529 of the Capital Companies Act, which states that:

*“The audit committee shall be comprised exclusively of non-executive directors appointed by the board of directors, most of whom, at least, must be independent directors and one of them shall be appointed taking into account their knowledge and experience in accounting, auditing or both.*

*As a whole, the committee members shall have the relevant expertise in relation to the business sector to which the audited entity belongs.”*

The Secretary of the Committee is the Secretary of the Board of Directors, as provided under Article 13.4 of the Regulations of the Board of Directors of "Codere, S.A.".

### 3.- 2016 ANNUAL ACTIVITY REPORT

As provided under article 14 of the Rules of Procedure of the Board of Directors, the Audit Committee has among its functions the following:

- (a) *Inform the General Meeting of Shareholders about the matters posed at said General Meeting by shareholders in regard to matters which are the competence of the Audit Committee.*
- (b) *Propose to the Board of Directors the appointment of external auditors in order that the Board may submit the proposal to the General Meeting of Shareholders.*
- (c) *Supervise internal audit services.*
- (d) *Be informed of the financial information process and internal control systems.*
- (e) *Maintain relations with external auditors in order to receive information in regard to those matters which might jeopardize the independence of the latter, and any other*

*matters related to the audit process, and likewise to receive information and maintain with the auditor the communications stipulated by law.*

*(f) Report on the annual accounts as well as on issue prospectuses, and on the periodical financial information which is to be sent to the regulatory agencies quarterly or every six months, paying special attention to compliance with the legal requirements and the correct application of the generally accepted accounting principles, to the existence of internal control systems and to the monitoring thereof, and to compliance with internal auditing.*

*(g) Once a year draft an annual report containing the activities carried out by the Committee.*

*(h) Supervision of the communication strategy and relations with shareholders and investors, including small and medium shareholders.*

*(i) Supervision and evaluation of processes associated with different stakeholders.*

### *3.- In particular, the Audit Committee shall:*

#### *1. In relation to the information systems and internal control:*

- a) Supervise the process for the drafting, presentation and completeness of the financial reporting related to the Company and, if applicable, to the group, reviewing compliance with the regulatory requirements, the proper delimitation of the scope of consolidation and the correct application of the accounting criteria.*
- b) Periodically revise the internal control and risk management systems, so that key risks may be adequately identified, managed and disclosed;*
- c) See to it that the internal audit function is run independently and efficiently; propose the selection, appointment, re-election and dismissal of the person in charge of the internal audit system; propose the budget for this service; receive periodical information on its activities; and verify that senior management take into account the conclusions and recommendations contained in its reports;*
- d) Report, at least once a year, to the Board of Directors in regard to matters of risk control and any malfunctions detected, if applicable, in the internal audit reports or in the exercise of the above listed functions.*

#### *2. In relation to the external auditor:*

- a) Submit to the Board proposals regarding the selection, appointment, re-election and replacement of the external auditor, as well as the auditor's contract conditions;*
- b) Receive on a regular basis from the external auditor information regarding the audit plan and the results of its implementation, and verify that senior management take into consideration the recommendations thereof.*
- c) Ensure the independence of the external auditor and, in this regard:*
  - i) That the company communicate the change in auditor as a relevant fact to the Spanish Securities and Market Commission (CNMV), together with a statement on the eventual existence of disagreements with the outgoing auditor and, if such disagreements had existed, what they consisted of;*
  - ii) Ensure that the company and the auditor respect the regulations in force regarding the provision of services other than auditing services, the limits to the concentration of the auditor's business and, in general, all other norms established to ensure the independence of the auditors;*
  - iii) That in the event that the auditor should choose to resign, the Committee examine the reasons why.*

- d) Favour the circumstance whereby the auditor of the group, if applicable, takes on the responsibility for auditing the companies comprising the group.*
  - e) Discuss with the auditors or audit firms any significant weaknesses in internal control identified in the performance of the audit.*
  - f) Establish appropriate relationships with the auditors or audit firms to receive information on any issues that might jeopardize their independence, for consideration by the Committee or any others related to the performance of the audit process, as well as other communications provided for in audit legislation and auditing standards. In any case, the Audit Committee shall receive annually from the auditors or audit firms written confirmation of their independence from any directly or indirectly related entity or entities thereof, and information of any additional services of any class provided to said entities by said auditors or audit firms, or by persons or entities linked to them in accordance with the provisions of Law 19/1988 of 12 July, on Account Auditing.*
  - g) Annually issue, prior to issuance of the audit report, a report which will express an opinion on the independence of the auditors or audit firms. This report shall, in any case, report on the provision of additional services as referred to above.*
- 3. Inform the Board, prior to adoption by the latter of the decisions which are reserved to it under article 7.17 of these Rules, in regard to the following matters:*
- a) The financial information which, given that it is a listed company, the company is required to make public periodically. The Committee should ensure that the intermediate accounts are drafted using the same accounting criteria as the annual accounts and, for this purpose, consider the suitability of a limited revision by the external auditor;*
  - b) The creation or acquisition of shareholdings in special-purpose companies or those domiciled in countries or territories considered to be tax havens, as well as any other similar transactions or operations which, given their complexity, may diminish the transparency of the group;*
  - c) Related-party transactions.*
- 4.- That the risk control and management policy identify at least the following:*
- a) The various types of risk (operational, technological, financial, legal, reputation, etc.) faced by the company, including among the financial or economic risks contingent liabilities and other off-balance-sheet risks.*
  - b) The establishment of the risk level which the company considers acceptable;*
  - c) The measures planned to mitigate the impact of identified risks, should they materialize;*
  - d) The information and internal control systems which will be used to control and manage the aforesaid risks, including contingent liabilities or off-balance-sheet risks.*

The main issues that have been handled and analysed by the Committee during 2016, and that have shaped its main areas of supervision, can be grouped into the following five areas:

**1) In relation to the external auditor:**

During the year 2016, and in relation to the external auditor, the Committee has undertaken various functions:

- a) With regard to the need to submit proposals to the Board of Directors for the selection, appointment, reappointment and removal of the external auditor, and the conditions of their employment (art. 14.3.2a. of the Regulations of the Board of Directors of Codere, S.A.), in 4 different meeting (25 February, 28 March, 12 May and 19 May 2016) the Committee discussed and decided to propose to the Board of Directors to replace the external auditor, PWC, and appoint a new auditor of the Company and its Group, "ERNST & YOUNG, S.L.". The Board of Directors agreed to propose the above appointment to the General Meeting of Shareholders in written agreements without a meeting dated 24 May 2016.
- b) In connection with its function of receiving information on the audit plan from the external auditor and the results of its execution (art. 14.3.2b. of the Regulations of the Board of Directors of Codere, S.A.), the Committee has undertaken this competency four times. Accordingly, in its meeting on 25 February, the Audit Committee received information from the auditors of PWC on the closure of the 2015 audit, reporting on the most relevant aspects. Subsequently, the Audit Committee received information from the new external auditor "ERNST & YOUNG, S.L." on the Work Plan and its performance, in the meetings of June, November and December 2016.
- c) To ensure the independence of the external auditor (art. 14.3.2 f and g. of the Regulations of the Board of Directors of Codere, S.A.) in its meeting of February 2016, prior to the issuance of the audit report, the Committee issued a report expressing its opinion on the independence of the audit firm. In the same meeting, the Committee received written confirmation from PWC of its independence from Codere, S.A. and its group, as well as information on additional services of any kind provided by said audit firm.

**2) With regard to its task of supervising the internal audit (art 14.2.c of the Regulations of the Board of Directors):**

During 2016, the Audit Committee supervised the internal audit services in four of its meetings.

Specifically, in the meeting in February, the head of the internal audit function submitted a report to the Committee on the activities undertaken during 2015. At the same meeting, the Committee was informed of the recommendations of internal audit work during the fourth quarter of 2015.



In the June meeting the head of internal audit informed the new members of the Committee of the objectives for 2016 and the planning of internal audit work. Additionally, he submitted to the Committee a summarisation of the results of the internal audit in the first quarter of 2016.

In the August and November meetings, the Committee was informed of the main findings of the internal audit in the second and third quarters of 2016 (respectively) and the recommendations of the department.

**3) With regard to the task of reporting on the annual financial statements, as well as the prospectuses and periodic financial information to be submitted to the regulatory authorities on a quarterly or semi-annual basis (art. 14.2.f of the Regulations of the Board of Directors):**

During 2016, the Audit Committee has handled these issues six times. Specifically, the Committee discussed the individual and consolidated financial statements and management reports for the year ended 31 December 2015 (February meeting), the results for the first quarter of 2016 (May meeting), the results of the first half of 2016 (August meeting) and the results for the third quarter of 2016 (November meeting). In March and April, the Committee also revised the prospectus which was later sent to the CNMV regarding the restructuring process.

**4) With regard to the task of supervising the information systems and internal control and regularly reviewing internal control and risk management systems, including tax systems (art 14.3.1.b of the Regulations of the Board of Directors):**

During 2016, the Committee exercised these functions throughout the year, and more specifically in four meetings.

In the January meeting, the Committee was informed about the tax status of the Company in order to be able to review the status of compliance with the new obligations. The review of the status of existing tax controls within the Group and to implement processes to analyse, prevent and mitigate risks in tax matters was entrusted to an external advisor.

In the February meeting, the Committee reviewed the document on tax communication policy of the Board of Directors, with the Committee agreeing to submit it to the Board for approval (which occurred in their meeting of 25 February 2016).

In the meeting of June 2016, the Committee was informed about the state of cybersecurity and action plans. The Committee instructed the supervisor of this field to prepare a risk



analysis, settlement mechanisms, cost and precise time set to move from the current situation to the desired.

Lastly, in November 2016, the Committee analysed the risk map for 2017, compared with that for 2016, which was approved in a meeting of the Board of Directors on 10 November.

#### **5) Other matters within the scope of the Committee:**

In addition, the Committee discussed and analysed other matters that are subject to its jurisdiction throughout 2016.

In relation to the proper application of generally accepted accounting principles, the Committee discussed and reviewed the accounting restructuring agreement on four separate occasions, specifically on 17 June and 23 and 25 August.

In addition, the Committee discussed the status of operations and financial position of the subsidiary Carrasco Nobile in 4 different meetings and duly informed the Board of Directors of the different options.

In addition, the Audit Committee has studied twice (in February and December 2016) the status of operations and financial position of the subsidiaries Codere Do Brasil Ltd. and Simulcasting Brasil Som e Imagem Ltd.

Lastly, in its meeting in December 2016, the Audit Committee analysed and discussed a first draft budget for 2017 and the advisability of extending certain loans granted previously to directors and officers of the group, among other matters.

**Madrid January 12th 2017**