



5 November 2012

Sebastian Bednarczyk
Australian Securities Exchange
Level 8 Exchange Plaza
2 The Esplanade
PERTH WA 6000

Dear Sebastian

ASX Query Response

Introduction

We refer to your letter dated 1 November 2012. Before responding to your letter, VDM Group Limited ("VDM"; "the Company") believes that it is important to provide some pertinent background so that the responses can be given some context.

On 24 September 2012, management provided the Board of Directors of the Company with its management report for the month of August that included the trading performance for the first two (2) months of the financial year, together with a projection regarding the forecast first half result. At this point in time, the trading performance, whilst behind budget expectations, forecast positive earnings for the first half that was consistent with previous guidance provided to the market of a profitable first half.

Included within this management report was a summary of risks and opportunities for each area of the business. The management report noted that the first half forecast was, in part, dependent upon resolution of certain contract claims and variations at levels acceptable to the Company.

During the course of October, a number of individual events occurred that would impact on the Company, not least of which was a change in the economic conditions of the core markets in which the Company operates.

The Company was verbally advised on 18 October 2012 by a client of its Western Operations business unit that the client intended to reduce the VDM contracted scope of work. The reduction in scope is due to client accommodation shortages at the remote project location. As at the date of preparing this response, the impact of the scope reduction is not clear, however, the Company does expect that the impact of this will be negative to our earnings for the period.

The Company is also performing another construction project at the same site. On or about that same date, the Company was advised by the superintendent of the second project that the number of rooms to be made available to the Company would be restricted. The consequence is that the Company is unlikely to be able to execute the works in a sequence and schedule that the Company would like to be able to, potentially leading to an increase in total cost on this project.

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Discussions regarding room numbers and possible alternate solutions are ongoing with the client and a definitive assessment of the impact to the Company cannot be completed until such time as these matters are certain, including resolution of any variations to the respective contracts that the Company may be entitled to as a result of the client directions regarding accommodation shortages.

On 19 October 2012, management provided the Board of Directors of the Company with its management report for the month of September that included the trading performance for the first three (3) months of the financial year. In this report, management noted to the Board that the first half earnings forecast had not yet been updated as management was in the process of reforecasting the period. This reforecast would also encompass the cost impact of redundancies that were also announced on the 26th October.

Management advised the Board that a preliminary review of the first half forecast would be completed and distributed to the Board on 24 October 2012. The Board then had an opportunity to briefly review the range of outcomes in the preliminary review before consulting with management during the Board meeting held on 25 October 2012. As a result of the review of the range of possible earnings outcomes and subsequent discussion in the Board meeting, the Company decided to enter a pre-open Trading Halt before the trading day of 26 October 2012 commenced, whilst it finalised its guidance.

Following the Board meeting on 25 October 2012, management and the Board completed a detailed review of the underlying assumptions concerning a number of individual matters that were likely to negatively impact on first half earnings, including the following:

- The recoverability and collectability of unpaid amounts billed to various clients by the NSW and Victorian consulting business prior to their disposal in early June 2012 (noting that invoices issued by the now disposed NSW and Victorian consultancy businesses prior to the date of disposal remain for the benefit of the Company);
- The ability to invoice work in progress, and the recoverability and collectability of unpaid amounts billed to various clients by the WA Engineering consulting business for work primarily done for property and land development clients;
- The recoverability and collectability of amounts owing to VDM from joint venture partners on a legacy land development transaction as a result of VDM taking possession of the land as mortgagee in possession in late October 2012;
- Assessment of the probable earnings of the aforementioned construction projects that have been subject to scope reductions and/or accommodation shortages;
- Re-assessment of the probable amounts to be recovered as claims and variations on a number of construction projects;
 - One project has recently been completed and is subject to a number of factors that determine final revenue and earnings on the project, including a complete re-measure of the quantity of work carried out on parts of the project. At the time of preparing this response, the complete re-measure was still in progress.
 - A second project is part way through construction and requires management to make an assessment of the likely amounts to be recovered as a result of delays caused by the client.



- A third project was subject to adjudication of claims under the Construction Contracts Act, 2004, and following a complex determination against the Company on the 20th September 2012, management has subsequently taken a more conservative position on the recoverability of outstanding payments that are in dispute.
- An assessment of variations on other projects under construction all of which were not material on either an individual or aggregated basis, but which in combination would impact on the likely range of profitability for the Company.

Management then met with the Board on 27 October 2012 to review the preliminary re-assessment of the probable earnings range. A further meeting between management and the Board occurred on 28 October 2012 to finalise outstanding questions raised by Directors to management, and to complete the finalisation of the likely earnings range (being that announced to the market on 29 October 2012).

Whilst the individual items that comprise all of the above, together with other operating performance outcomes, do not cause a material impact on earnings in their own individual capacity, the aggregation of all items has led to a material impact on earnings. As a result, the probability re-assessment of the likely outcomes of all of the above items gave rise to the aggregate expected earnings range that was announced on the ASX on 29 October 2012.

Engineering and Construction Profit Recognition

The primary source of revenue for the Company is the tendering and execution of construction projects, predominantly on a fixed price or schedule of rates basis. The determination of the amount of revenue to be recognised at any point in time requires management to estimate the probable revenue that will be derived from a project, together with the probable cost that will be incurred to complete the project. Both of these items are fluid in their nature, especially when the bulk of construction projects executed by companies in the same market segment as the Company are often subject to variation as a result of client directed scope changes during the performance of a project.

We would like to draw your attention to two (2) notes to our Financial Statements for the Year Ended 30 June 2012, as contained in our 2012 Annual Report.

Note 1(h) (Contracts in Progress) refers to the conditions upon which the outcome of a fixed price construction contract can be estimated reliably, including the satisfaction of the test requiring that "it is probable that the economic benefits associated with the contract will flow to the entity".

Note 3 (Significant Accounting Judgements, Estimates and Assumptions) makes reference to the fact that "management bases its judgements and estimates on historical experience and on other various factors it believes to be reasonable under the circumstances,.....". This note goes on to further state that "Actual results may differ from those estimates under different assumptions and conditions and may materially affect financial results or the financial position reported in future periods".

Whilst both of the aforementioned notes to the financial statements refer to the basis of preparing the financial statements, they apply equally to the basis of preparing forecast earnings on construction contracts. Most importantly, they require judgements and estimates to be made based on factors believed reasonable at the time, and that actual results may differ from these estimates under different assumptions and conditions.



In the case of the construction contracts referred to in the Introduction section above, the assumptions and conditions applying to those contracts are continually changing as construction activities on a project progress and as negotiations on claims and variations progress. As such, they require management to make assumptions and estimates at varying points in time that represent management's reasonable assessment of the probable outcome.

The Company would like to point out that the expected outcome on the contracts referred to in the announcement made to the ASX on 29 October 2012 represent management's assessment of the probable outcome of revenue, costs, claims and variations on these contracts. This assessment is made as of that date taking into account the factors that management believes to be reasonable as at that date.

As described in the Introduction section above, the Company is currently in negotiations with its clients on the two projects referenced in the ASX announcement that have not yet been resolved. At the time of making the ASX announcement, and at the time of preparing this response, no definitive position has been agreed with either client.

It is still possible that the final outcome on any of the referenced projects may vary from the outcome currently estimated by management.

Responses to Questions

Question 1

No, the Company does not consider that the Contract Claims and Variations on each individual contract is material.

Question 2

The Company has become progressively aware of the Contract Claims and Variations over the past four (4) months. No one single event or instance has caused the claims and variations. As negotiations with our clients on both contracts are currently in progress, the Company believes that the provisions of Listing Rule 3.1A apply. To disclose further information regarding the Contract Claims and Variations may materially jeopardise the commercial position of the Company.

Question 3

Not applicable.

Question 4

The basis that the Company does not consider the information to be material is that on an individual basis, they are not material.

Question 5

No.



Question 6

The Company became aware of the increased provisions during late October as part of a comprehensive review of all outstanding debtor amounts. This was a progressive awareness between 15 October 2012 and 26 October 2012.

Question 7

Not applicable.

Question 8

The Company does not consider that the individual circumstance of the increased provisions to be material. When treated in their own right on an individual circumstance basis, they do not result in a material impact.

Question 9

No.

Question 10

The accommodation shortages referred to in the announcement impact two construction projects on one site, with each project controlled by a different Superintendent. The Company became aware of the accommodation shortages at the site during the week ending 19th October. This information was provided verbally and in writing to the Company by the respective Superintendents at the end of that week, with some detail (including an alternative solution offered by the Company) still awaiting clarification.

Question 11

Not applicable.

Question 12

The Company does not consider that the individual circumstance of the accommodation shortage to be material.

Question 13

Yes.

Question 14.1

The Company did not make an announcement at an earlier time as management did not have a full complete assessment of all of the Impacting Factors until the time of the announcement. To have made an announcement any earlier may have resulted in a misleading earnings guidance range being released on the ASX.

The Company did not request a trading halt at an earlier time as the probable impact on earnings of the individual components within the Impacting Factors had to be assessed and completed by the Company. Until the assessment of probability across all of the Impacting Factors had been significantly progressed, the Company was not aware that the aggregate of the Impacting Factors would be material to the Company.



Question 14.2

The Impacting Factors cover a range of items that have led to a material impact to the Company. Most of the items are not yet commercially finalised, which has required management to make estimates and judgements of the probable outcome on all items over the final three months of the reporting period, taking in account reasonable factors and information available to management at the time.

Due to the nature of the Impacting Factors, a significant amount of time had to be spent estimating the impact of each individual item that comprises the Impacting Factors. Only when the probability factors of each individual had been completed, and aggregated, did the Company come into possession of information that required disclosure in accordance with Listing Rule 3.1.

Question 15

Not applicable.

Question 16

The Company confirms that it is in compliance with Listing Rule 3.1.

Yours faithfully

DAVID COYNE
Chief Financial Officer & Company Secretary



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1 November 2012

David Coyne
Company Secretary
VDM Group Limited
310 Selby Street North
OSBORNE PARK WA 6018

By email: david.coyne@vdmgroup.com.au

Dear David

VDM Group Limited (the "Company")

We refer to the following:

1. The trading halt request by the Company dated 26 October 2012 and released to the market at 10:05 AM AEDT on 26 October 2012 (the "Trading Halt").
2. The Company's announcement released to ASX at 9:49 AM AEDT on 29 October 2012 and titled "*Update on first half earnings guidance*" (the "Announcement"). The Announcement included amongst other things, the following:

"VDM now expects to report a loss before tax for the six month period to December 2012.

The greatest impact on the period has been the outcome of contract claims and variations that have not been resolved at a value that the Company originally expected..."

(the "Contract Claims and Variations")

"...[T]he necessity to increase provisions primarily relating to unrecoverable amounts on engineering and property development activities not previously provided for."

(the "Increased Provisions")

"In addition the Company has been impacted by accommodation shortages on a site where two projects are being constructed in Western Australia, resulting in a reduction in scope on one, and limitations in on-site labour on the other."

(the "Accommodation Shortages")

3. The decrease in the price of the Company's securities from a close price of \$0.025 on 26 October 2012 to \$0.017 at the close of trading on 29 October 2012.

We wish to draw your attention to the definition of “aware” in chapter 19 of the listing rules which states that:

“an entity becomes aware of information if a director or executive officer (in the case of a trust, director or executive officer of the responsible entity or management company) has, or ought reasonably to have, come into possession of the information in the course of the performance of their duties as a director or executive officer of that entity”.

Further we wish to draw your attention to listing rule 3.1 which requires an entity to give ASX immediately any information concerning it that a reasonable person would expect to have a material effect on the price or value of the entity's securities. The exceptions to this requirement are set out in listing rule 3.1A.

Paragraph 18 of Guidance Note 8 states:

“Once a director or executive officer becomes aware of information, he or she must immediately consider whether that information should be given to ASX. An entity cannot delay giving information to ASX pending formal sign-off or adoption by the board, for example.”

Please note that for disclosure not to be required under listing rule 3.1, all of the exceptions under listing rule 3.1A must apply:

- “3.1A.1 A reasonable person would not expect the information to be disclosed.
- 3.1A.2 The information is confidential and ASX has not formed the view that the information has ceased to be confidential.
- 3.1A.3 One or more of the following applies.
 - It would be a breach of a law to disclose the information.
 - The information concerns an incomplete proposal or negotiation.
 - The information comprises matters of supposition or is insufficiently definite to warrant disclosure.
 - The information is generated for the internal management purposes of the entity.
 - The information is a trade secret.”

Finally, we would like to draw your attention to ASX's policy position on the concept of “confidentiality” which is detailed in paragraphs 34 to 40 of Guidance Note 8. In particular, paragraphs 34 and 35 of the Guidance Note state that:

“‘Confidential’ in this context has the sense of ‘secret’...” and loss of confidentiality may be indicated by otherwise unexplained changes to the price of the entity's securities, or by reference to the information in the media or analysts reports”.

Having regard to the Announcement, the above definitions, listing rule 3.1 and Guidance Note 8 - Continuous Disclosure, we ask that you answer the following questions in a format suitable for release to the market in accordance with listing rule 18.7A.

1. Does the Company consider the Contract Claims and Variations referred to in the Announcement to be material to the Company?
2. When did the Company become aware of the Contract Claims and Variations referred to in the Announcement? Please include details of the relevant time and circumstances of the Company becoming aware of the Contract Claims and Variations.
3. If the answer to any part of question 1 is “yes” and the Company became aware of the Contract Claims and Variations, referred to in the Announcement, prior to the time the Company released the Announcement, please advise the following:

- 3.1. Please advise why the Company did not make an announcement at an earlier time or request a trading halt earlier.
 - 3.2. Why was the information relating to the Contract Claims and Variations not released to the market at that earlier time? Please comment specifically on the application of listing rule 3.1.
4. If the answer to question 1 is "no", please advise the basis on which the Company does not consider the Contract Claims and Variations referred to in the Announcement to be material.
5. Does the Company consider the Increased Provisions referred to in the Announcement to be material to the Company?
6. When did the Company become aware of the Increased Provisions referred to in the Announcement? Please include details of the relevant time and circumstances of the Company becoming aware of the Increased Provisions.
7. If the answer to any part of question 5 is "yes" and the Company became aware of the Increased Provisions, referred to in the Announcement, prior to the time the Company released the Announcement, please advise the following:
 - 7.1. Please advise why the Company did not make an announcement at an earlier time or request a trading halt earlier.
 - 7.2. Why was the information relating to the Increased Provisions not released to the market at that earlier time? Please comment specifically on the application of listing rule 3.1.
8. If the answer to question 5 is "no", please advise the basis on which the Company does not consider the Increased Provisions referred to in the Announcement to be material.
9. Does the Company consider the Accommodation Shortage referred to in the Announcement to be material to the Company?
10. When did the Company become aware of the Accommodation Shortage referred to in the Announcement? Please include details of the relevant time and circumstances of the Company becoming aware of the Accommodation Shortage.
11. If the answer to any part of question 9 is "yes" and the Company became aware of the Accommodation Shortage, referred to in the Announcement, prior to the time the Company released the Announcement, please advise the following:
 - 11.1. Please advise why the Company did not make an announcement at an earlier time or request a trading halt earlier.
 - 11.2. Why was the information relating to the Accommodation Shortage not released to the market at that earlier time? Please comment specifically on the application of listing rule 3.1.
12. If the answer to question 9 is "no", please advise the basis on which the Company does not consider the Accommodation Shortage referred to in the Announcement to be material.
13. With regard to questions 1, 5, and 9, does the Company consider the Contract Claims and Variations, Increased Variations, and the Accommodation Shortages, in combination or in part, (the "Impacting Factors") to be material to the Company?
14. If the answer to any part of question 13 is "yes" and the Company became aware of the Impacting Factors (or any part of them) prior to the time the Company released the Announcement, please advise the following:
 - 14.1. Please advise why the Company did not make an announcement at an earlier time or request a trading halt earlier.
 - 14.2. Why were the Impacting Factors (or any part of them) not released to the market at that earlier time? Please comment specifically on the application of listing rule 3.1

15. If the answer to question 13 is "no", please advise the basis on which the Company does not consider the Impacting Factors (or any part of them) referred to the Announcement to be material.
16. Please confirm that the Company is in compliance with listing rule 3.1.

Your responsibility under listing rule 3.1 is not confined to, or necessarily satisfied by, answering the questions set out in this letter.

Please note the ASX reserves its right under listing rule 18.7A to release this letter and the Company's response to the market. Accordingly the Company's response should address each question separately and be in a format suitable for release to the market.

If the information requested by this letter is information required to be given to ASX under listing rule 3.1 your obligation is to disclose the information immediately. Unless the information is required immediately under listing rule 3.1, a response is requested as soon as possible and, in any event, not later than **6:30am (WST) on Monday, 5 November 2012**.

Your response should be sent to ASX by facsimile on facsimile number (08) 9221 2020. It should not be sent to the Company Announcements Office.

If you have any queries regarding any of the above, please contact me on (08) 9224 0053.

Yours sincerely

[sent electronically without signature]

Sebastian Bednarczyk
Senior Adviser, Listings (Perth)