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| **Client:** ABC Bangladesh Limited | **Year End:** |
| **Subject:** Understanding the entity and its environment |  |

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**Company profile:**

XYZ Ltd was incorporated in Bangladesh on the [*Date Month Year*] as a private Ltd company in Bangladesh under companies Act 1994. This Company also obtained listing with Dhaka Stock Exchange and Chittagong Stock Exchange on [*Date Month Year]*

**Nature of Business:**

XYZ provides the people of Bangladesh with quality medicines and healthcare products. Its state-of-the art pharmaceutical plant represents Bangladesh's quest for a truly world class manufacturing facility. XYZ's rich heritage leads to innovative and higher value added formulations.

The comprehensive product range of XYZ pharmaceuticals include products from all major therapeutic classes and in various dosage forms like tablet, capsule, dry powder, liquid, cream, gel, ointment, ophthalmic and injectable. It produces world class Modified Release drug and medicine to cater the requirement of pharmaceutical manufacturer of domestic and international market.

It exports high quality pharmaceuticals to a good number of countries all over the world.

***Ownership structure***

The shareholding structure of the company is as follows:

|  |  |  |
| --- | --- | --- |
| **Name of the shareholder** | **No. of ordinary shares held** | **% of shareholding** |
| Directors/Sponsors | XXXXXX | 36.81 |
| Institutions | XXXX | 37.48 |
| General shareholders | XXXXX | 25.71 |
| **Total** | **XXXXX** | **100** |

During the year under audit there has been no change in the legal structure or ownership of the company.

***Corporate Governance***

XYZ Board of Directors is committed to meeting the highest standard of corporate governance and disclosure. The Directors are conscious of their responsibilities in supervision and direction of the affairs of the company in conformity with the practices of sound corporate governance. **In fulfillment of those responsibilities the Directors have set for themselves the principles that will be followed in their own involvement in the oversight functions and in setting up clear guidelines for the executive management.**

***Composition of the Board***

The Board presently consists of 10 members drawn from amongst the major shareowners, business professionals and bankers. Mr M occupies the position of the Chairman of the Board and Mr. A occupies the position of Managing Director of the company.

***Role of the Board***

The Board is the highest level of authority of the Company to oversee its operation through appropriate delegation and control.

***Responsibility of the Board***

The Directors hold the ultimate responsibility of conducting the activities on behalf of the Company in accordance with the law and in the interest of its shareowners and other stakeholders, keeping in view the long-term interest of the Company.

***Functioning of the Board***

The Board is required under the law to meet at least once in three months. The number of Board meetings held in 2014 was six. The Directors are kept informed of the results and the major activities through monthly reporting by the Managing Director. The Board agenda includes financial results, consideration of major investments, new business initiatives, borrowings, liquidity etc.

***Management committee***

The Board has delegated adequate operational and financial authority to the Managing Director to manage the operations of the company. The Managing Director conducts the affairs of the company through further delegation down the line and in consultation with a management committee. Senior Managers of the company with responsibilities for the business, operations and functional services are members of the management committee, which meets fortnightly to discuss the business results, to review the current business condition and discuss policy matters. Consensus building as a management style is encouraged in the deliberations of the management committee meetings. The Managing Director is responsible for implementing the Board’s decision and the uses the management committee as a consultative boldly to assist and advise him on issues under consideration. The management committee advises the Managing Director on new products, major items of capital expenditure and overall supervision of the affairs of the Company.

***Empowerment of people***

The Board has given a clear guideline to the Managing Director to ensure that there is appropriate delegation of authority and clear statement of accountability of the management staff all the way down to the Supervisory level and that performance of the individuals is judged on the basis of clearly set measurable goals and through objective assessment of their achievement.

***Internal control***

The Managing Director has to satisfy the Board those adequate internal checks and controls are in place through appropriate MIS and employment of Internal Audit team to check and validate the expenses and the systems in operation. To further strengthen the controls, the Company has introduced ISO XXXXX Quality Management System under which all activities are carried out on basis of Standard Operating Procedures. This standard has now been updated to its XXXXX version. The company also has introduced ISO XXXXX Environment Management System; the first Company in Bangladesh to do so and as a result has undertaken a task of continuing improvement through annual goals. In addition the Company has adopted the principles of Global Compact, an initiative taken by the Secretary General of the United Nations and adopted by world-wide by large and progressive companies.

***Reporting and Communication***

The Managing Director reviews and approves the strategic plans of each Business unit once a year. He also reviews monthly report and commentary on the sales and financial performance of the business from the head of businesses and the activities of the functional heads.

***Communication with Shareowners***

The Company holds the Annual General Meeting regularly in time. The Directors attending the Annual General Meeting take careful note of the views and suggestions of the shareowners and institutional stakeholders offered at the AGM and consider them with utmost seriousness. The Managing Director also brings to the notice of the Board any written communication received by him from the shareowners.

The Board of Directors consists of 10 members. There has been no change in governance structure in the year.

***Internal Audit***

The entity has an internal audit department headed by Mr. Uddin. IA reports functionally and administratively to the Audit Committee, IA works according to an annual internal audit plan. The audit plan contains which divisions are to be visited on which dates or which sides to be audited. The activities of IA focus primarily on:

* Follow up
* Compliance
* Division audit
* Internal regulations etc.

***Sources of fund:***

* Primarily, ordinary share capital.
* Long-term loans from Standard Chartered Bank (SCB) and HSBC
* Short-term borrowings and overdraft facilities from SCB, HSBC, Commercial Bank of Ceylon, Citi Bank N.A. and Mercantile bank.

**Objectives and strategies (from company profile)**

| Objectives | Strategy and method of implementing the strategy |
| --- | --- |
| To increase the Net Asset Value Per Share (On 31 December 2014 NAV was 192.08) | * Introduction of new product. * Increase of promotional activities such as publicity and advertisement, donation and gifts, samples, sales service, doctors’ entertainment, medical services, product bonus to customer, sales incentive to sales representative etc. * Increase production efficiency through reducing process loss * Penetration of new markets for animal health, fertilizers, tractors, seeds and consumer business. * Increase quality of customer service through prompt response of queries. * Sales and marketing department has been restructured from traditional to customer-oriented center. |
| Achieving a gross profit to sales ratio of 45% for Pharmaceutical | * By increasing concentrsting more on high margin products and increasing sales price and profit through product diversification and better utilization of resources and facilities. Furthermore they plan to penetrate the new markets for agro chemical products. In addition to the above, the company will emphasize on the promotional activities to the current addressed market of pharmaceuticals for capturing more sales. * Decrease of stock holding period * Increased of stock turnover based on sales * Decreased of stock to sales ratio |

***Conduct of operations***

The key operational activities may be summarized as follows:

* Inventory management and logistics
* Supplier selection and material procurement
* Production
* Sales and marketing
* Overall administration

**Customers**

**Major customer segments in relation to business divisions are mentioned as follows:**

* 5

**Suppliers**

*Local suppliers:*

Local suppliers include some press companies like K Press Limited, H Printing, I printing and packaging limited, L Plastic Industries Ltd.,X ltd, Y Ltd, Z Ltd E Ltd X Ltd, pharmaceutical company like Square Pharmaceuticals etc. CC & PH supplies crop protection chemicals, Seed supplies Hybrid Rice, vegetable and Maize seeds, Fertilizer Supplies Micronutrient and Foiler fertilizer, Agrimachineries supplies Tractors, Power Tiller and Harvester and Animal Health supplies high quality Nutritional, Veterinary and Poultry medicines and vaccines.

*Foreign suppliers from the following countries:*

UK, USA, Germany, Holland, Italy, France, Hungary, Japan, China, Korea, Thailand, Malaysia, Indonesia, India, Pakistan etc.

**Financing**

There have been no changes in the equity structure during 2014. There are no planned changes in the capital structure or in the financing strategies.

The working capital is financed by overdraft facitilities and short-term loans (secured) from four private commercial banks. The company is using overdraft facilities offered by Standard Chartered Bank, Commercial bank of Ceylon Ltd., HSBC and Citibank N. A.,in the current year.

***Employees***

There is a wide pool of suitably skilled labor available for workers in the factory.

Due to the high profile nature of the Company, many applications from suitable candidates are received for roles within senior management.

Competitive remuneration packages have also ensured that sufficient, appropriately skilled people have applied for roles within sales, marketing and finance.

***Types of employees***

There are two types of employees –

* Permanent Staff
* Contractual Staff

The company provides following benefits to its permanent employees as per Labour law/as per company policy:

* Bonus and Incentives
* WPPF:
* Contributory staff provident fund:
* Gratuity
* Pension

The entity’s industry and environment

The domestic market is highly concentrated and competitive. The local manufacturers dominate the industry capturing market share of 90%. While the multinationals cater to the remaining demand. According to IMS (intercontinental Medical statistics) Health, the top 10 companies hold 68.5% market share, the top 20 hold 85.73%, and the top 31 hold 94.1%, while the remaining 169 companies shared 5.9% among them. Square Pharmaceuticals led the industry with a market share of 18.7%. Incepta and Beximco took 2nd and 3rd positions with market shares of 10.42% and 8.47% respectively.

The domestic market Industrial/Mfg growth rate (6% of GDP) is XXX in 2014. At present there are XXX listed Pharmaceuticals & Chemicals companies operating in Bangladesh. Market share analysis of local pharmaceuticals companies in Bangladesh are given below:

**Economic, political and social environment**

**Economic**

The economy is mainly market based, but the Government still plays a significant role. The Government is trying to improve the climate for foreign investors and liberalizing the capital markets. A growth of 6%-6.5% is projected and inflation rate would be between 7.5% to 8.5%. There have been no significant changes in the tax regulations in the year. The taxation regime does not provide any significant new challenge to the company.

**Political**

Though the country is has stable political govt elected of major political parties and attempt for overruling corruption by the current government is the motivation for greater investment in established fair businesses. There is no such political issue that may adversely impact the operation of XYZ LTD Limited. However, uncertainty growing in anticipation of political instability regarding due national election issue remains a worry.

**Social**

The manufacturing processes do not generate any toxic or environmentally hazardous waste that cross the limit of any standard environmental parameter set for this industry. Moreover, the company has in place processes for safe waste disposal. So the risk of any toxic leak or spillage and the resultant social backlash is minimal. The establishment of its factory has brought with it greater employment opportunities for the local population. As a result, the social environment is on the whole favorable to the operation of the company. Anyway, the company is very concerned about the safety, health and environmental (Refer to SHE policy of XYZ) considerations of the country.

Considering the above factors, we have not identified any financial statement risk.

**Legal and regulatory environment**

The Companies Act 1994 provides the primary legal framework for the operation of the company. The principal regulatory authority with regard to corporate affairs is the Registrar of Joint Stock Companies (RJSC). As the company is public limited company and listed in stock exchange, it has to comply with the rules and regulations promulgated by Securities and Exchange Commission (SEC).

Other significant laws which form part of the company’s legal and regulatory framework are:

|  |  |  |
| --- | --- | --- |
| **Nature of legislation** | **Title** | **Impact on operations** |
| Tax laws | The Income Tax Ordinance 1984 & Income Tax Rules 1987  The VAT Act & Rules 2012 & 2016 | The company is liable to pay tax @35% on taxable income.  The company is also required to pay VAT @ 0% to 15% varied for its diverged business. VAT is a complex issue in this industry and the company has to comply with the strict laws, regulations, circulars issued by the VAT authority. |
| Industrial & Labor laws | The Bangladesh Labor Act and The Bangladesh Labor Code 2006 as ammended 2013 | These laws are related with the compliance of wages, safety, health and environmental factors in the factory premises. |

***Accounting framework***

***International Financial Reporting Standards (IFRS)***

The Company is required to prepare financial statements according to International Financial Reporting Standards (IFRS) and has to comply with some discloser requirements of the Companies Act 1994 while preparing financial statements. The company during the year has not change the accounting policy.

**Laws and regulations:**

***Companies Act 1994***

The Companies Act 1994 provides the primary legal framework for the operation of the Company. The principal regulatory authority in relation to corporate affairs is the RJSC. The entity is obliged to comply with the Companies Act 1994 governing its regulatory filing with the RJSC. This legislation includes provisions on the information to be filed, the time permitted to make required filing and penalties for non-compliance.

***Income Tax Ordinance 1984 and Income Tax Rules 1984***

The Company has to pay advance income tax and deduct tax at source on payment for goods and services as per the provisions of income tax ordinance. The Company also has to submit quarterly tax returns for deducted tax amount to National Board of Revenue (NBR) as per the said ordinance.

The current tax provision of the Company is calculated considering the allowable expenses as per income tax ordinance.

***Value Added Tax Act 2012 and Rules 2016***

To comply with VAT rules for the collection, charge and rebate of VAT on purchase of goods and services.

***Labour Act 2006 (as amended in 2013)***

To comply with labour act for payment of wages and participation of company's profit. The Company has to pay 5% of its profit before charging such expenses to the Workers' Profit Participation Fund (WPPF).

***Bangladesh Securities and Exchange Rules, 1987***

The Company is also required to prepare its financial statement in accordance with Bangladesh Securities and Exchange Rules, 1987. The Rule also guides the Company regarding the manner of share transaction in the stock exchange, maintenance of accounts and audit, required qualifications to be registered in the stock exchange, revaluation of assets etc.

Significant Accounting policies (write accounting policies mentioned in the FS)

Critical accounting policies are those that, in our judgment, are both most important to the portrayal of the entity’s financial condition, cash flows, and results of operations and require management’s most difficult, subjective, or complex judgments, often as a result of the need to make estimates about the effect of matters that are inherently uncertain.

* Revenue recognition
* Inventories
* Valuation of investment in subsidiaries, assosiates and joint ventures
* Related party transactions
* Accounts receivables
* Cash and bank balances
* Plant, property and equipment

***Compliance with legal and regulatory framework by the entity:***

The entity complies with the legal and regulatory framework by reviewing the compliance issues on regular basis. Legal department guided by the Company Secretary has devoted the team to ensure legal compliance as per legal regulation and instruction.

Moreover, the Company ensures compliance with the legal and regulatory framework by undertaking the followings:

1. Monitoring legal requirements and ensuring that operating procedures are designed to meet these requirements.
2. Instituting and operating appropriate internal control systems.
3. Maintaining a register of significant laws and regulations with which the entity has to comply within its particular industry.
4. Developing, publicizing and following employee handbook.
5. Ensuring employees are properly trained and understand the employee handbook.