

Issuer: STAR Pharmaceutical Limited

Security: STAR Pharmaceutical Limited

Meeting details:

Date: 27 April 2018

Time: 3.00 p.m.

Venue: Six Battery Road #10-01 Singapore 049909

Company Description

STAR Pharmaceutical Limited, an investment holding company, develops, manufactures, and trades pharmaceutical products for hospitals, clinics, and pharmacies in the People's Republic of China. It provides antibiotics, cardiovascular drugs, cerebrovascular drugs, and other specialized drugs in various dosages and administration forms, such as powder injections, lyophilized powder injections, liquid injections, tablets, capsules, and granules. The company was founded in 1993 and is based in Qionghai, the People's Republic of China. STAR Pharmaceutical Limited is a subsidiary of DB Nominees (Singapore) Pte Ltd.

(Source: http://www.sgx.com/wps/portal/sgxweb/home/company_disclosure/stockfacts?code=AYL)

1. Would the board/management provide shareholders with better clarity on the following operational matters? Specifically:

- (i) **Two-Invoice System:** With the implementation of the new system by the PRC government, what are the further changes to the group's business model and operations? Is the marketing and distribution charge of RMB31.3 million a one-time expense due to the implementation of the new system or will there be recurring higher marketing and distribution expenses annually? Please also help shareholders understand the measures taken by management to restore the group's profitability.
- (ii) **Refundable deposits:** As noted in the Independent Auditor's Report under key audit matters, the group wrote off intangible assets (product development in progress) and refundable deposits of RMB6,677,000 and RMB13,907,000 respectively, which are included in "Other operating expenses". Further in Note 12 (page 76 – Refundable deposits/other receivables, prepayments and deposits), it is shown that the group collected RMB12.3 million and is expected to collect another RMB2.4 million in October 2018. While writing off RMB13.9 million in the refundable deposits, the group also paid to 2 new third party research companies RMB12.7 million in the financial year. **Can the board explain in greater detail the reason(s) for these new R&D projects? How are these new R&D projects impacted by the recent changes in the policies? What are the projected benefits and specific deliverables from these R&D projects? Given the large write-offs, would the audit committee consider it necessary to review and refine the group's R&D/investment strategy?**

2. In the Corporate Governance Report, the following disclosure was provided by the company with regard to the board's composition (page 16).

STAR PHARMACEUTICAL LIMITED
Annual Report 2017

CORPORATE GOVERNANCE

Board Composition and Guidance

Principle 2: There should be a strong and independent element on the Board, which is able to exercise objective judgement on corporate affairs independently, in particular, from Management and 10% shareholders. No individual or small group of individuals should be allowed to dominate the Board's decision making.

Presently, the Board comprises of two (2) Executive Directors, one (1) Non-Executive Director and two (2) Independent Directors. There is a strong and independent element on the Board, with Independent Directors making up at least one-third of the Board

Name of Directors	Board	Date of First Appointment	Date of Last Re-Election	Audit Committee	Nominating Committee	Remuneration Committee
Xu Zhi Bin	Executive Chairman	19 November 2012	29 April 2016	-	-	-
Wang Qi	Executive Director	1 March 2017	27 April 2017	-	-	-
Li Tak Tai Leada	Non-Executive Director	24 August 2009	27 April 2017	Member	Member	Member
Ng Poh Khoon	Lead Independent Director	27 September 2005	27 April 2017	Chairman	Member	Chairman
Meng Tao	Independent Director	1 January 2015	30 April 2015	Member	Chairman	Member

(Source: Company annual report)

Guideline 2.2 of the 2012 Code of Corporate Governance states that, inter alia, where the the chairman of the part of the management team or is not an independent director, independent directors should make up at least half of the board.

- (i) **Can the board and especially the independent directors confirm that they are cognisant of Guideline 2.2 in the Code that recommends the independent directors make up at least half of the board as the company has an executive chairman?**
- (ii) **What were the deliberations the board and the nominating committee (NC) had with regard to Guideline 2.2?**
- (iii) **Would the board and the NC consider how it would make changes to the board composition so that it would comply with the Code?**
- (iv) **If not, would the board explain why it is necessary for the company to deviate from the Code?**

3. On 4 April 2018, the company announced that there were material discrepancies between the audited financial statements and the unaudited financial statements for the financial year ended 31 December 2017 which was first announced by the company on 28 February 2018.

Examples of the discrepancies following the finalisation of the audit include:

- Reversal of the overstated disposal loss of intangible assets of RMB368,000 to other operating income
- Reclassification of exchange loss of RMB3,405,000 from other operating expenses to finance expenses
- Under provision of amortisation of lease prepayments for the year ended 31 December 2017
- Overprovision of deferred tax assets for impairment loss of intangible assets and refundable deposits of a subsidiary in China

As a result, the loss for the year increased from RMB19.5 million to RMB20.9 million and the accumulated profit of RMB14.2 million (in the unaudited financial statement) turned into an accumulated (loss) of RMB(3.8) million (in the audited financial statement).

The audit committee (AC) comprises Ng Poh Khoon (Chairman), Meng Tao and Li Tak Tai Leada.

- (i) Can the AC members elaborate further and help shareholders understand their individual relevant and recent accounting expertise and/or experience, especially related to listed pharmaceutical companies?**
- (ii) As the directors have responsibilities to oversee the group's financial reporting process, can the directors, especially the directors in the AC, help shareholders understand their individual and collective efforts in the preparation of the group's financial statements to give a true and fair view in accordance with the provisions of the Act and FRSSs?**
- (iii) Has the AC evaluated if the internal finance team is sufficiently resourced with experienced and qualified staff to ensure the integrity of the financial statements?**
- (iv) Following the material changes made after the finalisation of audit, what improvement has the AC made to the group's systems and processes?**