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Research on internal control information disclosure of Guangdong taiantang Pharmaceutical Co., Ltd

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ABSTRACT
With the development of globalization and digital transformation, market competition is becoming more and more fierce. When the scale of enterprises expands to a certain extent, there will be a variety of problems, such as financial fraud. Pharmaceutical manufacturing industry has an important impact on the life and health of the public, and whether its internal control system is sound directly affects the development and stability of China's economy. Through the analysis of the delisting incident of Guangdong taiantang Pharmaceutical Co., Ltd., this paper finds that there are major defects in its internal control, and there are corresponding problems in the disclosure of internal control information, and puts forward suggestions for improvement. It is hoped that the public will attach great importance to the disclosure of internal control information of enterprises in China, and provide some reference and reference.

KEYWORDS
Internal control; Risk management; Information disclosure

1 Foreword

Since the reform and opening up, with the rapid development of China's economy, in order to occupy a place in the market, enterprises have expanded their scale through absorption and merger, forming a strong combination of talents, funds and funds in order to occupy a place in the market. However, while some enterprises are developing, there are still phenomena of financial fraud and false internal control information. The main reason is that the company does not pay enough attention to the disclosure of internal control information, which leads to a variety of violations in internal control. If left unchecked, there will be dire consequences. Therefore, good internal control information disclosure is very important for an enterprise. With the continuous introduction of relevant laws and regulations in China, the disclosure of internal control information has attracted more and more attention due to the particularity of pharmaceutical manufacturing industry.

2 Research status at home and abroad

China's internal control information disclosure started late, the relevant provisions lack systematicness and integrity, and the earlier normative documents can be traced back to 2006. In 2008 and 2010, five ministries and commissions jointly announced the basic guidelines and guidelines, making further precise requirements. Foreign research on internal control started earlier, and foreign listed companies have a strong incentive to report the implementation of internal control to the outside world in 1994. Liu Daxian (2000) believes that it is most appropriate for listed companies to disclose internal control information through self-test and self-assessment. Xu Ningning (2017) pointed out that the higher the management ability of listed companies, the more able they are to identify internal control defects; Yang Xudong (2019) believes that internal control defects will hinder the development of enterprises and reduce operational efficiency; Ittonen, Kim (2010) believes that the disclosure of internal control defects can produce a significant market reaction; Ben, Kwame, AGYEI Mensah (2016) believes that independent directors help to improve the quality of internal control information disclosure and increase information transparency.

3 Research significance

3.1 It is conducive to the correct decision-making of investors

The disclosure of the company's internal control information can provide investors with more information, so that investors can better understand the company's internal control situation, and judge whether the company is worth investing, so as to reduce risks, which to some extent enhances investors' caution. Through disclosure, investors can understand the development of the company, so as to determine the development direction of the company and whether its future development meets investment needs. Combining the ability of enterprises with their own investment needs organically and investing according to local conditions can better avoid risks.

3.2 Reduce violations

Making the actual operation of the company public can not only reflect the implementation of the internal control information disclosure system, but also enhance the credibility of information, and effectively prevent the company from illegal acts such as financial fraud. Through the disclosure of internal control information, the company's daily business activities can be effectively constrained, so as to promote the company's internal control information disclosure level to have a qualitative leap. At the same time, managers can also better understand the operation of the system, and when they encounter problems, they can take timely measures according to the real time situation to make the system and procedures more mature, which will become a strong support for the company's progress and enable the company to develop better.

3.3 Improve the quality of accounting information

With the basic completion of the reform of state-owned enterprises in China and the basic establishment of modern enterprise system, the internal control information provided by enterprises to the public is particularly important. In China, effective supervision of corporate behavior has always been the focus of government attention. A sound internal control information disclosure system is conducive to ensuring the authenticity, reliability and relevance of accounting information. Through information disclosure, it can effectively increase the transparency of accounting information, make stakeholders have a comprehensive and objective understanding of the financial situation of enterprises, and thus provide a basis for them to make correct decisions.

4 Background of delisting event of Guangdong taiantang pharmaceutical Co., Ltd

4.1 Key nodes and delisting procedures

On June 5, 2024, the Shenzhen Stock Exchange issued an audit report of "unable to express opinions" due to taiantang's 2022 financial report (previously, it had reserved opinions in 2021, and could not express opinions again in 2023), and decided to terminate its stock listing in accordance with article 9.3.11 of the stock listing rules.

Delisting timeline:

June 14: entering the delisting consolidation period, the stock abbreviation was changed to "Taian Tui".

July 4: on the last trading day, the stock price fell by the daily limit of 0.27 yuan per share, leaving only about 161 million yuan in market value (more than 16 billion yuan at its peak).

July 5: officially delisted.

4.2 Financial fraud and capital occupation: systematic violations

4.2.1 Financial fraud for four consecutive years (2018 - 2021)

According to the investigation of Guangdong securities regulatory bureau, the means of fraud include:

False increase in inventory and profit: kangaido, a subsidiary, falsely increased inventory by 424 million yuan in four years by carrying forward less costs and recording less expenses.

False increase in revenue: Hongxing pharmaceutical, a subsidiary, falsely increased the price of drugs, with a false increase in revenue of 17.69 million yuan in three years.

Total profit fraud: the cumulative false profit increased by 429 million yuan, accounting for 304.72% of the absolute value of the current profit (2020).

Table 1 scale of financial fraud of taiantang from 2018 to 2021

Year	False increase in inventory (100 million yuan)	false increase in revenue (10000 yuan)	false increase in profit (100 million yuan)
2018	0.65	261.23	0.66
2019	1.41	1007.85	1.44
2020	1.15	500.33	1.16
2021	1.03	-	1.03

4.2.2 Capital occupation of major shareholders

From 2018 to the first half of 2022, taiantang group, the controlling shareholder, occupied an average of more than 200 million yuan of funds of listed companies for non operating purposes in the name of advance equipment payment and drug purchase payment, with a peak of 277 million yuan in 2020, accounting for 5.87% of the current net assets.

4.3 Business collapse: from aggressive expansion to insolvency

4.3.1 Strategic mistakes: blind diversification and high debt expansion

After listing, 624 million yuan was raised, but more than 2 billion yuan was invested through mergers and acquisitions (such as 350 million yuan to acquire kangaido) and cross-border real estate (investment in Bozhou and Guangzhou Kangyang real estate).

Roe/ROA continued to be depressed: the expansion did not bring benefits, the debt ratio exceeded 23% in 2015, and the net operating cash flow lost 1.27 billion yuan (the net profit in the same year was only 190 million).

4.3.2 Performance avalanche and restructuring failure

The cumulative loss in three years was 4.3 billion yuan: the net profit in 2021-2023 was - 1.138 billion yuan, - 968 million yuan and - 2.210 billion yuan respectively, and the revenue dropped sharply from 2.264 billion yuan to 410 million yuan.

Reorganization attempt aborted: in December 2023, a pre reorganization agreement was signed with China Nuclear health, but in April 2024, Shantou court ruled to terminate the procedure, which directly led to the stock price falling below the delisting red line of 1 yuan.

5 Internal control analysis of Guangdong taiantang pharmaceutical Co., Ltd

5.1 Failure of internal control over financial reporting: long-term systematic fraud

Inflated profit and inventory.

Kangaido, a subsidiary, falsely increased its inventory through "less carrying forward costs and less recording expenses" from 2018 to 2021, with a cumulative falsely increased inventory of 424 million yuan and a total falsely increased profit of 429 million yuan in four years. Hongxing pharmaceutical factory, a subsidiary, falsely increased its revenue by 17.69 million yuan through falsely increasing the sales price of drugs from 2018 to 2020.

The proportion of fraud scale is abnormally high: in 2020, the proportion of falsely increased profits in the absolute value of current profits is as high as 304.72%, which seriously distorts the authenticity of financial reports.There is a lack of effective supervision over cost accounting and revenue recognition, and the financial data of subsidiaries are not included in the unified audit process of the group, resulting in fraud that has not been found for a long time.

5.2 Illegal disclosure of related party transactions: capital occupation and concealment of major shareholders

5.2.1 Huge capital occupation not disclosed

From 2018 to the first half of 2022, taiantang group, the controlling shareholder, occupied the funds of listed companies for non operation in the name of "advance equipment payment" and "drug purchase payment", with a cumulative amount of 977 million yuan.

As of June 2023, the outstanding balance was still as high as 492 million yuan.

5.2.2 Disclosure of material omissions

The occupation of funds was neither submitted to the board of directors for consideration nor disclosed in the annual report 2018-2021 and the semi annual report 2022, which constituted a major omission. The regulatory investigation found that the relevant transactions did not have the approval process of OECD regulations, and the internal control process was in vain.

5.3 Uncontrolled fund management: internal control mechanism fully paralyzed

5.3.1 Invalidation of fund payment approval

The multi-level approval system is not implemented for the payment of large advance payments, and the controlling shareholders can transfer the funds of listed companies at will. For example, in 2020, a single occupation of funds reached 277 million yuan, but there was no internal risk warning mechanism.

5.3.2 Absence of capital monitoring

The financial department did not establish a fund flow tracking system, resulting in the occupation behavior not being found for five years. Kangaido, a subsidiary, triggered 305 judicial lawsuits due to the rupture of the capital chain, with an execution amount of 224 million yuan, exposing the failure of the group's overall capital planning.

5.4 Failure of audit and regulatory functions

5.4.1 Continuous "non-standard" audit opinions

The 2021 financial report was issued with "qualified opinions" and upgraded to "unable to express opinions" in 2022. The main reasons include:Doubts about the ability to continue as a going concern (with a cumulative loss of more than 3 billion yuan in three years); Major defects in internal control (lack of financial information and turnover tide make the audit unable to advance).

5.4.2 Negative conclusion of internal control audit

The internal control audit report in 2022 directly identified "internal control failure", especially pointing to the undisclosed problem of capital occupation.

The exposure of these problems not only led to the delisting of the company in 2024, but also became a typical case of A-share time-honored enterprises delisting due to the lack of internal control, highlighting the deep crisis of the lack of governance independence of listed companies and the virtual supervision mechanism. The halo of "time honored brands" failed to transform into a compliance driving force, but became a cover for the actual controller to seize public interests, and ultimately destroyed the capital market life of a century old brand.

6 Suggestions on optimizing internal control information disclosure

6.1 Standardize the content of information disclosure

Establish a unified and standardized disclosure structure of internal control self-assessment reports to achieve overall consistency, rationality and compliance. The self-assessment reporting system in various industries and regions in China has not changed fundamentally. The criteria and contents contained in the self assessment report should have a clear criteria, so that the enterprise can be justified in the self assessment. Strengthen the management and guidance of enterprises in reporting information disclosure, promote enterprises to disclose relevant information in a timely, true, accurate and complete manner, and make its content and form comply with laws, regulations and the provisions of the CSRC. Therefore, the information disclosure of internal control system should be universal, but also have its own uniqueness. Through the standardization of internal control information disclosure, it can effectively restrict the behavior of the company and ensure investors to make correct investment decisions.

6.2 Raise management's attention

For pharmaceutical companies, it is of great significance for their healthy development to have a strong awareness of voluntary information disclosure. The process is very cumbersome, from purchase, development to sales, a complete set of processes, no one year is impossible. The higher managers pay attention to internal control, the more the function of internal control can be brought into play, so as to guide the company to better development. On the contrary, if the management of the company does not pay enough attention to the disclosure of internal control information, there may be acts such as financial fraud, which is not conducive to the sustainable development of the company. In the process of internal control information disclosure, companies often whitewash the relevant information, resulting in an illegal and false profit. Enterprise managers should raise awareness of fraud, reduce fraud psychology, improve employees' sense of responsibility, and be conducive to the inspection and feedback of internal and external regulators.

6.3 Strengthen the construction of internal control

Strengthening the construction of internal control is an important way to optimize the disclosure of internal control information. Internal control includes five elements, among which the construction of internal environment is the primary factor of internal control, which is particularly important for the development of enterprises. Ownership structure is the basis of corporate governance structure, and unreasonable ownership structure will affect the stability and long-term development of enterprises. Therefore, enterprises need to formulate a reasonable and perfect ownership structure according to their own situation, and standardize their internal behavior and other business activities. When designing and formulating the ownership structure, enterprises need to consider various factors, such as the external environment, governance structure and shareholder interests, in order to realize the rationalization and compliance of the ownership structure.

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