

**TO  
THE GENERAL MEETING  
OF SHAREHOLDERS  
OF BULGARTABAC – HOLDING AD**

## **REPORT**

**on the activity of the Audit Committee of  
Bulgartabac - Holding AD  
For 2014**

## **Introduction**

This Report is prepared in accordance with the requirements of Art. 40l of the Independent Financial Audit Act (IFAA), promulgated in the State Gazette, issue 67 dated 29 July 2008, in accordance with the requirements of Directive 2006/43/EC, and its goal is to inform the shareholders about the activity of the Audit Committee of Bulgartabac - Holding AD, Sofia, in the performance of its functions as stipulated in Art. 40h of IFAA.

## **Composition of the Audit Committee**

Being a public company, Bulgartabac - Holding AD falls within the scope of IFAA and therefore, the company shall elect an Audit Committee to perform the functions stipulated in Art. 40h of IFAA.

In accordance with Art. 40f, paragraph 2 of IFAA, the mandate and the number of the members of the Audit Committee were determined by the General Meeting of Shareholders held on 26 February 2013. The Audit Committee is composed of 3 members, including a chairperson with a three-year mandate. The following individuals are members of the Audit Committee:

1. Hristina Mihaylova Simeonova - Chairwoman

And members:

2. Ralitsa Pavlina Andreeva
3. Zoya Kancheva Petrova

## **Liability of the management of a public entity**

The management of a public company shall bear a liability for the development, implementation, effective application, and maintenance of financial management and control systems aiming at preventing any deviations and inconsistency in performance, whether due to fraud, error or underestimated risks; for the selection and implementation of suitable proactive, value adding and cost effective internal controls, with design that provides a reasonable assurance that the company complies with the requirements applicable to its activity; and for the preparation of reliable financial statements – interim results and published statements of the results.

### **Functions of the Audit Committee**

Pursuant to Art. 40h of IFAA, the Audit Committee shall carry out the following functions:

1. monitors the financial reporting process in the public – interests entity;
2. monitors the effectiveness of the company's internal control systems;
3. monitors the effectiveness of the company's risk management systems;
4. monitors the independent financial audit in the company;
5. reviews the independence of the statutory auditor of the company in compliance with the requirements of the law and the Code of Ethics of Professional Accountants, including monitoring of provision of additional services by the statutory auditor to the audited entity.

Pursuant to Art. 40i of IFAA, the statutory auditors shall report to the Audit Committee on key matters arising out of the audit, and in particular, on material weaknesses in internal control of the entity in relation to the financial reporting process.

Pursuant to Art. 40k of IFAA, the selection of a statutory auditor to carry out independent financial audit is based on a recommendation made by the Audit Committee. In pursuance of this recommendation, the General Meeting of Shareholders held on 30 June 2014 voted and appointed the specialised audit firm Deloitte Odit Ltd, registered with the register of the Certified Public Accountants Institute under No 033, to perform an audit and certification of the annual financial statements of the company for 2014.

### **Commitments of the Audit Committee of Bulgartabac —Holding AD**

In fulfilment of its commitments, in 2014 the Audit Committee carried out the following activities:

1. Monitoring and follow-up of the process of performance of the registered auditor's engagement to audit and certify the annual financial statements for 2014.
2. A workshop was held among the members of the Audit Committee and the Chief Accountant, a member of the Board of Directors and the person in charge of the Investors Relations;

3. The management report, the auditor's report and the annual financial statements for 2014 were presented to the Audit Committee;
4. A plan of the activities of the Audit Committee was elaborated;
5. The Audit Committee was introduced to the annual financial statements of the company, the draft of the auditor's report on the financial statements and the management report of Bulgartabac-Holding AD for the year ending 31 December 2014;
6. Documents evidencing the regulation of the internal control functions of the company's staff were presented;
7. A letter of recommendation for the election of an independent auditor to perform an audit and certification of the annual financial statements of the company for 2015 was drawn up.

At the workshop, significant issues were discussed concerning the performance of the independent financial audit of the annual financial statements for 2014 by the audit firm Deloitte Odit Ltd, elected by the General Meeting of Shareholders held on 30 June 2014, the process of financial reporting, the effectiveness of internal control and risk management systems, and their classification.

The Audit Committee was introduced to the annual management report, the auditor's report and the annual financial statements for 2014.

Based on the facts and evidence about the effectiveness of the financial management and control systems, the Audit Committee established the following:

#### **1. Regarding the financial reporting processes**

The reporting system applied by the company is compliant with the requirements of the Accountancy Act and the applicable accounting standards (IFRS/IAS). The statutory requirements about the way of initiating transactions are observed, the relevant entries are made in the respective primary and secondary accounting documents and registers using the accounts enumerated in the individual chart of accounts of the company and its specialised software. The access of individuals to information has been regulated by in-house acts of management.

Annual stocktaking and impairment reviews of the assets are conducted in order to determine whether there are any indications of impairment. Based on the review conducted as of 31 December

2014, the company's management decided that only certain assets were impaired and an impairment loss was reported in the financial statements for 2014.

Information gathered and the specialised procedures carried out by the registered auditor, Deloitte Odit OOD, provide a reasonable assurance that significant information has not been omitted from the financial statements.

## **2. Regarding the effectiveness of the company's internal control systems**

The company employs quality assurance systems. Within this system, a documentation procedure of the integrated management system was approved. This procedure ensures a reliable internal control of the individual production and reporting processes. Through direct or operating reporting by management employees, the existence of deviations or the lack of deviations in carrying out the operations is monitored and their compliance with the approved written orders, instructions or guidance is followed out.

In identifying risks or newly occurred circumstances, timely measures are taken through issuing new orders to regulate the performance.

## **3. Regarding the effectiveness of the company's risk management systems**

The company's management has conducted a review of operations and activities carried out by the company in view of the nature of its ordinary activity and areas of inherent risk have been identified. Bulgartabac-Holding AD applies coordinated, uniform and effective commercial and investments policies both within the economic group and towards its external markets and clients. In view of the above, management of Bulgartabac-Holding AD does not involve the company in projects involving risks and creating uncertainties. The structure of the Holding, which owns 12 subsidiaries in the country and abroad, directly or through subsidiaries, has been taken into account in the risk assessment. The Holding does not exercise effective control over three entities abroad.

Financial risks are currently identified, measured and monitored by employing various control mechanisms with the aim to determine adequate prices of products and services and adequately assess the forms of maintenance of free liquid resources. The management of individual specific risks –

currency, price, interest rate, credit, and liquidity risks – through non-derivative instruments is focused on the difficulties of forecasting the financial markets and minimizing the potential negative effects that might affect the financial result of the company.

Management has identified the bigger part of concomitant risks and the analysis of these risks and their management are presented in the annual financial statements for 2014.

#### **4. Regarding the monitoring of the independent financial audit in the company**

In order to fulfil their duties, the members of the Audit Committee have applied the approach of direct relationships and communication with the external auditors throughout the overall audit process of planning, executing and reporting the results from the audit and certification of the annual financial statements for 2014.

By letters to the external auditor, the members of the Audit Committee have requested information about findings made in the course of the audit of the annual financial statements and concerning the financial reporting process and effectiveness of internal controls and risk management systems of the company. Simultaneously, the internal documentation rules, the risk management internal rules, the annual financial statements for 2014, and the auditor's report were obtained.

The independent financial audit has been carried out in accordance with a pre-announced audit plan. The members of the Audit Committee were assured by the company's management that there had been an effective communication throughout the entire process of independent financial audit and that any possible disagreements had not served as reasons for conflict situations.

In the course of the independent financial audit, control procedures have been performed with the aim to obtain audit evidence about the amounts and disclosures made in the financial statements for 2014. Based on the tests and examinations conducted, the auditors have expressed an unqualified audit opinion that the financial statements present fairly, in all material respects, the financial position of Bulgartabac-Holding AD.

**5. Regarding the review of the independence of the statutory auditor of the company in compliance with the requirements of the law and the Code of Ethics of Professional Accountants**

The registered auditor that had performed an independent financial audit of the financial statements of Bulgartabac-Holding AD for the year ending 31 December 2014 was Deloitte Odit OOD. The audit firm was elected by a decision of the General Meeting of Shareholders of Bulgartabac-Holding AD held on 30 June 2014.

A review of the independent financial audit contract was conducted, as also a review if there were any auxiliary services provided by the auditor. An independence statement by the registered auditor Deloitte Odit OOD was presented to the Audit Committee.

Based on evidence gathered, it has been established that the registered auditor has not provided any other services that differ from the agreed engagement to perform an independent financial audit and that payments have been made for this service only. The facts declared in the independence statement provided by the auditor also support our findings that Deloitte Odit OOD is an independent firm that is able to perform an independent financial audit of the financial statements of the auditee for 2014 in accordance with the Independent Financial Audit Act and the Code of Ethics of Professional Accountants.

A check in the website of Deloitte Odit OOD shows that the specialised audit firm has issued a transparency report in accordance with the requirements of Art. 40m of IFAA.

**Date: 15 June 2015**

**Sincerely,**

**Audit Committee of Bulgartabac-Holding AD:**

Hristina Simeonova

*Chairwoman of the Audit Committee*

Ralitsa Andreeva

*Member of the Audit Committee*

Zoya Petrova

*Member of the Audit Committee*