

BY POST AND BY EMAIL (response@hkex.com.hk)

30 November 2018


Hong Kong Exchange and Clearing Limited
12th Floor, One International Finance Centre
1 Harbour View Street
Central
Hong Kong

Dear Sirs,

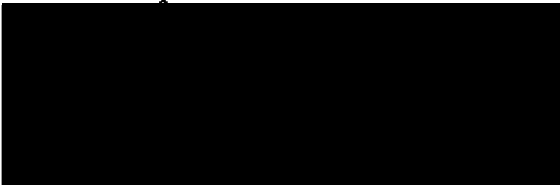
**RE: CONSULTATION PAPER ON THE PROPOSAL RELATING TO LISTED ISSUERS WITH
DISCLAIMER OR ADVERSE AUDIT OPINION ON FINANCIAL STATEMENTS**

1. Reference is made to the captioned consultation paper and the invitation to interested parties to respond to the Consultation Paper on the proposal relating to listed issuers with disclaimer or adverse audit opinion on financial statements. We attach herewith **Appendix I** and **Appendix II** the questionnaire and our responses to the Consultation Paper.
2. We, Asian Capital Limited, together with our predecessor Asian Capital (Corporate Finance) Limited, have been, in the past two decades, engaged in the provision of corporate finance advisory services, particularly in the areas of corporate restructuring and resumptions for listed companies in Hong Kong. We are licensed by the Securities and Futures Commission to carry out Type 1 (dealing in securities), Type 4 (advising on securities) and Type 6 (advising in corporate finance) regulated activities.
3. As a preeminent leader in providing restructuring advice especially for Hong Kong listed companies, we have been involved in a large number of very complicated engagements involving multi-jurisdiction debt restructuring and rescuing of financially distressed corporations, mitigating damages for lenders and other contributories including shareholders. Our roles as financial adviser to distressed companies and the relevant experience allow us to offer views and suggestions to the captioned Consultation Paper possibly in a perspective vastly different from regulators and other respondents. In recent Stock Exchange consultation papers relating to delisting matters, we have also contributed our views with justifications, albeit not accepted, and regrettably.
4. Whilst we appreciate the Stock Exchange's intention to promote timely publication of reliable financial information of issuers, we are concerned that the proposed amendments would be overly stringent and could lead to the suspension of issuers unnecessarily with audit qualifications which could possibly be rectified in a timely without being overkilled.
5. We also caution that an amendment of the Listing Rules to place issuers into suspension, and thus delisting stage, by *solely* relying on audit qualifications which are the subject of rules and regulations of another professional body, namely, the Hong Kong Institute of Certified Public Accountants, is a dangerous move, because the guidelines governing audit qualifications, the regulatory regime of auditors, the adoption of the relevant auditing guidelines and the policing of these are not necessarily in tune of regulatory objectives and principles of the Stock Exchange.

6. From our perspective, by way of example, we have seen genuine restructuring cases that would otherwise fall victim of the proposed amendments, in the sense that certain qualifications may be issued in the most recent financial period and would be required to be brought forward to the next financial year due to the inherent limitations of the audit qualifications such as, *inter alia*, deconsolidation of subsidiaries, incomplete books and records and comparable financial information by way of opening balances. Together with the recently introduced fixed period delisting criterion, chances for a successful restructuring or a rescue plan would be significantly reduced.
7. We are unable to support the proposed change that requires immediate trading suspension of issuers which had a disclaimer or an adverse opinion issued on their financial statements. In the consultation paper, there is a lack of empirical evidence (which the Stock Exchange can collect) to demonstrate that investors that have bought into shares of issuers with a disclaimer or an adverse opinion have actually suffered, as some may have profited as a result of successful resumption or otherwise rectification of those audit opinions in due course. Accordingly, we fail to see the justification for these issuers to be *immediately* suspended, given the Stock Exchange has, hitherto, allowed the market forces under the principle of *caveat emptor* for investors to trade freely provided that relevant information of the issuers are available to them to consider their investment options to match their risk profile and appetite.
8. Should the Stock Exchange decide to implement the proposal, we submit that the Stock Exchange must consider each individual issuer's circumstances on a case by case basis before concluding whether a trading suspension is warranted as a matter of fairness. It would also be beneficial if a grace period of say six months is given to issuers; this is particularly important to those which will require fund raising in the market, and those who are willing to go for a special audit. Given already there are tightened rules for resumption, a hard line stance should be taken cautiously, as an unjust decision to suspend issuers (thus perhaps inadvertently placing them into delisting stage) would deprive shareholders from trading their shares or realising their investments in the market; and would possibly lead to the delisting of issuers which is certainly not be in the best interest of shareholders.
9. To further elaborate our view on the Consultation Paper, we have prepared and attached a detailed response to specific consultation questions the Stock Exchange presented in the Consultation Paper as **Appendix II**.

Should you have any queries, please feel free to contact the undersigned at 

Yours faithfully
For and on behalf of
Asian Capital Limited


Joseph Lam
Executive Director

Encl.

Part B Consultation Questions

Please indicate your preference by checking the appropriate boxes. Please reply to the questions below that are raised in the Consultation Paper downloadable from the HKEX website at:

<http://www.hkex.com.hk/-/media/HKEX-Market/News/Market-Consultations/2016-Pre-sent/September-2018-Adverse-Audit-Opinion/Consultation-Paper/cp201809.pdf>

Where there is insufficient space provided for your comments, please attach additional pages.

1. Do you agree with the proposal to add a Rule to require trading suspension if an issuer has published a preliminary annual results announcement and its auditor has issued, or has indicated that it will issue, a disclaimer or an adverse opinion on the issuer's financial statements?

Yes

No

If your answer is "No", please give reasons for your views.

Please refer to Appendix II for details.

2. Do you agree with the proposed Rule 13.50A to require the issuer to address the issues giving rise to the disclaimer or adverse opinion, provide comfort that a disclaimer or adverse opinion in respect of such issues would no longer be required, and disclose sufficient information for investors to assess its updated financial position before trading resumption (as described in paragraph 32 of the Consultation Paper)?

Yes

No

If your answer is "No", please give reasons for your views.

Please refer to Appendix II for details.

- End -

APPENDIX I - QUESTIONNAIRE

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1. Consultation Question #1

Do you agree with the proposal to add a Rule to require trading suspension if an issuer has published a preliminary annual results announcement and its auditor has issued, or has indicated that it will issue, a disclaimer or an adverse opinion on the issuer's financial statements? If not, why?

Whilst we appreciate the Stock Exchange's intention to provide a regulatory framework to ensure investors are provided with timely financial information of which to form their investment decisions, it is also equally important not to be overly stringent. The consultation paper has not provided empirical evidence to demonstrate how many companies that have these preliminary annual results announcements have ended up delisted, we fail to see the rationale for these issuers to be immediately suspended.

In contrast, we are of the view that any issuer having issued a disclaimer or an adverse opinion might not warrant trading suspension or rendered unsuitable for listing. Combined with the fixed period delisting criterion, suspended issuers under the new proposal will in essence be fast tracked into a potential delisting. For this reason, we concur with Mr. David Webb that the proposal would imply *"in medical terms, it is a belief that the incidence of disease, accidents or self-harm can be reduced by walking around the intensive care ward and shooting the patients"*¹. The onus would be on the Stock Exchange to consider whether it is worth over-regulating to maintain "market quality" at the expense of its global reputation as a free market.

Should the Stock Exchange decide to implement the proposal, we submit that issuers should be provided with an equitable opportunity and sufficient time for them to address any qualifications in their financial statements. In this regard, we urge the Stock Exchange to assess each case individually on a case by case basis with reference to all the circumstances and allow a grace period of at least six months especially for issuers which require fund raising to address cash flow problems (if this is the cause of the audit qualifications), or to resolve their relevant audit qualifications if they are proceeding to a re-audit. A quick placement into delisting stage will only damage the issuer and provide insurmountable hurdle for its own rescue, leading to a total loss for the shareholders.

To reach a fair decision, the Stock Exchange must assess each individual issuer's circumstances on a case by case basis and whether a trading suspension is warranted. There may be circumstances where certain types of audit qualifications are either beyond the control of an issuer but are suitably remedied, or qualifications which do not have a material impact to the reliability of the financial statement.

We note that the Stock Exchange included an example of exceptions to the proposed suspension requirement. It would be beneficial for the Stock Exchange to issue a guidance letter to provide market practitioners with further details of any applicable exemptions.

The length of the grace period can be reasonably determined by the Stock Exchange in order to allow issuers sufficient time to address any audit qualifications; and where fund raising is the only issue leading to the qualifications, once the fund raising is completed, there shouldn't be a

¹David M. Webb (30 September 2018). HKEX: shoot patients to prevent illness.

need for an re-audit. In many instances, a trading suspension would have serious implications and limit issuers' ability and avenues to fund raising: it is common place that investors are prepared to take risk at a risk-adjusted price and will take up new shares on a condition precedent that the issuer's shares are not suspended. Similarly, banks will find it difficult to lend to issuers that are suspended, and indeed, there are usual covenants for lenders that the loans are immediately due if the issuer's shares are suspended for a prolonged period of time (by number of days!).

In any case, we submit that the trading suspension should only be begin if the auditor has issued a disclaimer or an adverse opinion on an issuer's financial statements (i.e. in its annual reports) as opposed to the issue of just a preliminary annual results announcement. Even though the preliminary annual results announcement has to be agreed with the auditors, we are of the view that grace period prior to the trading suspension that we suggest should only begin after the publication of the annual report with the disclaimer or an adverse opinion.

We have reservation to the proposed rule which sets such a stringent benchmark that it may no longer serve the best interests of shareholders. The Stock Exchange should have due regard to the potential ramifications of the proposal. The change could potentially promote the practice of opinion shopping and places undue pressure on auditors not to issue a disclaimer or adverse opinion as it would lead to a trading suspension of an issuer. We are concerned that by linking the audit opinion to the listing status of issuers, it contradicts the principles of an informed, disclosure-based market, and to some extent, the independence of the auditors, as their opinions would lead to consequences. There are important distinctions between the Stock Exchange making a decision based on the auditors' report, and the listing rule automatically triggering suspension based on the audit qualifications being a disclaimer or adverse.

Under the existing Rules, the Stock Exchange already has the discretion to suspend issuers under Rule 6.01. Given the Stock Exchange's pre-existing power to suspend problematic issuers, we submit that the Stock Exchange should adopt a rational approach towards issuers with a disclaimer or adverse audit opinion and at least determine whether a suspension of trading in an issuer's securities is required on a case by case basis having regard to all the particular circumstances.

2. Consultation Question #2(a)

Do you agree with the proposed Rule 13.50A to require the issuer to address the issues giving rise to the disclaimer or adverse opinion, provide comfort that a disclaimer or adverse opinion in respect of such issues would no longer be required, and disclose sufficient information for investors to assess its updated financial position before trading resumption (as described in paragraph 32 of the consultation paper)? If not, why?

We agree with the proposed Rule to a certain extent. We propose that the Stock Exchange should determine whether a suspension of trading in the issuer's securities is required on a case by case basis, having regard to all the particular circumstances. In order to address this, issuers will be required to submit detailed reasons to the Stock Exchange in relation to the disclaimer or adverse opinion, and disclose the relevant information before the end of the grace period. The Stock Exchange may at its discretion grant issuers a grace period of up to six months commencing from the publication of the annual report for them to address the audit qualifications before a trade suspension is imposed.

We have included the suggested changes to the Listing Rules below for your consideration.

A. Proposed Main Board Rule

13.50A The Exchange ~~will normally~~ may require suspension of trading in an issuer's securities if it publishes ~~a preliminary results announcement~~ an annual report for a financial year as required under rules 13.49~~46~~(1) and (2) and the auditor has issued, ~~or has indicated that it will issue,~~ a disclaimer of opinion or an adverse opinion on the issuer's financial statements. The Exchange will, having considered all the relevant circumstances, determine on a case by case basis whether a suspension of trading in the issuer's securities and/or a grace period (normally being six months) to remedy the issues giving rise to the disclaimer of opinion or adverse opinion is required. The suspension will normally remain in force until the issuer has addressed the issues giving rise to the disclaimer or adverse opinion, provided comfort that a disclaimer or adverse opinion in respect of such issues would no longer be required, and disclosed sufficient information to enable investors to make an informed assessment of its financial positions.

B. Proposed GEM Rule

17.49B The Exchange ~~will normally~~ may require suspension of trading in an issuer's securities if it publishes an annual report ~~a preliminary results announcement~~ for a financial year as required under rule 18.49~~18.48A~~ and the auditor has issued, ~~or has indicated that it will issue,~~ a disclaimer of opinion or an adverse opinion on the issuer's financial statements. The Exchange will, having considered all the relevant circumstances, determine on a case by case basis whether a suspension of trading in the issuer's securities and/or a grace period (normally being six months) to remedy the issues giving rise to the disclaimer of opinion or adverse opinion is required. The suspension will normally remain in force until the issuer has addressed the issues giving rise to the disclaimer or adverse opinion, provided comfort that a disclaimer or adverse opinion in respect of such issues would no longer be required, and disclosed sufficient information to enable investors to make an informed assessment of its financial positions.