

Direct line : [REDACTED]

Email : [REDACTED]

30th November 2018

By email & by hand

Hong Kong Exchanges and Clearing Limited
8th Floor, Two Exchange Square
8 Connaught Place, Central
Hong Kong

Dear Sirs,

Consultation Paper on Proposal relating to Listed Issuers with Disclaimer or Adverse Audit Opinion on Financial Statements

We are pleased to provide our comments on the captioned Consultation Paper. Capitalised terms used in this letter have the same meaning as ascribed to them in the Consultation Paper.

We fully support the Exchange's proposals to enhance investors' protection by improving the quality and reliability of financial information. In particular, we are pleased to note that the proposal's objective is to encourage issuers to maintain appropriate and effective risk management and internal control systems, and require them to act promptly to resolve audit issues with their auditors. We believe this is essential to maintain the status and reputation of the Hong Kong market benchmarked to international standards.

Our responses to the questions in the Consultation Paper are set out below:

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?)

As stated above, we agree with the principle of incentivising issuers to promptly resolve issues with their auditors. We appreciate the efforts made to ensure issuers provide accurate, timely and useful financial information to the market. We also agree that if there are matters identified during the audit, issuers should resolve the issues with their auditors and advise the public on a timely basis. However, we believe the immediate suspension of trading solely due to a disclaimer or adverse opinion, where auditors are reporting in accordance with the auditing standards, is not an appropriate incentive.

The proposed “strict application” of trading suspension could lead to auditors being pressurised by management not to issue a disclaimer or adverse opinion and that would not be in the public interest. For issuers not providing accurate and quality information, auditors need to feel they can inform the public of the situation.

In the UK, the Financial Conduct Authority (the “FCA”) exercises discretion and may suspend the listing of any securities if the smooth operation of the market is, or may be, temporarily jeopardised or it is necessary to protect investors. Examples include the issuer being unable to assess accurately its financial position and inform the market accordingly. In deciding whether to suspend trading, the FCA considers several factors including qualified reports. Similarly, the Securities and Exchange Commission (the “SEC”) of the US may suspend trading in a stock when it is of the opinion that a suspension is required to protect investors and the public interest. Both the FCA and the SEC enter a process whereby issuers are required to discuss with their auditors how to resolve the issues and how the public should be informed while the regulator considers any suspension under their rules.

We suggest that the Exchange should consider adopting a similar approach whereby the Exchange encourages a process for discussion and resolution of the issues prior to deciding if suspension is appropriate and continuing the process after suspension if this avenue has been invoked. The issuer and auditor could be required to discuss with the Exchange in advance if a disclaimer or adverse opinion is foreseen, including proposals on remedial actions and timeline, so that the Exchange could consider whether a trading suspension is required with the objective of investor protection and public interest and de-listing considered only after an appropriately relevant timeline as opposed to an automatic 18 months. We understand that in the US the system operates such that the auditors, if unable to resolve the issue in time to meet the timetable for reporting, simply do not issue an opinion. Then the strict application of failing to meet the reporting timetable triggers the suspension of trading and a process to inform the public.

Question 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?)

Yes, we fully agree with this proposal.

If you have any questions on these comments, please do not hesitate to contact the undersigned at [REDACTED]

Yours faithfully

[REDACTED]

Paul F. Winkelmann
Chief Executive Officer
Financial Reporting Council