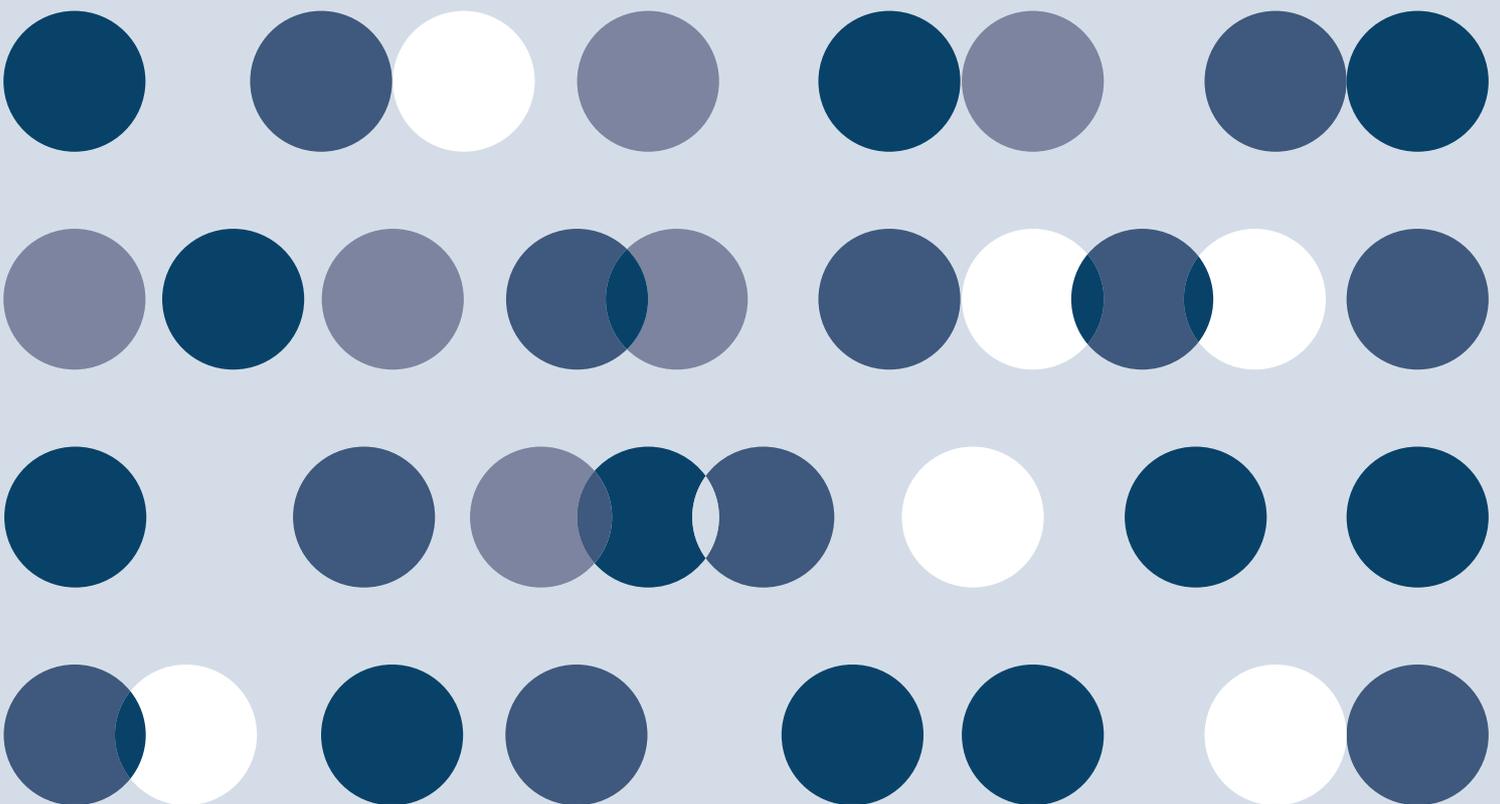


January 2018

REVIEW OF DISCLOSURE IN ISSUERS'
ANNUAL REPORTS TO MONITOR
RULE COMPLIANCE

REPORT 2017



Review of Disclosure in Issuers' Annual Reports to Monitor Rule Compliance Report 2017

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EXECUTIVE SUMMARY

The Listing Department reviews issuers' annual reports as part of its ongoing monitoring and compliance activities. This is the sixth published report which presents our findings and recommendations.

We have examined issuers' annual reports with a focus on Rule compliance, issuers' corporate conduct and their disclosure of material events and developments. In our review of an issuer's disclosure we consider not only the disclosure in the annual report, but also the consistency and materiality of disclosure in its corporate communications (such as announcements and circulars) over time.

The purpose of the issuers' annual report review is primarily to give meaningful guidance to issuers on specific areas to focus on when preparing the annual report. Where we note any particular non-compliance with any rules and regulations, we would consider appropriate disciplinary action under the Exchange Listing Rules and/or making referrals to other regulatory agencies.

For the purpose of this year's review, we have considered the findings and observations in our last review report and the latest market trends and developments of listed issuers, and have selected specific areas for assessing listed issuers' performance and providing appropriate guidance and recommendations. We noted in our last Review Report that issuers have generally followed our previous recommendations on disclosures about share award schemes, accordingly, this area was not covered in this year's review. The seven areas under review this year are as follows:

- (i) Fundraisings through issue of equity / convertible securities and subscription rights
- (ii) Updates on material asset impairments and results of performance guarantees after acquisitions
- (iii) Continuing connected transactions
- (iv) Disclosure in business review and significant securities investments in the MD&A section
- (v) Financial statements with auditors' modified opinions
- (vi) Contractual arrangements adopted by issuers
- (vii) Issuers listed in 2015 and 2016

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While issuers have made material improvements in disclosures and have followed our guidance in areas covered under items (i) and (ii) last year, we have continued our review in these areas given their importance. For material asset impairments under item (ii), we have expanded our review this year to include material asset impairments other than assets previously acquired by the issuers. Our findings in these areas are generally satisfactory.

Last year, in our review of continuing connected transactions (item (iii)) we noted that a minority of issuers did not provide supporting information to their independent directors for the purpose of making their annual confirmations under the Rules. We recommended that issuers should provide sufficient information to independent directors to assist their annual reviews of the continuing connected transactions. This year, we note that issuers have generally provided relevant information to the independent directors for their review of the continuing connected transactions and the adequacy of internal controls.

In view of our recommendations last year on disclosures in the business review in the MD&A section and in financial statements with auditors' modified opinions, we continued our review in these areas as set out in items (iv) and (v). Our review of financial statements with auditors' modified opinions suggested that there is a general improvement on the annual report disclosures about the modifications and how the issuers intend to address the issues giving rise to the modifications. This year, we made follow up enquiries with issuers about their progress in addressing modifications carried forward from previous years. In our review of business review in the MD&A section, we continue to find that issuers can improve the disclosures in these areas. Our recommendations are set out below.

We continued to review areas (vi) and (vii), in view of some changes to the Foreign Investment Industries Guidance Catalogue in 2017, and market concerns about potential listing applicants which exhibit certain "shell" characteristics, and which engaged in activities after listings that may be structured so that they are not subject to regulatory scrutiny under the reverse takeover Rules. We have not made material findings about disclosures of contractual arrangements. As regards newly listed issuers, we have noted an increase in these issuers engaging in activities involving changes in major shareholders, the boards of directors and their major businesses through a series of transactions or arrangements. We will continue to closely monitor these issuers and where justified, apply the reverse takeover Rules in extreme cases.

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The Exchange specifically recommends the following:

- (a) **Business review in MD&A** – we noted that a majority of issuers continued to provide only generic disclosure under the business review. Issuers should disclose relevant information for readers to make an informed assessment of their businesses and financial performance, explain how these factors impact their businesses and how they manage these risks. For example, issuers should disclose not only the principal risks faced by their businesses but also how they would affect their business operations and financial conditions, and measures taken to manage these risks; on environmental policies and performance and compliance with the relevant laws and regulations, issuers should disclose impact of the identified laws and regulations to their operations and provide compliance record; on key relationship with employees, customers and suppliers, issuers should disclose relevant information about these stakeholders and their length of relationship with the issuers; on key financial performance indicators, issuers should disclose meaningful information on how the selected KPIs are linked with their business objectives and discuss how the issuers' performance compared to their industry peers.
- (b) **Financial statements with auditors' modified opinions** – issuers should, in addition to detailed information regarding the audit modifications and their actual and potential impact on the financial position, disclose their action plans to address the audit modifications, timetable for implementation and the progress update on a timely basis. The board of directors should update shareholders on how they can, based on the audit committee's recommendations, promptly resolve the issues that gave rise to the audit modifications.
- (c) **Significant securities investments in MD&A** – Issuers which hold significant securities investments as part of their asset portfolio should disclose meaningful information on their strategy for investments, including their investment objectives, industry focus and other factors that would be considered for investment decisions to facilitate shareholders' understanding of the potential exposure, benefits and risks of future investments.

Issuers are kindly reminded to take note of our observations and recommendations discussed in this report and follow the guidance in their future annual reports to improve transparency and accountability to investors.

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I. INTRODUCTION

1. An annual report should provide material and relevant information about an issuer's financial results and position, and assist investors to assess its past performance and future prospects. As a general principle, disclosure in annual reports should be clear, straightforward, and provide a qualitative analysis that complements and explains quantitative information in the related financial statements. There should be a balanced discussion of all major aspects of the issuers' businesses, including both positive and negative circumstances, in the "management discussion and analysis" section (**MD&A**). Better disclosure improves transparency and promotes a fair, orderly and informed market.
2. As part of our monitoring of issuers' activities, we review annual reports with a particular focus on their Rule compliance, corporate conduct, and disclosure of material events and developments. In our review of an issuer's disclosure we consider not only the disclosure in the annual report, but also the consistency and materiality of disclosure in its corporate communications (such as announcements and circulars) over time. Our review of issuers' disclosure over time helps us identify cases of potentially misleading disclosure in corporate documents, issues on directors' role in safeguarding corporate assets, and possible corporate misconduct.
3. The Rules and applicable accounting standards set out the minimum information an issuer must include in its annual report. An issuer should provide additional information that is relevant to shareholders and investors according to its own circumstances. In our review, we also consider whether issuers adopted our guidance from our previous annual report reviews as well as guidance materials issued from time to time. Where appropriate, we have requested issuers to make further disclosures by way of announcements or in subsequent financial reports.

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4. This report presents our findings and recommendations from our review of the following seven areas. Our review covers the annual reports of issuers for the financial year ended between January and December 2016. Specifically, we reviewed the disclosures in the annual reports of issuers that carried out relevant activities in the financial year, or where applicable, in the previous financial years. We conducted a review on a sample basis of disclosures in the MD&A section (item (iv) below), and issuers' and independent directors' monitoring of continuing connected transactions (item (iii) below). The scope of review for each area is described in Parts II and III of this report.
 - (i) Fundraisings through issue of equity / convertible securities and subscription rights (Part IIA)
 - (ii) Updates on material asset impairments and results of performance guarantees after acquisitions (Part IIB)
 - (iii) Continuing connected transactions (Part IIC)
 - (iv) Disclosure in business review and significant securities investments in the MD&A section (Part IID)
 - (v) Financial statements with auditors' modified opinions (Part IIE)
 - (vi) Contractual arrangements adopted by issuers (Part IIIA)
 - (vii) Issuers listed in 2015 and 2016 (Part IIIB)
5. This review is separate from our Financial Statements Review Program (the **FSRP**). The FSRP reviews the periodic financial reports published by issuers for compliance with the financial reporting standards and the disclosure of financial information requirements under the Listing Rules.
6. In this report, "Rules" refer to both Main Board (**MB**) Rules and Growth Enterprise Market (**GEM**) Rules.

II. FINDINGS ON SPECIFIC AREAS OF DISCLOSURE

A. Fundraisings through issue of equity / convertible securities and subscription rights

7. Under the Rules, issuers should announce details of their equity fundraisings, including the terms and size of the equity issuance and the proposed use of proceeds. Issuers should also report to shareholders on the fundraisings conducted during the financial year in their annual reports¹.
8. In our previous Review Reports, we recommended issuers to provide meaningful updates on the actual use of proceeds in their annual reports during the reporting period. The updates should include details of the actual application, a breakdown of how the funds were allocated among different uses, whether the funds were applied consistently with the intended uses previously disclosed and the intended uses of the unutilized proceeds, if any².
9. Under the Rules³, issuers should disclose in their annual reports details of the classes, numbers and terms of any convertible securities and warrants issued during the financial year, and particulars of any exercise of the conversion or subscription rights during the year. Issuers should ensure that they have sufficient mandate to issue further shares upon conversion or subscription as a result of an adjustment to the conversion price or subscription price of convertible securities or warrants issued under a general mandate. Further, issuers should obtain the Exchange's prior approval before altering the terms of the issued convertible securities or warrants⁴.

¹ Paragraphs 11 and 32 of Appendix 16 to the MB Rules / GEM Rules 18.32 and 18.41

² In the [consultation paper on "Capital Raisings by Listed Issuers"](#) issued by HKEx (September 2017), we proposed to codify our recommended disclosures into the Rules (paragraphs 105 to 109).

³ Paragraphs 10(1) and (2) of Appendix 16 to the MB Rules / GEM Rules 18.11 and 18.12

⁴ MB Rules 15.06 and 16.03 / GEM Rules 21.06 and 22.03

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10. Guidance Letter ([GL80-15](#)) recommends disclosures in issuers' annual and interim reports details of shareholders' dilution impact in the event the convertible securities are fully converted as at the financial period end⁵. This includes (i) the number of shares that may be issued upon full conversion of the outstanding convertible securities; (ii) the dilutive impact on the then number of issued shares of the issuer and respective shareholdings of the issuer's substantial shareholders; (iii) the dilutive impact on earnings per share; (iv) an analysis on the financial and liquidity position of the issuer, discussing its ability to meet its redemption obligations under the convertible securities; and (v) an analysis on the issuer's share price at which it would be equally financially advantageous for the security holders to convert or redeem the convertible securities based on their implied internal rate of return (and therefore the security holders would be indifferent as to whether the convertible securities are converted or redeemed) at a range of dates in the future.

Scope

For all issuers

11. We reviewed the announcements and annual reports of all issuers that conducted equity fundraisings during the financial year, including placings under general and specific mandates and pre-emptive issues. We considered whether the issuers:
- (a) followed our recommended disclosures in paragraph 8 above;
 - (b) obtained the Exchange's prior approval for alteration of the terms of issued convertible securities or warrants in paragraph 9 above; and
 - (c) if applicable, followed our recommended disclosures on the dilution impact upon conversion of the outstanding convertible securities in paragraph 10 above.

⁵ Paragraph 13 of our Guidance Letter [GL80-15](#)

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For large scale fundraisings

12. The cash company Rules⁶ may apply to large scale fundraisings that involved investors injecting substantial amounts of cash into the issuers (see our Guidance Letter [GL84-15](#)). Factors for determining whether the cash company Rules would apply include, among others, whether the funds raised would be used for new businesses with little or no relation to and expected to be substantially larger than the issuers' existing principal businesses. In some cases, we did not apply the cash company Rules after considering, among others, the issuer's proposals about the intended use of proceeds and its business plans (for example, where the proceeds would be applied to the issuer's existing business, or new business not expected to be substantially larger than its existing business).
13. We reviewed the annual report disclosures made by issuers that conducted large scale fundraisings and considered whether their actual use of proceeds were consistent with their original plans. In particular, we looked at whether there was any change in the use of proceeds and whether the proceeds were applied according to the previously disclosed timeframe. A change in the proposed use of proceeds may raise concerns about circumvention of the cash company Rules.

Findings

For all issuers

14. Compared to last year, there was a slight increase in the number of issuers that followed our recommendations to disclose information regarding the actual application of proceeds. The disclosures generally covered whether the funds were applied according to the original plans and details about proposed application of unutilized proceeds. We noted a few issuers revised their uses of proceeds and disclosed the changes in their annual reports. Where the extent of the change was material, they also published announcements at the relevant time.
15. We noted that some issuers have disclosed detailed breakdown of the actual application of proceeds in table form, comparing the actual application against each different use as previously disclosed and disclosing the expected timeframe for application of the unutilized proceeds. We encourage issuers to adopt a similar approach in presenting the actual application of proceeds as this provides more clarity, particularly where the proceeds would be applied to a number of different uses.

⁶ MB Rules 14.82 to 14.84 / GEM Rules 19.82 to 19.84

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16. For issuers that have issued convertible securities and warrants, our review indicates that issuers have generally complied with the disclosure and approval requirements in paragraph 9 above.
17. We noted that over half of the issuers made the recommended disclosures on the potential dilution impact upon full conversion of the outstanding convertible securities as at the year-end. To enhance shareholders' understanding, we recommend that issuers follow our guidance set out in paragraph 10.

For large scale fundraisings

18. For issuers that conducted large scale fundraisings during the financial year, we found that they generally applied the proceeds according to the business plans and timeframe as previously disclosed. We did not note any concerns about circumvention of the cash company Rules.

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B. Updates on material asset impairments and results of performance guarantees after acquisitions

19. The Rules require issuers to announce material acquisitions, publish investment circulars and obtain shareholder approval for these acquisitions. Issuers should also disclose in the MD&A section of their annual reports information about the acquired businesses, including circumstances involving any material asset impairments.
20. Where an asset impairment is supported by an independent valuation, we recommended in our previous Review Reports that the issuer should disclose (a) details of the value of inputs used for the valuation together with the basis and assumptions; (b) the reasons for any significant changes in the value of the inputs and assumptions from those previously adopted; (c) the valuation method and the reasons for using that method; and (d) an explanation of any subsequent changes to the valuation method adopted. This enables shareholders to understand the basis for the impairments and the prospects of the acquired business.
21. In some acquisition agreements, the vendors guarantee the performance of the acquired businesses and agree to compensate the issuers for any shortfall or adjust the consideration based on agreed formulae if the guarantees are not met.
22. The Rules set out the information required to be disclosed in an announcement and the next annual report in respect of any performance guarantee given by a connected person where the actual performance fails to meet the guarantee. In our previous Review Reports, we recommended that, irrespective of whether the performance guarantee is given by a connected person or an independent party, the issuer should publish an announcement (and disclose in its next annual report) regarding the performance of the acquired business and whether the performance guarantee is met. If the performance guarantee is not met, the issuer should disclose how it would enforce the obligations of the guarantor under the acquisition agreement.

Scope

23. We reviewed the announcements, circulars and annual reports of the issuers that:
 - (a) completed material acquisitions in their last two financial years;
 - (b) recorded material impairments on the assets previously acquired during the financial year under review; or

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- (c) required performance guarantees in previous acquisitions with the guaranteed periods ended in the financial year under review.
24. For issuers which completed material acquisitions in their last two financial years, we reviewed their annual report disclosures about the developments of the acquired businesses and any significant changes to the value of intangible assets and goodwill. We considered whether:
- (a) the information disclosed in their original investment circulars was materially accurate;
 - (b) any material change to the acquired business was timely announced; and
 - (c) any impairment to assets was properly made and whether the annual reports discussed matters giving rise to the impairment.
25. For performance guarantees where the guaranteed periods ended in the financial year under review, we reviewed the issuers' annual reports, announcements and the accounts of the acquired businesses to assess whether the outcomes of the performance guarantees were properly disclosed. Where the performance guarantees were not met, we considered whether and how the issuers enforced the obligations of the guarantors.
26. We also reviewed the annual reports of the issuers that recorded material impairments on assets (other than the acquired assets) during the financial year under review, and considered whether the reasons for, and the circumstances leading to, the impairments were adequately disclosed in the annual reports.

Findings

(1) Update on material impairments on acquired assets

27. The number of cases involving material impairments on acquired assets was comparable to last year. Generally, these impairments were caused by slowdown in the market condition of the relevant industry or decline in the trading price of the commodities produced and/or traded by the acquired businesses subsequent to the acquisitions. Issuers generally announced the material impairments by way of profit warning announcements and discussed the matters giving rise to the impairments in their annual reports. A large majority of the issuers supported the material impairments with independent valuations and followed our recommendation to disclose details of the valuations as described in paragraph 20 to enhance shareholders' understanding.

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28. In one case, the issuer recorded a material impairment shortly after the acquisition due to its failure to renew sales contracts with major customers under their original terms. These contracts had expired at the time of the proposed acquisition but this information was not disclosed in the acquisition circular. This suggested that the information in the acquisition circular might be misleading or incomplete. In addition, the acquisition consideration was determined with reference to an independent valuation report which also did not take into account the expiry of the several major sales contracts. This raised concerns about the proper valuation of the acquired assets and the consideration. We have taken appropriate action in this case.
29. We also remind issuers to observe the SFC guidance⁷ on directors' duties in the context of valuations in corporate transactions. This guidance note reminds directors of their duties in ensuring that acquisition targets are properly considered and investigated. Directors should carry out independent due diligence on the acquisition targets. They should not accept blindly and unquestioningly financial forecasts, assumptions or business plans provided to them typically by the target's vendor or management.

(2) Results of performance guarantees

30. Our review of performance guarantees indicated that:
- (a) Generally, issuers continued to follow our recommendations as set out in paragraph 22 above. In all cases except one, issuers disclosed whether the performance guarantee was met and if not, whether and how the guarantors fulfilled their obligations under the agreements.
 - (b) Two-thirds of the performance guarantees were met. Of the performance guarantees that were not met, five were provided by the issuers' connected persons.
 - (c) Where the performance guarantees were not met:
 - (i) in a majority of cases, the issuers were compensated by the guarantors according to the terms of the agreements;
 - (ii) in the other cases, issuers generally took legal actions to seek compensation or, in one case, renegotiate the compensation arrangement to expedite the settlement. Issuers that had initiated legal actions to seek compensation generally updated shareholders about status of the legal actions in their announcements or annual reports; and

⁷ [Guidance note on directors' duties in the context of valuations in corporate transactions \(May 2017\)](#) issued by the SFC

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- (iii) in one case, a substantial portion of the acquired business's profits during the guarantee period under review was generated from an one-off disposal gain which was not generated in the target's ordinary course of business. This raises a question about whether the shortfall in performance guarantee was materially understated. We have taken appropriate action in this case.
- (d) Where issuers confirmed that the performance guarantees had been met, in all cases, our review of the accounts of the acquired businesses did not indicate any concern about the truthfulness of such confirmations.

(3) Update on material impairments on assets

31. Issuers made material impairments on assets (other than the acquired assets), including intangible assets, financial assets, property, plant and equipment and receivables, during the financial year under review. Generally, these impairments were caused by unfavourable market condition or business downturn. Issuers generally announced the material impairments by way of profit warnings announcements. Further, issuers discussed the reasons for, and the circumstances leading to, the impairments in their annual reports. For those issuers that supported the material impairments with independent valuations, we noted that they followed our recommendation to disclose details of the valuations as described in paragraph 20 to enhance shareholders' understanding.

C. Continuing connected transactions

32. Under the Rules, shareholders may give an issuer a prior mandate to conduct connected transactions, subject to the terms of the agreement which provide a framework for negotiating each individual transaction, and annual caps which limits the aggregate size of the transactions. It is important that the terms of the agreement are specific and measurable, and that there are adequate internal controls in place to ensure that the individual transactions are indeed conducted within the framework of the agreement.
33. The Rules also require that, in each financial year:
- (a) An issuer must report its continuing connected transactions in its annual report. It must confirm whether its related party transactions (as disclosed in the financial statements) were connected transactions under the Rules and, if so, whether these transactions complied with the connected transaction requirements.
 - (b) Independent non-executive directors (**INEDs**) and auditors must review the issuer's continuing connected transactions and report their findings in the issuer's annual reports. INEDs must also confirm whether such transactions were made (i) according to the agreement governing them on terms that are fair and reasonable and in the interests of the issuer's shareholders as a whole; (ii) on normal commercial terms or better; and (iii) in the issuer's ordinary and usual course of business.
34. Guidance Letter [GL73-14](#) provides guidance to issuers on establishing pricing policies in agreements for continuing connected transactions and internal controls to monitor these transactions, and to INEDs on their roles in reviewing the transactions' compliance with the terms of the agreements and the connected transaction Rules. In particular:
- (a) An issuer should have in place adequate internal control procedures to ensure that individual continuing connected transactions are indeed conducted in accordance with the pricing policies or mechanism under the framework agreements. It should also ensure that its internal audit function⁸ will review these transactions and the internal control procedures, and provide the findings to the INEDs to assist them in performing their annual review.

⁸ Under the Corporate Governance Code, an issuer should also have an internal audit function which carries out an analysis and independent appraisal of the adequacy and effectiveness of its risk management and internal control systems.

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- (b) INEDs should ensure that (i) the methods and procedures established by the issuer are sufficient to ensure that the transactions will be conducted on normal commercial terms and not prejudicial to the interests of the issuer and its minority shareholders; and (ii) appropriate internal control procedures are in place and the issuers' internal audit function would review these transactions. Where appropriate, they should make enquiries with the management to ensure that they are given sufficient information to review the transactions and the internal control procedures.

Scope

Internal control procedures and INED annual review

35. We sent questionnaires to 49 selected issuers⁹ and requested information concerning pricing policies in their continuing connected transaction agreements, and the issuers' internal controls and procedures to monitor whether the individual connected transactions were conducted in compliance with the agreements and the continuing connected transaction Rules. We also requested information about the annual reviews performed by INEDs.

Annual report disclosure

36. We reviewed the annual reports of all issuers that conducted continuing connected transactions (excluding those with specific pricing terms such as a rental agreement) during the financial year. We reviewed their announcements and circulars against the disclosures in their annual reports to assess their compliance with the annual reporting requirements.

Findings

Internal control procedures and INED annual review

37. Our review indicated that (i) issuers generally have followed the guidance in [GL73-14](#) when establishing pricing policies in agreements for continuing connected transactions. Such pricing policies were specific and measurable. Further, issuers generally have in place internal control procedures to ensure that individual continuing connected transactions were conducted in accordance with the pricing policies or mechanism under the agreements. They have also engaged their finance, internal audit function and/or internal designated teams to periodically counter-check whether the internal controls and procedures were enforced.

⁹ We sent questionnaires to 8, 33 and 8 issuers with market capitalization of more than \$5 billion, between \$1 billion to \$5 billion, and less than \$1 billion respectively. These issuers were selected on a random sampling basis within the three bands of issuers categorized by size of market capitalization.

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38. Last year, we noted that a majority of issuers provided material information to the INEDs for the performance of their reviews on internal control measures (see paragraph 34(a)), and to make their confirmations in the annual reports in the manner set out in paragraph 33(b). However, a minority of issuers provided only limited information to the INEDs, including (a) management confirmation on the fairness and reasonableness of the transactions, and (b) external auditor's confirmation letter¹⁰ to the INEDs. We reminded INEDs to ensure that they have sufficient information to properly review the transactions and the internal control procedures.
39. This year, we noted that issuers have generally provided relevant information to INEDs for the purpose of their annual review, including:
- (a) Information to support that the issuer has in place adequate internal control procedures to comply with the connected transactions Rules, such as internal guidelines which require the operation teams to conduct the continuing connected transactions in accordance with the terms of framework agreements, including the pricing policy and mechanism, within the annual cap limits, and on normal commercial terms, or internal approval procedures that require multiple-level and/or cross-department approvals to ensure independent assessment of connected transactions.
 - (b) Information related to the assessment of the appropriateness and effectiveness of the internal control procedures. Most issuers engaged their internal audit function to regularly check the internal control procedures and provided the findings and recommendations, if any, to the INEDs. In other cases external professional parties were appointed to review the internal control procedures and provided reports to the INEDs for their information and review.
 - (c) Information related to the underlying continuing connected transactions. This included vouchers, quotations, invoices, receipts for the relevant transactions and related price or market trend data to support that the terms of the individual continuing connected transactions were comparable to those of third parties. Sample checking was also performed by internal audit function and the findings were provided to the INEDs for their consideration.

¹⁰ Under MB Rule 14A.56 / GEM Rule 20.54, an issuer must engage its auditors to report on the continuing connected transactions every year. The auditors must provide a letter to the issuer's board of directors confirming whether anything has come to their attention that causes them to believe that the continuing connected transactions: (1) have not been approved by the issuer's board of directors; (2) were not, in all material respects, in accordance with the pricing policies of the issuer's group if the transactions involve the provision of goods or services by the issuer's group; (3) were not entered into, in all material respects, in accordance with the relevant agreement governing the transactions; and (4) have exceeded the cap.

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40. In addition to annual reviews some INEDs had oversight over the ongoing monitoring of continuing connected transactions. For example, some INEDs participated in the issuer's periodic meetings for reviewing continuing connected transactions or sat on the special committee in charge of the internal audit work.
41. The above measures supported INEDs in providing the annual confirmation about the continuing connected transactions¹¹ in the annual reports.

Annual report disclosure

42. We noted that a vast majority of issuers continued to comply with the annual report disclosure requirements set out in paragraph 33 above. A few issuers failed to confirm in their annual reports whether their related party transactions were connected transactions under the Rules. Without this statement, the shareholders would not know whether the issuers have reviewed and properly identified all connected transactions and complied with the Rule requirements. Issuers should take note and ensure this disclosure is made.

¹¹ see paragraph 33(b).

D. Disclosure in business review and significant securities investments in the MD&A section

43. The MD&A section serves to provide meaningful information that enables shareholders and investors to appraise an issuer's performance and prospects. Paragraphs 32 and 52 of Appendix 16 to the MB Rules / GEM Rules 18.41 and 18.83 set out the minimum required disclosure and recommended additional disclosure for the section.
44. Following the amendments of the Companies Ordinance that took effect in March 2014, paragraph 28(2)(d) of Appendix 16 to the MB Rules / GEM Rule 18.07A(2)(d) were introduced in 2015 and require the annual reports to include a business review. This serves to promote transparency of an issuer's business and financial performance in the interests of the shareholders and investors.
45. In addition, paragraph 32(4) of Appendix 16 to the MB Rules / GEM Rule 18.41(4) requires issuers to disclose their significant investments held, their performance during the financial year and future prospects. Sufficient information concerning the investments should be disclosed for shareholders to better appraise the underlying value, potential risk exposure and future prospect of such investments to the issuer.

Scope

46. We reviewed the annual reports of 37 selected issuers¹² and considered whether there was sufficient information in their business review sections for shareholders and investors to make a reasonable assessment of their businesses and financial performance.
47. We reviewed the annual reports of 52 selected issuers¹³ which made substantial investments during the financial year and considered whether they followed our last year's recommendations on annual report disclosures.

¹² Issuers are selected with the following characteristics: (a) significant growth in revenue, profit margin, or changes in financial position; (b) reliance on a small number of key customers or suppliers; and (c) abnormal effective tax rates.

¹³ This represented issuers with total investments which accounted for 20% or more of their total assets as at the financial year end dates.

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Findings

Business review

48. In our last report, we recommended disclosures on various topics under the business review section, including principal risks and uncertainties affecting the issuer, environmental policies and performance and compliance with the relevant laws and regulations, key relationships with employees, customers and suppliers and financial key performance indicators (**KPIs**).
49. Based on our review, we noted that a majority of issuers continued to provide only generic disclosure under the business review. We set out our observations as well as recommendations for improvement as follows:

(a) Principal risks and uncertainties affecting the issuer

50. In our last report, issuers were recommended to discuss specifically how the major risk areas would affect their business operations, the potential financial impact, and whether they had undertaken any measures to manage the risk area.
51. Most issuers did not follow the disclosure recommendation and merely provided general description on their risk exposure. In these cases, issuers generally only stated the categories of the risks such as credit risk, risk associated with reliance on one key customer or supplier, or that they have certain measures in place to address the risks. However, they did not further elaborate to what extent each of the risks would adversely affect their business or financial conditions, and specific details of the measures they have undertaken and how they would operate to mitigate such risks. Issuers are expected to follow our recommended disclosure in paragraph 50 above.

(b) Environmental policies and performance and compliance with the relevant laws and regulations

52. To meet this disclosure requirement, we recommended in our last report that issuers should include more detailed disclosures, including whether and how the laws or regulations in question would have a material implication or impact on their operations and, where applicable, the historical compliance record and details of the non-compliance.

Review of Disclosure in Issuers' Annual Reports to Monitor Rule Compliance Report 2017

53. We noted that some issuers only made general statements such as “*the issuer was not aware of any material breach of the relevant laws and regulations*” or “*the issuer has complied with the relevant laws and regulations in material aspects*”. These statements did not provide meaningful information on the specific legal or regulatory requirements that are applicable to the issuer and the potential impact on the issuer’s business and financial performance. We remind issuers to follow our recommended disclosure.

(c) Key relationship with employees, customers and suppliers

54. In the past years, we recommended issuers to disclose details of their key relationships with employees, customers and suppliers. This year, we noted some improvements in this aspect. A few issuers disclosed key employee data such as gender / age distribution or turnover rate, and the identity and background of key customers as well as the length of relationship with them.
55. Sufficient information concerning an issuer’s key relationship with its employees, customers and suppliers can enhance shareholders and investors’ understanding of the issuer’s business model, and how each of these key stakeholders fits into the model and their impact on the operations. This can improve transparency and minimize unnecessary speculation or misconception on the issuer’s business and financial performance.
56. We reiterate our recommendation that issuers should disclose meaningful information on their key stakeholders such as the background of the major customers / suppliers and their length of relationship with the issuers, the credit terms granted to / by these customers / suppliers, details of subsequent settlement, the underlying risks associated with their major customers / suppliers and the measures undertaken to mitigate such risks.

(d) Financial KPIs

57. In our last report, we recommended issuers to disclose the reasons for selecting certain KPIs, how they are linked with their objectives, and what trend each of the KPIs represented.
58. Based on our review this year, we continued to note that the issuers only cited some financial ratios as their KPIs. However, they did not explain why these ratios were selected, how they were linked with their objectives, and what trend each of the KPIs represented. We recommend issuers to enhance disclosure in this area such that shareholders can assess whether the selected KPIs are relevant to the issuer and whether they would be effective tools for the management to measure the business and financial performance.

Review of Disclosure in Issuers' Annual Reports to Monitor Rule Compliance Report 2017

59. In addition, we encourage issuers to disclose additional commentary on discussion and analysis as recommended under paragraph 52 of Appendix 16 / GEM Rule 18.83, including efficiency indicators, industry specific ratios and an overview of trends in the issuer's industry and business. This industry trend and ratios, in conjunction with the issuer's KPIs analysis and comparison, would present shareholders with a better picture of the issuer's performance compared to the industry peers.

Significant securities investments

60. In our last report, we noted that a majority of issuers did not provide adequate information about their investments in the annual reports. We reminded issuers to disclose a breakdown of their major investments held, their performance during the year, their investment strategy and future prospects. In this year, we selected a sample of 52 issuers which made substantial investments during the financial year and assessed whether they have followed our recommendations.
61. Based on the sample review, we noted that issuers, particularly after our enquiries, have generally improved their annual reports with breakdown of their investments and additional information on their fair value and past performance during the financial year.
62. However, we noted that the discussion of strategy for future investments is limited. We therefore recommend issuers to enhance disclosure in this area, including discussion on their investment objectives, industry focus and other factors that would be considered for investment decisions to facilitate shareholders' understanding of the potential exposure, benefits and risks of future investments.

E. Financial statements with auditors' modified opinions

63. Issuers are obliged to provide shareholders with financial statements which fairly present their financial position and performance and are free from material misstatements. Such financial information is necessary for shareholders and investors to make an informed investment decision.
64. Paragraph 3 of Appendix 16 / GEM Rule 18.47 requires an issuer to provide more detailed or additional information if its financial statements do not give a true and fair view of its state of affairs, results of operations and position of cashflows.
65. Under the Corporate Governance Code¹⁴, the board is responsible for ensuring that (a) the issuer establishes and maintains appropriate and effective internal control systems for proper financial reporting; and (b) a review of the effectiveness of internal control systems is conducted at least annually and reported in its Corporate Governance Report. Further, the audit committee should monitor the integrity of the issuer's financial statements and review any significant financial reporting judgments contained in the annual reports, the going concern assumptions and any modifications, and compliance with accounting standards. It should also give due consideration to any matters raised by the auditors and oversee the issuer's internal control systems.

Scope

66. This year, we reviewed the annual reports of 62 issuers with auditors' modified opinions on their financial statements for the financial year ended 31 December 2016¹⁵. We reviewed (a) the issuers' disclosures regarding the modified opinions; and (b) their plans to address the modifications.

¹⁴ Sections C.2 and C.3 of Appendix 14 to the MB rules / Appendix 15 to the GEM Rules

¹⁵ There are 23 issuers with auditors' modified opinion on their financial statements for the financial year ended 31 March 2017 and 30 June 2017. We are reviewing their annual reports and the scope of review is similar to that mentioned in paragraph 66 above. The findings will be covered in our next review report.

Review of Disclosure in Issuers' Annual Reports to Monitor Rule Compliance Report 2017

Findings

67. In last year's report, we reminded issuers with auditors' modified opinions on their financial statements to enhance their disclosure in annual reports to enable shareholders to better understand the audit modifications, their actual or potential impact on the financial position and the proposed plans for addressing the modifications. For modifications involving judgment (such as going concern assumptions and the valuation to support the fair value of assets), the management should clearly explain their position and the basis for forming that position in the annual reports. Moreover, the audit committee should critically review these judgmental areas. Any disagreement by the audit committee with the management's position should be disclosed in the annual report.
68. We noted that there is a general improvement on the annual report disclosures about the modifications and how the issuers intend to address the issues giving rise to the modifications. A majority of the issuers provided additional information regarding the modifications which covered the following areas:
- (a) details of the modifications and their actual or potential impact on the issuers' financial position;
 - (b) management's position and basis on major judgmental areas (such as basis for impairment or valuation of assets), and how the management's view is different from that of the auditors;
 - (c) audit committee's view towards the modifications, and whether the audit committee reviewed and agreed with the management's position concerning major judgmental areas; and
 - (d) issuer's proposed plans to address the modifications.
69. We noted that some issuers did not provide some of the above information, such as the audit committee's view towards the modifications or the issuers' plans to address the modifications, in the annual reports. Following our enquiries, these issuers disclosed such information in their supplemental announcements.
70. We continue to recommend issuers to make proper disclosure on their audit modifications to enhance transparency of their financial condition to shareholders.

Review of Disclosure in Issuers' Annual Reports to Monitor Rule Compliance Report 2017

71. For some issuers, we noted that certain modifications remained unresolved and were brought forward from the previous financial years. These modifications mainly include:
- (a) *Failure to provide books and records of subsidiaries/ associates* – some issuers were unable to provide auditors with books and records of subsidiaries or associates due to ongoing disagreements with other shareholders of the subsidiaries or associates.
 - (b) *Recoverability of prepayment or loans* – some issuers were unable to provide auditors with sufficient audit evidence to substantiate the substance and rationale of making certain prepayments or loans.
 - (c) *Valuation of assets* – some issuers were unable to provide auditors with sufficient audit evidence to substantiate the valuation of assets as these assets are subject to uncertainty on the outcome of future events (e.g. on-going litigation or certain governmental policy becoming effective) which might affect the impairment assessment.
72. We made follow up enquiries with these issuers about their progress in addressing the modifications and the proposed further actions for resolving them. In most cases, these issuers have provided their proposed plans to resolve the modifications. For example,
- (a) *Failure to provide books and records of subsidiaries/ associates* – these issuers were in the process of negotiating the access to the books and records with the other shareholders of the subsidiaries or associated companies, or where negotiations failed, initiated legal proceedings against these parties to gain access.
 - (b) *Recoverability of prepayment or loans* – these issuers discussed and agreed to certain repayment schedules with their customers or debtors for collecting the outstanding prepayments or loans over a period of time.
 - (c) *Valuation of assets* – these issuers generally formulated plans to substantiate or update the asset valuation for the purpose of removing the previous audit modifications on asset impairment. For example, where the previous audit modification arose due to the delay in launch of new products, the issuer took measures to update its internal systems and ensure timely launch of its new products in the market in order to support the profit forecast in the updated valuation.

Review of Disclosure in Issuers' Annual Reports to Monitor Rule Compliance Report 2017

73. Based on the issuers' responses to our enquiries, we noted that issuers generally have followed their plans for resolving the audit modifications. In some cases, the issues giving rise to the modifications required longer time to resolve because some procedures undertaken by the issuers were not within their control (e.g. on-going litigation or certain actions were subject to negotiations involving various parties). As such, the modifications would recur in the next financial year.
74. To facilitate shareholders' understanding, we recommend issuers to disclose their action plans for addressing the audit modifications, timetable for implementation and the progress update on a timely basis. We consider that the integrity of the issuer's financial statements is of the utmost importance as they serve to provide information to shareholders to make an informed assessment of the issuer's performance and financial position. Where there is any audit modification, shareholders should be timely updated on how the board can, based on the audit committee's recommendations, promptly resolve the issues that gave rise to the modifications.

III. FINDINGS ABOUT RULE COMPLIANCE BY SPECIFIC TYPES OF ISSUERS

A. Contractual arrangements adopted by issuers

75. Issuers engaged in businesses subject to foreign ownership restrictions listed on the Foreign Investment Industries Guidance Catalogue commonly use contract-based arrangements or structures (the **Contractual Arrangements** or **Structured Contracts**) to indirectly own and control such businesses and the operating entities.
76. Guidance Letter ([GL77-14](#)) sets out factors for issuers to consider when adopting Contractual Arrangements, and requires disclosures in their transaction announcements and circulars about the legality and validity of the Contractual Arrangements and subsequent changes thereto. Contractual Arrangements adopted by issuers must be narrowly tailored to address the foreign ownership restrictions. Where the business is no longer subject to foreign ownership restrictions, issuers should unwind the Structured Contracts and comply with all relevant PRC laws and regulations.
77. For requirements other than the foreign ownership restriction (the **Other Requirements**)¹⁶, the issuer should, upon advice from its legal adviser, reasonably assess the requirements under the applicable rules and take all reasonable steps to comply with them. While the issuer may not be able to fully comply with the Other Requirements before the establishment of the Contractual Arrangements, it must commit financial and other resources to achieve full compliance as soon as practicable.

¹⁶ Certain industry regulators impose certain qualification requirements which are other than the foreign ownership restriction listed in the Foreign Investment Industries Guidance Catalogue. For example:

- (a) Under the Provisions on the Administration of Foreign-Invested Telecommunications Enterprises, the major foreign investor of a foreign-invested telecommunications enterprise providing value-added telecommunications services shall have a good performance record and experience in providing value-added telecommunications services.
- (b) Sino-foreign cooperation in operating schools or training programs in the PRC is subject to the Regulation on Sino-Foreign Cooperation in Operating Schools. The foreign investor in a sino-foreign joint venture private school must be a foreign educational institution with relevant qualification and high educational quality (subject to evaluation by the relevant authority).

Review of Disclosure in Issuers' Annual Reports to Monitor Rule Compliance Report 2017

78. Guidance Letter ([GL77-14](#)) also provides disclosure guideline for issuers adopting Contractual Arrangements (the **VIE-Issuers**) when preparing their annual reports. The recommended disclosures include:
- (a) particulars of the operating entity and its registered owners, and a summary of the major terms of the Structured Contracts;
 - (b) a description of the operating entity's business activities and their significance to the issuer;
 - (c) appropriate quantitative information including revenue and assets subject to the Structured Contracts;
 - (d) the extent to which the Structured Contracts relate to requirements other than the foreign ownership restriction;
 - (e) the reasons for using the Contractual Arrangements, the risks associated with the arrangements and the actions taken by the issuer to mitigate the risks;
 - (f) any material change in the Contractual Arrangements and/or the circumstances under which they were adopted, and its impact on the issuer group; and
 - (g) any unwinding of the Structured Contracts or failure to unwind when the restrictions that led to the adoption of the Structured Contracts are removed.
79. The issuers are also recommended to publish the Structured Contracts on their websites to promote transparency.

Scope

80. We reviewed and considered whether (a) the VIE-Issuers' annual reports followed our disclosure guidance, and (b) whether the VIE-Issuers have published the Structured Contracts on their websites. Our review covered all issuers which have announced Contractual Arrangements.

Review of Disclosure in Issuers' Annual Reports to Monitor Rule Compliance Report 2017

Findings

81. Compared to last year, the disclosures in VIE-Issuers' annual reports have slightly improved, with over 85% of the VIE-Issuers having made disclosures in their annual reports as recommended under our guidance. A few VIE-Issuers did not disclose any information about their Contractual Arrangements but, after our follow up, have either published supplemental announcements or agreed to make the disclosures in their forthcoming annual reports.
82. About one-third of the VIE-Issuers are also subject to Other Requirements. A majority of VIE-Issuers followed our recommendation and disclosed details of the Other Requirements and the proposed action plans for meeting such requirements in their annual reports. For example, some VIE-Issuers stated that they have been gradually building up their track record of overseas business operations for the purpose of satisfying the relevant Other Requirements. To provide shareholders with more meaningful update, we continue to encourage all the VIE-Issuers that are subject to Other Requirements to disclose details of the Other Requirements, the proposed action plans for meeting such requirements and the status update thereof in their future annual reports.
83. We noted that a majority of the VIE-Issuers have published the Structured Contracts on their websites. To promote transparency, we encourage those VIE-Issuers which have not done so to follow the recommended practice.
84. In June 2017, the PRC government published a revised Foreign Investment Industries Guidance Catalogue (the **Catalogue**) which released certain businesses from the foreign ownership restriction. As the Contractual Arrangements adopted by issuers must be narrowly tailored to address the foreign ownership restriction, issuers should assess any implications arising from changes to the Catalogue on the continued use of the Structured Contracts from time to time. Where the issuers' businesses are no longer subject to the foreign ownership restriction, issuers should unwind the Structured Contracts and comply with the relevant PRC laws and regulations as soon as practicable.

Review of Disclosure in Issuers' Annual Reports to Monitor Rule Compliance Report 2017

B. Issuers listed in 2015 and 2016

85. As part of the Listing Department's ongoing monitoring activities, we reviewed new issuers' Rules compliance and annual report disclosure. This section highlights our general observations and recommendation.

Scope

86. 138 and 126 issuers were listed in 2015 and 2016 respectively (the **Newly Listed Issuers**). We considered their Rule compliance and annual report disclosure in the following areas:

- (a) profit forecasts and material changes in financial results;
 - (b) changes in the use of IPO proceeds;
 - (c) undertakings provided by major shareholders;
 - (d) fulfilment of conditions or undertakings imposed before listing; and
 - (e) non-compliance with the Listing Rules after listing.
87. We also reviewed the post-listing developments of these issuers to examine their compliance behaviors.

Findings

(a) Profit forecasts and material changes in financial results

Profit forecasts

88. A vast majority of the Newly Listed Issuers did not publish any profit forecast in their prospectus. All profit forecasts published by Newly Listed Issuers were met.

Review of Disclosure in Issuers' Annual Reports to Monitor Rule Compliance Report 2017

Profit warnings / Positive profit alerts

89. Some Newly Listed Issuers published profit warning or positive profit alert announcements in respect of their first financial year after listing. Generally, these announcements (mostly profit warnings) were published within one and a half month after their financial year ends.
90. In previous years, we reminded issuers to observe the guidance published in the [SFC Corporate Regulation Newsletter of April 2015](#) and our previous Review Reports. According to the guidance, profit warning or positive profit alert announcement that repeats facts previously disclosed in the prospectus is not necessary and may even cause confusion. If an issuer feels that it needs to make such an announcement, it should clarify the extent to which the information in the announcement differs from those previously disclosed in the IPO prospectus. If there has been a significant change in the facts and circumstances since the IPO prospectus was issued, the issuer may be required to make an announcement under the Inside Information Provisions. In addition, issuers are encouraged to quantify potential impact to the profit figures and use clear and concise language in profit alert announcements¹⁷.
91. Based on our review, a large majority of the Newly Listed Issuers issued profit warning or positive profit alert announcements disclosing the expected changes to the profit or loss and the major reasons for such changes. More than half of these issuers quantified such financial impact in terms of percentages or in dollar amounts. However, a minority of the Newly Listed Issuers merely repeated facts previously disclosed in the IPO prospectus in the profit alert announcements. We remind all new issuers and their compliance advisers to follow the above guidance in paragraph 90 above.

(b) Changes in the use of IPO proceeds

92. The disclosure in an IPO prospectus and an annual report regarding the use of the IPO proceeds indicates how a Newly Listed Issuer deploys resources to develop and expand its business. This is relevant information for investors to appraise the issuer's business development and make informed investment decisions. Where there are changes to the use of IPO proceeds, an issuer should timely and properly explain any material changes by way of announcement.
93. We identified a few Newly Listed Issuers that announced changes to their proposed uses of IPO proceeds within the first two years after listing. We noted that these issuers generally explained the reasons for the changes in their annual reports.

¹⁷ SFC Corporate Regulation Newsletters of [April 2015](#) and [December 2016](#).

Review of Disclosure in Issuers' Annual Reports to Monitor Rule Compliance Report 2017

(c) Undertakings provided by major shareholders

94. It is common that a new issuer would be given a non-competition undertaking (**NCU**) by its major shareholder for the purpose of establishing a clear delineation between the issuer's business and that of the major shareholder. In our review of the annual reports we found that a vast majority of these issuers disclosed information regarding the compliance with the NCUs by the major shareholders, as well as the steps taken to confirm compliance (e.g. the INEDs' review of the confirmation provided by the major shareholder).

(d) Fulfilment of conditions or undertakings imposed before listing

95. In some cases, the Listing Committee imposed specific conditions on, or required undertakings to be provided by, a Newly Listed Issuer before listing. These conditions or undertakings included obtaining permits for properties, updates on business exposure to sanctions risks and disclosures on the actual use of advance mandates for asset acquisitions. The issuer should disclose its compliance with such conditions or undertakings in its annual report after listing.
96. We identified a few cases where the Newly Listed Issuers were required to disclose in their annual reports whether the relevant conditions or undertakings imposed before listing were fulfilled. These issuers either disclosed such information in their annual reports, or, upon our follow up, by way of supplemental announcements.

(e) Non-compliance with the Listing Rules after listing

97. Compared to last year, there is a notable increase in the number of the Newly Listed Issuers that breached the Rules after listing. The breaches included:
- (a) non-compliance with notifiable / connected transaction requirements (15 cases), including failures to announce transactions in a timely manner and failures to seek shareholder approval for the proposed transactions; and
 - (b) failures to maintain the minimum public float requirement (2 cases). Both cases involved connected persons (other than controlling shareholders) holding shares in the issuers. Both issuers subsequently restored the minimum public float to comply with the Rules.

We have taken appropriate actions against the issuers involving in the above breaches.

Review of Disclosure in Issuers' Annual Reports to Monitor Rule Compliance Report 2017

98. Chapter 3A (or Chapter 6A of GEM Rules) requires an issuer to consult with its compliance adviser on a timely basis in certain circumstances, including (a) before the publication of any regulatory announcement, circular or financial report; (b) where a transaction which might be a notifiable or connected transaction is contemplated including share issues and share repurchases; and (c) where there is a proposed change of the use of IPO proceeds, or a proposed change in business activities, developments or results which deviated from any forecast, estimate or other information in the prospectus. In our previous Review Reports, we reminded newly listed issuers to observe the Rule requirements to consult with their compliance advisers. Despite this reminder, we noted from our review that some Newly Listed Issuers failed to do so. We reiterate our guidance that Newly Listed Issuers should consult with their compliance advisers in a timely manner to ensure compliance with the Rules.

Post-listing developments of the Newly Listed Issuers

99. In June 2016, we issued guidance ([GL68-13A](#)) on IPO vetting of potential listing applicants which exhibit certain “shell” characteristics. The Guidance Letter noted that activities by such companies after listings may be structured so that they are not subject to regulatory scrutiny under the reverse takeover Rules. In this regard, we reviewed the post-listing developments of Newly Listed Issuers, particularly regarding their material transactions and changes in control. Our observations are as follows:
- (a) There were 14 Newly Listed Issuers (last year: 14 new issuers) where the controlling shareholders disposed of their controlling interests in the issuers shortly after the lock-up periods expired. This included 13 issuers listed in 2015 and one listed in 2016. In one case, the disposal took place only 15 months after listing.
 - (b) 29 Newly Listed Issuers (last year: 22 new issuers) were identified by the SFC as having high concentration of shareholding shortly after listing. This included 14 issuers listed in 2015 and 15 issuers listed in 2016. In two cases, the high concentration announcements were published within one month after listing.

Review of Disclosure in Issuers' Annual Reports to Monitor Rule Compliance Report 2017

- (c) 32 Newly Listed Issuers conducted very substantial acquisitions, major acquisitions and/or major disposals since listing. Three of these issuers acquired new businesses that were not disclosed under the business plans in their IPO prospectuses. Further, five of these issuers conducted major disposals of part of the existing operations that were their core businesses at the time of the IPO. Particularly, six of the 14 Newly Listed Issuers which had change in control as mentioned in sub-paragraph (a) above also conducted major or discloseable acquisitions after the change in control. One of them related to acquisition of a target engaging in new businesses.
 - (d) As mentioned in paragraph 93 above, a few Newly Listed Issuers made changes in the use of IPO proceeds within the first two years after listing.
100. We have noted an increase in Newly Listed Issuers engaging in activities involving changes in major shareholders, the boards of directors and their major businesses through a series of transactions or arrangements. In October 2017, we published a listing decision ([LD113-2017](#)) about a newly listed issuer involving in such transactions that raised concerns whether those transactions together represented an attempt to conduct a reverse takeover. We will continue to closely monitor these issuers and where justified, apply the reverse takeover Rules in extreme cases.

IV. CONCLUSION

101. From our review of issuers' annual reports this year, we noted further improvements in disclosures in areas including the use of proceeds from fundraisings through issue of equity securities, results of performance guarantees, continuing connected transactions, significant securities investments in the MD&A section, and contractual arrangements. The majority of issuers have considered and adopted our guidance to enhance their disclosures in annual reports. We also noted that issuers have generally provided relevant information to INEDs for the purposes of their annual review.
102. In respect of disclosures in business reviews in the MD&A section and in financial statements with auditors' modified opinions, we have highlighted in this report aspects that issuers should take into account when making disclosures.
103. As a general measure to improve communications with shareholders, enhance Rule compliance and promote a fair, orderly and informed market, issuers should take note of and consider our observations discussed in this report in preparing their annual reports.

- End -

