

Regarding:

- 1) **HKEX publishing the *Frequently asked questions on the Joint Statement in relation to Results Announcements in light of Travel Restrictions related to the Severe Respiratory Disease associated with a Novel Infectious Agent*; and**
- 2) **Practical recommendations on the relevant directors' duties**



On 28 February 2020, the Stock Exchange of Hong Kong Limited (the “**HKEX**”) issued the *Frequently asked questions on the Joint statement* (the “**Joint Statement**”) in relation to *Results Announcements in light of Travel restrictions related to the Severe Respiratory Disease associated with a Novel Infectious Agent* (the “**FAQs**”). We hereby provide further explanation on these questions and the Joint Statement issued by HKEX and the Securities and Futures Commission (the “**SFC**”).

We have summarised the Joint Statement and the FAQs to assist Hong Kong listed companies to understand the guidance from the HKEX and the SFC and to take respective actions.

1. Publication of preliminary results on or before 31 March 2020

Listed companies (with financial year ended on 31 December 2019) are still required to issue its preliminary results without the agreement with auditors on or before 31 March 2020 containing:

- ▶ a statement to the effect that the results have not been agreed with its auditors;
 - ▶ an explanation for the lack of agreement with auditors and where available, the expected date that the results may be agreed with auditors;
 - ▶ whether the results have been agreed with the audit committee and if there is disagreement, details of the disagreement; and
 - ▶ (where applicable) details of the any uncertainties as to potential adjustments to the financial figures (whether due to the lack of supporting evidence, or relating to the impairment or valuation of assets or liabilities).
- **Recommendations:** Directors should now discuss with their auditors on the audit plan and the timetable and, after having a tentative audit plan, make verbal enquiries with the HKEX on the audit plan and the financial information that can be reported. If a listed company can publish its preliminary results in accordance with the above requirements and/or is just unable to provide breakdown of financial figures normally in notes to its financial statements, the HKEX will not normally suspend trading of the securities of the listed company.

2. Consider if there is inside information that requires disclosure

If the business operations, reporting controls, systems, processes or procedures of the listed company are materially disrupted by the epidemic and/or the related travel restrictions, directors should assess whether any inside information has arisen, and if so make a separate announcement as soon as reasonably practicable, independent of any applicable requirement under the Listing Rules.

- Recommendations: Director should now discuss with the senior management on the possible impact of the epidemic. Any doubt on the definition of inside information or whether certain information constitutes inside information should be directed to Hong Kong lawyers as soon as possible.

3. Application for postponement of publication of annual reports is allowed, but the date of holding of annual general meeting (“AGM”) is still subject to the place of incorporation of the company

If necessary, a listed company can now apply to the HKEX to publish its annual report after 30 April 2020. However, it should be noted that the deadline(s) for holding shareholders’ meeting and laying financial statements for approval at shareholders’ meeting in accordance with the relevant requirements under the laws and regulations of the place of incorporation of the company will not be postponed by virtue of such application to HKEX. For example, the relevant deadline under the Companies Ordinance (Chapter 622 of the Laws of Hong Kong) is six months after the end of a financial year. The HKEX will generally allow listed company to use of technology (e.g. webcast or video conference) to maximise shareholder participation in AGM. However, the company should clearly explain whether shareholders attending the AGM by webcast at a remote site can vote and if so, how.

- Recommendations: Listed companies should consult the legal advisers of its place of incorporation on the relevant laws and regulations on the deadline(s) for holding shareholders’ meeting, sending notice for meeting and the requirement on the format of general meetings. After that, listed companies should discuss with auditors on the suitability of its audit plan and timetable.

4. Extension of the blackout period to the date of the release of the audited financial results

The blackout period will end only when the listed company releases the audited financial results (or an announcement confirming that the released results have now been agreed with auditors).

- Recommendations: If a director has any financial difficulty and has to sell his shares during the blackout period, he should consult a Hong Kong lawyer as soon as possible.

5. Responses to situation where there are material differences between the circumstances and unaudited financial information published, and the reality

If the development of the epidemic renders the information in the announcement published inaccurate or there are material differences between the items in the audited financial results and those in the published unaudited financial results announcement or material information can be supplemented, the listed company should issue a supplemental announcement to explain the difference and the reason behind. Generally speaking, the SFC and the HKEX will not take disciplinary action solely because of material differences in financial information published. Yet the listed company and its directors have the duty to be diligent and reasonable in their treatment of accounts and evaluation of the information available in good faith.

- **Recommendations:** In order to reduce the potential material differences, a listed company, its board of directors and its audit committee should discuss the key audit matters with its auditors timely. To facilitate the preparation of the financial information and the analysis of the financial conditions, one may refer to the e-News published by the Financial Reporting Council (the "FRC") on 6 February 2020 (https://www.frc.org.hk/en-us/enews/202002/enewsletter_202002_en_Final_website.pdf) (Note: see section 6 below for simplified extract of the said publication), and the Hong Kong Institute of Directors' response to the Joint Statement published on 7 February 2020 (https://www.hkiod.com/7Feb2020_final.pdf) (Note: see section 7 below for simplified extract of the said publication).

6. Key advices to directors by the FRC (simplified extract)

FRC focuses its inspection work on areas which are more vulnerable to changes in the economic environment (e.g. management's impairment assessment, revenue recognition and auditors' independence and scepticism), they would like to draw the attention of the board of directors of Hong Kong listed companies and audit committee to the followings:

- ▶ delegation to the audit committee of the oversight of financial reporting and external audit do not absolve the board of its obligations. The board of directors have ultimate responsibility for the integrity and accuracy of financial statements, ensuring that the finance-related function is appropriately resourced and has suitably qualified staff to prepare financial statements that give a true and fair view in accordance with the applicable financial reporting framework. They must also put in place necessary internal control so that the financial statements are free from material misstatement, whether due to fraud or error;
- ▶ directors, have a key responsibility to approve the assumptions adopted by the entity, exercise judgment and make estimations in the key areas, with due care. In the preparation of the financial statements, directors should base on realistic but not overly optimistic assumptions. When assessing the entity's ability to continue as a going concern, directors should take into account all available information about the future (e.g. economic slowdown, epidemic, industry challenges, operating losses, suspension of operations, working capital deficiencies, loan defaults or denial of credit from suppliers) which is at least, twelve months from the end of the reporting period.;
- ▶ audit committee has the duty to supervise the process of financial reporting, focusing on the emerging risks and questioning management's judgements and assumptions (e.g. forecasts and underlying assumptions used in impairment and going concern assessments) which may have significant impact on financial reporting; and significant subsequent events;
- ▶ there is a clear relationship between audit fees and audit quality. After considering the size, complexity, and risk profile of the entity, the audit committee should strike the right balance between the level of audit fees, and the efficiency and effectiveness of the audit process. Audit fees should be realistic so that the auditor is able to undertake a proper and thorough audit in accordance with auditing standards;
- ▶ management, audit committee, and auditors should jointly assess the implication of the epidemic on the year-end audit, such as if it has any significant impact on the entity that requires adjustments and disclosure in the financial statements; whether the auditor has sufficient time and resources to complete the audit by 31 March 2020; and what are the specific and practical impediments that are not capable of resolution and would lead to an expected delay in the completion of the audit; and
- ▶ in case of the abovementioned situations, the FRC urges the audit committee to have an independent discussion with the auditor of the listed company, without the absence of or acting through the management to ensure that the auditor is not under undue pressure from management to complete the audit, ensuring audit that quality would not be compromised.

7. Extract of the advice to the directors by the Hong Kong Institute of Directors

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If the development of the epidemic renders the information in the announcement published inaccurate or there are material differences between the items in the audited financial results and those in the published unaudited financial results announcement or material information can be supplemented, the listed company should issue a supplemental announcement to explain the difference and the reason behind. Generally speaking, the SFC and the HKEX will not take disciplinary action solely because of material differences in financial information published. Yet the listed company and its directors have the duty to be diligent and reasonable in their treatment of accounts and evaluation of the information available in good faith.

All board members:

- ▶ are collectively responsible, whether they are executive or non-executive directors;
- ▶ should pay attention to key issues that would affect the listed company's financial position, such as cash flow conditions and expectations, valuation of assets, recognition of revenue, re-classification of liabilities caused by certain covenants in loan agreements, etc.;
- ▶ should ensure that the audit committee and board deliberations are well recorded in a way that demonstrates they have made the necessary inquiry and met their duty of care (*Note: Any doubt on directors' duties should be directed to Hong Kong lawyers as soon as possible*);
- ▶ should pay attention to the continuous disclosure obligations. Events or occurrences whether due to the coronavirus outbreak (*Note: as well as inside information not exempted from disclosure*) which could have a material impact on share price will need to be disclosed by way of an announcement (*Note: Any doubt on the definition of inside information or whether certain information constitutes inside information should be directed to Hong Kong lawyers as soon as possible*); and
- ▶ that cannot attend in person any committee or board meeting should assess that if they are prevented from obtaining sufficient information to form an opinion. Although committee and board meetings can take place as video conferences, nuances in dialogue and exchanges of views in video conferences may be more difficult to sense than they otherwise could in an in-person meeting. To the extent a director feels this impedes their ability to explain a matter or to make enquires, the director should express his/her worry and not be pressed to go along with the agenda.

Non-executive directors:

- ▶ should have obtained from the appropriate executive members (e.g. CFO, CEO, or other positions of senior management as the case may be) written assurance that there has been no failure in internal control, no material inconsistency or omission between the financial records and reality, no unusual event or occurrence at relevant times that could affect the scope, accuracy and reliability of the financial information. Non-executive directors should also keep close contact with key members of the audit team to get help to identify the key areas (*Note: Executive directors should be aware of the above situation in their daily works. Any doubt on directors' duties should be directed to Hong Kong lawyers as soon as possible*); and
- ▶ should be proactive in audit committee and board meetings to question and verify the information, assumptions and assurances given by management. Non-executive directors who are not audit committee members may consider sitting in audit committee meetings to help their understanding

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