

HKEX News Update: Review of Issuers' 2023 Annual Reports and New Guide on Preparation of Annual Report

(A) Review of Issuers' Annual Reports 2024 (the "Report")

On 10 December 2024, the Stock Exchange published the Report on the findings and recommendations of its annual review of issuers' annual reports for the 2023 financial year end.

The Stock Exchange assessed issuers' compliance with the specific disclosure requirements for annual reports under the Listing Rules and selected several areas, which were declared to be of regulatory interest, for thematic review.

The Report covers the following key findings / recommendations:

(a) Review of compliance with specific disclosure requirements

Share schemes

- Some issuers only disclosed shares issuable under the options available for grant under the remaining scheme limit but failed to disclose shares issuable under the options already granted under the scheme but not yet exercised.

Significant investments

- "Significant investments" are not confined to securities in companies. Funds or wealth management products also fall under the ambit of the relevant rules and must be disclosed if the materially threshold is exceeded.

Performance guarantees and use of proceeds from fundraisings

- Some issuers omitted to disclose expected timeline for applying unutilized proceeds from fundraisings. In the absence of a definitive timetable for fund deployment, issuers should indicate an approximate timing for fund usage and update investors through announcements and/or in subsequent financial reports when there is better clarity on the timeline.

(b) Thematic review

Financial statements with auditors' modified opinions

- Most common audit modification was attributable to going concern uncertainty, which typically due to deterioration in economic condition and/or business, and/or difficulties in obtaining financing. Issuers should make their best endeavour to resolve the issue as soon as practicable;
- Another common audit modifications were valuation of assets and limited access to accounting records, which often due to lack of adequate risk identification policies and mitigating measures, resulting in the issuers' failure to supply satisfactory evidence to auditors to substantiate the fairness of the reported balances and in extreme cases, genuineness of the transactions. Issuers should put in place adequate risk management and internal control systems to avoid such deficiencies; and
- Issuers should discuss with the auditors on their remedial plans, closely monitor the execution and make adjustment to expedite issue resolution.

Material lending transactions

- Room for improvement in disclosure of material lending transactions was identified as below:
 - For money lenders: disclosure of customer profile, concentration risks and major loan terms; and
 - For non-money lenders: disclosure of rationale for lending;
- There were several cases involving director misconduct and/or internal control breakdown (e.g. material loan impairment, repeated rollovers without apparent commercial rationale and/or failure to safeguard loan rights);
- The Exchange takes director misconduct and material internal control deficiencies seriously and will not hesitate to take disciplinary actions where circumstances necessitate; and
- Issuers should ensure their controls over material lending transactions are adequate to safeguard shareholders' funds.

Management discussion and analysis (MD&A)

- Room for improvement in quality of disclosure, particularly in discussion of year-on-year performance variances; and significant events and risks, their impacts and issuers' counter measures, was identified. Examples include:
 - Failure to identify and discuss specific underlying causes or business factors that drove the results; and
 - Highlighting business plans (which would demand significant investment) but failure to discuss the estimated capital expenditure requirement and how the issuer intended to meet such requirement; and
- Newly listed issuers should strive for their MD&A disclosure on par with the disclosure standard of a listing document. They should provide update on significant matters highlighted in the prospectus to enable investors to evaluate whether the post-listing developments are in line with the track record, business plan and prospects outlined in the prospectus.

Review of financial disclosure under prevailing requirements (including accounting standards)

- Room for improvement in the qualitative disclosure, e.g. material accounting policy information, key judgements and estimates, was identified; and
- Issues relating to presentation of non-GAAP measures, including improper labelling, omission of reconciliation and unclear explanation of adjusting items, were also highlighted.

(B) New Guide on Preparation of Annual Report (the "Guide")

The Stock Exchange also published the Guide which will be updated as and when necessary.

The Guide covers the following areas:

(a) Section 1 - Mandatory disclosure requirements under the Listing Rules

It provides all the disclosure requirements for annual reports under the Listing Rules and related guidance materials published by the Stock Exchange in respect of the following (where applicable):

- Directors, senior management and shareholders;
- Financial reporting, accounting and auditing matters;
- Issue of securities or resale of treasury shares and related matters;

- Public float;
- Repurchase of securities and treasury shares;
- Notifiable transactions;
- Connected transactions;
- Share schemes;
- Newly listed issuers;
- Issuers listed under special listing regimes or other listing structures;
- Corporate governance / environmental, social and governance; and
- Others.

(b) Section 2 - Recommended disclosure in specific areas from thematic review

It contains prevailing recommended disclosure and provides source of other reference materials for the following specific areas:

- Financial statements with auditors' modified opinions – provides minimum disclosure in annual report in case an issuer receives a modified audit opinion;
- MD&A section – provides general guidance on areas to be considered (including business review, principal risks and uncertainties, and liquidity and financial resources) and recommended presentation;
- Material asset impairments – highlights that a discussion in respect of the circumstances that led to the impairment shall be made as part of discussion on significant events or transactions during the financial year;
- Material lending transactions – provides disclosure requirements for both money lenders and non-money lenders;
- Performance guarantees – provides disclosure requirements where performance guarantee of the acquired business is not met;
- Newly listed issuers – provides disclosure requirements in respect of update on the developments of major matters highlighted in the prospectus in MD&A section, and requirement to consult compliance advisers; and
- Biotech companies – sets out disclosure requirements in respect of research and developments status of core products and non-core products at the time of IPO and newly in-licensed or self-developed products after listing.

(c) Section 3 - Financial disclosure under prevailing requirements

It highlights the following common areas requiring particular attention when preparing financial information in annual reports and provides relevant guidance for disclosure:

- Accounting policy information, judgements and estimates;
- Revenue;
- Business combinations;
- Material intangible assets – impairment testing;
- Valuation of Level 3 financial assets;
- Credit risk disclosure on trade receivables;
- Presentation of non-GAAP measures; and
- Disclosure of possible impact of applying a new or amended standard in issue but not yet effective.

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