

MEMBERS' HANDBOOK

Update No. 125

(Issued 28 February 2013)

Document Reference and Title	Instructions	Explanations
<u>VOLUME III</u>		
Contents of Volume III	Discard the existing pages i, iii and iv and replace with the new pages i, iii and iv.	Revised contents pages
PRACTICE NOTES		
PN 620.2 <u>Communication between the Auditor and the Insurance Authority</u>	Discard PN 620.2 issued in May 1998 and replace with revised PN 620.2.	Note 1
PN 750 <u>Review of Financial Information under the Hong Kong Listing Rules for a Very Substantial Disposal</u>	Insert PN 750 after PN 740.	New Practice Note - Note 2

Notes:

1. The key revisions to PN 620.2 are mainly changes to align with the clarified HKSAs and current drafting conventions for PNs.
2. The purpose of PN 750 is to provide guidance to practitioners as to their responsibilities when they are engaged to review the financial information included in a circular issued in relation to a very substantial disposal (VSD) under the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited Rule 14.68(2)(a)(i) or the Rules Governing the Listing of Securities on the Growth Enterprise Market of The Stock Exchange of Hong Kong Limited Rule 19.68(2)(a)(i) issued by The Stock Exchange of Hong Kong Limited and on the form and content of their reports. This PN is effective for reviews of financial information included in a VSD circular dated on or after 1 June 2013. Earlier adoption of the PN is permissible.



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Practice Note 620.2

Communication between the Auditor and the Insurance Authority



Hong Kong Institute of
Certified Public Accountants
香港會計師公會

PRACTICE NOTE

620.2

**COMMUNICATION BETWEEN THE AUDITOR AND
THE INSURANCE AUTHORITY**

(Issued May 1998; revised September 2004 (name change); revised February 2013)

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Practice Note (PN) 620.2 “Communication between the Auditor and the Insurance Authority” should be read in the context of the “Amended Preface to the Hong Kong Quality Control, Auditing, Review, Other Assurance, and Related Services Pronouncements” which sets out the application and authority of PNs.

PRACTICE NOTE

620.2

COMMUNICATION BETWEEN THE AUDITOR AND THE INSURANCE AUTHORITY

The purpose of Practice Notes issued by the Hong Kong Institute of Certified Public Accountants (HKICPA) is to assist the auditor in applying Hong Kong Engagement Standards of general application to particular circumstances and industries.

Practice Notes are persuasive rather than prescriptive. However they are indicative of good practice and have similar status to the explanatory material in Hong Kong Engagement Standards. This Practice Note provides guidance to assist the auditor to fulfill the objectives of the engagement. The auditor should be prepared to explain departures when called upon to do so.

Introduction

1. In this Practice Note all the sections mentioned below are in respect of the Hong Kong Insurance Companies Ordinance ("the Ordinance") unless otherwise stated.
2. Section 53D of the Ordinance provides statutory protection for the auditor from liability to the client for breach of confidentiality when the auditor communicates directly with the Insurance Authority. Sections 15A and 53E impose a statutory obligation on the auditor to report certain matters directly to the Insurance Authority.
3. This Practice Note refers to the auditor, audits, reports on the annual financial statements and reports on the accounts and statements ("financial information") an insurer is required to submit to the Insurance Authority.
4. This Practice Note is applicable to:
 - a. an auditor or former auditor of an insurer or a former insurer appointed under section 15 or section 4(1A) of Part 1 of the Third Schedule to the Ordinance ("the Third Schedule");
 - b. an accountant or former accountant of an insurer or a former insurer appointed in compliance with a requirement under section 35(1); and
 - c. an auditor or former auditor of an insurance broker or a former insurance broker appointed under section 72.

Scope of the Ordinance

5. The Ordinance regulates the carrying on of insurance business in Hong Kong. One of the primary purposes of the Ordinance is the protection of policy holders and potential policy holders. The Insurance Authority is charged under section 4A with the functions set out below.
 - a. The principal function of the Insurance Authority shall be to regulate and supervise the insurance industry for the promotion of the general stability of the insurance industry and for the protection of existing and potential policy holders (section 4A(1)).
 - b. Without limiting the generality of section 4A(1), the Insurance Authority shall:
 - i. be responsible for supervising an insurer's and an insurance intermediary's compliance with the provisions of the Ordinance;
 - ii. consider and propose reforms of the law relating to insurance business;

- iii. promote and encourage proper standards of conduct and sound and prudent business practices amongst insurers;
 - iv. promote and encourage proper standards of conduct of insurance intermediaries and, where necessary, review and revise the regulatory system for the same;
 - v. promote and develop self-regulation by market and professional bodies of the insurance industry; and
 - vi. co-operate with and assist financial services supervisory authorities of Hong Kong or of any place outside Hong Kong, whenever appropriate, to the extent permitted by the Ordinance (section 4A(2)).
- c. The Insurance Authority may from time to time cause to be prepared and published by notice in the Gazette, for the guidance of authorized insurers, insurance intermediaries, and the auditors and actuaries of such insurers and intermediaries, guidelines not inconsistent with the Ordinance, indicating the manner in which the Insurance Authority proposes to exercise functions imposed or conferred upon by the Ordinance (section 4A(3)).
6. The Third Schedule specifies the form and content of the financial information which an insurer is required to submit annually to the Insurance Authority. The auditor is required to report on the financial information and the report will in general terms cover such matters as:
- a. the maintenance of proper books and records by the insurer;
 - b. the proper preparation of the financial information;
 - c. the fairness of presentation of the financial information;
 - d. the valuation of assets and liabilities in accordance with applicable valuation regulations; and
 - e. the maintenance of assets in accordance with the Ordinance.

Detailed guidance is set out in PN 810.2 "The Duties of Auditors under the Insurance Companies Ordinance".

7. Section 73(1) specifies the form of financial statements which an authorized insurance broker, authorized by the Insurance Authority under section 69(2), is required to submit annually to the Insurance Authority. The auditor is required to report on the authorized insurance broker's financial statements and compliance with the minimum requirements regarding
- a. capital and net assets;
 - b. professional indemnity insurance;
 - c. keeping of separate client accounts; and
 - d. keeping proper books and accounts.

Under section 73(2) the auditor of an approved body of insurance brokers, approved by the Insurance Authority under section 70(2), is required to report:

- a. whether the body of insurance brokers has received from each of its members the audited financial statements and report by the auditor on the compliance with the minimum requirements specified by the Insurance Authority in accordance with its membership rules and regulations; and

- b. that the auditor has reviewed all reports by auditors of members in respect of the financial statements and the minimum requirements and none contained any adverse statement or qualification except those listed by the auditor in the auditor's report.

Detailed guidance is set out in PN 810.1 "Insurance Brokers – Compliance with the Minimum Requirements Specified by the Insurance Authority Under Sections 69(2) and 70(2) of the Insurance Companies Ordinance".

8. In addition, insurers, authorized insurance brokers and approved bodies of insurance brokers who are incorporated in Hong Kong are required to prepare financial statements and to have them audited under the provisions of the Hong Kong Companies Ordinance.
9. In the course of performing the work necessary to discharge these routine audit reporting responsibilities, the auditor may become aware of matters which the auditor considers need to be brought to the Insurance Authority's attention through an "ad hoc report", other than through the medium of the routine formal audit report.
10. This Practice Note is concerned only with ad hoc communications between the auditor and the Insurance Authority:
 - a. by the auditor to the Insurance Authority under the obligations established in sections 15A(2) and 53E;
 - b. by the auditor to the Insurance Authority under the protection of section 53D; and
 - c. by the Insurance Authority to the auditor under section 53A(3)(da) and (3)(f).

It does not cover the auditor's approach to the audit of an insurer, an authorized insurance broker or an approved body of insurance brokers or the routine audit reporting responsibilities.

11. Certain expressions used in the Ordinance may be matters for legal interpretation. There may, therefore, be circumstances in which, notwithstanding the guidance in this Practice Note, the auditor will wish to take legal advice.

Reporting under the Ordinance

12. The Insurance Authority expects that the management of an insurer or an insurance broker will continue to be its primary source of information and that the normal authorized reporting procedures, including returns, discussions, examinations and any tripartite meetings will normally provide the Insurance Authority with most of the information it needs to carry out its responsibilities under the Ordinance.
13. Nevertheless under the Ordinance the auditor has various statutory responsibilities to report to the Insurance Authority. The auditor is automatically protected in making a report in discharge of such a statutory responsibility. Certain provisions also provide the auditor with immunity from any liability the auditor might otherwise incur by reason of the auditor's making other reports to the Insurance Authority which the auditor may consider to be relevant to the functions of the Insurance Authority. These responsibilities and avenues available for reporting do not require the auditor to change the scope of the audit work, nor the frequency or timing of the visits.

14. When the circumstances where reporting may be appropriate are being considered, it should be noted that obtaining insurance services or products carries inherent risks. It is not the purpose of the Ordinance, nor the duty of the auditor, to protect the policy holder from the normal risks relating to such activities.
15. The auditor is advised to bear in mind that the auditor's decision may have to stand up to examination at a future date on the basis of the following considerations:
 - a. what the auditor knew at the time;
 - b. what the auditor should have known in the course of the audit;
 - c. what the auditor should have concluded; and
 - d. what the auditor should have done.

The auditor's notices to the Insurance Authority under section 15A(2)

16. The auditor has a statutory duty to give immediate written notice to the Insurance Authority in the circumstances set out below.
 - a. If the auditor resigns (section 15A(2)(a)).
 - b. If the auditor decides not to seek reappointment (section 15A(2)(b)).
 - c. If the auditor decides to add a qualification or adverse statement to the auditor's report annexed to the financial information of the insurer required to be submitted under the Third Schedule (section 15A(2)(c)).

The decision to give written notice would normally only be taken after extensive discussions with management and when a problem is either irremediable or when the circumstances indicate that the auditor intends to qualify.

Section 15A(2) applies to the auditor of an insurer appointed under section 15 or section 4(1A) of Part 1 of the Third Schedule.

Ad hoc reports under section 53E

17. Section 53E provides that where an auditor, during the performance of the duties in that capacity:
 - a. becomes aware of any matter... which in the auditor's opinion adversely affects the financial condition of the insurer to a material extent, the auditor shall, as soon as practicable thereafter, send to the Insurance Authority a report in writing of the matter (section 53E(1)); and
 - b. becomes aware of evidence...
 - i. of a failure by the insurer to comply with any conditions imposed under section 8(1)(a);
 - ii. that there exists a ground on which the Insurance Authority would be prohibited by section 8(3)(a), (b), (d) or (f) from authorizing the insurer if the insurer were to make application in that behalf;
 - iii. of a failure by the insurer to comply with any of the provisions of section 22, 22A or 23; or

- iv. of any default of the insurer in complying with any requirement under section 27, 28, 29, 30, 31, 32, 33, 34 or 35(1),

the auditor shall, as soon as practicable thereafter, send to the Insurance Authority a report in writing of the failure, ground or default (section 53E(3)).

Section 53E applies to:

- a. an auditor or former auditor of an insurer or a former insurer appointed under section 15 or section 4(1A) of Part 1 of the Third Schedule; and
- b. an accountant or former accountant of an insurer or a former insurer appointed in compliance with a requirement under section 35(1).

These are statutory obligations and the following paragraphs of the Practice Note provide the auditor with procedures to follow when such circumstances arise.

Reporting criterion under section 53E

- 18. The auditor would take the initiative and ensure that an ad hoc report under section 53E is made to the Insurance Authority if the conditions specified in paragraph 17 exist. A distinction must be drawn here between an auditor's duty as stated in paragraph 17(a) and that stated in paragraph 17(b). The duty under paragraph 17(b) is clear and unequivocal; if the auditor becomes aware of a contravention of the provisions in the Ordinance which are specified, the auditor is not given any latitude for exercising judgement. The auditor is obliged to make a report. The duty under paragraph 17(a) is different. The auditor is given the right to form an opinion based on applying criteria as to the materiality of an adverse effect on the insurer's financial position in deciding whether reporting would be appropriate.

The HKICPA has developed a criterion for use by the auditor in deciding to take the initiative in making an ad hoc report under section 53E in addition to the regular audit reporting responsibilities. The criterion is that the auditor would make the report when the auditor considers it expedient to do so in order for the Insurance Authority to protect the interests of policy holders because there has been a material loss or there exists a significant risk of material loss.

- 19. This criterion can be more fully explained as follows:
 - a. there must be a significant adverse occurrence or a change in the auditor's perception of an existing situation, that may include an adverse change in the circumstances of the business; and
 - b. the situation described in a. above has given rise to or has indicated that a reasonable probability exists that it may give rise to:
 - i. a material financial loss to the business, or
 - ii. loss of control over the assets or records.
- 20. Examples of the circumstances in which the situation set out in paragraphs 18 and 19 may be met include:
 - a. the auditor discovers a failure by the insurer to comply with the relevant provisions of the Ordinance which may have material consequences; or
 - b. there is evidence of imminent financial loss of serious proportions which might cast doubt on the continuing viability of the insurer.

Reporting procedures under section 53E

21. In circumstances where the auditor concludes that an ad hoc report under section 53E to the Insurance Authority is necessary, the auditor would normally adopt the procedures set out below, bearing in mind that speed may be of the essence and that the statutory obligation to report under section 15A or 53E remains subject to the criterion discussed in paragraphs 18 - 20.
- a. The auditor would normally discuss the matter with the insurer and explain the statutory duty to make a report to the Insurance Authority under section 53E. In addition, the insurer may be advised to make its own report to the Insurance Authority immediately.
 - b. The auditor would normally then immediately inform the Insurance Authority of the circumstances in writing. It is suggested that a copy of both the written notification and the ad hoc report be made to the directors or management of the insurer.
22. The auditor is reminded that making an ad hoc report alone may not discharge all the responsibilities. For example, the auditor would consider the implications of the matter giving rise to the ad hoc report for the auditor's opinion on the financial statements.

Other ad hoc communications by the auditor

Statutory protection under section 53D

23. Section 53D provides that:
- "(1) No duty which a prescribed person may be subject to shall be regarded as contravened by reason of his communicating in good faith to the Insurance Authority, whether or not in response to a request made by the Insurance Authority, any information or opinion on a matter:
- a. of which he becomes aware in his capacity as a prescribed person...; and
 - b. which is relevant to any function of the Insurance Authority under this Ordinance.
- (2) For the avoidance of doubt, it is hereby declared that a matter referred to in subsection (1) may be a matter which relates to a person other than an insurer or former insurer."
24. For the purposes of section 53D, "prescribed person" in this context refers to:
- a. an auditor or former auditor of an insurer or a former insurer appointed under section 15 or section 4(1A) of Part 1 of the Third Schedule;
 - b. an accountant or former accountant of an insurer or a former insurer appointed in compliance with a requirement under section 35(1); and
 - c. an auditor or former auditor of an insurance broker or a former insurance broker appointed under section 72.
25. Section 53D does not lay down any rules nor specify the circumstances in which the auditor is to communicate any matter to the Insurance Authority. It provides a statutory mechanism whereby the auditor may make matters known to the Insurance Authority without breaching the auditor's duty of confidentiality.

26. This section of the Practice Note contains guidance on the circumstances in which matters (which fall outside those which the auditor is obliged to report (see paragraphs 16 to 22 above)) may be brought to the attention of the Insurance Authority by way of a report with statutory protection. In interpreting this guidance, the auditor is advised to bear in mind the fundamental objectives of the legislation, which are to ensure that the Insurance Authority is able to fulfil its functions summarised in paragraph 5.
27. Confidentiality is an implied term of an auditor's contract with the client, but in certain circumstances and under conditions specified in section 53D it does not prevail, since the auditor is entitled to communicate information or opinions on a matter relating to the business or affairs of the client relevant to the Insurance Authority's functions without the duty of confidentiality owed to the client being regarded as having been contravened.
28. The matters which may be communicated under section 53D are any of those relevant to the Insurance Authority's functions under the Ordinance.
29. Matters which may be reported under the protection of section 53D will only arise in circumstances where the auditor is under no duty to report under section 15A or 53E. Considerable care needs to be taken in disclosing matters arising during any tripartite meeting with the Insurance Authority as the auditor's knowledge of these matters may have been obtained while assisting the Insurance Authority other than in the capacity as the auditor (see paragraph 32).

Examples of circumstances in which the auditor may communicate a matter to the Insurance Authority under section 53D include:

- a. the auditor considers policy holders have incurred, or are at significant risk of incurring, a material loss as a result of insurers or authorized insurance brokers carrying on business in a manner that is not fit and proper or that is in breach of the Ordinance;
 - b. there is evidence of
 - i. fraud, dishonesty or serious incompetence; or
 - ii. serious failure to observe requirements of the Ordinance or conditions imposed on the insurer or authorized insurance broker by the Insurance Authority;
 - c. it has come to the attention of the auditor that the procedures, records or systems fail significantly to comply with, or to demonstrate compliance with, requirements set by the Insurance Authority to which the insurer or authorized insurance broker is subject; and
 - d. the position is such that because of a significant risk which is material to the collective interests of policy holders, the policy holders' interests would be better safeguarded if the Insurance Authority were aware of the position, even if only to organise protective action.
30. Clearly the potential nature of matters which may be reported is very wide, but as explained in paragraph 33 this does not, of itself, require the auditor to extend the scope of the work in order to discover matters and it will only be in exceptional circumstances such as those described in paragraph 48 that the auditor may choose to seek statutory protection.

31. Any protected communication can be made either on the auditor's initiative or in response to a request from the Insurance Authority for information. The auditor would normally cooperate with the Insurance Authority and respond to any requests from the Insurance Authority for information, provided the auditor has no reason to doubt that the request is relevant to the Insurance Authority's functions. The auditor may communicate a matter to the Insurance Authority with the protection of section 53D regardless of the source of that information, provided the auditor became aware of the matter in the capacity as the auditor of the client and the auditor does so in good faith.
32. Matters of which the auditor becomes aware "in the capacity as the auditor" may not be restricted to those matters identified by the auditor during the course of the audit work. The auditor may become aware of a matter which is relevant to the functions of the Insurance Authority during the course of the work for the insurer or authorized insurance broker other than audit work or through private discussions on social or other occasions, in which case the information will be known to the auditor as individual. In circumstances which suggest that a matter would be reported to the Insurance Authority if knowledge of it had been obtained in the capacity as the auditor, it would be prudent to make enquiries in the course of the audit work in order to establish whether this is the case from information obtained in this capacity. In addition, a matter which is relevant to the functions of the Insurance Authority and which is identified during the course of work for the client by another partner (or member of staff) such as a management consultant or tax partner may be deemed to be known to the auditor (see also paragraph 34). The auditor may follow the guidance set out in HKSA 250 "Consideration of Laws and Regulations in an Audit of Financial Statements"
33. The auditor cannot be expected to be aware of all circumstances which, had the auditor known of them, would have led the auditor to exercise the right to communicate under section 53D. This section does not require the auditor to change the scope of the audit or other work for the client, nor the frequency or timing of the visits. The auditor has no obligation to seek out grounds for making a report under section 53D. The section does not place an obligation on the auditor to conduct the work in such a way that there is reasonable certainty that the auditor will discover a matter upon which the Insurance Authority may need to act. It is only when the auditor does become aware in the ordinary course of the work of such a matter, or of circumstances which suggest the existence of such a matter, that the auditor would consider using the protection of section 53D.
34. The auditor would, however, ensure that the auditor is made aware of any other relationships which may exist between any department of the firm and the client which could affect the work as the auditor. The Insurance Authority expects that the auditor will ensure that the auditor is informed of all potentially exceptional circumstances (paragraphs 48 and 49) by all other departments within the firm which have a relationship with the insurer or authorized insurance broker. It would, therefore, be prudent for the audit firm to ensure any exceptional circumstances which may give rise to reports under section 53D are brought to the attention of the auditor of the client in order that the auditor can, if appropriate, make enquiries in the capacity as the auditor to ascertain whether such matters should be reported to the Insurance Authority.
35. The Insurance Authority recognises that it would not be appropriate for the auditor to report information which the auditor has obtained or matters which the auditor has identified through the professional relationship with another client, even though the information obtained or the matters identified may relate to an insurer or an authorized insurance broker. However, the Insurance Authority expects an insurer or authorized insurance broker to advise its auditor when it appoints a third party (including another department of the same firm) to review, investigate or report on any aspects of its records and systems and to provide the auditor with copies of reports by such a third party promptly after their receipt. The auditor can, if appropriate, make enquiries in the capacity as the auditor to ascertain whether any findings of the reports should be reported to the Insurance Authority.

36. It should be noted that section 53D will not provide protection to the auditor where the auditor could be held to have acted maliciously or in bad faith or if the information reported is outside the scope of that section. The Ordinance does not, therefore, provide complete immunity from all types of legal action by all parties affected, or subsequently affected, by the auditor's action in reporting to the Insurance Authority. The auditor would consider taking legal or other professional advice before making the decision about whether, or in what manner, to report and in order, for example, to ensure that the form and content of the report are such as to secure the protection of section 53D and that it only includes relevant material.
37. The auditor is protected, however, even if the information which the auditor communicates falls short of proof, or the opinion which the auditor communicates cannot be verified. The auditor who can demonstrate that the auditor has acted reasonably and in good faith in informing the Insurance Authority of a reportable matter would not be held in breach of duty to the client even if, after an investigation, it were found there was not a matter which needed to be reported. These are areas where the auditor may wish to consider taking legal advice before making a report.
38. Whilst no breach of statutory duty might arise, it should be appreciated that there is no protection given by the Ordinance if the auditor, after becoming aware of an occurrence, fail to report, promptly, or at all, to the Insurance Authority. Furthermore, it should be recognised that speed of reporting is likely to be important in order to enable the Insurance Authority to protect the interests of policy holders.

Meetings with the Insurance Authority

39. As part of the Insurance Authority's system of supervision of insurers or authorized insurance brokers, meetings involving the Insurance Authority, the insurer or authorized insurance broker and its auditor may be called. These meetings may be categorised as "routine meetings" called by the Insurance Authority or "special meetings" which may be called by either the Insurance Authority, or the insurer or authorized insurance broker possibly at the auditor's suggestion.
40. The agenda for a tripartite meeting between the Insurance Authority, the insurer or authorized insurance broker and the auditor will be prepared by the Insurance Authority and will include items requested by the insurer or authorized insurance broker and auditor and be circulated in advance. The auditor is expected to participate fully in tripartite meetings and to have regard to the breadth of the Insurance Authority's functions. Normally, however, it is expected that the auditor will discuss with the client any matter which is to be raised at a meeting with the Insurance Authority, before the meeting is held.
41. The auditor would be expected to discuss with the Insurance Authority the affairs of the insurer or authorized insurance broker including, if necessary, information about its policy holders or other companies within the group obtained in the course of that work. However, the Insurance Authority recognises that it would not be appropriate for the auditor to report to the Insurance Authority information about the insurer or authorized insurance broker which the auditor has obtained through the professional relationship with another client.
42. Meetings may be called by the Insurance Authority to assist in its forming a judgement on an insurer or authorized insurance broker. In particular discussions may cover:
 - a. the presentation and content of the annual financial statements;
 - b. the scope, conduct and outcome of the annual audit;
 - c. the scope and outcome of any report made under section 53E;
 - d. explanations for, the reasons for and the nature of a qualified report or of a change in a previously reported intention to qualify a report;

- e. any step or course of action which may be necessary in the light of the reports, for example, the commissioning of a more detailed report in a particular area; and
 - f. matters raised by the Insurance Authority or those which the insurer or authorized insurance broker or auditor have drawn to its attention since any previous meeting, including how such matters have been resolved to the satisfaction of the auditor or have been reflected or treated in the financial statements.
43. Any party may seek to call a tripartite meeting at any other time if important matters affecting the insurer or authorized insurance broker come to their attention as further discussed in paragraph 45. Normally, the auditor would raise the concerns with the insurer or authorized insurance broker first and if the problem cannot be resolved to the auditor's satisfaction, suggest that the insurer or authorized insurance broker asks the Insurance Authority to convene a meeting.
44. In exceptional circumstances, for example, those outlined in paragraphs 48 and 49, the auditor may consider it necessary to have a bipartite meeting with the Insurance Authority to discuss the affairs of the insurer or authorized insurance broker or to draw the attention of the Insurance Authority to information about the insurer or authorized insurance broker without its knowledge. Before doing so, however, the auditor would consider taking timely legal advice and whether a representative of the insurer or authorized insurance broker at an appropriately senior level would be informed and invited to attend the meeting.

Reporting via the insurer or authorized insurance broker

45. Where the auditor becomes aware of a matter which, in the auditor's professional judgement, the auditor considers is not required to be reported under section 15A or 53E but ought to be reported to the Insurance Authority, the auditor would consider the facts and, unless inappropriate in the circumstances (described in paragraph 48), discuss the matter with the management.
46. It is important for the auditor to act in a manner that will maintain the professional relationship with the client. Normally, therefore, the auditor would ask the insurer or authorized insurance broker to draw matters about which the auditor is concerned to the attention of the Insurance Authority. An example of the circumstances under which the auditor is not required to report but about which the auditor might wish to persuade the client to inform the Insurance Authority are where the auditor forms the opinion that management has reported materially misleading financial information to the Insurance Authority or becomes aware that management has failed, or does not intend, to report something and the failure to report is, or would be, materially misleading.
47. Where the insurer or authorized insurance broker will not himself inform the Insurance Authority of a matter, having been advised to do so by the auditor, or where it has not been done within the period of time specified, or where there is not adequate evidence that the client has properly reported the matter in question, the auditor would make such a report direct to the Insurance Authority.

Reporting direct to the Insurance Authority

48. In exceptional circumstances, where the auditor doubts whether management are fit and proper persons to carry on the business of insurance and it would be in the interest of protecting policy holders that the management of the insurer or authorized insurance broker should not be informed in advance, the auditor would report directly to the Insurance Authority after first considering the appropriateness of taking independent legal advice. Examples of such circumstances include:
- a. where there has been an occurrence which causes the auditor no longer to have confidence in the integrity of the directors or senior management, e.g. where the auditor believes that a fraud or other irregularity has been committed by the directors or senior management of the insurer or authorized insurance broker, or the auditor

has evidence of the intention of directors or senior management to commit such a fraud or other irregularity; or

- b. where there has been an occurrence which causes the auditor no longer to have confidence that the directors or senior management will conduct the business of the insurer or authorized insurance broker in a prudent manner so as to protect the interests of policy holders, e.g. where the auditor has discovered that the directors or senior management are acting in an irresponsible or reckless manner with respect to the affairs of the business or its policy holders, or the auditor has evidence of the inclination so to act.
49. The auditor would also report directly to the Insurance Authority when speed is of the essence. For example, when the auditor becomes aware that the insurer or authorized insurance broker may be about to cease being authorized, the auditor would consider the need to disclose to the Insurance Authority any information in the auditor's possession relevant to its functions without delay. The fact of such impending cessation of authorization may bring forward the desirability of disclosing matters to the Insurance Authority, as it is easier for the Insurance Authority to take appropriate action while the insurer or authorized insurance broker is still authorized, particularly where such matters have a bearing on the security of third party interests.

Communications by the Insurance Authority to the auditor under section 53A(3)(da) and (3)(f)

50. The Ordinance also deals with communications by the Insurance Authority to the auditor of an insurer, an authorized insurance broker or an approved body of insurance brokers.
- a. Section 53A(3)(da) permits the communication of restricted information to the auditor of an insurer or authorized insurance broker for the purpose of enabling or assisting the Insurance Authority to discharge its functions under the Ordinance without the consent of the person from whom it is received or to whom it relates.
 - b. Section 53A(3)(f) permits the communication by the Insurance Authority to the auditor if, in the opinion of the Insurance Authority, such information is necessary for the auditor to perform the duties under the Ordinance.
51. It should be noted that disclosure by the Insurance Authority of confidential information to the auditor is to the auditor only; the auditor is not free to pass that information to others, such as the client insurer or authorized insurance broker without the consent of the Insurance Authority under section 53A(3D) of the Ordinance.
52. The Insurance Authority has indicated that it will take the initiative in reporting any matter to the auditor of an insurer or authorized insurance broker under the provisions of section 53A(3)(da) and (3)(f), where it believes that it is of such importance that the auditor's knowledge of it could significantly affect the form of the audit report or the way in which the auditor carries out the reporting responsibilities. The Insurance Authority has also indicated that it will inform the auditor whether the management of the insurer or authorized insurance broker has been informed of the matter and, if so, who has been advised.
53. In the absence of any notification, the auditor is entitled to assume that the Insurance Authority has considered the need to take such an initiative and has concluded that it has no matters to report to the auditor of an insurer or authorized insurance broker. Accordingly there is no need for the auditor to request the Insurance Authority to confirm this.

Practice Note 750

Review of Financial Information under the Hong Kong Listing Rules for a Very Substantial Disposal



Hong Kong Institute of
Certified Public Accountants
香港會計師公會

PRACTICE NOTE 750

**REVIEW OF FINANCIAL INFORMATION UNDER THE HONG
KONG LISTING RULES FOR A VERY SUBSTANTIAL DISPOSAL**

(Issued February 2013)

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PRACTICE NOTE 750

REVIEW OF FINANCIAL INFORMATION UNDER THE HONG KONG LISTING RULES FOR A VERY SUBSTANTIAL DISPOSAL

The purpose of Practice Notes issued by the Hong Kong Institute of Certified Public Accountants (HKICPA) is to assist the practitioner in applying Hong Kong Engagement Standards of general application to particular circumstances and industries.

Practice Notes are persuasive rather than prescriptive. However they are indicative of good practice and have similar status to the explanatory material in Hong Kong Engagement Standards. This Practice Note provides guidance to assist the practitioner to fulfill the objectives of the engagement. The practitioner should be prepared to explain departures when called upon to do so.

Introduction

1. The purpose of this Practice Note (PN) is to provide guidance to practitioners as to their responsibilities when they are engaged to review the financial information included in a circular issued in relation to a very substantial disposal (VSD) under the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited (Main Board Listing Rules) Rule 14.68(2)(a)(i) or the Rules Governing the Listing of Securities on the Growth Enterprise Market of The Stock Exchange of Hong Kong Limited (GEM Listing Rules) Rule 19.68(2)(a)(i) (collectively referred to as the "Listing Rules on a VSD") issued by The Stock Exchange of Hong Kong Limited (the "Stock Exchange") and on the form and content of their reports.
2. This PN is directed towards the review of financial information, and is to be read in conjunction with the "Amended Preface to the Hong Kong Quality Control, Auditing, Review, Other Assurance, and Related Services Pronouncements". Guidance in other PNs and in Hong Kong Standards on Review Engagements (HKSREs) may be useful to the practitioner in applying this PN. This PN may also be applied to engagements conducted in accordance with International Standards on Review Engagements.
3. Main Board Listing Rule 14.68(2)(a)(i) / GEM Listing Rule 19.68(2)(a)(i) requires that the financial information contained in a VSD circular must be prepared by the directors of the listed issuer using accounting policies of the listed issuer. The financial information must contain at least the income statement, balance sheet, cash flow statement¹ and statement of changes in equity. In addition, the financial information must be reviewed by the listed issuer's auditor or reporting accountant. The circular must contain a statement that the financial information has been reviewed by the issuer's auditor or reporting accountant and details of any qualifications or modifications in the review report.
4. The term "practitioner" is used throughout this PN as a matter of convenience and to cover both situations i.e. where the practitioner is the auditor of the listed issuer and where the practitioner is not the auditor, but the reporting accountant, of the listed issuer. The use of the term "practitioner" should not be construed as meaning the engagements which are covered by this PN are in the nature of an audit. Where the term "auditor" or the term "reporting accountant" is used in this PN it is a specific reference to a practitioner who is the auditor of the listed issuer or to a practitioner who is not the auditor, but the reporting accountant, of the listed issuer respectively.
5. This PN has been prepared in consultation with the Stock Exchange and with staff of the Securities and Futures Commission and is based on the 'Main Board Listing Rules and GEM Listing Rules as at 31 December 2012. A summary of the relevant Listing Rules is set out in Appendix 3 to this PN.

¹ Different terms such as statement of comprehensive income, statement of financial position and statement of cash flows may be used.

6. The Main Board Listing Rule 14.68 / GEM Listing Rule 19.68 (see Appendix 3 of this PN) allows a number of ways of presenting financial information in a VSD circular in relation to the disposal of a company or business:

- (a) financial information of either:
 - (i) the business or companies being disposed of (14.68 / 19.68 (2)(a)(i)(A)); or
 - (ii) the listed issuer's group with the business or companies being disposed of shown separately as (a) disposal group(s) or (a) discontinuing operation(s) (14.68 / 19.68 (2)(a)(i)(B)).
- (b) an accountants' report prepared in accordance with Chapter 4 of Main Board Listing Rules/ Chapter 7 of GEM Listing Rules.

The relevant guidance for a practitioner engaged to prepare the accountants' report and examine financial information of this nature is contained in Auditing Guideline (AG) 3.340, "Prospectuses and The Reporting Accountant" and practitioners should refer to AG 3.340.

7. This PN is mainly focused on the review performed by a practitioner of financial information of the business or companies being disposed of, described in option (a)(i) above. However, the practitioner may also refer to this PN if option (a)(ii) is selected, pursuant to which the financial information of the disposal group or discontinuing operations is required to be disclosed in addition to the financial information of the listed issuer. For financial information presented using option (a)(ii) above, the financial information should be prepared in accordance with the financial reporting framework adopted in the preparation of the annual financial statements of the listed issuer.

8. A practitioner who is engaged to perform a review of the financial information included in a VSD circular, and who is not the auditor of the listed issuer, or where applicable, the companies being disposed of, should perform the review with reference to this PN and in accordance with HKSRE 2400 "Engagements to Review Financial Statements".² The practitioner in this situation does not ordinarily have the same understanding of the reporting entity and its environment, including internal control, as the auditor of the reporting entity, therefore, the practitioner needs to carry out different or additional inquiries and procedures to meet the objective of the review.

9. A practitioner who is engaged to perform a review of the financial information included in a VSD circular, and who is also the auditor of the listed issuer, or where applicable, the companies being disposed of should perform the review with reference to this PN and in accordance with HKSRE 2410 "Review of Interim Financial Information Performed by the Independent Auditor of the Entity".

Basis of Preparation of the Financial Information

10. As stated in paragraph 3 above, the financial information contained in the VSD circular must be prepared by the directors of the listed issuer and must contain at least the income statement, balance sheet, cash flow statement and statement of changes in equity. Thus, there may be situations where the listed issuer wishes to comply only with the minimum disclosure requirements and disclose only the four primary statements without any or with only selected explanatory notes. In this situation, the financial information provided would not be a complete set of financial statements as described in Hong Kong Accounting Standard 1 "Presentation of Financial Statements". The financial information may also not be a complete condensed interim financial report as defined in Hong Kong Accounting Standard 34 "Interim Financial Reporting".

² HKSRE 2400 was revised in December 2012 as HKSRE 2400 (Revised) "Engagements to Review Historical Financial Statements", which will be effective for reviews of financial statements for periods ending on or after 31 December 2013.

11. While there is no specific requirement on the extent of explanatory notes to the financial information included in the VSD circular, the listed issuer must comply with the general disclosure obligations under Main Board Listing Rule 14.63 / GEM Listing Rule 19.63 (see extracted in Appendix 3 to this PN) and, include any notes that are considered necessary by the directors for shareholders to make an informed assessment of the transaction which is the subject of the VSD circular.
12. The financial information included in a VSD circular should include:
 - (i) the basis of preparation and presentation of the financial information and accompanied by necessary note(s) referring to relevant requirements of the Listing Rules on a VSD; and
 - (ii) the principal accounting policies adopted. In the interest of conciseness, the principal accounting policies adopted for the preparation of the financial information included in the VSD circular may make reference to the accounting policies included in the latest published financial statements of the listed issuer.
13. In addition, the explanatory notes to the financial information should include a statement to address that the financial information prepared in accordance with Main Board Listing Rule 14.68(2)(a)(i) / GEM Listing Rule 19.68(2)(a)(i), whichever is appropriate, is not a complete set of financial statements as described in Hong Kong Accounting Standard 1 "Presentation of Financial Statements", and that it should be read in connection with the relevant published annual and/or interim financial statements of the listed issuer.

The Objective of the Review Engagement

14. The objective of the review engagement under the scope of this PN is to report on the financial information as mentioned in paragraph 6(a) in accordance with the basis of preparation of the financial information pursuant to the relevant Listing Rules on a VSD. The practitioner should also refer to the objective stated in HKSRE 2400 or HKSRE 2410, as appropriate.

Performing the Review in Accordance with HKSRE 2400/ HKSRE 2410

15. The practitioner should apply the requirements, principles and guidance in HKSRE 2400/ HKSRE 2410 and, where appropriate, adapt them for application in the specific circumstances of an engagement to review the financial information included in a VSD circular.

Terms of Engagement

16. The procedures required to conduct a review of financial information in a VSD circular should be determined by the practitioner having regard to the guidance of this PN and the Listing Rules on a VSD.
17. The practitioner should exercise professional judgment in accepting and planning the review engagement as to whether the financial information provided is sufficient for the practitioner to complete the review engagement under the particular circumstances of the business or companies being disposed of.
18. The practitioner and the listed issuer should agree on the terms of the engagement. The agreed terms would be recorded in an engagement letter. Appendix 1 sets out illustrative examples of engagement letters.
19. If the review engagement is performed by a reporting accountant, the reporting accountant should clarify the scope of work with the listed issuer including that the review engagement does not constitute an audit of the disposal entity and that the listed issuer is required to make appropriate arrangements in relation to its subsequent annual audit. If the review engagement is performed by the listed issuer's auditor, the auditor should plan for the work in relation to the subsequent annual audit of the listed issuer. This arrangement should help to avoid a possible modification in the annual audit report of the listed issuer as a result of limited access to the books and records of the business or companies disposed of. The responsibility for ensuring

that adequate books and records of the business or companies disposed of is that of the directors of the listed issuer.

Conclusion and Reporting

20. Based on the work performed, the practitioner's review report should include a review conclusion as to whether anything has come to the practitioner's attention that causes the practitioner to believe that the financial information is not prepared, in all material respect, in accordance with the basis of preparation set forth in such note(s) to the financial information.
21. The practitioner should ensure that the review conclusion does not mention that the financial information is "fairly presented, in all material respects" or "gives a true and fair view" as the financial information prepared under the minimum requirements of the Listing Rules on a VSD does not constitute a complete set of financial statements. Guidance is set out in paragraphs 43(i) and (j) of HKSRE 2410.

Modifications

22. Circumstances may arise where the practitioner believes that a modified report is appropriate. The practitioner should consider the impact on the review report of any modification contained in an auditor's report on the listed issuer's financial statements covering the relevant period.

Emphasis of matter

23. The practitioner may, where appropriate, include an emphasis of matter paragraph in the review report to draw users' attention to a matter presented or disclosed in the financial information that, in the practitioner's judgement, is of such importance that it is fundamental to users' understanding of the financial information. The paragraph would preferably be included after the conclusion paragraph and ordinarily refer to the fact that the conclusion is not modified in this respect.

Illustrative examples of statement by the listed issuer's board of directors

24. Main Board Listing Rule 14.68(2)(a)(i) / GEM Listing Rule 19.68(2)(a)(i) requires that the listed issuer's board of directors must include a statement in a VSD circular that the financial information has been reviewed by the listed issuer's auditor or reporting accountant and details of any qualifications or modifications in the review report.

- (a) An illustrative example of a disclosure where the review report issued does not contain any modification is set out below.

The Listed Issuer's [auditor/ reporting accountant] was engaged to review the financial information of the Disposal Entity set out in pages... to ... in accordance with Hong Kong Standard on Review Engagements [2400 "Engagements to Review Financial Statements"]/ [2410 "Review of Interim Financial Information Performed by the Independent Auditor of the Entity"] and with reference to Practice Note 750 "Review of Financial Information under the Hong Kong Listing Rules for a Very Substantial Disposal" issued by the Hong Kong Institute of Certified Public Accountants. A review is substantially less in scope than an audit conducted in accordance with Hong Kong Standards on Auditing and consequently does not enable the [auditor/ reporting accountant] to obtain assurance that the [auditor/ reporting accountant] would become aware of all significant matters that might be identified in an audit. Accordingly, the [auditor/ reporting accountant] does not express an audit opinion. The [auditor/ reporting accountant] has issued an unmodified review report.

- (b) An illustrative example of a disclosure where the review report issued contains a modification is set out below.

The Listed Issuer's [auditor/ reporting accountant] was engaged to review the financial information of the Disposal Entity set out in pages... to ... in accordance with Hong Kong

Standard on Review Engagements [2400 "Engagements to Review Financial Statements"]/ [2410 "Review of Interim Financial Information Performed by the Independent Auditor of the Entity"] and with reference to Practice Note 750 "Review of Financial Information under the Hong Kong Listing Rules for a Very Substantial Disposal" issued by the Hong Kong Institute of Certified Public Accountants. A review is substantially less in scope than an audit conducted in accordance with Hong Kong Standards on Auditing and consequently does not enable the [auditor/ reporting accountant] to obtain assurance that the [auditor/ reporting accountant] would become aware of all significant matters that might be identified in an audit. Accordingly, the [auditor/ reporting accountant] does not express an audit opinion. The [auditor/ reporting accountant] has issued a qualified review report which states that (explain reason for report qualification, for example,

"The Disposal Entity's investment in DEF Limited, a foreign associate accounted for by the equity method, is carried at xxx on the statement of financial position as at 31 December 20X1, and the Disposal Entity's share of DEF's net income of xxx is included in the Disposal Entity's income for the year then ended. We were unable to obtain access to the relevant financial information of DEF concerning the carrying amount of the Disposal Entity's investment in DEF as at 31 December 20X1 and the Disposal Entity's share of DEF's net income for the year then ended. Consequently, we were unable to perform the procedures we considered necessary.

Based on our review, except for the possible effects of the matters described in the preceding paragraph, nothing has come to our attention that causes us to believe that the financial information of the Disposal Entity for the relevant periods is not prepared, in all material respects, in accordance with the basis of preparation set out in note x to the financial information").

- (c) An illustrative example of a disclosure where the review report issued contains an emphasis of matter paragraph is set out below.

The Listed Issuer's [auditor/ reporting accountant] was engaged to review the financial information of the Disposal Entity set out in pages... to ... in accordance with Hong Kong Standard on Review Engagements [2400 "Engagements to Review Financial Statements"]/ [2410 "Review of Interim Financial Information Performed by the Independent Auditor of the Entity"] and with reference to Practice Note 750 "Review of Financial Information under the Hong Kong Listing Rules for a Very Substantial Disposal" issued by the Hong Kong Institute of Certified Public Accountants. A review is substantially less in scope than an audit conducted in accordance with Hong Kong Standards on Auditing and consequently does not enable the [auditor/ reporting accountant] to obtain assurance that the [auditor/ reporting accountant] would become aware of all significant matters that might be identified in an audit. Accordingly, the [auditor/ reporting accountant] does not express an audit opinion. The [auditor/ reporting accountant] has included an emphasis of matter paragraph (without modification) in the review report which states that:

"Without modifying our review conclusion, we draw attention to note X to the financial information which indicates that the Disposal Entity incurred a net loss of zzz during the year ended 31 December 20X1 and, as of that date, the Disposal Entity's current liabilities exceeded its total assets by yyy. These conditions, along with other matters as set forth in note X, indicate the existence of a material uncertainty that may cast significant doubt about the Disposal Entity's ability to continue as a going concern."

Effective Date

25. This PN is effective for reviews of financial information included in a VSD circular dated on or after 1 June 2013. Earlier adoption of the PN is permissible.

Appendix 1

Examples of Engagement Letters for a Review of Financial Information Included in a VSD Circular

- Illustration 1: Engagement letter for a review of financial information included in a VSD circular.³
- Illustration 2: Engagement letter for a review of financial information included in a VSD circular conducted in accordance with HKSRE 2400 (Revised) for periods ending on or after 31 December 2013.³

³ Illustration 1 is used for engagements carried out in accordance with HKSRE 2410 or for engagements carried out in accordance with HKSRE 2400 for periods ending before 31 December 2013. Illustration 2 will be used for engagements carried out in accordance with HKSRE 2400 (Revised) for periods ending on or after 31 December 2013.

Illustration 1: Engagement letter for a review of financial information included in a VSD circular

The following letter is to be used as a guide in conjunction with the considerations outlined in paragraph 12 of HKSRE 2400/ paragraph 11 of HKSRE 2410 and will need to be adapted according to individual requirements and circumstances.

To the Board of Directors of [name of the listed issuer]⁴

We are providing this letter to confirm our understanding of the terms and objectives of our engagement to review ABC Entity's [balance sheets][statements of financial position]⁵ as of [respective reporting period end dates] and the [income statements][statements of comprehensive income]⁵, statements of changes in equity and [cash flows statements][statements of cash flows]⁵ for each of the periods then ended and explanatory notes (the "financial information"), which is prepared solely for the purpose of inclusion in the circular to be issued by [name of the listed issuer] (the "Issuer") in connection with the disposal of ABC Entity (the "Disposal Entity").

Our review will be conducted in accordance with Hong Kong Standard on Review Engagements [2410 "Review of Interim Financial Information Performed by the Independent Auditor of the Entity"] / [2400 "Engagements to Review Financial Statements"] and with reference to Practice Note 750 "Review of Financial Information under the Hong Kong Listing Rules for a Very Substantial Disposal" issued by the Hong Kong Institute of Certified Public Accountants with the objective of providing us with a basis for reporting whether anything has come to our attention that causes us to believe that the financial information is not prepared, in all material respects, in accordance with the basis of preparation set out in notes to the financial information. Such a review consists of making inquiries, primarily of persons responsible for financial and accounting matters, and applying analytical and other review procedures and does not, ordinarily, require corroboration of the information obtained. The scope of a review of the financial information is substantially less than the scope of an audit conducted in accordance with Hong Kong Standards on Auditing whose objective is the expression of an audit opinion regarding the financial information and, accordingly, we shall express no such opinion.⁶

We expect to report on the financial information as follows:

[Include text of sample report]

Responsibility for the financial information of the Disposal Entity is that of the directors of the Issuer. This includes designing, implementing and maintaining internal control relevant to the preparation and presentation of the financial information that is free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances. [Main Board Listing Rules 14.68(2)(a)(i) / GEM Listing Rules 19.68(2)(a)(i)] requires the financial information to be prepared by the directors of the Issuer using accounting policies of the Issuer and must contain at least the income statement, balance sheet, cash flow statement and statement of changes in equity. The directors are responsible for determining the adequacy of additional notes contained in the circular. [As part of our review, we will request written representations from management concerning assertions made in connection with the review.]

A review of the financial information does not provide assurance that we will become aware of all significant matters that might be identified in an audit. Further, our engagement cannot be relied upon to disclose whether fraud or errors, or illegal acts exist. However, we will inform you of any material matters that come to our attention.

⁴ According to Main Board Listing Rules 14.68(2)(a)(i) / GEM Listing Rules 19.68(2)(a)(i), the financial information must be prepared by the directors of the listed issuer and reviewed by the listed issuer's auditor or reporting accountant.

⁵ Delete as appropriate, different terms may be used as long as they are consistent with the titles of the corresponding statements.

⁶ Practitioners may consider it appropriate to clarify to whom they are responsible here in accordance with their risk management policies and with reference to Professional Risk Management Bulletin No.2 "Auditors duty of Care to Third Parties and The Audit Report".

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We look forward to full cooperation with your staff and we trust that they will make available to us whatever records, documentation and other information we request in connection with our review.

[Insert additional information here regarding fee arrangements and billings, as appropriate.]

Please sign and return the attached copy of this letter to indicate that it is in accordance with your understanding of the arrangements for our review of the financial information.

Yours faithfully,

XYZ & Co.
Certified Public Accountants (Practising) [or Certified Public Accountants]

We agree to the terms of this letter.

(signed)

.....
Director, for and on behalf of the Board of [name of the listed issuer]

Date

Illustration 2: Engagement letter for a review of financial information included in a VSD circular conducted in accordance with HKSRE 2400 (Revised) for periods ending on or after 31 December 2013

The following letter is to be used as a guide in conjunction with the considerations outlined in paragraph 37 of HKSRE 2400 (Revised) and will need to be adapted according to individual requirements and circumstances.

To the Board of Directors of [name of the listed issuer]⁷

[The objective and scope of the review]

You⁸ have requested that we review ABC Entity's [balance sheets][statements of financial position]⁹ as of [respective reporting period end dates] and the [income statements][statements of comprehensive income]⁹, statements of changes in equity and [cash flows statements][statements of cash flows]⁹ for each of the periods then ended and explanatory notes (the "financial information"), which is prepared solely for the purpose of inclusion in the circular to be issued by [name of the listed issuer] (the "Issuer") in connection with the disposal of ABC Entity (the "Disposal Entity"). We are pleased to confirm our acceptance and our understanding of this review engagement by means of this letter.

Our review will be conducted with the objective of expressing our conclusion on the financial information. Our conclusion, if unmodified, will be in the form "Based on our review, nothing has come to our attention that causes us to believe that the financial information of the Disposal Entity for the relevant periods is not prepared, in all material respects, in accordance with the basis of preparation set out in note X to the financial information."

[The practitioner's responsibilities]

We will conduct our review in accordance with Hong Kong Standard on Review Engagements (HKSRE) 2400 (Revised), *Engagements to Review Historical Financial Statements* and with reference to Practice Note 750 "Review of Financial Information under the Hong Kong Listing Rules for a Very Substantial Disposal" issued by the Hong Kong Institute of Certified Public Accountants.¹⁰ HKSRE 2400 (Revised) requires us to conclude whether anything has come to our attention that causes us to believe that the financial information, taken as a whole, is not prepared in all material respects in accordance with the basis of preparation set out in the financial information. HKSRE 2400 (Revised) also requires us to comply with relevant ethical requirements.

A review of financial information in accordance with HKSRE 2400 (Revised) is a limited assurance engagement. We will perform procedures, primarily consisting of making inquiries of management and others within the Issuer and the Disposal Entity, as appropriate, and applying analytical procedures, and evaluate the evidence obtained. We will also perform additional procedures if we become aware of matters that cause us to believe the financial information as a whole may be materially misstated. These procedures are performed to enable us to express our conclusion on the financial information in accordance with HKSRE 2400 (Revised). The procedures selected will depend on what we consider necessary applying our professional judgment, based on our understanding of the Issuer and the Disposal Entity and their environment, and our understanding of the basis on which the financial information is prepared and the accounting policies adopted and its application in the industry context.

A review is not an audit of the financial information, therefore:

⁷ According to Main Board Listing Rules 14.68(2)(a)(i) / GEM Listing Rules 19.68(2)(a)(i), the financial information must be prepared by the directors of the listed issuer and reviewed by the listed issuer's auditor or reporting accountant.

⁸ Throughout this letter, references to "you," "we," "us," "management," and "practitioner" would be used or amended as appropriate in the circumstances.

⁹ Delete as appropriate, different terms may be used as long as they are consistent with the titles of the corresponding statements.

¹⁰ Practitioners may consider it appropriate to clarify to whom they are responsible here in accordance with their risk management policies and with reference to Professional Risk Management Bulletin No.2 "Auditors duty of Care to Third Parties and The Audit Report".

REVIEW OF FINANCIAL INFORMATION UNDER THE HONG KONG LISTING RULES
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- (a) There is a commensurate higher risk than there would be in an audit, that any material misstatements that exist in the financial information reviewed may not be revealed by the review, even though the review is properly performed in accordance with HKSRE 2400 (Revised).
- (b) In expressing our conclusion from the review of the financial information, our report on the financial information will expressly disclaim any audit opinion on the financial information.

[The responsibilities of directors and identification of the basis of preparation]

Our review will be conducted on the basis that the directors acknowledge and understand that they have the responsibility:

- (a) To prepare the financial information using accounting policies of the Issuer which must contain at least the income statement, balance sheet, cash flow statement and statement of changes in equity as required under [Main Board Listing Rules 14.68(2)(a)(i) / GEM Listing Rules 19.68(2)(a)(i)].
- (b) To determine the adequacy of additional notes contained in the circular.
- (c) To design, implement and maintain internal control as management determines is necessary to enable the preparation of financial information that is free from material misstatement, whether due to fraud or error; and
- (d) To provide us with:
 - i. Access to all information of which management is aware that is relevant to the preparation of the financial information, such as records, documentation and other matters;
 - ii. Additional information that we may request from management for the purpose of the review; and
 - iii. Unrestricted access to persons within the Issuer and the Disposal Entity from whom we determine it necessary to obtain evidence.

As part of our review, we will request from the directors, written confirmation concerning representations made to us in connection with the review.

We look forward to full cooperation from your staff during our review.

[Other relevant information]

[Insert other information, such as fee arrangements, billings and other specific terms, as appropriate.]

[Reporting]

[Insert appropriate reference to the expected form and content of the practitioner's report.]

The form and content of our report may need to be amended in the light of our findings obtained from the review.

REVIEW OF FINANCIAL INFORMATION UNDER THE HONG KONG LISTING RULES
FOR A VERY SUBSTANTIAL DISPOSAL

Please sign and return the attached copy of this letter to indicate your acknowledgement of, and agreement with, the arrangements for our review of the financial information including our respective responsibilities.

XYZ & Co.
Certified Public Accountants (Practising) [or Certified Public Accountants]

We agree to the terms of this letter.

(signed)

.....
Director, for and on behalf of the Board of [name of the listed issuer]

Date

Appendix 2

Examples of Review Reports on Financial Information Included in a VSD Circular

- Illustration 1: A review report for an engagement conducted in accordance with HKSRE 2400.
- Illustration 2: A review report for an engagement conducted in accordance with HKSRE 2400 (Revised).
- Illustration 3: A review report for an engagement conducted in accordance with HKSRE 2410.

Illustration 1: A review report for an engagement conducted in accordance with HKSRE 2400 (Effective for reviews of financial information for periods ending before 31 December 2013)

Report on Review of Financial Information of the Disposal Entity

To the Board of Directors of [Name of the listed issuer]

Introduction

We have reviewed the financial information set out on pages to which comprise the [balance sheets][statements of financial position]¹¹ of ABC Entity (the "Disposal Entity") as of [respective reporting period end dates] and the [income statements][statements of comprehensive income]¹¹, statements of changes in equity and [cash flows statements][statements of cash flows]¹¹ for each of the periods then ended and explanatory notes (the "financial information"). The financial information has been prepared solely for the purpose of inclusion in the circular to be issued by [name of the listed issuer] (the "Issuer") in connection with the disposal of ABC Entity in accordance with the [Main Board Listing Rule 14.68(2)(a)(i)(A)][GEM Listing Rule 19.68(2)(a)(i)(A)].¹²

The directors of the Issuer are responsible for the preparation and presentation of the financial information of the Disposal Entity in accordance with the basis of preparation set out in note X to the financial information and [Main Board Listing Rule 14.68(2)(a)(i)][GEM Listing Rule 19.68(2)(a)(i)]. The directors are also responsible for such internal control as management determines is necessary to enable the preparation of financial information that is free from material misstatement, whether due to fraud or error. [The financial information does not contain sufficient information to constitute a complete set of financial statements as defined in Hong Kong Accounting Standard 1 "Presentation of Financial Statements" or an interim financial report as defined in Hong Kong Accounting Standard 34 "Interim Financial Reporting" issued by Hong Kong Institute of Certified Public Accountants.] Our responsibility is to express a conclusion on this financial information based on our review.¹³

Scope of Review

We conducted our review in accordance with Hong Kong Standard on Review Engagements 2400, "Engagements to Review Financial Statements" and with reference to Practice Note 750 "Review of Financial Information under the Hong Kong Listing Rules for a Very Substantial Disposal" issued by the Hong Kong Institute of Certified Public Accountants. These require that we plan and perform the review to obtain moderate assurance as to whether the financial information is free of material misstatement. A review is limited primarily to inquiries of entity personnel and analytical procedures applied to financial data and thus provides less assurance than an audit. We have not performed an audit and, accordingly, we do not express an audit opinion.

¹¹ Delete as appropriate, different terms may be used as long as they are consistent with the titles of the corresponding statements.

¹² In circumstances when the financial information has been presented in accordance with Main Board Listing Rule 14.68(2)(a)(i)(B) / GEM Listing Rule 19.68(2)(a)(i)(B), this paragraph would be worded as follows: "We have reviewed the financial information set out on pages to which comprise the balance sheets of [name of the listed issuer] (the "Issuer") as of [respective balance sheet dates] and the income statements, statements of changes in equity and cash flows statements for each of the periods then ended and explanatory notes (the "financial information"). The financial information has been prepared solely for the purpose of inclusion in the circular to be issued by the Issuer in connection with the disposal of ABC Entity (the "Disposal Entity") in accordance with the [Main Board Listing Rule 14.68(2)(a)(i)(B)][GEM Listing Rule 19.68(2)(a)(i)(B)]."

¹³ Practitioners may consider it appropriate to clarify to whom they are responsible here or elsewhere in the report in accordance with their risk management policies and with reference to Professional Risk Management Bulletin No. 2 "Auditors' Duty of Care To Third Parties and The Audit Report".

REVIEW OF FINANCIAL INFORMATION UNDER THE HONG KONG LISTING RULES
FOR A VERY SUBSTANTIAL DISPOSAL

*Conclusion*¹⁴

Based on our review, nothing has come to our attention that causes us to believe that the financial information of the Disposal Entity for the relevant periods is not prepared, in all material respects, in accordance with the basis of preparation set out in note X to the financial information.

XYZ & Co.
Certified Public Accountants (Practising) [or Certified Public Accountants]
Date
Address

¹⁴ For example modified reports, the practitioners may refer to Appendix 4 of HKSRE 2400 for guidance.

Illustration 2: A review report for an engagement conducted in accordance with HKSRE 2400 (Revised) (Effective for reviews of financial information for periods ending on or after 31 December 2013)

Independent Practitioner's Review Report on the Financial Information of the Disposal Entity

To the Board of Directors of [Name of the listed issuer]

We have reviewed the financial information set out on pages to which comprise the [balance sheets][statements of financial position]¹⁵ of ABC Entity (the "Disposal Entity") as of [respective reporting period end dates] and the [income statements][statements of comprehensive income]¹⁵, statements of changes in equity and [cash flows statements][statements of cash flows]¹⁵ for each of the periods then ended and explanatory notes (the "financial information"). The financial information has been prepared solely for the purpose of inclusion in the circular to be issued by [name of the listed issuer] (the "Issuer") in connection with the disposal of ABC Entity in accordance with the [Main Board Listing Rule 14.68(2)(a)(i)(A)][GEM Listing Rule 19.68(2)(a)(i)(A)].¹⁶

Directors' Responsibility for the Financial Information

The directors of the Issuer are responsible for the preparation and presentation of the financial information of the Disposal Entity in accordance with the basis of preparation set out in note X to the financial information and [Main Board Listing Rule 14.68(2)(a)(i)][GEM Listing Rule 19.68(2)(a)(i)]. The directors are also responsible for such internal control as management determines is necessary to enable the preparation of financial information that is free from material misstatement, whether due to fraud or error. [The financial information does not contain sufficient information to constitute a complete set of financial statements as defined in Hong Kong Accounting Standard 1 "Presentation of Financial Statements" or an interim financial report as defined in Hong Kong Accounting Standard 34 "Interim Financial Reporting" issued by Hong Kong Institute of Certified Public Accountants.]

Practitioner's Responsibility

Our responsibility is to express a conclusion on this financial information.¹⁷ We conducted our review in accordance with Hong Kong Standard on Review Engagements 2400 (Revised), *Engagements to Review Historical Financial Statements* and with reference to Practice Note 750 "Review of Financial Information under the Hong Kong Listing Rules for a Very Substantial Disposal" issued by the Hong Kong Institute of Certified Public Accountants. HKSRE 2400 (Revised) requires us to conclude whether anything has come to our attention that causes us to believe that the financial information, taken as a whole, is not prepared in all material respects in accordance with the applicable financial reporting framework. This Standard also requires us to comply with relevant ethical requirements.

¹⁵ Delete as appropriate, different terms may be used as long as they are consistent with the titles of the corresponding statements.

¹⁶ In circumstances when the financial information has been presented in accordance with Main Board Listing Rule 14.68(2)(a)(i)(B) / GEM Listing Rule 19.68(2)(a)(i)(B), this paragraph would be worded as follows: "We have reviewed the financial information set out on pages to which comprise the balance sheets of [name of the listed issuer] (the "Issuer") as of [respective balance sheet dates] and the income statements, statements of changes in equity and cash flows statements for each of the periods then ended and explanatory notes (the "financial information"). The financial information has been prepared solely for the purpose of inclusion in the circular to be issued by the Issuer in connection with the disposal of ABC Entity (the "Disposal Entity") in accordance with the [Main Board Listing Rule 14.68(2)(a)(i)(B)][GEM Listing Rule 19.68(2)(a)(i)(B)]."

¹⁷ Practitioners may consider it appropriate to clarify to whom they are responsible here or elsewhere in the report in accordance with their risk management policies and with reference to Professional Risk Management Bulletin No. 2 "Auditors' Duty of Care To Third Parties and The Audit Report".

REVIEW OF FINANCIAL INFORMATION UNDER THE HONG KONG LISTING RULES
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A review of financial information in accordance with HKSRE 2400 (Revised) is a limited assurance engagement. The practitioner performs procedures, primarily consisting of making inquiries of management and others within the entity, as appropriate, and applying analytical procedures, and evaluates the evidence obtained.

The procedures performed in a review are substantially less than those performed in an audit conducted in accordance with Hong Kong Standards on Auditing. Accordingly, we do not express an audit opinion on this financial information.

*Conclusion*¹⁸

Based on our review, nothing has come to our attention that causes us to believe that the financial information of the Disposal Entity for the relevant periods is not prepared, in all material respects, in accordance with the basis of preparation set out in note X to the financial information.

XYZ & Co.

Certified Public Accountants (Practising) [or Certified Public Accountants]

Date

Address

¹⁸ For example modified reports, the practitioners may refer to Illustrations 2 to 5 of Appendix 2 in HKSRE 2400 (Revised) for guidance.

Illustration 3: A review report for an engagement conducted in accordance with HKSRE 2410

Report on Review of Financial Information of the Disposal Entity

To the Board of Directors of [Name of the listed issuer]

Introduction

We have reviewed the financial information set out on pages to which comprise the [balance sheets][statements of financial position]¹⁹ of ABC Entity (the "Disposal Entity") as of [respective reporting period end dates] and the [income statements][statements of comprehensive income]¹⁹, statements of changes in equity and [cash flows statements][statements of cash flows]¹⁹ for each of the periods then ended and explanatory notes (the "financial information"). The financial information has been prepared solely for the purpose of inclusion in the circular to be issued by [name of the listed issuer] (the "Issuer") in connection with the disposal of ABC Entity in accordance with the [Main Board Listing Rule 14.68(2)(a)(i)(A)][GEM Listing Rule 19.68(2)(a)(i)(A)].²⁰

The directors of the Issuer are responsible for the preparation and presentation of the financial information of the Disposal Entity in accordance with the basis of preparation set out in note X to the financial information and [Main Board Listing Rule 14.68(2)(a)(i)][GEM Listing Rule 19.68(2)(a)(i)]. The directors are also responsible for such internal control as management determines is necessary to enable the preparation of financial information that is free from material misstatement, whether due to fraud or error. [The financial information does not contain sufficient information to constitute a complete set of financial statements as defined in Hong Kong Accounting Standard 1 "Presentation of Financial Statements" or an interim financial report as defined in Hong Kong Accounting Standard 34 "Interim Financial Reporting" issued by Hong Kong Institute of Certified Public Accountants.] Our responsibility is to express a conclusion on this financial information based on our review.²¹

Scope of Review

We conducted our review in accordance with Hong Kong Standard on Review Engagements 2410, "Review of Interim Financial Information Performed by the Independent Auditor of the Entity" and with reference to Practice Note 750 "Review of Financial Information under the Hong Kong Listing Rules for a Very Substantial Disposal" issued by the Hong Kong Institute of Certified Public Accountants. A review of the financial information consists of making inquiries, primarily of persons responsible for financial and accounting matters, and applying analytical and other review procedures. A review is substantially less in scope than an audit conducted in accordance with Hong Kong Standards on Auditing and consequently does not enable us to obtain assurance that we would become aware of all significant matters that might be identified in an audit. Accordingly, we do not express an audit opinion.

¹⁹ Delete as appropriate, different terms may be used as long as they are consistent with the titles of the corresponding statements.

²⁰ In circumstances when the financial information has been presented in accordance with Main Board Listing Rule 14.68(2)(a)(i)(B)/ GEM Listing Rule 19.68(2)(a)(i)(B), this paragraph would be worded as follows: "We have reviewed the financial information set out on pages to which comprise the balance sheets of [name of the listed issuer] (the "Issuer") as of [respective balance sheet dates] and the income statements, statements of changes in equity and cash flows statements for each of the periods then ended and explanatory notes (the "financial information"). The financial information has been prepared solely for the purpose of inclusion in the circular to be issued by the Issuer in connection with the disposal of ABC Entity (the "Disposal Entity") in accordance with the [Main Board Listing Rule 14.68(2)(a)(i)(B)][GEM Listing Rule 19.68(2)(a)(i)(B)]."

²¹ Practitioners may consider it appropriate to clarify to whom they are responsible here or elsewhere in the report in accordance with their risk management policies and with reference to Professional Risk Management Bulletin No. 2 "Auditors' Duty of Care To Third Parties and The Audit Report".

REVIEW OF FINANCIAL INFORMATION UNDER THE HONG KONG LISTING RULES
FOR A VERY SUBSTANTIAL DISPOSAL

*Conclusion*²²

Based on our review, nothing has come to our attention that causes us to believe that the financial information of the Disposal Entity for the relevant periods is not prepared, in all material respects, in accordance with the basis of preparation set out in note X to the financial information.

XYZ & Co.
Certified Public Accountants (Practising) [or Certified Public Accountants]
Date
Address

²² For example modified reports, the practitioners may refer to Appendices 5 to 7 of HKSRE 2410 for guidance.

Appendix 3

Summary of Relevant Main Board Listing Rules and GEM Listing Rules

Below is a summary of the Main Board Listing Rules and GEM Listing Rules that are referred to in the body of this PN and that are effective at the date of issuance of this PN. This summary is broadly replicated from the Main Board Listing Rules and the GEM Listing Rules are broadly aligned to the Main Board Listing Rules.

In all cases, auditors should refer to Chapter 14 of the Main Board Listing Rules / Chapter 19 of GEM Listing Rules for the original rules in respect of a very substantial disposal, and note that The Stock Exchange of Hong Kong Limited may update these Rules from time to time.

Main Board Listing Rules / GEM Listing Rules

Definitions

- 14.04 / 19.04 For the purposes of this Chapter:—
-
- 14.04 (6) a "listed issuer" means a company or other legal person whose securities are already listed on the Main Board, including a company whose shares are represented by listed depositary receipts, and unless the context otherwise requires, includes its subsidiaries;
- 19.04 (6) a "listed issuer" means a company or other legal person whose securities are already listed on GEM and, unless the context otherwise requires, includes its subsidiaries;
- 14.04 / 19.04 (7) a "notifiable transaction" means a transaction classified as a share transaction, discloseable transaction, major transaction, very substantial disposal, very substantial acquisition or reverse takeover under Main Board Listing Rule 14.06 / GEM Listing Rule 19.06;
-

Classification and explanation of terms

-
- 14.06 / 19.06 The transaction classification is made by using the percentage ratios set out in Main Board Listing Rule 14.07 / GEM Listing Rule 19.07. The classifications are:—
-
- (4) very substantial disposal — a disposal or a series of disposals (aggregated under Main Board Listing Rules 14.22 and 14.23 / GEM Listing Rules 19.22 and 19.23) of assets (including deemed disposals referred to in Main Board Listing Rule 14.29 / GEM Listing Rule 19.29) by a listed issuer where any percentage ratio is 75% or more;
-

Contents of circulars

General principles

- 14.63 / 19.63 A circular for a major transaction, very substantial disposal or very substantial acquisition and a listing document for a reverse takeover sent by a listed issuer to holders of its listed securities must:—
- (1) provide a clear, concise and adequate explanation of its subject matter having regard to the provisions of Main Board Listing Rule 2.13 / GEM Listing Rule 17.56; and
 - (2) if voting or shareholders' approval is required:
 - (a) contain all information necessary to allow the holders of the securities to make a properly informed decision;
 - (b) contain a heading emphasising the importance of the document and advising holders of securities, who are in any doubt as to what action to take, to consult appropriate independent advisers;
 - (c) contain a recommendation from the directors as to the voting action that shareholders should take, indicating whether or not the proposed transaction described in the circular is, in the opinion of the directors, fair and reasonable and in the interests of the shareholders as a whole; and
 - (d) contain a statement that any shareholder with a material interest in a proposed transaction and his associates will abstain from voting on resolution(s) approving that transaction; and
 - (3) a confirmation that, to the best of the directors' knowledge, information and belief having made all reasonable enquiry, the counterparty and the ultimate beneficial owner of the counterparty are third parties independent of the listed issuer and connected persons of the listed issuer.

.....

Very substantial disposal circulars

- 14.68 / 19.68 A circular issued in relation to a very substantial disposal must contain:—
- (1) the information required under Main Board Listing Rules 14.66 and 14.70 / GEM Listing Rules 19.66 and 19.70;
 - (2) (a) on a disposal of a business, company or companies:
 - (i) financial information of either:
 - (A) the business, company or companies being disposed of; or
 - (B) the listed issuer's group with the business, company or companies being disposed of shown separately as (a) disposal group(s) or (a) discontinuing operation(s),
- for the relevant period (as defined in the note to Main Board Listing Rule 4.06(1)(a) / GEM Listing Rule 7.05(1)(a)). The financial information must be prepared by the directors of the listed issuer using accounting policies of the listed issuer and must contain at least the income statement, balance sheet, cash flow statement and statement of changes in equity.

The financial information must be reviewed by the listed issuer's auditors or reporting accountants according to the relevant standards published by the Hong Kong Institute of Certified Public Accountants or the International Auditing and Assurance Standards Board of the International Federation of Accountants or the China Auditing Standards Board of the China Ministry of Finance. The circular must contain a statement that the financial information has been reviewed by the issuer's auditors or reporting accountants and details of any qualifications or modifications in the review report; and

Notes: 1. The listed issuer may include an accountants' report instead of a review by its auditors or reporting accountants. In that case, the accountants' report must comply with Chapter 4 of the Main Board Listing Rules / Chapter 7 of the GEM Listing Rules.

2. The Exchange may be prepared to relax the requirements in this rule if the assets of the company or companies being disposed of are not consolidated in the issuer's accounts before the disposal.

- (ii) pro forma income statement, balance sheet and cash flow statement of the remaining group on the same accounting basis. The pro forma financial information must comply with Chapter 4 of the Main Board Listing Rules / Chapter 7 of the GEM Listing Rules;
- (b) on a disposal of any revenue-generating assets (other than a business or company) with an identifiable income stream or assets valuation:
- (i) a profit and loss statement and valuation (where available) for the 3 preceding financial years (or less, where the asset has been held by the listed issuer for a shorter period) on the identifiable net income stream and valuation in relation to such assets which must be reviewed by the auditors or reporting accountants to ensure that such information has been properly compiled and derived from the underlying books and records. The financial information on which the profit and loss statement is based must relate to a financial period ended 6 months or less before the circular is issued; and
 - (ii) a pro forma profit and loss statement and net assets statement on the remaining group on the same accounting basis. The pro forma financial information must comply with Chapter 4 of the Main Board Listing Rules / Chapter 7 of the GEM Listing Rules;