Charltons - Hong Kong Law Newsletter - 29 May 2013

[online version](http://www.charltonslaw.com/stock-exchange-publishes-guidance-on-listing-document-risk-factor-disclosure/)

# Stock Exchange Publishes Guidance On Listing Document Risk Factor Disclosure

Hong Kong Exchanges and Clearing Limited (the **Exchange**) has published [Guidance letter GL54-13](http://www.hkex.com.hk/eng/rulesreg/listrules/listguid/iporq/Documents/gl54-13.pdf) (the **Letter**) [[archived copy](gl54-13.pdf)] providing guidance on the "Risk Factors" section of listing documents. The Letter replaces standard comment 4.10 of IPO Checklists I.N and I.T of the rules (**Rules**) governing the listing of securities on the Main Board and the Growth Enterprise Market, respectively. The stated purpose of the Letter is to help listing applicants ensure that the Risk Factors sections in their listing documents: (i) are concise, logically organised and easy to read in plain language; (ii) are relevant to applicants and contain sufficient information for investors to understand the specific risks that affect the applicant, its business and its securities; and (iii) explain how the risk affects the applicant or its securities. The Exchange may consider any Risk Factors section that fails to follow the guidance set out in the Letter to be incomplete.

## Listing Rule Requirements

Rules 2.03(2) and 2.13(2) (GEM Rules 2.06(2) and 17.56(2)) require that investors are provided with sufficient information to enable them to make an informed assessment of the listed issuer and that such information must be accurate and complete in all material respects and not be misleading or deceptive. Material facts should not be omitted and favourable possibilities should not be presented as more probable than they are. GEM Rule 14.22 sets out the following general categories of risks that should be disclosed:

* risks that are relevant to the listed issuer;
* risks that are relevant to the listed issuer’s business; and
* risks on a macro-scale that are relevant to the listed issuer.

## Specific Guidance for the Risk Factors Section

The Letter set out specific guidance as follows:

### Relevance to applicants

The Risk Factors section should set out risks that are relevant to the particular listing applicant and should explain clearly how these risks are related to/apply to, and have a significant effect on, the applicant, its industry and/or the offering. Context should be provided for each risk factor so that its nature and the circumstances that give rise to it are set out. Risk factors that are out-dated and no longer applicable should be excluded. Standardised language, if used, should be modified so that it is relevant to the particular circumstances of the listing applicant.

Disclosure in the Risk Factors section should be consistent with the information included in the rest of the listing document. If a significant risk or uncertainty is suggested in another part of the listing document, it should be included in the Risk Factors section as well.

### Quantitative disclosure

The nature and extent of risk factors should be elaborated. The Letter encourages meaningful quantitative disclosures of the likely impact of the risks in addition to qualitative disclosure to enable investors to assess their magnitude and likely impact on the applicants’ business operations and financial position. Unnecessary factual background should be avoided and the focus should be providing only detail to place the risk in context. The circumstances that gave rise to the risk factor should not be overemphasised to the detriment of explaining the risk itself. More detailed background information should be included in other parts of the listing document and only-cross referenced in the Risk Factors section.

### Avoiding repetition

The principal risks should be disclosed separately and not bundled together. Closely related risks should however be bundled if their disclosure as multiple separate risk factors would result in undue repetition and overlapping disclosures.

### Immitigable risks

Disclosure should be limited to risks that the listing applicant cannot adequately mitigate. Risks that the listing applicant is expected to deal with should not be included in the Risk Factors section. For example, it is not appropriate to include as a risk factor the applicant’s possible failure to comply with legal requirements because applicants are expected to be in compliance with relevant laws and regulations unless there is a legitimate reason for non-compliance.

However, risk factor disclosure should not be limited to risks that are considered reasonably likely to occur. If the occurrence of a particular risk would have a significant effect on the listing applicant, that risk should be disclosed even if the likelihood of it occurring is low. The Letter states that mitigating facts should not be included in the description of risk factors, so as not to divert attention from the risk factor itself.

### Appropriate headings and sub-headings

Related risk factor disclosures should be grouped together, adopting appropriate and meaningful headings and sub-headings. Examples include:

* “risks relating to the applicant”;
* “risks relating to the applicant’s business”;
* “risks relating to the applicant’s industry”;
* “social, economic or political risks relating to countries where the applicant has substantial operations”; and
* “risks that are specific to the securities”.

Sub-headings should be more specific than headings and should indicate what the risk is and not simply the facts or circumstances that gave rise to its existence. The Letter gives the example of the sub-heading “Reliance on major customers” as merely stating a fact, in contrast to “Our top 5 customers accounted for 75% of our revenue and any decrease in our sales to any one of them would affect our operations and financial results”, additionally describes the risk.

Headings should be listed from most important to least important. Similarly, sub-headings under each heading should be listed from most important to least important under the heading. Listing applicants should therefore set risks out in order of magnitude in terms of both likelihood of occurrence and potential impact.

### No mitigating facts

Mitigating facts may be included in other sections of the listing document and cross referenced in the Risk Factors section. They should not however be included in the Risk Factors section as this risks diverting investors’ attention from their magnitude and potential impact.

### Disclaimer statements

The Risk Factors section should not include any disclaimer statements that merely state that there may be undisclosed risks. The Letter emphasises that it is the listing applicant’s sole responsibility to determine the risks that should be disclosed. Consequently, the listing applicant may face legal or regulatory consequences for any undisclosed risk that should be disclosed.

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**Charltons - Hong Kong Law Newsletter - Issue 192 - 29 May 2013**