

- 2.2 The Respondent was the managing director of the Practice. She was also the engagement director of all the Practice's engagements and therefore responsible for the engagements' audit quality.
- 2.3 During the practice review, the practice review team ("Reviewer") reviewed the Practice's audit of the financial statements of a listed entity ("Client S") and its subsidiaries for the year ended 31 March 2017 ("2017 Financial Statements").
- 2.4 Client S is a company listed on the Growth Enterprise Market of the Stock Exchange of Hong Kong Limited. The group's principal activities included provision of computer services, equine services, securities brokerage and money lending business.
- 2.5 The 2017 Financial Statements were stated to have been prepared in accordance with Hong Kong Financial Reporting Standards. The auditor's report of the 2017 Financial Statements stated that the audit was conducted in accordance with Hong Kong Standards on Auditing ("HKSA").
- 2.6 The Practice expressed an unmodified opinion in the auditor's report of the 2017 Financial Statements dated 16 June 2017.
- 2.7 In reviewing the audit of Client S, the Reviewer found a number of deficiencies which indicated that the Respondent failed to perform adequate audit work to obtain sufficient and appropriate audit evidence to support the audit opinion on Client S.
- 2.8 In view of the Reviewer's findings and the public interest element involved in Client S, the Practice Review Committee ("PRC") decided to raise a complaint against the Respondent.

3. **The Complaint**

- 3.1 Section 34(1)(a)(vi) of the Professional Accountants Ordinance applies to the Respondent in that she had failed or neglected to observe, maintain or otherwise apply professional standard(s) in respect of her audit of Client S for the year ended 31 March 2017.

4. **Facts and circumstances in support of the Complaint**

Breach of Hong Kong Standard on Auditing ("HKSA") 500 "Audit Evidence"

- 4.1 Paragraph 6 of HKSA 500 requires an auditor to design and perform audit procedures that are appropriate in the circumstances for the purpose of obtaining sufficient appropriate audit evidence.
- 4.2 The audit working papers of Client S did not show that adequate audit procedures had been carried out for the purpose of obtaining sufficient appropriate audit evidence in respect of the following accounts which are material to the 2017 Financial Statements:

4.2.1 *Impairment assessment for cash-generating units ("CGU") with total net assets of HK\$62 million and goodwill of HK\$53 million.*

In assessing the valuation of the CGU on a value-in-use basis as at 31 March 2017, the auditor obtained the valuation reports prepared by Client S's valuer and relied on them to assess the impairment of the CGU and the associated goodwill at the year-end date. However, there was no evidence that the auditor had performed adequate audit procedures to evaluate the key assumptions and data used in the valuation, including annual growth rates of revenue, net profit margins, discount rate, adjustments to changes in working capital, and terminal value.

In addition, the working papers show that the auditor had carried out an impairment assessment of the CGU by comparing the carrying amount of goodwill with the recoverable amount of the CGU. However, the auditor's assessment was not properly performed as the assessment took account of only the goodwill but did not take into account the carrying amount of the cash-generating assets of the CGU.

The above raised doubts as to whether the auditor had obtained sufficient and appropriate audit evidence to support their conclusion on the impairment assessment of the CGU and the goodwill at the year-end date.

In her submission, the Respondent stated that the documentation and analysis on the CGU's valuation was sufficient and well documented.

4.2.2 *Medium-term bonds of HK\$248 million*

Client S issued the captioned bonds in financial years ended 31 March 2015 and 2016. The accounting policy of Client S was to measure the medium-term bonds at amortised cost, using the effective interest method.

Client S recognised the commission and handling charges relating to the issuance of medium-term bonds totalling HK\$8.4 million in profit or loss in the periods when they occurred. This accounting treatment is a departure from HKAS 39, which requires the transaction costs to be amortised over the expected life of bonds.

In addition, the effective interest of bonds of HK\$3.8 million was separately presented and included in accruals and other payables in the 2017 Financial Statements, instead of being allocated to the carrying amount of the bonds as at 31 March 2017 in accordance with HKAS 39.

The wrong accounting treatment as aforementioned impacted the effective interest rate used in calculating the amortised cost of the bonds, and consequently impacted the total liability relating to the bonds recorded in the 2017 Financial Statements. There was no evidence that the auditor had performed audit

procedures to ascertain that the effective interest rates used was appropriate and that Client S's treatment of the medium-term bonds complied with HKAS 39.

In her submission, the Respondent did not dispute this finding and admitted that the accounting treatment for the bonds was not correct.

4.2.3 *Biological assets of HK\$155 million*

Client S's accounting policy was to measure biological assets at fair value less costs to sell. The fair value of the biological assets as at 31 March 2017 was measured based on the fair market values determined by Client S's valuer.

There was no evidence that, in accepting the above valuation, the auditor had performed procedures to assess the relevance and reasonableness of the valuation method, key input data and assumptions used by the valuer. This lack of evidence of audit work was inconsistent with the auditor's report which stated that the audit team had checked, on a sample basis, the accuracy and relevance of the input data used.

The Respondent asserted that the audit team had discussed with the valuer of the work performed and also communicated with the component auditor. However, the working papers contain no documentation of any discussion with the valuer or component auditor regarding assessment of method, input and assumptions used in the valuation. There was no evidence to show how the asserted discussions, even if they did take place, could support the auditor's conclusion on the valuation of the biological asset at the year-end date.

4.2.4 *Distribution expenses of HK\$10 million and distribution payable of HK\$4 million*

There was no evidence of any audit work performed to verify the validity of distribution expenses and the payable amount recorded in 2017.

Breach of HKSA 230 "Audit Documentation"

- 4.3 According to paragraph 14 of HKSA 230, an auditor shall assemble the audit documentation in an audit file and complete the administrative process of assembling the final audit file on a timely basis after the date of the auditor's report. A21 of HKSA 230 states that a time limit within which to complete the assembly of the final audit file is ordinarily not more than 60 days after the date of the auditor's report.
- 4.4 During the practice review, the Reviewer noted that certain audit working papers and supporting documents of Client S, which were shown to the Reviewer during the review in March 2018, were not originally included in the assembled audit files. The working papers in question were a loan facility letter to support a going concern assessment and additional working papers to support the CGU impairment assessment.

- 4.5 As the auditor's report of Client S was issued in June 2017, the above demonstrated that the Respondent did not complete the assembly of final engagement files within 60 days after the issuance of the auditor's report, in accordance with paragraphs 14 and A21 of HKSA 230.

THE PROCEEDINGS

5. By a letter dated 7 February 2020, the Committee was informed by the Respondent that she admitted the complaint against her. She also suggested that it was no longer necessary for the parties to follow the steps set out in paragraphs 17 to 20 of the Disciplinary Committee Proceedings Rules.
6. The Notice of Commencement of Proceedings was issued on 14 May 2020. Having considered the aforementioned letter and the Respondent's admission of the complaint, the Committee approved the parties' proposal and directed that they made submissions on sanctions by 11 June 2020.
7. The Respondent applied for time extension to make submissions and costs and it was approved by the Committee.
8. The Complainant and Respondent provided their written submission on sanction and costs on 11 and 22 June 2020 respectively.
9. On 31 January 2021, Mr. Robin D'Souza, the Disciplinary Panel A member originally appointed to chair this committee stepped down. Mr. Malcolm Lim was appointed as the Chairman of this committee. Parties were informed of the the same, and by the end of February 2021, they confirmed that they do not have any objections nor comments regarding Mr. Lim's appointment.

SANCTIONS

10. It was noted that the Respondent had admitted liability at an early stage of the proceedings. However, the Disciplinary Committee has to take into account the interest of the public in particular as the audit relates to a listed entity.
11. Having considered the facts of the case and the written submissions from the parties, the Disciplinary Committee considers that a financial penalty of HK\$150,000.00 is appropriate.

COSTS

12. As regards to costs, in view of the findings, the Disciplinary Committee considers that the costs of the complainant in the sum of HK\$63,141.00 should be borne by the Respondent.

ORDERS

13. The Disciplinary Committee therefore makes the following orders :-

- (a) the Respondent be reprimanded under Section 35(1)(b) of the PAO;
- (b) the Respondent pays a penalty of HK\$150,000.00 under Section 35(1)(c) of the PAO;
- (c) the Respondent do pay the costs and expenses of and incidental to the proceedings of the Complainant in the sum of HK\$63,141.00 under Section 35(1)(iii) of the PAO.

The above shall take effect on the 42nd day from the date of this Order.

Dated: 28 April 2021

Mr. Malcolm Lim
Chairman
Disciplinary Panel A

Mr. Fong Wai Kuk Dennis
Member
Disciplinary Panel A

Mr. Kwok Kai Bun
Member
Disciplinary Panel B

Ms. Hilda Lam
Member
Disciplinary Panel A

Mr. Yeung King Hung Adrian
Member
Disciplinary Panel B

IN THE MATTER OF

A Complaint made under section 34(1A) of the Professional
Accountants Ordinance, Cap. 50

BETWEEN

The Registrar of the Hong Kong Institute of COMPLAINANT
Certified Public Accountants

AND

Kwong Kam Kwan Alex (A06661) RESPONDENT

Before a Disciplinary Committee of the Hong Kong Institute of Certified Public
Accountants

Members: Mr. Malcolm Lim (Chairman)
 Ms. Hilda Lam
 Mr. Fong Wai Kuk Dennis
 Mr. Kwok Kai Bun
 Mr. Yeung King Hung Adrian

ORDER AND REASONS FOR DECISION

1. This is a complaint made by the Registrar of the Hong Kong Institute of Certified Public Accountants against Mr. Kwong Kam Kwan Alex, CPA (Practising) no. A06661 (the "Respondent").

2. **Background**

- 2.1 A complaint was made by the Practice Review Committee (“**PRC**”) against a practising director of Andes Glacier CPA Limited (corporate practice no. M0401)(the “**Practice**”) as a result of a practice review of the Practice in March 2018.
- 2.2 During the practice review, the practice review team (“**Reviewer**”) reviewed the audit engagement of a listed entity (“**Client S**”) and its subsidiaries for the year ended 31 March 2017 (“**2017 Financial Statements**”).
- 2.3 The Respondent was the engagement quality control reviewer (“**EQCR**”) of the relevant audit.
- 2.4 The 2017 Financial Statements were stated to have been prepared in accordance with Hong Kong Financial Reporting Standards. In the auditor’s report dated 16 June 2017, the Practice expressed an unmodified opinion and stated that the audit of the 2017 Financial Statements was conducted in accordance with Hong Kong Standards on Auditing (“**HKSAs**”).
- 2.5 In the review process, the Reviewer found a number of significant deficiencies which showed that the audit of Client S did not comply with HKSAs. In particular, there were insufficient audit procedures on the (i) impairment assessment of cash-generating units (“**CGU**”) and the relevant goodwill; (ii) valuation of biological assets; and (iii) medium-term bonds. These items involved significant judgements made by the engagement team, which Kwong was expected to review and assess as EQCR.
- 2.6 In view of the Reviewer’s findings, the Registrar had reason to believe that the Respondent did not perform an effective engagement quality control review in that he failed to identify the audit issues as aforementioned.
- 2.7 The Registrar therefore raised a complaint against the Respondent under section 34(1A) of the Professional Accountants Ordinance (“**PAO**”).

3. **The Complaint**

- 3.1 Section 34(1)(a)(vi) of the PAO applies to the Respondent for having failed or neglected to observe, maintain or otherwise apply a professional standard when carrying out an engagement quality control review in the audit of Client S for the year ended 31 March 2017.

4. Facts and circumstances in support of the Complaint

4.1 Paragraph 20 of Hong Kong Standard on Auditing 220 “*Quality Control for an Audit of Financial Statements*” (“**HKSA 220**”) requires an EQCR to perform an objective evaluation of the significant judgments made by the engagement team, and the conclusions reached in formulating the auditor’s report. This evaluation involves, among other things, discussion of significant matters with the engagement partner and review of selected audit documentation relating to significant judgments made and evaluate the conclusions reached by the engagement team.

4.2 During the practice review, the Reviewer found that the engagement team failed to design and perform audit procedures to obtain sufficient appropriate audit evidence in respect of the two audit areas which involved significant accounting judgements and estimation¹:

- (i) The engagement team had performed an impairment assessment for CGU with total net assets of HK\$62 million and goodwill of HK\$53 million based on the valuations of the CGU prepared by Client S’s valuer².

The valuations involved a number of assumptions and estimations made by the management and valuer. These included annual growth rates of revenue, net profit margins, discount rate, adjustments to changes in working capital, and terminal value.

There was no evidence that the engagement team had performed audit procedures to evaluate the relevance and reasonableness of the above key assumptions and data used in the valuations.

Moreover, the impairment assessment performed by the engagement team was found to be improper, in that they only compared the recoverable amount of CGU with the carrying amount of goodwill, without taking into account the carrying amount of the cash-generating assets of the CGU.

The above raised doubts as to whether the engagement team had obtained sufficient and appropriate audit evidence to support their conclusion on the impairment assessment of the CGU and the goodwill at the year end date.

- (ii) The fair value of biological assets of HK\$155 million³ at the year end date was determined based on the valuation prepared by Client S’s valuer. The valuation involved various assumptions and estimations made by the management and valuer. There was no evidence that the engagement team

¹ The group’s audit materiality was HK\$5.6 million.

² Pages 3-85 of File#1DB

³ Pages 132 -159 of File#10, Pages 148-169 of File #11 and Pages 143-159 of File#1DB

had performed procedures to assess the relevance and reasonableness of the valuation method, key input data and assumptions used in the valuation.

- 4.3 Further, Client S did not comply with HKAS 39⁴ in determining the effective interest rate used in calculating the amortised cost of medium-term bonds and recognising the effective interest in the 2017 Financial Statements. The bonds were issued by Client S at an aggregate principal amount of HK\$248 million⁵ in financial years ended 31 March 2015 and 2016.
- Client S recognised the commission and handling charges relating to the medium-term bonds totalling HK\$8.4 million in profit or loss in the periods when they occurred, instead of amortising the transaction costs over the expected life of bonds;
 - The effective interest of bonds of HK\$3.8 million⁶ was separately presented and included in accruals and other payables in the 2017 Financial Statements, instead of being allocated to the carrying amount of the bonds at the year end date.
- 4.4 The wrong accounting treatments as aforementioned impacted the effective interest rate used in calculating the amortised cost of the bonds, and consequently impacted the total liability relating to the bonds recorded in the 2017 Financial Statements. There was no evidence that the engagement team had performed audit procedures to ascertain that the effective interest rates used was appropriate and that Client S's treatment of the medium-term bonds complied with HKAS 39.
- 4.5 The audit areas in 3.2 and 3.3 above involved significant judgements and estimation and/or significant amounts in the 2017 Financial Statements. The Respondent as EQCR should have performed an adequate review of those audit areas to ensure that the audit evidence obtained and procedures performed by the engagement team were sufficient and appropriate to support the audit conclusions.
- 4.6 However, the Respondent failed to identify the insufficient work done by the engagement team in respect of their impairment assessment of the CGU and the goodwill, and the biological assets. Also, the Respondent failed to identify the improper accounting treatment of the material account of medium-term bonds (which represented 44% of the group's total liabilities as at 31 March 2017). The working papers did not show how the Respondent had evaluated the significant matters and judgments made by the engagement team to conclude that the audit procedures performed by the engagement team were sufficient and appropriate.

⁴ Hong Kong Accounting Standard 39 "Financial Instruments: Recognition and Measurement"

⁵ Pages 92-94 of File #1C and pages 39-41 of File#1DC

⁶ Page 73 of File#1C and Pages 20-21 of File#1DC

- 4.7 On the basis of the above findings, it is evident that the Respondent failed to perform an adequate engagement quality control review in accordance with paragraph 20 of HKSA 220.

THE PROCEEDINGS

5. By a letter dated 26 March 2020, the Committee was informed that the Respondent had admitted the complaint against him. It has also suggested that it is no longer necessary for the parties to follow the steps set out in paragraphs 17 to 20 of the Disciplinary Committee Proceedings Rules.
6. The Notice of Commencement of Proceedings was issued on 14 May 2020. Having considered the said letter and the Respondent's admission of the complaint, the Committee approved the proposal and directed that the Respondent make submissions on sanctions by 11 June 2020.
7. The Respondent applied for time extension to make submissions and on the issue of costs. This was approved by the Committee.
8. The Complainant and Respondent provided their written submission on sanction and costs on 11 June and 10 July 2020 respectively.
9. On 31 January 2021, Mr. Robin D'Souza, the Disciplinary Panel A member originally appointed to chair this committee stepped down. Mr. Malcolm Lim was appointed as the Chairman of this committee. Parties were informed of the aforesaid, and by the end of February 2021, they confirmed that they did not have any objections nor comments regarding the same.

SANCTIONS

10. It was noted that the Respondent had admitted liability at an early stage of the proceedings. However, the Disciplinary Committee has to take into account the interest of the public in particular as the audit relates to a listed entity.
11. Having considered the facts of the case and the written submissions from the parties, the Disciplinary Committee considers that a financial penalty of HK\$80,000.00 is appropriate.

COSTS

12. As regards to costs, in view of the findings, the Disciplinary Committee considers that the costs of the complainant in the sum of HK\$32,715.00 should be borne by the Respondent.

ORDERS

13. The Disciplinary Committee therefore makes the following orders :-

- (a) the Respondent be reprimanded under Section 35(1)(b) of the PAO;
- (b) the Respondent pays a penalty of HK\$80,000.00 under Section 35(1)(c) of the PAO;
- (c) the Respondent do pay the costs and expenses of and incidental to the proceedings of the Complainant in the sum of HK\$32,715.00 under Section 35(1)(iii) of the PAO.

The above shall take effect on the 42nd day from the date of this Order.

Dated: 28 April 2021

Mr. Malcolm Lim
Chairman
Disciplinary Panel A

Mr. Fong Wai Kuk Dennis
Member
Disciplinary Panel A

Mr. Kwok Kai Bun
Member
Disciplinary Panel B

Ms. Hilda Lam
Member
Disciplinary Panel A

Mr. Yeung King Hung
Adrian
Member
Disciplinary Panel B