

IN THE MATTER OF

A Complaint made under Section 34(1)(a) of the Professional Accountants Ordinance (Cap.50) (“the PAO”) and referred to the Disciplinary Committee under Section 33(3) of the PAO

BETWEEN

The Registrar of the Hong Kong Institute of
Certified Public Accountants

COMPLAINANT

AND

The Respondent

RESPONDENT

Before a Disciplinary Committee of the Hong Kong Institute of Certified Public Accountants (“the Institute”)

Members:

Date of Hearing: 14 May 2013

REASONS FOR DECISION

1. This is a complaint made by the Registrar of the Hong Kong Institute of Certified Public Accountants (“the Institute”) as the Complainant against [the Respondent] as the Respondent, a certified public accountant (practising), under Section 34(1)(a)(ix) and Section 34(1)(a)(vi) of the PAO.
2. The particulars of the Complaint as set out in a letter dated 4 July 2012 (“the Complaint”) from the Complainant to the Council of the Institute for consideration of the Complaint for referral to the Disciplinary Panels, are as follows:-

- 2.1 On 24 May 2011, the Institute received a complaint from Ms. C ("Ms. C"), a director and shareholder of [Company A] ("[Company A]") regarding an apparent failure by the Respondent in dealing with her enquiries relating to the financial statements of [Company A] audited by the Respondent.
- 2.2 The Respondent was the auditor and tax representative of [Company A]. He also provided certain company secretarial services to the Company. The Respondent expressed an unqualified opinion in his own name on the company's financial statements for each of the years ended 31 March 2003 to 31 March 2006.
- 2.3 [Company A] was required to furnish accounting records and information to the Inland Revenue Department ("IRD"). Based on the documents she received from the IRD and [Company A], Ms. C suspected that the Financial Statements might not be correct. Ms. C's main concerns include the following:-
 - (a) the 2003 Financial Statements were signed by a person who was not a director of [Company A]; and
 - (b) certain expenditures incurred by [Company A] were personal in nature and not related to the operations of company's business.
- 2.4 Ms. C contended that she had first attempted to contact the Respondent in August 2010 because of her concerns that [Company A]'s audited financial statements might not be correct. Ms. C alleged that, despite her repeated requests and promises received from the Respondent, she was never provided with the information or documents she had requested from him. In relation to Ms. C's concern about the 2003 Financial Statements being signed off by an unauthorized signatory, the Respondent advised Ms. C on 24 December 2010 that he would need to seek legal advice. On 10 March 2010, the Respondent indicated to Ms. C that he had received his legal adviser's opinion and would contact Ms. C a few days later. The Respondent provided no further response afterwards. It appears that the Respondent accepted the 2003 Financial Statements which were co-signed by a person who was not a director.
- 2.5 The Respondent was at all material times a member of the Institute.

3.1 **First Complaint**

Section 34(1)(a)(ix) of the PAO applies to the Respondent in that he had refused or neglected to comply with a direction lawfully given to him by the Council under section 18B of the PAO under cover of a letter from the Institute dated 13 February 2012.

3.2 **Facts and Circumstances in Support of First Complaint**

3.2.1 Following receipt of the Complaint from Ms. C, the Institute sought representations from the Respondent on the allegations raised and observations that had been made on 2 August 2011. Despite applying for and receiving a time extension to respond to the Institute's enquiries, the Respondent failed to provide his response.

3.2.2 In view of the lack of response from the Respondent, a direction under s.18B of the PAO was issued to him on 13 February 2012 ("18B Notice") requiring him to provide an explanation of the matters set out in the Institute's enquiry letter dated 2 August 2011.

3.2.3 On 25 February 2012, the Respondent acknowledged receipt of the 18B Notice and sought an extension of time to 19 March 2012, to respond. A time extension up to 14 March 2012 was granted to the Respondent.

3.2.4 As of the date of this Complaint, the Institute had received no response to the 18B Notice.

3.3 **Conclusion**

In the circumstances, the Disciplinary Committee is satisfied that it has been proved that the Respondent has breached section 34(1)(a)(ix) of the PAO in that he had refused or neglected to comply with a direction lawfully given to him by the Council under section 18B of the PAO under cover of a letter from the Institute dated 13 February 2012.

4.1 **Second Complaint**

Section 34(1)(a)(vi) of the PAO applies to the Respondent in that he failed or neglected to observe, maintain or otherwise apply a professional standard, namely the then effective Statement of Auditing Standards 600 "Auditors' Reports on Financial Statements" (Issued August 1994; revised April 2000, June 2001, February 2004, September 2004 (name change), December 2005 and October 2006) ("SAS 600") in that he failed to express a qualified opinion on a breach of the requirements of the Companies Ordinance (Cap 32) ("CO") that were applicable to the preparation of the financial statements of [Company A] ("[Company A]") for each of the years ended 31 March 2003, 31 March 2004, 31 March 2005 and 31 March 2006.

4.2 **Third Complaint (in the alternative to the Second Complaint)**

Section 34(1)(a)(vi) of the PAO applies to the Respondent in that he failed or neglected to observe, maintain or otherwise apply a professional standard, namely, the then effective Statement of Auditing Standards 120 "Consideration of Laws and Regulations in an Audit of Financial Statements" (Effective for audits of financial statements for periods beginning before 15 December 2004) ("SAS 120") for the financial statements of [Company A] for each of the years ended 31 March 2003 and 31 March 2004 and Hong Kong Standard on Auditing 250 "Consideration of Laws and Regulations in an Audit of Financial Statements" (Effective for audits of financial statements for the periods beginning on or after 15 December 2004) ("HKSA 250") for the financial statements of [Company A] for each of the years ended 31 March 2005 and 31 March 2006, as he had failed to obtain sufficient audit evidence to support an audit opinion that the management of [Company A] could properly adopt the section 141D CO procedure for the financial statements of those periods.

4.3 **Facts and Circumstances in Support of Second and Third Complaints**

4.3.1 *Background*

4.3.1.1 At all material times, [Company A] had two directors and two shareholders of which Ms. C was one of the directors and shareholders.

4.3.1.2 In the course of its investigations, the Institute sought and received further information from Ms. C. On 14 July 2011, the Institute received a letter from Ms. C confirming that she had not agreed to the adoption of section 141D of the CO.

4.3.2 *Requirements of the Companies Ordinance*

4.3.2.1 Section 121(2) of the CO requires every company in Hong Kong to keep proper books of accounts in such way as "to give a true and fair view of the state of the company's affairs and to explain its transactions" and section 123 sets out the disclosures required in the company's financial statements.

4.3.2.2 Section 141D of the CO exempts certain private companies from complying with the full disclosure requirements of the CO. All the shareholders must agree before the provisions of section 141D can be applied. The agreement must be in writing and must be obtained every year.

4.3.2.3 If section 141D is applied, under section 141D(1)(e), "the auditors' report shall state –

- (a) whether or not the auditors have obtained all the information and explanations which they have required; and
- (b) whether in their opinion, the balance sheet referred to in the report is properly drawn up so as to exhibit a true and correct view of the state of the company's affairs...". (underline added)

4.3.2.4 If section 141D is not applicable, the auditor's report is governed by section 141(3) which requires the auditor to state in its report whether, in his opinion, the company's balance sheet and profit and loss account have been properly prepared in accordance with the provisions of the CO and whether they give a true and fair view of the company's state of affairs as at the end of the financial year and of its profit or loss for the financial year.

4.3.3 *Requirements of SAS 600*

4.3.3.1 Paragraph 1 of SAS 600 states that "The purpose of this Statement of Auditing Standards (SAS) is to establish standards and provide guidance on the form and content of auditors' reports issued as a result of an audit of the financial statements ..."

4.3.3.2 Paragraph 7 states that "This SAS applies to all reports issued by auditors which express an opinion in terms of whether financial statements give a true and fair view, or where statutory or other specific requirements prescribe the use of a term such as "present fairly" "exhibit a true and correct view" or "properly prepared in accordance with"..."

4.3.3.3 Paragraph 79 further states that auditors are required to comply with SAS 600 for all auditor's reports "dated on or after 1 May 2000 but before 31 December 2006."

4.3.3.4 Various paragraphs of SAS 600 (including the appendix) provide when a qualified audit opinion should be expressed. Had the Respondent properly applied SAS 600, he should have expressed a qualified audit opinion and reported on [Company A]'s non-compliance with section 141D of the CO for each of the years ended 31 March 2003, 31 March 2004, 31 March 2005 and 31 March 2006.

(a) **"29. *An auditors' report should contain a clear expression of opinion on the financial statements and on any further matters required by statute or other requirements applicable to the particular engagement. (SAS 600.5)***

30. The auditors would use their best endeavour to obtain sufficient, relevant and reliable audit evidence to enable them to express an unqualified opinion. Failing that, the auditors would include a qualified opinion in the auditors' report....

33. An unqualified opinion on financial statements is expressed when in the auditors' judgement they give a true and fair view (where relevant) and have been prepared in accordance with relevant accounting and other requirements. This judgement entails concluding whether inter alia:...

b. the financial statements have been prepared in accordance with relevant legislation, regulations ..."

In order to comply with his obligations under SAS 600, the Respondent should have qualified his audit opinion if there was no shareholders' written consent to adopt the s.141D procedure.

- (b) *"67. For the requirements under the Companies Ordinance, reference should be made to PN 600.1 "Reports by auditors under the Hong Kong Companies Ordinance" and PN 600.2 "Audit approach to companies applying section 141D of the Companies Ordinance"."*

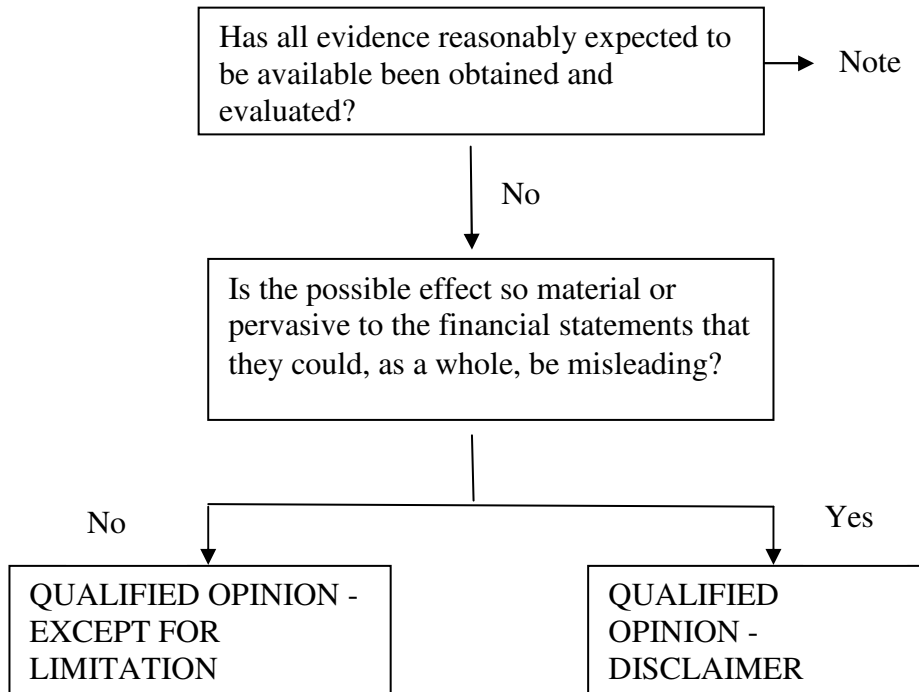
Paragraph 9 of PN 600.2 provides that:

"In addition to carrying out the essential audit procedures contained in SASs, the auditors should ensure:

- a. that the company is entitled to take advantage of the exemptions permitted under section 141D(3);*
- b. that the shareholders have entered into a new unanimous written agreement for the particular financial year under review; and*
- c. ..."*

Applying PN 600.2 , the Respondent was required to carry out audit procedures to establish that the shareholders of [Company A], including Ms. C, had entered into a new unanimous written agreement for the financial statements for each of the years ended 31 March 2003 to 31 March 2006.

- (c) Appendix 1 of SAS 600 sets out a flowchart identifying the steps involved in forming an audit opinion. The relevant steps are reproduced below:



Note: As Ms. C contended that she did not sign the shareholders consent to adopt the s.141D procedure, the answer cannot be "Yes".

Without evidence of written consent of the shareholders to the adoption of section 141D, the Respondent should have (1) assessed the effect of such noncompliance and (2) determined which qualified audit opinion (except for limitation or disclaimer) should be expressed.

4.3.4 *What the Respondent failed to do*

4.3.4.1 Given the absence of written shareholders consent to the s.141D procedure, the Respondent should have qualified his audit opinion as required by SAS 600.

4.3.4.2 Further, in his audit report, the Respondent stated that:

"I conducted my audit in accordance with Statements of Auditing Standards issued by the Hong Kong Institute of Certified Public Accountants. The audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the balance sheet and the notes thereon. It also includes an assessment of the significant estimates and judgements made by the directors in the preparation of the balance sheet and the notes thereon, and of whether the accounting policies are appropriate to the company's circumstances, consistently applied and adequately disclosed."

I planned and performed my audit so as to obtain all the information and explanations which I considered necessary in order to provide me with sufficient evidence to give reasonable assurance as to whether the balance sheet together with the notes thereon is free from material misstatement. In forming my opinion I also evaluated the overall adequacy of the presentation of information in the balance sheet together with the notes thereon. I believe that my audit provides a reasonable basis for my opinion." (underline added)

4.3.4.3 The notes to the financial statements for each of the years ended 31 March 2003 to 31 March 2006 stated that "All the shareholders have agreed in writing that the provisions of section 141D of the Hong Kong Companies Ordinance have been adopted in preparing these financial statements." However, this was incorrect and demonstrates that the Respondent could not have carried out a proper review of the audit evidence. If the Respondent had carried out a proper review of the audit evidence, he would have appreciated that there was no written shareholders consent to adoption of the s.141D procedure as required by the Companies Ordinance and, as a result, he should have qualified his audit opinion.

4.4 Conclusion

In the circumstances, the Disciplinary Committee is satisfied that it has been proved that the Respondent has breached Section 34(1)(a)(vi) of the PAO in that he failed or neglected to observe, maintain or otherwise apply SAS 600.

5. On 23 November 2012, the Notice of Commencement of Proceedings was issued to the Parties and they were requested to make filings in accordance with the Procedural Timetable. The Complainant's Case was filed on 14 December 2012 and the Complainant's checklist was filed on 19 February 2013. However, the Respondent did not make any submissions to the Disciplinary Committee.
6. The Clerk contacted the Respondent by telephone on 4 January 2013, 7 January 2013, 19 February 2013 and 26 February 2013. Despite voice messages were left with the Respondent, the Respondent did not return his call to the Clerk. On 21 March and 17 April 2013, the Clerk had a telephone conversation with the Respondent. On both occasions, the Respondent represented he needed more time to consider the matter and would communicate with the Disciplinary Committee. However, no further response has been obtained from him.
7. Even though the Respondent was kept informed throughout the proceedings, he did not attend the substantive hearing on 14 May 2013. In particular, the date and venue of the substantive hearing in the Clerk's letter to the parties dated 30 April 2013 was, as usual, sent to his correspondence address registered with the Institute.
8. In considering the proper order to be made in this case, the Disciplinary Committee has had regard to all the aforesaid matters, including the particulars in support of the Complaint, and the conduct of the Complainant and the Respondent throughout the proceedings and the fact that the Third Complaint was made in the alternative to the Second Complaint.

9. Having considered all the information before it, the Committee, ORDERS that:
- (1) for the First Complaint,
 - (a) the name of the Respondent be removed from the register of certified public accountants temporarily for 6 months under Section 35(1)(a) of the PAO. The removal shall be effective from 1 August 2013; and
 - (b) the Respondent pay a penalty of HK\$20,000 under Section 35(1)(c) of the PAO;
 - (2) for the Second Complaint,
 - (a) the Respondent be reprimanded under Section 35(1)(b) of the PAO; and
 - (b) the Respondent pay a penalty of HK\$30,000 under Section 35(1)(c) of the PAO;
 - (3) the Respondent do pay the costs and expenses of and incidental to the proceedings of the Complainant in the sum of HK\$69,411 under Section 35(1)(iii) of the PAO.

Dated the 11th day of June 2013

IN THE MATTER OF

A Complaint made under Section 34(1)(a) of the Professional Accountants Ordinance (Cap.50) ("the PAO") and referred to the Disciplinary Committee under Section 33(3) of the PAO

BETWEEN

The Registrar of the Hong Kong Institute of
Certified Public Accountants

COMPLAINANT

AND

The Respondent

RESPONDENT

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

Members:

Date of Hearing: 14 May 2013

ORDER

Upon reading the complaints against the Respondent as set out in a letter from the Complainant dated 4 July 2012, the Complainant's Case dated 14 December 2012, the Complainant's checklist dated 19 February 2013 and the relevant documents, the Disciplinary Committee is satisfied by the documentary evidence adduced before it that the following Complaints are proved:

- (1) Section 34(1)(a)(ix) of the PAO applies to the Respondent in that he had refused or neglected to comply with a direction lawfully given to him by the Council under section 18B of the PAO under cover of a letter from the Institute dated 13 February 2012.
- (2) Section 34(1)(a)(vi) of the PAO applies to the Respondent in that he failed or neglected to observe, maintain or otherwise apply a professional standard, namely the then effective Statement of Auditing Standards 600 "Auditors' Reports on Financial Statements" (Issued August 1994; revised April 2000, June 2001, February 2004, September 2004 (name change), December 2005 and October 2006) ("SAS 600") in that he failed to express a qualified opinion on a breach of the requirements of the Companies Ordinance (Cap 32) ("CO") that were applicable to the preparation of the

financial statements of [Company A] ("[Company A]") for each of the years ended 31 March 2003, 31 March 2004, 31 March 2005 and 31 March 2006.

The Disciplinary Committee ORDERS that:-

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 - (a) the name of the Respondent be removed from the register of certified public accountants temporarily for 6 months under Section 35(1)(a) of the PAO. The removal shall be effective from 1 August 2013; and
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 - (b) the Respondent pay a penalty of HK\$30,000 under Section 35(1)(c) of the PAO;
- (3) the Respondent do pay the costs and expenses of and incidental to the proceedings of the Complainant in the sum of HK\$69,411 under Section 35(1)(iii) of the PAO.

Dated the 11th day of June 2013