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

Hong Kong Institute of Certified Public Accountants takes disciplinary action against a certified public accountant (practising)

(HONG KONG, 20 January 2022) A Disciplinary Committee of the Hong Kong Institute of Certified Public Accountants reprimanded Mr. Law Fei Shing, certified public accountant (practising) (A15863) on 3 December 2021 for his failure or neglect to observe, maintain or otherwise apply professional standards issued by the Institute. The Committee further ordered the cancellation of Mr. Law's practising certificate, with no issuance of a practising certificate to him for 15 months, with effect from 14 January 2022. In addition, the Committee ordered Mr. Law to pay a penalty of HK$160,000 and costs of the disciplinary proceedings of HK$4,943,123.

Mr. Law is the sole proprietor of F.S. Law & Co. The firm audited the financial statements of a private company for the two years ended 31 March 2010 and 2011.

Deficiencies were found in the audits and in how Mr. Law conducted his professional relationship with the company. Mr. Law failed to:

(i) obtain sufficient evidence to justify his concurrence with the company's adoption of the exemptions under section 141D of the then Companies Ordinance and the financial reporting standard for small and medium-sized entities as a basis of financial statement preparation, when the company's holding of a subsidiary at the time would have disqualified it from the exemptions;

(ii) qualify his auditor's opinion for a limitation of audit scope over provision for impairment loss on an investment;

(iii) obtain sufficient appropriate evidence to support his acceptance of the company's breach of statutory disclosure requirements applicable to a charge over the company's assets that was made to secure banking facilities granted to a director-controlled entity;

(iv) segregate funds transferred to him by a shareholder (who was also a director) of the company, and make adequate enquiries to ensure the transfer complied with relevant laws and regulations; and

(v) maintain professional knowledge and skill at the level required to ensure the company received competent professional service.

After considering the information available, the Institute lodged the complaints against Mr. Law under section 34(1)(a) of the Professional Accountants Ordinance.

In the course of the disciplinary proceedings, Mr. Law applied for judicial review twice. The proceedings were held over for some five years until the judicial reviews were completed and dismissed by the court.

The Disciplinary Committee found that Mr. Law was in breach of Hong Kong Standard on Auditing ("HKSA") 250 *Consideration of Laws and Regulations in an Audit of Financial Statements*, HKSA 701 *Modifications to the Independent Auditor's Report*, section 270 *Custody of Client Assets* of the Code of Ethics for Professional Accountants ("Code of Ethics") and the fundamental principle of professional competence and due care in section 100 of the Code of Ethics.

Having taken into account the circumstances of the case, the Disciplinary Committee made the above order against Mr. Law under section 35(1) of the Ordinance, which included an enhanced order requiring him to bear the Institute's cost in full due to his conduct and resulting delays. The Committee noted Mr. Law's breaches were very serious in that they demonstrated a serious lack of understanding of auditing and ethical standards, and the fundamental and basic legal requirements relating to preparation and presentation of financial statements under the Companies Ordinance. The breaches were aggravated by Mr. Law's limited remorse and lack of candour, as seen in his changing and evolving defences in the course of the disciplinary proceedings, and by his obstructive conduct that resulted in significant delays to the proceedings, substantial wasted costs and the Institute's need to instruct external counsel to act for it.

About HKICPA Disciplinary Process

The Hong Kong Institute of Certified Public Accountants ("HKICPA") enforces the highest professional and ethical standards in the accounting profession. Governed by the Professional Accountants Ordinance (Cap. 50) and the Disciplinary Committee Proceedings Rules, an independent Disciplinary Committee is convened to deal with a complaint referred by Council. If the charges against a member, member practice or registered student are proven, the Committee will make disciplinary orders setting out the sanctions it considers appropriate. Subject to any appeal by the respondent, the order and findings of the Disciplinary Committee will be published.

For more information, please see:
http://www.hkicpa.org.hk/en/standards-and-regulations/compliance/disciplinary/

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About HKICPA

The Hong Kong Institute of Certified Public Accountants ("HKICPA") is the statutory body established by the Professional Accountants Ordinance responsible for the professional training, development and regulation of certified public accountants in Hong Kong. The Institute has over 47,000 members and 17,000 registered students.

Our qualification programme assures the quality of entry into the profession, and we promulgate financial reporting, auditing and ethical standards that safeguard Hong Kong's leadership as an international financial centre.

The CPA designation is a top qualification recognised globally. The Institute is a member of and actively contributes to the work of the Global Accounting Alliance and International Federation of Accountants.

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

香港會計師公會對一名執業會計師作出紀律處分

（香港，二零二一年一月二十日）香港會計師公會轄下一紀律委員會，於二零二一年十二月三日就執業會計師羅輝城先生（會員編號：A15863）沒有或忽略遵守、維持或以其他方式應用公會頒佈的專業準則，對他予以譴責。紀律委員會另命令由二零二二年一月十四日起，吊銷羅先生的執業證書，並在十五個月內不向其另發執業證書。此外，羅先生須繳付罰款 160,000 港元及紀律程序費用 4,943,123 港元。

羅先生為羅輝城會計師事務所的獨資經營者。該事務所曾審計一間私營公司截至二零一零年及二零一一年三月三十一 日為止，共兩個年度的財務報表。

羅先生在上述的審計中及其與該公司的專業關係下所作的行為均犯有缺失，因他未有：

(i) 獲取足夠證據，以支持其同意該公司採納公司條例第141D條，及中小型公司財務報告準則內的豁免條文作為編制財務報表的基礎。根據該等條例及準則，該公司因持有一間附屬公司而不能享有豁免；

(ii) 就一項投資的減值撥備出現的審計範圍限制，發出有保留的核數師意見；

(iii) 獲取充分適當的證據，以支持他接受該公司違反法定的披露要求。該等披露要求乃關於該公司為一間董事控制實體獲得的銀行融資所作出的資產抵押；

(iv) 分隔處理由該公司的一名股東兼董事轉移給他的資金，並作出充分調查，以確保該項資金轉移符合相關法規； 及

(v) 維持專業知識和技能水平，以確保該公司獲得稱職的專業服務。

公會經考慮所得資料後，根據《專業會計師條例》第 34(1)(a)條對羅先生作出控訴。

在紀律過程中，羅先生曾兩次申請司法覆核。 紀律程序曾暫停約五年，至司法覆核完成及被法院駁回為止。

紀律委員會裁定羅先生違反了 Hong Kong Standard on Auditing (「HKSA」) 250「Consideration of Laws and Regulations in an Audit of Financial Statements」, HKSA 701 「Modifications to the Independent Auditor's Report」, Code of Ethics for Professional Accountants (「Code of Ethics」) 第 270 條 「Custody of Client Assets」及 Code of Ethics 第 100 條中的「 Professional Competence and Due Care」的基本原則。

經考慮有關情況後，紀律委員會根據條例第 35(1)條對羅先生作出上述命令，其中包括一項加重責令，要求他全額承擔公會因其行為及其引致的延誤所產生的費用。 紀律委員認為羅先生的違規非常嚴重，因為該等違規顯示他對審計及專業道德準則，以及《公司條例》內關於編制及呈報財務報表的基本法則，均嚴重缺乏理解。 此外，羅先生在紀律程序中不斷變更的答辯，及因其阻撓性的舉動而導致程序嚴重延誤、浪費大量成本，及令公會需外聘大律師代表等，皆顯示他缺乏悔意及坦誠，因而構成加重因素。

香港會計師公會的紀律處分程序

香港會計師公會致力維持會計界的最高專業和道德標準。公會根據香港法例第 50 章《專業會計師條例》及紀律委員會訴訟程序規則，成立獨立的紀律委員會，處理理事會轉介的投訴個案。委員會一旦證明對公會會員、執業會計師事務所會員或註冊學生的檢控屬實，將會作出適當懲處。若答辯人未有提出上訴，紀律委員會的裁判將會向外公佈。

詳情請參閱：
http://www.hkicpa.org.hk/en/standards-and-regulations/compliance/disciplinary/

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關於香港會計師公會

香港會計師公會是根據《專業會計師條例》成立的法定機構，負責培訓、發展和監管本港的會計專業。公會會員逾 47,000 名，學生人數逾 17,000。

公會開辦專業資格課程，確保會計師的入職質素，同時頒佈財務報告、審計及專業操守的準則，以鞏固香港作為國際金融中心的領導地位。

CPA 會計師是一個獲國際認可的頂尖專業資格。公會是全球會計聯盟及國際會計師聯合會的成員之一，積極推動國際專業發展。

香港會計師公會聯絡資料：

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Proceedings No. D-12-0734C

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 Certified Public Accountants — COMPLAINANT

AND

Mr. Law Fei Shing (A15863) — RESPONDENT

DECISION

Disciplinary Committee:

Ms. POON, Suk Ying, Debora (Chairperson)
Mr. CHAN, Stephen
Ms. LAM, Po Ling, Pearl
Mr. KAN, Siu Lun, Philip
Ms. LAW, Elizabeth

Dates of Hearing: 25 and 26 January 2021 and 1 February 2021
Date of Decision: 3 August 2021

INTRODUCTION

1. The Respondent is the sole proprietor of F.S. Law & Co. ("**the Firm**"), which was the auditor of a Hong Kong company known as Chong Luen Hing

Garments Limited ("**CLH**") for the financial years ended 31 March 2009, 31 March 2010 and 31 March 2011.

2. At all material times, there were three shareholders of CLH, namely, Ms. Wu Wing Che Deven ("**Ms. Wu**"), Mr. Lee Kwong On ("**Mr. Lee**") and Mr. Johnny Alan Vorzimer. They held 60%, 20% and 20% of CLH's shares respectively. Ms. Wu and Mr. Lee were the only directors of CLH.

3. CLH held 100% ownership interest in a Mainland company known as Foshan Shunde Mao Nian Garments Limited (佛山市順德區茂年製衣有限公司) ("**the Factory**") which was established in the People's Republic of China.

4. On 13 November 2009, 22 November 2010 and 10 January 2012, the Firm issued auditor's reports signed by the Respondent on CLH's financial statements for the years ended 31 March 2009, 31 March 2010 and 31 March 2011 ("**the 2009 Financial Statements**", "**the 2010 Financial Statements**" and "**the 2011 Financial Statements**") respectively.

5. The complaints in these proceedings only concerned with the 2010 and 2011 Financial Statements.

6. There are 7 complaints which the Disciplinary Committee is requested to determine:-

   (1) The 1st and 2nd Complaints relate to the Respondent's concurrence with CLH's adoption of Section 141D of the Companies Ordinance (Cap. 32) ("**the Ordinance**") and the Small and Medium-sized Entity Financial Reporting Framework and Financial Reporting Standard ("**SME-FRF**") for preparing the 2010 and 2011 Financial Statements when CLH was not qualified to do so. The 1st and 2nd Complaints, according to the Complainant, are in the alternative:-

   (a) The 1st Complaint relates to the Respondent's alleged failure to

obtain sufficient appropriate audit evidence to substantiate CLH's adoption of Section 141D and the SME-FRF, in breach of HKSA 250.19 (for 2010) and HKSA 250.13 (for 2011); and

(b) The 2nd Complaint relates to the Respondent's alleged failure to prepare sufficient and appropriate audit documentation for his concurrence with CLH's adoption of Section 141D and the SME-FRF, in breach of HKSA 230.2 (for 2010) and HKSA 230.7 (for 2011).

(2) The 3rd Complaint relates to the Respondent's alleged failure to qualify his opinion on the 2010 and 2011 Financial Statements concerning a scope limitation in verifying the accumulated provision for impairment loss in respect of the investment in the Factory in the sum of HK$10,875,000 ("**the Impairment Provision**"), in breach of HKSA 701.18.

(3) The 4th and 5th Complaints relate to the Respondent's concurrence with the non-disclosure in the 2011 Financial Statements of securities given by CLH for banking facilities granted to CLH Group (HK) Limited ("**CGHK**"), a company in which Ms. Wu held a controlling interest. The 4th and 5th Complaints are in the alternative:-

(a) The 4th Complaint relates to the Respondent's alleged failure to obtain sufficient appropriate audit evidence to substantiate CLH's non-compliance with disclosure requirements under Section 161B of the Ordinance, in breach of HKSA 250.13; and

(b) The 5th Complaint relates to the Respondent's alleged failure to prepare sufficient and appropriate audit documentation for his concurrence with CLH's non-disclosure, in breach of HKSA 230.7.

(4) The 6th Complaint relates to the Respondent's alleged failure to segregate monies received from Ms. Wu on 13 January 2012 and to

make appropriate inquiries on the source of funds to ensure compliance with relevant laws and regulations, in breach of Section 270 of the Code of Ethics for Professional Accountants ("**the Code**").

(5) Lastly, the 7th Complaint relates to the Respondent's alleged failure to maintain professional knowledge and skill at the level required to ensure that CLH received competent professional service based on current developments in practice, legislation and techniques, in breach of Section 100.4(e) (for 2010) and 100.5(c) (for 2011) of the Code.

BURDEN AND STANDARD OF PROOF

7. The burden of proving the Complaints rests on the Complainant and the standard of proof in disciplinary proceedings is the civil standard, namely, on the balance of probabilities.

ADVERSE INFERENCE TO BE DRAWN

8. The Complainant asked the Committee to note that whilst the Respondent had put forward Ms. Wu as his factual witness to give evidence in the proceedings, the Respondent himself had chosen not to give evidence albeit that he had direct personal knowledge in respect of his own audit work of the 2010 and 2011 Financial Statements and his dealings with Ms. Wu regarding the RMB 2.2 million. This is a matter which the Committee is entitled to take into account when determining any facts relevant to the Complaints. In support of the said submission, the Complainant referred us to the Guidelines for the Chairman and the Committee on Administering the Disciplinary Committee Proceedings Rules (paragraph 11) and the Disciplinary Committee Proceedings Rules (paragraph 15) which provide that "if any party fails or refuses to make submissions or answer questions on any matter or issue, the Committee is entitled to draw an adverse inference against that party".

9. In response to this, the Respondent did not dispute that the Committee is so entitled to draw such adverse inferences but submitted that caution must

be exercised in (1) drawing inference of facts based on circumstantial evidence and (2) drawing adverse inferences against the Respondent on grounds that he has not elected to give evidence. In particular, the Committee should not merely choose what may be considered to be the more likely of two guesses if neither is properly justified by the primary facts found (**Nina Kung v Wang Din Shin** (2005) 8 HKCFAR 387 at paragraphs 185 – 186, see also **Natuzzi Spa v De Coro Ltd**., unreported, HCA 4166/2003, 16/6/2006 at paragraphs 11 – 12).

THE COMPLAINTS

1ST COMPLAINT

10. The 1st Complaint relates to the Respondent's alleged failure to obtain sufficient appropriate audit evidence to support his concurrence with CLH's adoption of Section 141D of the Ordinance and the SME-FRF in the 2010 and 2011 Financial Statements, in breach of HKSA 250.19 (for the audit of the 2010 Financial Statements) and HKSA 250.13 (for the audit of the 2011 Financial Statements).

11. For easy reference, HKSA 250.19 (issued June 2005) provides that:-

"Further, the auditor should obtain sufficient appropriate audit evidence about compliance with those laws and regulations generally recognized by the auditor to have an effect on the determination of material amounts and disclosures in financial statements. The auditor should have a sufficient understanding of these laws and regulations in order to consider them when auditing the assertions related to the determination of the amounts to be recorded and the disclosures to be made."

12. HKSA 250.13 (issued July 2009 and revised July 2010) provides that:-

"The auditor shall obtain sufficient appropriate audit evidence regarding compliance with the provisions of those laws and regulations generally recognized to have a direct effect on the determination of material amounts and disclosures in the financial statements (Ref: Para. A8)."

13. In order to qualify for reporting under the SME-FRF, CLH as a company incorporated under the Ordinance has to satisfy the criteria set out in Section 141D of the Ordinance. This is also expressly stated in paragraph 16 of the SME-FRF.

14. Section 141D(3) of the Ordinance provides that Section 141D would **not** apply to, inter alia, any private company which had a "subsidiary". As defined in Section 2(4)(a) of the Ordinance, a company would be **deemed to be a "subsidiary"** of another company if the other company:-

(i) controlled the composition of the board of directors of the first-mentioned company;

(ii) controlled more than half of the voting power of the first-mentioned company; or

(iii) held more than half of the issued share capital of the first-mentioned company (excluding any part of it which carries no right to participate beyond a specified amount in a distribution of either profits or capital).

15. The Complainant submits that the Factory was at all material times wholly owned by CLH, thus falling squarely within Section 2(4)(a)(iii) of the Ordinance and was clearly a "subsidiary" of CLH.

16. In fact, the status of the Factory as a subsidiary of CLH has been repeatedly and expressly acknowledged in the 2010 and 2011 Financial Statements: See Note 10 of the 2010 Financial Statements and Note 9 of the 2011 Financial Statements. Further, the Respondent has issued a qualified opinion for CLH's non-consolidation of its subsidiary's financial statements as required by Section 124(1). The Respondent stated that except for the failure to prepare financial statements in compliance with Section 124(1), the financial statements were considered to have been properly prepared in all material respects in accordance with the SME-FRF. In the Audit Working Papers for 2010 and 2011, the Respondent explained that

consolidated accounts could not be prepared because no accounts or other relevant information of the Factory could be obtained.

17. In the circumstances, the Complainant submits that CLH was not qualified under Section 141D of the Ordinance for reporting under the SME-FRF for the 2010 and 2011 Financial Statements. Yet, the Respondent concurred with CLH's adoption of Section 141D of the Ordinance and the SME-FRF for preparing the 2010 and 2011 Financial Statements and did not qualify his opinion in the auditor's reports in this respect.

18. In answer to the Complainant's above allegations, the Respondent put forward various representations or defences. In particular:-

(1) In his written representations dated 5 February 2013 ("**the February 2013 Representations**"), the Respondent stated that according to paragraph 4 of HKAS 27, a subsidiary was an entity controlled by another entity and that "control" meant "the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities". The Respondent claimed that CLH had no control over the Factory's financial and operating policy because CLH was unable to provide any accounts of the Factory. Accordingly, the Factory did not qualify as a subsidiary of CLH for the purposes of HKAS 27. Further, by reasons of (1) the agreement made by CLH's management and (2) the practice of CLH's former auditor in not preparing consolidated accounts, the Respondent did not object to CLH's purported reliance on Section 141D of the Ordinance.

(2) In his subsequent written representations dated 12 July 2013 ("**the July 2013 Representations**"), the Respondent contended that CLH did not have control over the Factory. First, the Respondent was told by Ms. Wu at the pre-audit meeting that she had no actual control over the Factory. She said that the legal representative of the Factory had his own way of running it. Second, CLH confirmed in the course of the audit that it was unable to provide any accounts of the Factory. The

Respondent stated that the two said reasons were reconfirmed in the final audit meeting and set out in the "Representation Letters" signed by all directors of CLH. Nevertheless, we note that the said "Representation Letters" were not exhibited to the Audit Working Papers nor produced by the Respondent in these proceedings.

That said, the Respondent did expressly acknowledge in the July 2013 Representations that "**it might not be entirely correct**" to apply Section 141D of the Ordinance as the basis of preparation of the 2010 and 2011 Financial Statements but it was the "**preference**" of the directors of CLH to do so. The Respondent found it unnecessary to qualify his opinion because the three shareholders of CLH, being the actual users of the 2010 and 2011 Financial Statements, already had the first-hand knowledge of the company's business and operation. None of them could have been misled by reason of the Respondent's unqualified opinion.

(3) It was contended in the Respondent's Case dated 16 April 2018 that a "subsidiary" under Section 141D(3) of the Ordinance is restricted to subsidiary companies formed and registered in Hong Kong. The Respondent cited the case of **Re Dejin Resources Group Co Ltd** [2015] 1 HKLRD 973 and submitted that since the Factory was incorporated in Mainland China, it is not a "subsidiary" for the purpose of Section 141D(3). As such, though the Respondent had previously stated through his solicitors that it might not have been entirely correct to apply Section 141D as the basis of preparation of the 2010 and 2011 Financial Statements, the Committee must form its independent view on whether a subsidiary within the meaning of Section 141D(3) of the Ordinance can be incorporated outside Hong Kong.

(4) In his Reply dated 10 May 2019, the Respondent contended that whether CLH adopted the SME-FRF had no material effect on the financial statements or the shareholders because the sole difference

between the SME-FRF and the Hong Kong Financial Reporting Standards ("**HKFRS**") is the deferred tax provision and that the shareholders had already agreed to apply Section 141D of the Ordinance and the SME-FRF.

(5) Lastly, the Respondent newly suggested in his oral opening submissions that the Complainant's interpretation of Section 2(4) of the Ordinance is inconsistent with the requirements in HKAS 27. The deeming provision in Section 2(4) was a presumption rebuttable by evidence that CLH had no control over the Factory. It was also contended that since the Complainant had never raised any factual dispute on the issue of CLH's control over the Factory, it cannot now suggest that the evidence on loss of control is inadequate or insufficient.

Discussion

Whether the Factory is a subsidiary and Relevance of HKAS 27

19. There is no dispute that CLH held 100% ownership in the Factory at the material times. By the clear wordings in Section 2(4)(a), the Factory is deemed to be a subsidiary. Accordingly, CLH shall not be entitled to rely on Section 141D to adopt the SME-FRF in preparing the 2010 and 2011 Financial Statements. The auditor's reports issued by the Respondent had failed to reflect such non-compliance. However, the Respondent relied on HKAS 27 and argued that the Factory is not a subsidiary of CLH by reason that CLH had no control over the Factory.

20. The SME-FRF is designed to allow small and medium sized entities to adopt a simplified reporting framework. A company incorporated under the Ordinance would qualify for reporting under the SME-FRF if it satisfies the criteria set out in Section 141D. The simplified reporting framework does not apply to a private company which has a **subsidiary**: Section 141D(3).

21. HKAS 27, on the other hand, is the accounting standard to be applied in the preparation of **consolidated and separate financial statements** for a

group of entities under the control of a parent (See HKAS 27 (December 2007: para 1) and HKAS 27 (Revised December 2008: para 1)). The statutory obligation to lay group accounts by a company with subsidiaries is provided in Section 124 of the Ordinance. It is plain that the 2010 and 2011 Financial Statements are **not** prepared under Section 124 of the Ordinance.

22. Ms. Tong for the Complainant submitted that the distinction between the SME-FRF relating to Section 141D on one hand and HKAS 27 relating to Section 124 on the other hand is highlighted by the fact that the definitions of "subsidiary" in Sections 141D and 124 are different. A "subsidiary" for the purposes of Section 141D is defined in Section 2(4). For Section 124, a "subsidiary" or "subsidiary company" shall be deemed to include a "subsidiary undertaking" and which, according to Section 2B(1) and paragraph 2 of the Twenty-third Schedule of the Ordinance, would be subject to dominant influence by its parent.

23. We agree with Ms. Tong's submission that the difference of definition of "subsidiary" in Sections 141D and 124 is consistent with the legislative intent behind the Companies (Amendment) Ordinance 2005. The amendments changed the definition of "subsidiary" specifically for the purposes of provision of group accounts under Section 124, which were intended to make it more closely align with International Accounting Standards ("**IASs**"). As seen from the Legislative Council Brief for Companies (Amendment) Bill 2004 (particularly at paragraphs 2 and 4(a)), those changes were specifically stated **not** applied to Section 141D, which retained the old definition. The said Legislative Council Brief provides:-

"**JUSTIFICATIONS**

2. Section 124 of the Companies Ordinance (CO) requires a company having subsidiaries to lay before the company in general meeting accounts dealing with the state of affairs and the profit and loss of the company itself and its subsidiaries. These accounts are known as group accounts. The **definition of the term "subsidiary" in section 2(4) which applies to accounting and other provisions in the CO is narrower than that**

adopted in the IASs. We consider it necessary to amend the statutory definition for the purposes of group accounts to make it more closely aligned with the IASs. This would ensure that under the law, the group accounts would better reflect the financial position of the company. The definition of "subsidiary" for purposes other than the preparation of group accounts would not be affected".

THE BILL

4. The main provisions are as follows:-

   (a) In relation to the **definition of "subsidiary" for the purposes of group accounts**, clause 2 and the new Twenty-third Schedule added under clause 18 introduce new terms of "subsidiary undertaking", "parent company" and "parent undertaking". The term "undertaking" includes body corporates, partnerships and other unincorporated associations. This is an important improvement to the existing provision where a subsidiary of holding company must be a body corporate. Without this amendment, assets and liabilities of partnerships and unincorporated associations within a group can be kept out of the group accounts, even when substantially all the risks and rewards are retained in the group. The "right to exercise a dominant influence over another undertaking" (defined as the right to give directions with respect to the operating and financial policies of that other undertaking which its directors will be obliged to comply with) would be added to the existing tests of determining the existence of a parent/subsidiary relationship; ..."
   [emphasis added]

24. As such, we consider that the definitions of "subsidiary" in Sections 2(4) and 124 are intended to be different and for good reasons as stated in the Legislative Council Brief. We take the view that the SME-FRF relates to Section 141D and its underlying objective, namely, to allow simplified reporting framework, is different from HKAS 27 which relates to Section 124 on the preparation of group accounts. As such, we agree with Ms. Tong

that it is wholly irrelevant to refer to HKAS 27 and the concept of "control" therein in interpreting the meaning of "subsidiary" in the context of the SME-FRF and Section 141D.

25. In any event, we consider that the definitions of "subsidiary" in any accounting standards including HKAS 27 cannot override the statutory definition of "subsidiary" provided in Section 2(4) of the Ordinance. We consider that the concept of "control" in HKAS 27 is irrelevant in determining if a company is a "subsidiary" under Section 141D and the applicability of the SME-FRF. In the circumstances, the Respondent's evidence from Ms. Wu and Mr. Chen He ("**Mr. Chen**") (see paragraph 30 below) concerning loss of control by CLH over the Factory as well as the report compiled by Mr. Chen are irrelevant to the 1st Complaint.

26. Whether a company is a subsidiary is a question of both law and facts. On the issues of law, evidence of common practice of professional accountants would not be wholly relevant in assisting the Committee to decide whether a company is a subsidiary. On the issues of facts, the Committee will of course consider all the available facts and evidence peculiar to the case. It would be difficult to imagine how the evidence of common practice of professional accountants would override the particular facts and circumstances of the case in determining if a company is a subsidiary. In any event, if it is a party's case that such evidence of common practice of professional accountants would be relevant and necessary to be adduced for the purpose of deciding whether a company is a subsidiary, that party should seek to adduce such evidence to be given by an accounting expert. In the present case, the Respondent had elected not to adduce such evidence. Accordingly, he is not entitled to introduce such evidence by way of counsel's submissions and we shall not take into account of those submissions.

Relevance of the loss of control

27. The Complainant submits that even if there is any legal basis to apply the concept of "control" under HKAS 27, there is still a lack of evidence to show

that CLH had lost control over the Factory.

28. Mr. Lai for the Respondent submitted, inter alia, that the Complainant rests its case on the 1st Complaint solely on the basis of its erroneous interpretation of Section 2(4)(a)(iii). Mr. Lai said that throughout the disciplinary proceedings, it has never advanced an alternative case that in any event there was no or insufficient evidence of loss of control by CLH over the Factory. The Complainant also took the stance that there was no factual dispute in the case. It thus shows that CLH's control or the lack thereof over the Factory does not form part of the Complainant's case insofar as the 1st Complaint is concerned. Mr. Lai submitted that if the Respondent's interpretation of Section 2(4)(a)(iii) prevails, the 1st Complaint must be dismissed.

29. It was the Respondent who raised the issue of "control" as a material factual dispute and argued that the Factory cannot be regarded as a subsidiary of CLH by reason of the lack of control by CLH. This was why the Respondent called Ms. Wu and Mr. Chen to give evidence in the proceedings. It is one thing the Complainant takes the stance that "control" is irrelevant in determining whether the Factory is a subsidiary of CLH, it is quite another thing to suggest that the Complainant, given its stance, is not entitled to challenge or dispute whatever evidence the Respondent shall lead on the issue of control. In all fairness, we consider that upon the Committee receiving evidence adduced by the Respondent on the issue of "control", it would be open for the Complainant to deal with those evidence by way of cross-examining the Respondent's witnesses to test their credibility and making submissions where appropriate.

Respondent's evidence of loss of control

30. The Respondent submits that in any event, there is ample evidence to show that CLH had no control over the Factory at the material time. As such, the Factory cannot be taken as a subsidiary of CLH. The Respondent emphasized the following:-

(1) Mr. Lee assumed the position of legal representative of the Factory at the material time from about June 2006 or at least from August 2007;

(2) Mr. Chen, the Chinese lawyer called by the Respondent, gave unchallenged expert evidence that a legal representative of a company enjoyed extensive powers of the affairs of the company;

(3) Mr. Chen said that Mr. Lee continued to be the "superficial agent" of the Factory capable of transacting business binding the Factory unless and until a change of legal representative is completed and/or the counter-party having been notified Mr. Lee's ceasing to have such authority.

(4) The Factory's financial statements have never been made available to CLH throughout all relevant years. The inability to obtain such information demonstrated that at the material time CLH had no control over the financial matters of the Factory. The Factory's financials only came into light when Mr. Lee produced the same to the Institute.

(5) Ms. Wu gave evidence that Mr. Lee had been in control of the Factory in all respects to the exclusion of CLH, including the refusal to sign the agreement ("股權轉讓合同") against the direction of CLH which had approved and signed the same.

31. The Respondent contended that the above evidence clearly showed the lack of control of CLH over the Factory and the Complainant had failed to rebut. Accordingly, the Complainant had failed to prove its case and thus the 1st Complaint should be dismissed.

32. In Mr. Lai's submissions, it was not expressly stated if there is any threshold and if so, what is the level of threshold which the Respondent's evidence on "control" should meet. However, HKAS 27, which the Respondent heavily relies upon, has clearly set out the threshold: Paragraph 13 of HKAS 27 on the "scope of consolidated financial statements" provides that "**control is**

presumed to exist when the parent owns, directly or directly through subsidiaries, more than half of the voting power of an entity **unless, in exceptional circumstances, it can be clearly demonstrated that such ownership does not constitute control**" (emphasis added). In other words, the Respondent has to establish that there were exceptional circumstances showing that CLH had lost control over the Factory. We note Ms. Tong's submissions that even if HKAS 27 should apply, the Respondent's evidence fell far short of establishing the same.

33. Simply for the sake of completeness, we shall deal with the evidence given by the Respondent's witnesses on the issue of control.

34. In essence, Ms. Wu's evidence can be highlighted as follows:-

(1) All shareholders of CLH including Ms. Wu herself had allowed Mr. Lee to operate the Factory since about July 2005 to some time before 2010. According to Ms. Wu, Mr. Lee was doing what he had done all along. Ms. Wu never made inquiries as to the affairs of the Factory. She left it to the hands of Mr. Lee.

(2) There used to be a legal representative of the Factory known as Mr. Wong. Following his passing away in about July 2005, the shareholders of CLH had not discussed nor passed any resolution to appoint a new legal representative in place of the late Mr. Wong.

(3) Thereafter, Mr. Lee procured himself to be appointed as the Factory's new legal representative on about 30 June 2006. Ms. Wu said, however, that the said appointment was unlawful because Mr. Lee had forged documents to effect his appointment. That said, Ms. Wu represented that she was legally advised that there was no use to report the forgery.

(4) At a pre-audit meeting in about July to August 2010, Ms. Wu told the Respondent that she had no control over the Factory because Mr. Lee as the legal representative of the Factory had his own way of running the Factory.

(5) Ms. Wu confirmed that **the only reason** she gave the Respondent as to why CLH purportedly lost control over the Factory was that Mr. Lee had **refused to sign an agreement** to enable CLH to sell the Factory. As a result, CLH was unable to complete with the deal. Ms. Wu said she did follow up on this matter once with the Head of the Factory but was told that the deal could not be proceeded as Mr. Lee refused to sign. As such, no further follow up action was taken and Ms. Wu considered that there was nothing she could do about it.

(6) Ms. Wu confirmed that she requested the Respondent to adopt the SME-FRF in 2010. Since CLH had lost control over the Factory and most of CLH's business had been transferred to CGHK, Ms. Wu requested the Respondent to adopt the simplified accounting standards for the audit report in 2010. Based on her instructions, Ms. Wu believed that the Respondent was satisfied that CLH was qualified for adopting such simplified accounting standards in 2010.

(7) Ms. Wu said there was no documentary proof evidencing the agreement between the shareholders of CLH regarding the change in accounting standards to simplified accounting standards in 2010. The said agreement was reached orally during a chat and she had never informed the Respondent of this agreement.

(8) Ms. Wu said she did not present any special request to the Respondent urging him to adopt simplified accounting standards for the audit report in 2011.

(9) Sometime in 2010, Ms. Wu was informed by the Mainland lawyers and the Administration for Industry and Commence ("**AIC**") that Mr. Lee could be replaced, although not immediately. In the same year, she requested the Mainland lawyers to remove Mr. Lee.

(10) However, nothing really happened until 2012 when CLH's shareholders passed a resolution to remove Mr. Lee as the Factory's legal representative.

(11) Though Mr. Lee did not surrender the Factory's business licence and the seal, the Head of the Factory was able to retrieve both the licence

and the seal from the office of the Factory while Mr. Lee was away from office and to bring them both to AIC.

(12) Within a short period of time, the process of removing Mr. Lee was completed without any significant difficulty or complicated formalities. On 12 July 2012, he was formally removed from the office of the Factory's legal representative.

35. Before turning to Mr. Chen's evidence, we note it is the Respondent's submissions that the Factory's financial statements had never been made available to CLH throughout the years from about 2006/2007 to 2010/2011. The Respondent submitted that the inability to obtain such information vividly demonstrated that at the material times CLH had no control over the financial matters of the Factory. These submissions, however, are not supported by Ms. Wu's evidence. Ms. Wu actually never asked about the affairs of the Factory or made inquiries relating to the Factory's operations. Ms. Wu never said in her evidence that CLH had ever attempted to obtain or failed to obtain financial information from the Factory.

36. The evidence of Mr. Chen can be highlighted as follows:-

(1) Mr. Chen confirmed that he tendered his report on the basis of information provided by the Respondent and/or his solicitors, namely, that Mr. Lee would not listen to the arrangement, and he was not willing to surrender the seal and the business licence of the Factory.

(2) Mr. Chen agreed that the board of a company has the highest authority. It may use its powers to remove the legal representative of the company.

(3) In order to effect a change of legal representative, a company is required by Article 27 of 《中华人民共和国企业法人登记管理条例》to submit (i) an application form signed by the legal representative (which Mr. Chen considered that either or both of the new and existing legal representative should sign thereon but he accepted under cross-

examination that the relevant regulations actually did not require signature of the existing legal representative); (ii) the relevant resolution in accordance with the PRC Companies Law (such resolution, according to Mr. Chen, could be a Board resolution or a shareholders' resolution depending on the articles of association of the company); and (iii) any other items required by the AIC.

(4) Mr. Chen stated in his report that the AIC would only accept an application for change of legal representative if the company could provide, inter alia, an application form affixed with the official seal of the company and the original of the business licence of the company. However, under cross-examination, he was unable to cite any legal provision in support of his opinion that (i) the application form had to be affixed with the official seal of the company and (ii) the original of the company's business licence has to be submitted.

(5) Mr. Chen considered that there was no way to remove Mr. Lee from the office of the Factory's legal representative if he refused to cooperate. There were also no effective remedies in the PRC law for a company to retrieve its seal and business licence if the legal representative insisted on retaining them or where the legal representative had been removed. Mr. Chen opined that the only viable solution would be for the parties to negotiate and reach settlement. If no settlement agreement can be reached, the company may have to be wound up.

(6) Mr. Chen opined that it was not possible for a company to apply for cancellation and re-issue of company seal and business licence because it would appear extraordinary. However, Mr. Chen was unable to cite any legal authority in support of his view.

37. We have carefully considered the evidence of Ms. Wu and Mr. Chen and we are not satisfied that their evidence are sufficient to show that there were exceptional circumstances evidencing that there was loss of control by CLH over the Factory. Ms. Wu gave evidence that all the shareholders of CLH

had allowed Mr. Lee to operate the Factory from about July 2005 to some time before 2010. She herself never made inquiries as to the Factory's affairs. In 2006, following the decease of the former legal representative of the Factory, Mr. Lee procured himself to be appointed as the new legal representative of the Factory but his appointment was said to have been effected by forged documents. Strangely, Ms. Wu said she was legally advised that it would be of no use to report the matter to the authorities. No follow up action whatsoever was taken by Ms. Wu or the other shareholder of CLH against Mr. Lee as a result of such unlawful appointment. Mr. Lee was allowed by Ms. Wu and the other shareholder to remain in the office of the legal representative of the Factory for as long as about 6 years until 2012. The only reason which Ms. Wu told the Respondent for CLH's loss of control over the Factory was due to Mr. Lee's refusal to sign the agreement for sale of the Factory, which was against the plan of CLH. However, Ms. Wu only followed up the matter once by talking to the Head of the Factory. Ms. Wu listened to the Head of the Factory and readily accepted that there was nothing she could do. Neither Ms. Wu nor the other shareholder had followed up the matter directly with Mr. Lee so as to ask him to sign the agreement as planned. Neither Ms. Wu nor the other shareholder had turned to the potential buyer to see if the buyer was still interested in the transaction or if anything could be done to salvage the deal. According to Ms. Wu, she had inquired her Mainland lawyers and AIC about the possibility of removing Mr. Lee in 2010. However, Ms. Wu and the other shareholder had been dilatory in taking any follow up action on the matter. It was only until 2012 when a shareholders' resolution was finally passed to have Mr. Lee removed. Mr. Lee was finally removed in July 2012. We also note Ms. Wu's evidence that whilst Mr. Lee was alleged to have failed and/or refused to surrender the Factory's seal and business licence, the Head of Factory had no difficulty in retrieving these items from the Factory office when Mr. Lee was away from office.

38. Having considered Ms. Wu's evidence as a whole, we are of the view that the way in which Ms. Wu and the other shareholder of the Factory conducted

themselves in response to Mr. Lee's alleged unlawful appointment and wilful refusal to sign the agreement did not show any loss of control by CLH over the Factory. These evidence only show delegation or maladministration on the part of CLH over the Factory. To put simply, CLH had demonstrated its indifference on these matters and chose not to take any prompt action about it. Any claim of Mr. Lee controlling the Factory in all aspects to the exclusion of CLH is clearly overstated. Further, Ms. Wu never said in her evidence that CLH had ever tried to obtain financial information from the Factory and the Factory refused to pass CLH such information. Any suggestion that CLH had lost control over the Factory as a result of its inability to obtain such financial information is without merit and not supported by evidence. Taking Ms. Wu's evidence to the highest, we do not consider that there existed any exceptional circumstances which showed that there was loss of control of the Factory by CLH.

39. Mr. Chen's view that there was no effective way to remove Mr. Lee as the legal representative of the Factory if he refused to cooperate was wholly against common sense and unsupported by law. Similarly, his view that there were no effective remedies under the PRC law for a company to retrieve its seal and business licence if the legal representative insisted on retaining them or where the legal representative was removed also defies common sense and is not supported by any statutory provision or authority. In the course of cross-examination, Mr. Chen adjusted his evidence time and again when being confronted that the relevant legal provisions did not support his view. In any event, we consider Mr. Chen's evidence as unhelpful, unreliable and it adds nothing to the Respondent's evidence on the point of "loss of control".

40. In the premises, we consider that the Respondent's claim of loss of control by CLH over the Factory is without merit and in any event, unsubstantiated by evidence.

41. In fact, the Respondent's claim of loss of control by CLH over the Factory by virtue of HKAS 27 is squarely contradicted the information contained in

the 2010 and 2011 Financial Statements where the Respondent expressly acknowledged that the Factory was a subsidiary: Note 2(j) of the 2010 and 2011 Financial Statements clearly provides that subsidiaries are "all entities (including special purpose entities) over which **the Company has the power to govern the financial and operating policies** so as to obtain benefits from its activities, generally accompanying a shareholding of more than half of the voting rights." [emphasis added] In the 2010 and 2011 Financial Statements (at Note 10 and Note 9 respectively), the Factory was expressly recognized as the Company's only subsidiary. With such clear and unequivocal recognition in the 2010 and 2011 Financial Statements, we cannot see how the Respondent can argue that the Factory was not a subsidiary of CLH by reason of CLH's loss of control over the Factory. We agree with Ms. Tong for the Complainant that had the Respondent considered that the Factory was not a subsidiary due to loss of control by CLH, the Factory should have been re-designated as an investment in the accounts, with an impairment provision to reflect that CLH had no control over the Factory. This has not been done. Quite the contrary, the Respondent concurred with the recognition of the Factory as a subsidiary of CLH in the two Financial Statements and gave a qualified opinion for CLH's non-consolidation of the Factory's financial statements as required by Section 124(1). It simply defies common sense and logic for the Respondent to contend in these proceedings that he had truly assessed and concluded that CLH had no control over the Factory at the time of his audits of the 2010 and 2011 Financial Statements.

Respondent's ex post facto arguments

42. Other than the main defence of "loss of control", the Respondent has raised other defences or arguments including that (1) a "subsidiary" under Section 141D must be registered in Hong Kong so that Section 141D does not apply to the Factory (raised in 2018); (2) the SME-FRF has no impact on financial statements save for deferred tax provision (raised in 2019); and (3) Section 2(4)(a) created a rebuttable presumption and such presumption has been rebutted by the Respondent's evidence of "loss of control" (raised in opening

submissions). Having carefully considered the submissions made by both parties, we agree with the submissions made by Ms. Tong and have come to the view that all such defences are without merit.

43. In this connection, we note that the said defences were not recorded contemporaneously in the Audit Working Papers. Rather, they changed and evolved over time. For instance, contrary to his express acknowledgement in the 2010 and 2011 Financial Statements that the Factory was a subsidiary of CLH, the Respondent claimed in the written representations in 2013 that there was loss of control by CLH over the Factory. It was also expressly acknowledged that it might not have been entirely correct to apply Section 141D of the Ordinance as the basis of preparation of the 2010 and 2011 Financial Statements. Yet, in 2018, the Respondent contended in his written case that the expression "subsidiary" under Section 141D(3) should be restricted to subsidiary companies formed and registered in Hong Kong and as such the Factory is not a subsidiary of CLH. Then in 2019, the Respondent contended that whether CLH adopted the SME-FRF or not had no material effect on the financial statements or the shareholders. Having carefully considered the Respondent's said defences and all the relevant circumstances, we are of the view that the defences are after-thoughts made by himself and/or his legal advisers for the purposes of the proceedings. As Ms. Tong rightly submitted, these ex post facto cannot exonerate the Respondent from liability.

44. Pursuant to HKSA 230.2 (February 2006 version) and 230.7 (July 2010 version), an auditor should prepare audit documentation on a timely basis. He must prepare contemporaneous records of the audit procedures performed, relevant audit evidence obtained, significant matters arising during the audit, analyses, conclusions and significant professional judgments he made during his audit. All these would demonstrate the basis of his audit opinion at the time when the opinion was made.

45. As in the case of **Registrar of the Hong Kong Institute of Certified Public Accountants v Chan Bing Chung** [2018] HKCA 158, the Court of Appeal

held that ex post facto arguments cannot exonerate the appellant's omission to perform his duties in the past. The court held that the appellant's responses which evolved over time also displayed a degree of lack of candour in responding to his professional governing body (Paragraphs 28.4 and 35.2 of the Judgment).

46. In the circumstances, we consider that the Respondent has failed or neglected to observe, maintain or otherwise apply a professional standard, namely, HKSA 250 in his audits of the 2010 Financial Statements and 2011 Financial Statements as a result of his concurrence with CLH's adoption of Section 141D of the Ordinance and the SME-FRF for preparing its financial statements when CLH was not qualified to do so given that it had a subsidiary. We are satisfied that the Complainant has proved the Respondent's breach of HKSA 250.19 (for the audit of the 2010 Financial Statements) and HKSA 250.13 (for the audit of the 2011 Financial Statements).

2ND COMPLAINT

47. The 2nd Complaint concerns the Respondent's failure in the audits of the 2010 and 2011 Financial Statements to prepare sufficient and appropriate audit documentation as to the basis and reasons for concurring with CLH's adoption of Section 141D of the Ordinance and the SME-FRF, thereby in breach of HKSA 230.2 (to be read in light of HKSA 230.9 and 230.16) (for the audit of the 2010 Financial Statements) and HKSA 230.7 (to be read in light of HKSA 230.8 and 230.10) (for the audit of the 2011 Financial Statements). For the sake of easy reference, the relevant provisions in HKSA 230 are reproduced herein below:-

For the audit of the 2010 Financial Statements

HKSA 230 (issued February 2006)

HKSA 230.2

"The auditor should prepare, on a timely basis, audit documentation that provides:-

(a) A sufficient and appropriate record of the basis for the auditor's report;

and

(b) Evidence that the audit was performed in accordance with HKSAs and applicable legal and regulatory requirements."

HKSA 230.9

"The auditor should prepare the audit documentation so as to enable an experienced auditor, having no previous connection with the audit, to understand:-

(a) The nature, timing, and extent of the audit procedures performed to comply with HKSAs and applicable legal and regulatory requirements;

(b) The results of the audit procedures and the audit evidence obtained; and

(c) Significant matters arising during the audit and the conclusions reached thereon."

HKSA 230.16

"The auditor should document discussions of significant matters with management and others on a timely basis."

For the audit of the 2011 Financial Statements

HKSA 230 (issued June 2009, revised July 2010)

HKSA 230.7

"The auditor shall prepare audit documentation on a timely basis. (Ref: Para. A1)"

HKSA 230.8

"The auditor shall prepare audit documentation that is sufficient to enable an experienced auditor, having no previous connection with the audit, to understand: (Ref: Para. A2 – A5, A16 – A17)

(a) The nature, timing, and extent of the audit procedures performed to comply with the HKSAs and applicable legal and regulatory requirements; (Ref: Para. A6 – A7)

(b) The results of the audit procedures performed, and the audit evidence obtained; and

(c) Significant matters arising during the audit, the conclusions reached thereon, and significant professional judgments made in reaching those conclusions. (Ref: Para. A8 – A11)."

HKSA 230.10

"The auditor shall document discussions of significant matters with management, those charged with governance, and others, including the nature of the significant matters discussed and when and with whom the discussions took place. (Ref: Para. A14)"

Discussion

48. As it is rightly pointed out by Ms. Tong, it was a significant matter for the Respondent to record in the audits of the 2010 and 2011 Financial Statements the basis and reasons for his concurrence with CLH's adoption of Section 141D and the SME-FRF. This is particularly so when the two Financial Statements specifically recognized that the Factory was wholly-owned by CLH. However, the Audit Working Papers did not document any reason for the Respondent's said concurrence and for not qualifying his opinion in this respect in the auditor's reports. No compliance checklist can be found in the Audit Working Papers to show that the Respondent had considered if CLH had duly complied with the relevant laws and regulations.

49. On the available evidence, there can be no dispute that none of the considerations purportedly taken into account by the Respondent such as the alleged loss of control by CLH over the Factory, the applicability of the definitions of "subsidiary" and "control" under HKAS 27, the definition of "subsidiary" under Section 141D were documented in the Audit Working Papers. Instead, the Respondent expressly acknowledged in the February 2013 Representations that his opinion or qualifications to or basis of such opinion "**could have been more clearly expressed by way of notes in CLH's audited financial statements**." He also agreed in the July 2013 Representations that **appropriate explanatory notes, if included in the auditor's reports, "would provide a clearer and more complete picture"**.

50. Insofar as the 2nd Complaint is concerned, we note that the Respondent's only defence was contained in the Respondent's Case, namely, that whether the Factory is a subsidiary within the meaning of Section 141D(3) is a matter of law, and hence audit evidence is not required to, and in any event cannot resolve the issue.

51. However, there is nothing in the clear wordings of HKSA 230 which limited the scope of an auditor's duty as suggested by the Respondent. As provided by HKSA 230.2 (for the audit of the 2010 Financial Statements) and HKSA 230.5 (for the audit of the 2011 Financial Statements), it is the objective of the auditor to prepare documentation that provides, inter alia, evidence that the audit was planned and performed in accordance with HKSAs and applicable legal and regulatory requirements. HKSA 230.9 (for the audit of the 2010 Financial Statements) and HKSA 230.8 (for the audit of the 2011 Financial Statements) further stated that the auditor should prepare the audit documentation such that an experienced auditor having no previous connection with the audit would understand, inter alia, the nature, timing, and extent of the audit procedures performed to comply with HKSAs and applicable legal and regulatory requirements, and significant matters arising during the audit and the conclusions reached thereon. We agree with Ms. Tong's submissions that the conflicting and evolving explanations put forward by the Respondent only show the inadequacy of audit documentation in his audits of the 2010 and 2011 Financial Statements and this would make it impossible for any experienced auditor to understand the basis of the Respondent's opinion.

52. In his closing submissions, Mr. Lai for the Respondent repeated his arguments made in relation to the 1st Complaint by reason that the premise of the 1st Complaint is similar to that of the 2nd Complaint. We have already indicated above that we do not accept Mr. Lai's submissions made in relation to the 1st Complaint. Based on the available evidence, we are satisfied that the Respondent had failed to prepare in the audits of the 2010 and 2011 Financial Statements sufficient and appropriate audit documentation as to

the basis and reasons for his concurrence with CLH's adoption of Section 141D and the SME-FRF as required by HKSA 230.

53. In his closing submissions, Mr. Lai submitted for the very first time that, without prejudice to the Respondent's submissions which had already been made under the 1st Complaint, expert evidence is required when the Committee considers a complaint concerning compliance with HKSA 230 because such complaint must be considered from the perspective of an "experienced auditor". Under HKSA 230, "sufficient and appropriate" record would be required to show the basis for the auditor's opinion and such sufficiency and appropriateness of audit documentation shall be judged by reference to the standard of an "experienced auditor". Without expert evidence, the Committee shall not have the appropriate yardstick to judge whether the Respondent has failed to comply with HKSA 230 from the perspective of an experienced auditor. In the premises, the 2nd Complaint should be dismissed. Alternatively, it is said that the Respondent had in the audit working papers documented the lack of financial statements of the Factory. Such documentation has already provided a basis that CLH did not have control over the Factory and hence the Factory should not be considered a subsidiary of CLH. On this basis, therefore, the 2nd Complaint should be dismissed.

54. The Respondent's point that expert evidence should have been adduced for the purposes of the 2nd Complaint was only raised in his closing submissions. We agree with Ms. Tong that this is highly undesirable as the Complainant is entitled to know the Respondent's case in advance. In any event, the Committee is fully aware that it was the Respondent himself who chose not to file any expert evidence. So now it is not up to the Respondent to say that there was no expert evidence adduced to assist the Committee. Furthermore, the Committee is tasked to consider all the available evidence and circumstances of the case and apply common sense and independent judgment in deciding the disputed issues and make findings of fact. As in the case of **Kennedy v Cordia Services LLP** [2016] UKSC 6, the English Supreme Court held that even in cases where expert witnesses were called,

the expert assistance did not extend to supplanting the court as the decision-maker. The fact-finding judge cannot delegate the decision-making role to the expert. Therefore, even if experts were called in these proceedings, the Committee cannot simply accede to the experts' views and defer their own judgment because we are tasked to decide the ultimate questions framed in the complaints. It shall not be the experts' job to perform such tasks.

55. Whilst there was no expert evidence adduced herein for the purpose of the 2nd Complaint, we do not agree that without the benefit of having expert evidence from an experienced auditor the Committee would be handicapped in deciding whether the Respondent had breached HKSA 230. The available evidence had already demonstrated clearly that the Respondent had failed to comply with HKSA 230. The Respondent's failure in the Audit Working Papers to state the reasons or basis for his concurrence to adopt Section 141D and the SME-FRF is so obvious that it does not require any auditing expertise to find that the Respondent's failure to comply with HKSA 230 is proved.

56. Turning to the Mr. Lai's contention that the Respondent had already documented in the audit working papers the lack of financial statements of the Factory and that such documentation should be taken as having provided a basis as to why CLH had no control over the Factory, thereby supporting that the Factory is not a subsidiary of CLH. We are unable to accept such contention. The fact is that the Respondent had not documented in the Audit Working Papers as to any alleged loss of control, the reasons why the Factory should not be regarded as a subsidiary; and the reasons why the Respondent nevertheless concurred with CLH's adoption of Section 141D and the SME-FRF. It should be remembered that it was the Respondent who had expressly accepted the status of the Factory as a subsidiary of CLH in both the 2010 and 2011 Financial Statements by issuing a qualified opinion in the auditor's reports on the non-preparation of consolidated financial statements. It is simply not acceptable for the

Respondent to now say that the Factory was not a subsidiary of CLH due to loss of control on the part of CLH. If the Respondent had really considered that CLH was qualified to adopt Section 141D and the SME-FRF, he should have properly documented the basis and reasons supporting his conclusion in the Audit Working Papers. However, no such contemporaneous record could be found. In the premises, we reject Mr. Lai's contention and take the view that the 2nd Complaint has been proved against the Respondent.

3RD COMPLAINT

57. The 3rd Complaint concerns the Respondent's alleged failure in the 2010 and 2011 Financial Statements to express a qualified opinion relating to the scope limitation in assessing the Impairment Provision, in breach of HKSA 701.18.

58. For easy reference, HKSA 701.18 (at HKSA 701 issued October 2006) provides:-

"Where there is a limitation on the scope of the auditor's work that requires expression of a qualified opinion or a disclaimer of opinion, the auditor's report should describe the limitation and indicate the possible adjustments to the financial statements that might have been determined to be necessary had the limitation not existed."

59. The Complainant submits that in order to properly assess the Impairment Provision, the Respondent should compare the carrying amount of the Factory with its recoverable amount, i.e. the higher of the Factory's fair value less costs to sell and its value in use. Without the relevant financial information of the Factory, it is unlikely that an assessment could be properly done.

60. In order to understand how the said "Impairment Provision" came out, it may be useful to go to the 2006 Financial Statements of CLH as a starting point.

61. The 2006 Financial Statements were audited by the former auditor of CLH.

In the Notes to the 2006 Financial Statements, the principal accounting policies relating to subsidiary companies (paragraph 2(c) on p. 582) were stated as follows:-

"Subsidiary companies are those companies in which the company holds more than 50% of the equity capital as long term investment or control more than half of the voting power. The investment in subsidiary companies is stated at cost less provision for diminution in value where appropriate... **The investment cost are written off over the period of 120 months according to mutual agreement between the parties**" [emphasis added].

62. Since the investment cost was expressly stated to be "written off" over the period of 120 months (i.e. 10 years), a sum of HK$1,500,000 representing one-tenth of the investment cost of HK$15,000,000 was written off every year. It is clear that the concept of impairment had not yet come into play. As seen from paragraph 8 on "Interest in Subsidiary Company" of the same Notes (p. 589), the investment cost was written off as follows:-

	2006	**2005**
	HK$	HK$
Unlisted investment, at cost	15,000,000	15,000,000
Unlisted investment **written off**		
At 31.03.2005	6,375,000	4,875,000
Addition	1,500,000	1,500,000
At 31.03.2006	**7,875,000**	**6,375,000**

63. In the 2007 Financial Statements (p. 595), the former auditor expressed a qualified opinion in relation to, inter alia, the underlying value of the investment. It was stated that in the absence of audited accounts of the subsidiary, the then auditor was unable to ascertain the underlying value of the investment although an aggregate **amortization** of cost of the investment amounting to HK$9,375,000 have been effected up to the balance sheet date. It is common ground that "amortization" is a concept similar to depreciation and the amount of aggregate amortization of the

investment cost stated in the said qualified opinion was in line with the then accounting policy whereby one-tenth of the investment cost was to be written off every year.

64. In the Notes to the 2007 Financial Statements (p. 604, at paragraph 2(c)), the accounting policy relating to subsidiary companies was stated as follows: "A subsidiary is entity over which the company directly or indirectly controls more than half of the voting power, or otherwise has the power to govern the financial and operating policies of the entity so as to obtain benefits from its activities." Interestingly, there was no more mention that the investment cost was to be written off over the period of 10 years.

65. In the 2008 Auditor Report (p. 617), the former auditor gave his qualified opinion in respect of the underlying value of the investment as follows: "... in the absence of audited accounts of the subsidiary, we are unable to ascertain the underlying value of the investment although an aggregate **amortization of cost** of the investment amounting to HK$10,875,000 have ben effected up to balance sheet date." As such, it can be seen that since one-tenth of the investment cost in the sum of HK$1,500,000 was written off every year, the aggregate amortization of cost had amounted to the said sum of HK$10,875,000 by 2008.

66. As seen from paragraph 9 on "Interest in Subsidiary Company" of the Notes to the 2008 Financial Statements (p. 634), the amount of the **aggregate amortization of cost** was shown:-

	2008	**2007**
	HK$	HK$
Unlisted investment, at cost	15,000,000	15,000,000
Unlisted investment **written off**		
At 31.03.2007	9,375,000	7,875,000
Addition	1,500,000	1,500,000
At 31.03.2008	**10,875,000**	**9,375,000**

67. The Respondent was engaged as the auditor of CLH in 2009. In the 2009 Auditor's Report (p. 128), the Respondent gave his **qualified opinion** regarding the underlying value of investment as follows: "... in absence of audited accounts of the subsidiary, we are unable to ascertain the underlying value of the Investment although an **aggregate impairment loss of the investment amount to HK$10,875,000** have been provided". This is the first time the "Impairment Provision" in question came into play. Effectively a change of accounting treatment was adopted here: The sum of HK$10,875,000 being the aggregate amortization of investment cost carried forward from previous year was treated as an aggregate impairment loss ("Impairment Provision") of investment. The term "Impairment Provision" was brought up in 2009, not the prior years.

68. As seen in the Income Statement dated 31 March 2009 (p. 129), no more amortization of cost of investment in the sum of HK$1,500,000 was made for the year. Though the comparative amount was clearly carried forward from the previous year, the sum was now categorized as "impairment loss on investment in subsidiary". Similarly, in the Notes to the 2009 Financial Statements (p. 143), the sum of HK$10,875,000 being the aggregate amortization cost of investment carried forward from 2008 was suddenly labelled as "accumulated provision for impairment loss".

	2009	**2008**
	HK$	HK$
		(restated)
Unlisted shares, at cost	15,000,000	15,000,000
Less: **Accumulated provision for impairment loss**	(10,875,000)	(10,875,000)
	4,125,000	**4,125,000**

69. From then on, there was no more mention of "written off" or "amortization of cost of investment" in the 2009 Financial Statements. However, there was no explanation as to why there was such a change of accounting. It was merely stated at paragraph 25 of the Notes to the 2009 Financial Statements

(p. 149) that "certain comparative figures have been reclassified to conform with the current year's presentation." However, given that the accounting concepts of "writing off" and "amortization" are different from "impairment", the change from "amortization" to "impairment" should have been explained. A mere suggestion of "a reclassification" is far from satisfactory.

70. In the 2010 Auditor's Report, the Respondent did not issue any qualified opinion in respect of the underlying value of the investment as he did in the 2009 Auditor's Report. However, if one turns to Note 10 to the 2010 Financial Statements (p. 163), the "accumulated provision for impairment loss" was still there:-

	2010	**2009**
	HK$	HK$
Unlisted shares, at cost	15,000,000	15,000,000
Less: **Accumulated provision for impairment loss**	(10,875,000)	(10,875,000)
	4,125,000	**4,125,000**

71. As seen from the figures above, the accumulated provision for impairment loss in the sum of HK$10,875,000 remained the same for the financial years in 2009 and 2010. In fact, the same figures also appeared in Note 9 to the 2011 Financial Statements (p. 179 at paragraph 9: Investment in a subsidiary):-

	2011	**2010**
	HK$	HK$
Unlisted shares, at cost	15,000,000	15,000,000
Less: **Accumulated provision for impairment loss**	(10,875,000)	(10,875,000)
	4,125,000	**4,125,000**

72. It is yet to be seen as to why the Respondent had chosen not to qualify his opinion regarding the Impairment Provision after 2009.

73. In the Audit Working Papers, it was expressly noted by the Respondent that

there was a scope limitation, at the end of the relevant reporting periods, regarding his audit work in assessing the appropriateness of the Impairment Provision. In the audit working papers for the 2010 Financial Statements (p. 382), it was stated, inter alia, that the Respondent could not obtain any accounts, management accounts and other relevant information of the Factory. Due to the absence of information, the Respondent **could not do any valuation test of the investment of the Factory**. As such, the **recoverable amount of the impairment cannot be determined**. However, the Respondent considered that as the Factory kept supplying goods to CLH continuously, he accepted the directors' view to maintain the amount of Impairment Provision made by the former auditor.

74. In the Audit Working Papers for the 2011 Financial Statements (p. 405), similar remarks were made. It was also stated that the Respondent followed the amount of the Impairment Provision made by the former auditor in accordance with the directors' view.

75. The Complainant's case is that the lack of financial information on the Factory presented a scope limitation on the Respondent's audit work in assessing, at the end of each reporting period, whether the Impairment Provision recognized in prior periods for the Factory was still appropriate at that date. Pursuant to HKSA 700.17 and 700.18, the Respondent should have issued a limitation of scope audit opinion on the inability to audit the propriety of the Impairment Provision to address both the limitation he encountered and the possible adjustments which may be necessary. This is particularly important as the Impairment Provision related to a significant amount in the 2010 and 2011 Financial Statements. A limitation in scope relating to the said amount should have been reflected in the auditor's reports. However, the Respondent did not qualify his opinion on the grounds of the limitation of scope of audit work in the auditor's reports on the 2010 and 2011 Financial Statements.

76. As we have set out hereinabove, the Respondent had issued a qualified opinion on the 2009 Financial Statements for the scope limitation. Without

the benefit of having the audited accounts of the subsidiary (i.e. the Factory), the Respondent stated that he was unable to ascertain the underlying value of the investment albeit that an Impairment Provision against the investment amounting to HK$10,875,000 had been provided. After 2009, no such audit qualifications were made by the Respondent.

77. In answer to the 3rd Complaint, the Respondent had put forward various defences which are highlighted below. They can be found in the February 2013 Representations, the July 2013 Representations, the Respondent's Case, the Respondent's Reply as well as the Respondent's oral opening and written closing submissions.

78. First, in the February 2013 Representations, it was stated that the Respondent had **not been provided with the Factory's audited accounts, management accounts or other relevant information** in the course of his audits of the 2009, 2010 and 2011 Financial Statements. In the absence of such accounts and information and any contrary view expressed by the management of CLH at the material times, the Respondent was of the opinion that the **recoverable amount cannot be determined and there was not any basis to reverse the Impairment Provision made by the former auditor**. The Respondent did accept, however, that his opinion (or qualifications to or basis of such opinions) could have been more clearly disclosed in a note to the 2010 and 2011 Financial Statements and in similar note to the 2009 Financial Statements.

79. Second, in the July 2013 Representations, it was stated, inter alia, that:-

(1) the **respondent *had* considered the recoverable amount** in CLH's investment in the Factory and hence the appropriate value of Impairment Provision during pre-audit meetings and in the course of the audits, despite the unavailability of the Factory's accounts;

(2) In considering the recoverable amount in CLH's investment in the Factory, the Respondent had taken into account the fact that the **Factory**

was a going concern, with its factory under normal operation mode, producing goods over HK$100 million in value each year. This showed that the **Factory's financial status was sound** and it appeared that the Respondent had **no basis to adjust the Impairment Provision**, in the absence of the Factory's accounts and other contrary indicators.

(3) Whilst the Respondent had made qualification for scope limitation in the auditor's report for 2009, similar qualification was removed in 2010 and 2011 because the Respondent had accumulated a greater understanding of CLH's affairs.

80. Third, in the Respondent's Case, he contended for the very first time that during the audit of the CLH for the year ended 31 March 2010, Ms. Wu suggested to the Respondent that a **potential buyer was willing to acquire the entire interest of the Factory at approximately HK$4 million**. That was why the Respondent did not do anything in relation to the Impairment Provision for the years ended 31 March 2010 and 2011. In the Respondent's Reply, it was also stated that since there was a potential buyer willing to acquire the entire interest of the Factory at approximately HK$4 million, this is **solid evidence to prove the Factory's fair value less costs to sell**.

81. Fourth, it was submitted in the Respondent's Case that the **impact of the 3rd Complaint could not have caused any prejudice to any shareholder** because Mr. Lee had full access and control over the Factory's accounts and he signed all the 2006 – 2011 Financial Statements in his capacity as a then director of CLH, which showed that he understood and approved those Financial Statements. It was submitted that the Respondent was not in a position to raise circumstances which he should investigate any change of Impairment Provision when there was none.

82. Lastly, in the Respondent's oral opening, Mr. Lai suggested for the very first time that there was **no need for the Respondent to estimate the recoverable amount** because there was no evidence of any indication that

an impairment loss recognized in prior periods may no longer exist or may have deceased.

83. Ms. Tong for the Complainant submitted that these defences have been constantly evolving and internally inconsistent. She said that none of the defences to the 3rd Complaint above could validly address the Respondent's failure to qualify his opinion in respect of the scope limitation for the Impairment Provision.

Discussion

Recoverable amount cannot be determined and no basis to reverse impairment provision (February 2013 Representations)

84. In the February 2013 Representations, the Respondent considered that the recoverable amount could not be determined and there was no basis for him to reverse the impairment provision made by the former auditor because of the lack of accounts regarding the Factory. It was the Respondent who expressly acknowledged that he was not in a position to assess the appropriateness of the Impairment Provision at the end of each of the reporting periods (i.e. 31 March 2010 and 2011) due to the lack of access to the financial information of the Factory. As such, he should have qualified his opinion.

85. Further, there was no basis for the Respondent to maintain the "Impairment Provision" allegedly made by the former auditor without applying his own independent assessment during the 2010 and 2011 audits.

Respondent had conducted impairment loss assessment: recoverable amount considered and potential sale noted (July 2013 Representations and the Respondent's Case)

Recoverable amount considered and the Factory having sound financial status (July 2013 Representations)

86. Contrary to what was said in the February 2013 Representations, namely,

that "the recoverable amount cannot be determined", it was newly contended in the July 2013 Representations that the Respondent *had* considered the recoverable amount and came to the view that the Factory was a going concern, thus having sound financial status and evidencing why the Respondent did not make adjustment to the Impairment Provision made by the former auditor.

87. The Respondent's new stance that he *had considered* the recoverable amount is wholly inconsistent to what was said in the February 2013 Representations. If the Respondent had indeed conducted an assessment on the Impairment Provision at the material times, he should have documented such assessment in the Audit Working Papers but no such record could be found.

88. According to the Respondent, the Factory was operating as a going concern with annual production of over HK$100 million, thus having a sound financial basis and offering no basis for him to make any adjustment to the Impairment Provision. Again, without any financial information or accounts of the Factory, it is wholly uncertain as to how the Respondent obtained the said information relating to the Factory, whether such information had been verified and how the Respondent could be satisfied that the Factory was operating as a going concern, producing goods over HK$100 million in value each year and having a sound financial status as alleged. In any event, we cannot see how the Respondent would be able to make a proper assessment on the recoverable amount, being the higher of the Factory's fair value less costs to sell and its value in use, merely on the basis of the said information relating to the Factory and without reviewing its accounts.

89. We consider that the lack of financial information and accounts of the Factory has clearly presented a scope limitation on the Respondent's audit work for assessing the Impairment Provision. Such limitation in audit scope relating to a significant amount in the 2010 and 2011 Financial Statements should have been duly reflected in the relevant auditor's report as an audit qualification. However, this was not done. In the

circumstances, we consider that the Respondent's failure to express a qualified opinion concerning the said limitation of scope is a breach of HKSA 701.18.

Potential sale of the Factory as solid evidence to prove the Factory's fair value less cost to sell (the Respondent's Case)

90. It was contended by the Respondent for the first time in the Respondent's Case (paragraph 17) that he learnt from Ms. Wu that a potential buyer would like to acquire the interest of the Factory at about HK$4 million. The Respondent said this explained why he did not do anything in relation to the Impairment Provision for the 2010 and 2011 Financial Statements. In the Respondent's Reply (paragraph 17), the same argument was adopted and it stated that the presence of a potential buyer willing to acquire the entire interest of the Factory at about HK$4 million is solid evidence to prove the Factory's fair value less cost to sell. We note that this line of argument is not repeated in Mr. Lai's closing submissions albeit that Mr. Lai told us he had no instructions to abandon any submissions previously made on behalf of the Respondent.

91. We have carefully considered the submissions made on behalf of both the Respondent and the Complainant and we agree with Ms. Tong for the Complainant that the Respondent's contention relating to the potential sale of the Factory is insufficient for making a proper assessment on the carrying amount and Impairment Provision. In particular, the following points should be highlighted:-

(1) There is no suggestion that the Respondent had ever tried to obtain relevant information relating to the said potential sale before placing reliance on it, such as the background of the purchaser, whether the transaction was at arms-length; the basis upon which the purchase price was agreed; the business rationale for the sale; and when the transaction was intended to be completed.

(2) The Respondent never mentioned whether in the Respondent's Case

or the Respondent's Reply that he had seen any documentation evidencing the said potential sale. It was only mentioned for the first time in Ms. Wu's witness statement that there was a contract relating to the sale yet to be signed by all parties. Ms. Wu gave evidence that in about July or August 2010, she informed the Respondent of the said potential sale and showed him a copy of the said draft contract. She said that she asked the Respondent not to make photocopy of the draft contract because the execution by Mr. Lee was still pending.

(3) Ms. Wu gave evidence under cross-examination, inter alia, that Mr. Lee was the only shareholder responsible for negotiating the price and liaising with the buyer in respect of the sale. The sale would be abandoned by February 2011 the latest, i.e. one year after negotiation by CLH and the buyer in February 2010. That said, Ms. Wu had never informed the Respondent that the potential sale would be abandoned and the Respondent never asked about the progress of the sale. As it transpired that Mr. Lee refused to sign the contract on behalf of the Factory, and Ms. Wu followed up the matter with the Head of the Factory on one occasion. The Head of the Factory said, however, that given Mr. Lee's refusal to sign the contract, the transaction could not be completed. Then Ms. Wu did not instruct the Head of the Factory to take further follow up action on the matter.

(4) It is clear from Ms. Wu's evidence that the details of the potential sale were not known to her. It followed that such details would neither be known to the Respondent as Ms. Wu had been his only source of information. Further, as the potential sale was considered abandoned by February 2011 the latest, there cannot be any question of using the sale price of the Factory to estimate the Impairment Provision of the Factory for the 2011 audit.

92. By reason of the above, we consider that even if the Respondent had conducted an assessment on Impairment Provision at the relevant times, such assessment was insufficient to justify an unqualified opinion, not to

mention that it was never documented in the Audit Working Papers and was actually contradicted by those Papers which expressly recorded that the Respondent decided to keep Impairment Provision unchanged because (1) no valuation test could be done and (2) the recoverable amount could not be determined due to the absence of financial information and accounts of the Factory.

No prejudice caused to any shareholder (Respondent's Case)

93. The Respondent contended in the Respondent's Case (paragraph 18) that no prejudice would be caused to any shareholder as a result of the matters complained of in the 3rd Complaint. In essence, the Respondent stated that Mr. Lee having control and access to the accounts of the Factory knew the financial affairs of the Company well. He signed on all the 2006 – 2011 Financial Statements as a director of CLH. This clearly shows he understood and approved the financial statements and he could not have been misled in any way.

94. Ms. Tong commented that the Respondent's contention above is no longer actively pursued by the Respondent. We also note that such contention is not repeated in the Respondent's written closing submissions. In any event, we do not consider the Respondent's contention that no prejudice was caused to anyone could strengthen his defence in any way or provide a sufficient answer to the 3rd Complaint. It is not up to the Respondent to suggest that so long as a shareholder is not misled or prejudiced, it does not matter if the Respondent had failed to qualify his opinion concerning the limitation of scope in assessing the Impairment Provision. Whether or not a lack of qualification for scope limitation has caused prejudice to any shareholder of CLH is irrelevant in determining if there is a breach of professional standards on the part of the Respondent. The fact that little or no prejudice was caused should be relevant when it comes to mitigation of sanctions. For these reasons, the Respondent's above contentions cannot stand.

No need to carry out assessment of recoverable amount (Respondent's Opening and Closing Submissions)

95. The Respondent submitted for the very first time in his oral opening submissions that there was no need to carry out assessment of the recoverable amount in the absence of any evidence of any indication that an impairment loss recognized in prior periods may no longer exist or may have decreased ("**the Requisite Indication**"). This became the Respondent's main argument in his written closing submissions. The Complainant commented that the Respondent had never raised such argument whether at the investigation stage or in the proceedings and that it was yet another ex post facto attempt on the part of the Respondent to try to exonerate his responsibility.

96. In his closing submissions, Mr. Lai for the Respondent submitted that the 3rd Complaint is flawed in a number of material aspects. First, neither HKAS 36.110 nor SME-FRF paragraph 9.5 requires the assessment as contended by the Complainant. HKAS 36.110 is put under the section of "reversing an impairment loss" which provides that "an entity shall assess at the end of each reporting period whether there is any indication that an impairment loss recognized in prior periods for an asset other than goodwill may no longer exist or may have decreased. If any such indication exists, the entity shall estimate the recoverable amount of the asset." Accordingly, Mr. Lai said that HKAS 36.110 imposes a three-stage test, namely, (1) looking for an indication; (2) satisfying that the indication suggesting that the previously provided impairment loss might be excessive (either in whole or in part); (3) if such indication exists, estimate the recoverable amount of that asset.

97. Mr. Lai submitted that insofar as indications are concerned, HKAS 36.111 provides a list of sources of information but financial statements are not on the list. This is understandable because financial statements only present historical performance of an entity and shed very little light, if any, on the future prospect of the entity. Accordingly, Mr. Lai submitted that the absence of the Factory's financial statements did not present a limitation of scope for the Respondent's compliance with HKAS 36.110 or SME-FRF

paragraph 9.5.

98. Further, Mr. Lai submitted that in the Complainant's own case, an assessment of appropriateness of impairment loss would involve comparison of the carrying amount of the entity and its recoverable amount. Insofar as the carrying amount is concerned, it is a "given" in CLH's financial statements throughout the years (i.e. HK$15 million – HK$10,875,000 = HK$4,125,000). As to recoverable amount, HKAS 36 has provided definitions for "recoverable amount", "fair value less costs to sell" and "value in use" as follows with emphasis added by Mr. Lai:-

(1) "recoverable amount" – the higher of its fair value less costs to sell and its value in use;
(2) "fair value less costs to sell" – the amount obtainable from **the sale of the entity** in an arm's length transaction, less the costs of disposal;
(3) "value in use" – the present value of the **future** cash flows **expected to be deprived** from the entity.

99. Mr. Lai said that the Complainant failed to advance how the presence or absence of the Factory's financial statements would have assisted or inhibited the Respondent's compliance with HKAS 36.110 (or SME-FRF paragraph 9.5), in particular gauging the "recoverable amount" by reference to the Factory's financial statements (which only came into light after the 2010 and 2011 Financial Statements). Mr. Lai submitted that the Factory's financial statements could hardly be relevant in assessing the recoverable amount because (1) they were not prepared on the "realizable" value basis and hence would not indicate the fair value; and (2) they present only historical performance and shed no light on the future performance, let alone future cash flows expected to be deprived.

100. Other than the above, Mr. Lai further submitted that the transaction volume between CLH and the Factory (i.e. purchase by CLH from the Factory) experienced a decreasing trend in 2008/09 and 2010/11. Such trend could hardly give rise to an indication that the standing impairment provision was

too excessive. Accordingly, there is no basis to suggest that the Respondent suffered a limitation of scope in complying with HKAS 36.110 (or SME-FRF paragraph 9.5) in the absence of the Factory's financial statements.

101. We have carefully considered Mr. Lai's submissions but we are not impressed by what he had said. Most important of all, what Mr. Lai advanced now is wholly inconsistent with what the Respondent had expressly stated in the Audit Working Papers. We also note that the Respondent had never mentioned in the Audit Working Papers, his representations to the Institute during the investigation stage, the Respondent's Case and the Respondent's Reply that he had in fact considered the list of sources of information stipulated in HKAS 36.111.

102. Contrary to Mr. Lai's new submission that the recoverable amount does not need to be assessed, the Respondent had all along recognized the need to ascertain such amount for the purpose of making a proper assessment of the Impairment Provision. Further, the Respondent never disputed that the Factory's financial information and accounts were relevant for the purposes of assessing the recoverable amount for the purpose of impairment assessment:-

(1) In the Audit Working Papers, the Respondent noted that for both 2010 and 2011, so far as the Impairment Provision was concerned, **due to the absence of information, he could not do any valuation test of the investment of the Factory. Thus, the recoverable amount of the investment cannot be determined**. Plainly, the Respondent himself did acknowledge the need to estimate the recoverable amount and noted the reason why he was unable to do so. According to the Respondent himself, the lack of financial information of the Factory had made it impossible for him to carry out any valuation test of the investment of the Factory. That was why the recoverable amount for the purpose of the impairment could not be determined.

(2) In the February 2013 Representations, it was stated that the Respondent had not been provided with the Factory's audited accounts, management accounts or other relevant information in the course of his audits of the 2009, 2010 and 2011 Financial Statements. **In the absence of such accounts and information (including financial cashflow forecasts)** and any contrary view expressed by the management of CLH at the relevant times, the Respondent was of the opinion that the **recoverable amount cannot be determined** and there was no basis to reverse the Impairment Provision made previously.

(3) Further, as evidenced by the Audit Working Papers and the February 2013 Representations, the Respondent had never suggested that the financial information and accounts of the Factory were irrelevant for the purpose of assessing the recoverable amount. What the Respondent expressly stated in the Audit Working Papers and the February 2013 Representations was wholly contradictory to Mr. Lai's new submission. For the same reason, we are also not impressed by the Respondent's contention that the past financial statements only represented the past performance of CLH and shed little light on its future performance, thereby serving no purpose in the assessment of recoverable amount.

(4) We consider that the subject matter in the 3rd Complaint is straightforward. The lack of financial information and accounts of the Factory had presented a scope limitation for the Respondent to assess the Impairment Provision. He should have qualified his opinion on the grounds of such limitation in the auditor's reports on the 2010 and 2011 Financial Statements. His failure to do so is a clear breach of HKSA 701.18.

(5) In the July 2013 Representations, the Respondent changed his stance and asserted that he ***had*** **considered the recoverable amount** in CLH's investment in the Factory **and hence the appropriate value of Impairment Provision** during the pre-audit meetings and in the course

of the audits, despite the **unavailability of the Factory's accounts**. Be that as it may, the Respondent never suggested that the Requisite Indication did not exist thereby rendering any assessment on recoverable amount unnecessary. Again, what the Respondent had said in the Audit Working Papers did not support Mr. Lai's submissions at all. The fact remains that the Respondent, having identified the scope limitation mentioned above, had failed to express a qualified opinion thereof.

103. By reason of the above, we consider that the 3rd Complaint is proved.

4TH COMPLAINT

104. The 4th Complaint concerns the Respondent's alleged failure in respect of the 2011 Financial Statements to substantiate CLH's compliance with Section 161B of the Ordinance and his concurrence with CLH's non-disclosure of securities given by CLH for banking facilities granted to CGHK (being a company in which Ms. Wu held a controlling interest), in breach of HKSA 250.13.

105. HKSA 250.13 provides that "the auditor shall obtain sufficient appropriate audit evidence regarding compliance with the provisions of those laws and regulations generally recognized to have a direct effect on the determination of material amounts and disclosures in the financial statements."

106. The Complainant's case is that pursuant to a facility letter dated 2 September 2010 ("**the Facility Letter**") issued by the Bank, CLH and CGHK obtained banking facilities secured by the following charges created by CLH over its cash deposits and landed property ("**the Charges**"):-

(1) On 15 September 2010, CLH entered into a Charge on Cash Deposit(s) as a continuing security for all or any money and liabilities which shall from time to time (and whether on or at any time after demand) be due, owing or incurred in whatsoever manner to the Bank by CLH or CGHK, whether actually or contingently, solely or jointly and whether as

principal or surety.

(2) On 25 October 2010, CLH entered into a Deed of Variation creating a Charge over its landed property.

107. The Complainant contended that pursuant to Section 161B of the Ordinance, a company must provide in its financial statements specified particulars of every "relevant transaction" entered into by the company which is connected with a director of the company. For the present purposes, the expression "relevant transaction" is defined under Section 161B(14)(b) as:-

"a loan or quasi-loan made to, or a credit transaction entered into for... a body corporate in which **a director of the company**, at any time during the financial year, held (jointly or severally or directly or indirectly) a **controlling interest**, whether or not such controlling interest was so held at the time the loan, quasi-loan or credit transaction was made or entered into". [emphasis added]

108. Since Ms. Wu was a director of CLH and the sole shareholder and director of CGHK during the 2011 financial year, the banking facilities under the Facility Letter were relevant transaction under Section 161B(14) and that the Charges provided by CLH to secure such facilities were required to be disclosed in the 2011 Financial Statements in accordance with Section 161B(3) and (4).

109. As Section 161B specifies matters which must be disclosed in the accounts and imposes a strict legal requirement to disclose securities which fall within that Section, HKSA 250.13 requires an auditor to obtain sufficient appropriate audit evidence regarding CLH's compliance. However, no disclosure of the Charges in the 2011 Financial Statements was made. Section 161B was contravened. The Complainant thus submitted that the Respondent had failed to obtain sufficient appropriate audit evidence to substantiate CLH's compliance with Section 161B and his concurrence with

the non-disclosure of the Charges. As such, the Respondent was in breach of HKSA 250.13.

110. The Respondent advanced various defences to the 4th Complaint as follows:-

(1) In the letter dated 30 July 2013 from the Respondent's solicitors to the Institute, the Respondent contended, inter alia, that in about 2009, it was agreed by the three shareholders of CLH that the company would, for commercial reasons, be gradually phased out and that all major future businesses of their commercial venture would be carried on through another corporate vehicle, namely, CGHK, beneficially owned by them in shares pro rata to their respective interests in the company. For the purpose of the said phase-out plan, Ms. Wu would be the sole director of CGHK and she would hold the sole share in CGHK on trust for all three shareholders in proportions pro rata to their respective interests in the company. In short, CGHK was an **alter ego** of the original commercial venture of the company and was treated as such by all three shareholders of CLH. Therefore Ms. Wu was not the beneficial owner of CGHK and was not treated as such by all the three shareholders. Accordingly, **Section 161B was inapplicable** because the Charges did not constitute security for a loan to a director but were security for a loan to CGHK, the alter ego of the commercial venture of CLH.

(2) In the Respondent's Case and the Respondent's Reply, it was contended that by virtue of HKSA 250.13, 250.19 and 250.21 that it was **a matter within the professional judgment** of the Respondent to have come to the decision that it was unnecessary to issue a qualified opinion on the non-disclosure regarding the Facility Letter and the Charges in the 2011 Financial Statements. In particular, the Respondent contended that the Facility Letter was countersigned by Mr. Lee and Ms. Wu. Thus, Mr. Lee must have approved of the terms of the Facility Letter and the fact that CLH provided security for loans to

be advanced to CGHK and/or CLH. Further, the Respondent was given to understand, by a letter from CLH dated 3 November 2010 signed by Ms. Wu, that all shareholders of CLH planned to transfer business from CLH to CGHK.

(3) In the Respondent's Case, it was contended that "no evidence suggesting that anyone, whether shareholder or creditor has been prejudiced by the omission of details of CGHK, the Facility Letter and the Charge" in the 2011 Financial Statements. In particular, Mr. Lee was fully aware of the Charges and that Ms. Wu had provided a bank statement which showed that CGHK had sufficient funds to repay the debt under the Facility Letter. In any event, any such omission would **not prejudice anyone's interests and hence any breach would be technical** as the disclosure would not serve to protect anyone's interests.

(4) In the Respondent's Reply, it was contended that whether CLH disclosed the securities given to CGHK or not, the **financial statements taken as a whole, were free from material misstatements**, whether caused by fraud or error. The Respondent considered that the liquidity risk to CLH was low because the possibility of default payment by CGHK was very low; and that CLH had its ground for non-disclosure and the possibility of fraud was assessed to be low.

Discussion

Alter Ego argument and Section 161B inapplicable?

111. We have no hesitation in rejecting the Respondent's line of argument that CGHK was an alter ego of CLH and hence Section 161B should not apply in the present case. We do not see how the contention that Ms. Wu held all the three shareholders' interests in CGHK on trust could provide a sufficient answer to the 4th Complaint because Ms. Wu was still having a controlling interest, i.e. 60% of CGHK's shares and the loan facilities provided under the Facility Letter remain relevant transactions for the purpose of Section 161B(14)(b) of the Ordinance. The contentions made

by the Respondent are no reasons for non-compliance with Section 161B(14) which gives no exemption for non-disclosure.

A matter within professional judgment

112. We do not agree that the 4th Complaint turns on a question of professional judgment. HKSA 250.13 requires an auditor to "obtain sufficient appropriate audit evidence regarding compliance with the provisions of those laws and regulations generally recognized to have a direct effect on the determination of material amounts and disclosures in the financial statements". There is no evidence in the Audit Working Papers showing that the Respondent had done so. The failure to disclose the Charges would be in direct contravention to Section 161B and the Respondent should not have permitted CLH to have done so.

113. Whilst the Respondent tried to rely on HKSA 250.19 and 250.21 in support of his contention, we cannot see how these provisions could advance the Respondent's arguments at all. HKSA 250.19 provides that where the auditor suspects non-compliance, he shall discuss the matter with management; and if in the auditor's judgment the non-compliance might be material to the financial statements, the auditor shall consider the need to obtain legal advice. HKSA 250.21 provides that the auditor shall evaluate the implications of non-compliance in relation to other aspects of the audit, including the auditor's risk assessment and the reliability of written representations, and take appropriate action. Both HKSA 250.19 and 250.21 did not provide a defence of "professional judgment" to non-disclosure of relevant transaction in contravention of Section 161B which is a legal requirement which CLH had to strictly comply. There is nothing in the Audit Working Papers showing that the Respondent had identified the non-compliance or had taken any steps to obtain appropriate legal advice or audit evidence that CLH had duly complied with Section 161B(14).

114. It cannot be disputed on the available evidence, CLH had provided securities for the Bank granting loan to CGHK and Ms. Wu as a director of CLH was the 60% majority shareholder of CGHK. We consider that the

alter ego argument now raised by the Respondent is not a concept that can take the circumstances of any Charges outside the requirement of Section 161B. It is clear that in the Respondent's Audit Working Papers he had failed to obtain sufficient audit evidence to substantiate CLH's compliance with Section 161B.

No one's interests are prejudiced and any breach was technical

115. We take the view that whether or not anyone's interests are prejudiced by reason of the non-disclosure of the Charges is irrelevant in determining whether the Respondent was in breach of professional standards. As we have mentioned earlier, this matter would be relevant when it comes to mitigation of sanctions.

116. In any event, Section 161B strictly requires disclosure of securities and does not provide any exemption for non-disclosure by reason that the relevant transaction was known to all shareholders. In any event, an auditor cannot knowingly concur with non-disclosure of securities in a company's accounts in contravention of Section 161B. It cannot be said that the Respondent's breach was merely technical. If the Respondent's contention were to be accepted, an auditor could concur in major departures from the statutory requirements simply because the shareholders knew about the situation or that they were not prejudiced, thus rendering it unnecessary to make disclosure as required by the Ordinance. That cannot be right.

117. In passing, we note that whilst the Respondent stated that Ms. Wu had provided a bank statement to show CGHK's ability to repay, such statement was never exhibited in the Audit Working Papers nor produced by the Respondent.

The Financial Statements are free from material misstatements

118. The 4th Complaint does not concern whether the Financial Statements were materially misstated either. The real question is whether the

Respondent had obtained sufficient appropriate evidence showing that CLH had complied with Section 161B(14) as required by HKSA 250.13. We have already stated our view that the Respondent had failed to obtain such evidence showing that CLH had complied with Section 161B(14). We would only add that there is no documentary proof or records in the Audit Working Papers which support the Respondent's contentions that (1) CGHK was able to repay the debt to the Bank; and (2) the liquidity risk in 2011 was allegedly low.

119. By reason of all the above, we consider that the 4th Complaint is proved.

5TH COMPLAINT

120. The 5th Complaint concerns the Respondent's alleged failure in the audit of the 2011 Financial Statements to prepare sufficient and appropriate audit documentation of the basis and reasons of concurring with CLH's non-disclosure of securities given by CLH for banking facilities granted to CGHK, in breach of HKSA 230.7 (which should be read in light of HKSA 230.8 and 230.10).

121. HKSA 230.7 provides that "the auditor shall prepare audit documentation on a timely basis.

122. HKSA 230.8 provides:-

"The auditor shall prepare audit documentation that is sufficient to enable an experienced auditor, having no previous connection with the audit, to understand:-

(a) The nature, timing, and extent of the audit procedures performed to comply with the HKSAs and applicable legal and regulatory requirements;

(b) The results of the audit procedures performed, and the audit evidence obtained; and

(c) Significant matters arising during the audit, the conclusions reached thereon, and significant professional judgments made in reaching those conclusions."

123. HKSA 230.10 provides that "the auditor shall document discussions of significant matters with management, those charged with governance, and others, including the nature of the significant matters discussed and when and with whom the discussions took place.

124. It is the Complainant's case that the Audit Working Papers did not document any reasons for the Respondent's concurrence with the non-disclosure of the Charges by CLH. No compliance checklist can be found in the Audit Working Papers to show that CLH's compliance with Section 161B had been duly considered.

125. In the Respondent's Reply, it was alleged, inter alia, that the Respondent had applied his professional judgment and decided that it was unnecessary to issue a qualified opinion on the non-disclosure regarding the Facility Letter and the Charges in the 2011 Financial Statements. It followed that the Respondent had come to the view that this was not a "significant matter" arising during the audit for which the audit documentation had to be prepared pursuant to HKSA 230.8(c).

126. In Mr. Lai's closing submissions, he submitted that the Respondent had obtained CLH's written representation that CGHK was an alter ego of CLH. Such written representation formed part of the audit evidence and provided the basis for the Respondent to arrive at the conclusion he did.

127. We have carefully considered the submissions made on behalf of the Respondent and we are unable to accept them. First and foremost, none of the considerations and arguments now being advanced by the Respondent are documented in the Audit Working Papers. Even if the Respondent had applied his professional judgment in coming to the view

that there was no need to issue a qualified opinion on the said non-disclosure, the Respondent had prepared no audit documentation which would enable an experienced auditor having no previous connection with the audit, to understand the professional judgment made by the Respondent and why disclosure of the Charges was considered unnecessary. This is a clear breach of HKSA 230.8.

128. There cannot be any doubt that compliance with Section 161B is a strict legal requirement and it is not up to the Respondent to lightly allege that non-disclosure was not a "significant matter" for which audit documentation had to be prepared. As to the Respondent's argument on "alter ego", we have already stated above that we are not impressed by the argument and we do not agree that such argument could exempt CLH from making the disclosure as required by Section 161B.

129. In the light of the above, we are satisfied that the 5th Complaint is proved.

6TH COMPLAINT

130. The 6th Complaint relates to the Respondent's failure to segregate monies received from Ms. Wu on 13 January 2012 and to make appropriate inquiries on the source of the funds to ensure compliance with relevant laws and regulations, in breach of Section 270 of the Code of Ethics for Professional Accounts ("**the Code**").

131. It is accepted that the Code applies to all professional accountants who are individuals who are members of the Hong Kong Institute of Certified Public Accountants ("**HKICPA**"). The Respondent is a member of the HKICPA.

132. For the sake of easy reference, Section 270 of the Code provides:-

"**SECTION 270**

Custody of Client Assets

270.1 A **professional accountant in public practice** shall not assume custody of client monies or other assets unless

permitted to do so by law and, if so, in compliance with any additional legal duties imposed on a professional accountant in public practice holding such assets.

270.2 The holding of client assets creates threats to compliance with fundamental principles; for example, there is a self-interest threat to professional behaviour and may be a self interest threat to objectivity arising from holding client assets. A **professional accountant in public practice** entrusted with **money (or other assets) belonging to others** shall therefore:

(a) **Keep such assets separately from personal or firm assets**;
(b) Use such assets only for the purpose for which they are intended;
(c) At all times be ready to account for those assets and any income, dividends, or gains generated, to any persons entitled to such accounting; and
(d) Comply with all relevant laws and regulations relevant to the holding of and accounting for such assets.

270.3 As part of client and engagement acceptance procedures for services that may involve the holding of client assets, a professional accountant in public practice shall **make appropriate inquiries about the source of such assets** and **consider legal and regulatory obligations.** For example, if the assets were derived from illegal activities, such as money laundering, a threat to compliance with the fundamental principles would be created. In such situations, the professional accountant may consider seeking legal advice."

[emphasis added]

133. Under the Code, a "**professional accountant in public practice**" refers to a professional accountant, irrespective of functional classification (e.g., audit, tax or consulting) in a firm that provides professional services. This term is also used to refer to a firm of professional accountants in public practice. The expression of "**professional services**" refers to services requiring accountancy or related skills performed by a professional accountant including accounting, auditing, taxation, management consulting and financial management services.

134. The Complainant contended that the Respondent received RMB 2.2 million from Ms. Wu on 13 January 2012, i.e. 3 days after the auditor's report on the 2011 Financial Statements was signed. The transfer of funds was made from a bank account under Ms. Wu's name in Mainland China to a bank account under the Respondent's name in Mainland China. There is a Chinese voucher ("支出証明單") produced before us which described the said sum of RMB 2.2 million as "莊聯興往來款" which suggested that the monies belonged to CLH instead of personal funds belonging to Ms. Wu.

135. Relating to the above transfer of funds, the Respondent stated in the February 2013 Representations that the transfer of funds took place on about 13 January 2012 when the Respondent had already resigned as the auditor of CLH and that the monies were only handled by the Respondent as a "ministerial agent" and the same sum, after conversion into Hong Kong dollars, was repaid to Ms. Wu on the same date. In the July 2013 Representations, it was further stated that the Respondent only handled the RMB 2.2 million in order to help Ms. Wu to exchange RMB into Hong Kong dollars. The Respondent was unable to provide any supporting document as none was available.

136. The Complainant's case is as follows:-

(1) Even though the Firm resigned as auditor of CLH on 10 January 2012 as evidenced by a letter from the Firm to CLH, this does not itself mean that the Respondent's dealings with Ms. Wu could not thereafter be in the capacity of a professional accountant providing "professional services" for the purposes of the Code.

(2) The Respondent never suggested that he received and handled the RMB 2.2 million in his personal capacity. He chose to remain completely silent in his written Case or Reply as to the capacity in which he received or handled the said monies. He also chose not to give evidence before the Committee on the matter.

(3) In the light of the Respondent's admission that he acted as "ministerial agent" in assisting Ms. Wu to convert the RMB into HK dollars and Ms. Wu's confirmation in oral evidence that the Respondent was acting as a "professional agent" ("專業代理") in the transaction, he ought to be regarded as acting as a "professional accountant in public practice" and providing "professional services" for the purpose of the Code. In this connection, the Respondent never suggested that he had any prior relationship or dealings with Ms. Wu other than in his professional capacity as the auditor of CLH. This was also confirmed by Ms. Wu.

(4) In the absence of any plausible explanation from the Respondent as to the purpose for which and context in which Ms. Wu transferred the RMB 2.2 million to him, it can be clearly inferred that Ms. Wu sought the Respondent's assistance to convert the said sum into Hong Kong dollars with a view to circumvent the State Administration of Foreign Exchange currency restrictions ("**the SAFE currency restrictions**"). In fact, Ms. Wu also gave evidence that if the transaction were to be conducted through official channels e.g. through a bank, it would be "very complicated". Further, the assistance involved requires knowledge of relevant foreign exchange regulations and the risks involved, and ought to be regarded as a professional service for the

purposes of the Code.

137. The Complainant thus submitted that the Respondent had failed to (1) segregate from his personal account the said sum received from Ms. Wu, (2) make inquiries about the source of the said sum; and (3) consider the relevant legal and regulatory obligations.

138. As mentioned hereinabove, the Respondent stated that he had handled the said sum of RMB 2.2 million as ministerial agent to help Ms. Wu to exchange the RMB into Hong Kong dollars. According to the Respondent, he had already resigned as auditor of CLH at the time when the transfer of funds was effected, so that he no longer had an auditor-client relationship at that time; and that he did not receive the said monies in his professional capacity and/or on behalf of the Firm. Whilst there is no documentary evidence before us showing that the monies after converted into Hong Kong dollars had been repaid to Ms. Wu, the Respondent produced a cheque as evidence and contended that the said sum in its Hong Kong dollars equivalent was deposited by Ms. Wu into the bank accounts of CGHK by way of that cheque on the same day. The Respondent maintained that he did not take any advantage or interest in such transaction.

139. It is stressed in the Respondent's defence that the burden of proof rests on the Complainant to prove all elements of the Complaint, including to whom the RMB 2.2 million belonged to, the existence of a client-auditor relationship, the professional services rendered, the failure of the Respondent to segregate client's money from his own money etc.

140. In her witness statement, Ms. Wu gave an account relating to the transfer of RMB 2.2 million as follows:-

> "20. On 13 January 2012, I intended to transfer the RMB from my personal account with [a PRC] Bank to Hong Kong. I therefore discussed with Mr. Law as I felt that he was upright and reliable. Besides, he had served as director of multiple

listed companies, for example [citing the names of some listed companies]. As such, I trusted him very much so I earnestly requested him to **do me a favour as a friend** and he agreed. Hence, I transferred RMB 2,200,000.00 to Mr. Law's [Mainland] account. After Mr. Law received RMB 2,200,000.00, he transferred back to me HK$2,699,386.50 at the exchange rate of that day.

21. From beginning to end, the dealings aforementioned were dealt with between Mr. Law and me in our **private capacity**. **I myself am not Mr. Law's client**, and Mr. Law has neither charged nor demanded any fee or benefit. I feel very sorry for Mr. Law in this matter as he was really innocent, **he was framed by Mr. Lee for helping me**."

[emphasis added]

141. The salient points of Ms. Wu's evidence under cross-examination are highlighted as follows:-

(1) Ms. Wu confirmed that she requested the Respondent to convert and transfer her RMB 2.2 million into Hong Kong dollars, since the CGHK required cash on an urgent basis. She asked the Respondent for assistance because the banks had effectively told her that the transaction would be "very complicated".

(2) The Respondent agreed to Ms. Wu's request and their agreement was not recorded in writing.

(3) The RMB 2.2 million came from the proceeds of her sale of certain properties in the Mainland China.

(4) Ms. Wu only saw the Chinese voucher ("支出証明單") for the very first

time during cross-examination. She said she did not sign on the voucher and that the voucher was not genuine.

(5) She insisted that the Respondent did transfer back to her HK$2,699,386.50 though she was unable to state the means by which the Respondent effected such transfer or produce any documentary proof showing that the Respondent paid her such sum.

(6) Ms. Wu had not been acquainted with the Respondent before engaging the Firm as CLH's auditor in 2009. Her relationship with the Respondent at all material times until 10 January 2012 was solely one of client and auditor, namely, a professional relationship. It was **not entirely accurate to describe the Respondent as a friend** but rather that **he was a professional agent (專業代理) with respect to the transfer of RMB 2.2 million**.

142. It is the Respondent's case that since he had already resigned as auditor of CLH at the time when Ms. Wu transferred the RMB 2.2 million to him, there was no professional service provided to Ms. Wu by the Respondent in his capacity as a professional accountant. The only factual evidence was a voucher dated 13 January 2012 titled "結算業務申請書" evidencing that the RMB 2.2 million was transferred from Ms. Wu's personal bank account to the Respondent's personal bank account. Such evidence could hardly provide any evidential basis upon which the Complainant could ask the Committee to draw inference in relation to matters such as (1) other than Ms. Wu, to whom the RMB 2.2 million belong; (2) the existence of a client-auditor relationship, (3) professional services were rendered to Ms. Wu by the Respondent; (4) the Respondent had mixed his own funds with the RMB 2.2 million, (5) the Respondent made no inquiry about the source of funds; and/or (6) the relevant legal and regulatory regime which the Respondent had failed to consider. The Respondent stressed that the burden of proof rests on the Complainant to prove each and every element to its case and

it is not for the Respondent to prove his innocence.

143. Further, the Respondent submitted that the following evidence is directly against the Complainant's case:-

(1) The voucher titled "結算業務申請書" provided contemporaneous evidence that the RMB 2.2 million belonged to Ms. Wu but not any other source.

(2) The Respondent only held the said sum for a fraction of a day. Ms. Wu gave evidence that she received the Hong Kong dollars equivalent of the RMB 2.2 million on the same day. This did not support any business relationship between a client and a professional accountant in public practice, and/or provision of any professional services.

(3) Ms. Wu said under cross-examination that she had informed the Respondent as to the source of the RMB 2.2 million: It was from the sale proceeds from her real estate investment in the Mainland China.

(4) The dealing only involved the Respondent remitting the Hong Kong dollars equivalent of RMB 2.2. million at the prevailing exchange rate to Ms. Wu from Mainland China to Hong Kong. This did not support any provision of professional services which involves accountancy or related skills of a professional accountant for the purposes of the Code.

(5) It was never the Complainant's written case that the said sum belonged to an entity or other sources but not Ms. Wu. The Complainant is bound by its own case and cannot change its case during the course of the proceedings.

(6) In any event, the voucher titled "結算業務申請書" was produced by Mr. Lee who was privy to the affairs of both CLH and the Factory when the document was created. Mr. Lee himself did not even contend that the RMB 2.2 million originated from a source other than Ms. Wu.

(7) The voucher titled "支出証明單" with the words "莊聯興往來款" thereon had no evidential value. It did not bear the name of the entity to which the voucher belonged and was incomplete in the sense that it lacked the double entries. Ms. Wu also gave evidence that the voucher was not genuine and she did not sign thereon. Alternatively, even if such voucher had been genuine, it remains for the Complainant to prove that the Respondent knew that the monies had originated from the entity which remains unknown.

For the above reasons, the Respondent contended that the 6th Complaint is liable to be dismissed.

Discussion

144. We agree with Mr. Lai that at all material times the burden of proof lies on the Complainant to prove on the balance of probabilities each and every element of its case. The burden is not on the Respondent to prove that he was not in breach of the Code. It is also a matter for the Respondent to decide whether to give evidence before the Committee. That said, we agree with Ms. Tong that by virtue of the Guidelines for the Chairman and the Committee on Administering the Disciplinary Committee Proceedings Rules (paragraph 11) and the Disciplinary Committee Proceedings Rules (paragraph 15), the Committee is entitled to draw adverse inference against the Respondent by reason that that he had chosen not to give evidence on the material issues relating to this Complaint despite having personal and direct knowledge thereof.

145. We have carefully considered all the available evidence and the submissions made on behalf of the parties. We consider that the following points are of particular importance:-

(1) Ms. Wu had never been acquainted with the Respondent before engaging his Firm as the auditor of CLH in 2009. At all material times and until 10 January 2012, the relationship between Ms. Wu and the

Respondent was solely a client-auditor and hence a professional relationship. Ms. Wu said in her witness statement that she trusted the Respondent very much. It is apparent that her trust to the Respondent had been built up on the client-auditor relationship since or after 2009.

(2) Ms. Wu said in her witness statement that she intended to transfer RMB 2.2 million from her Mainland account to Hong Kong on 13 January 2012. She then discussed with the Respondent and asked him to do her a favour as a friend. In her oral evidence, Ms. Wu said that the transfer was necessitated by the urgent need of the CGHK for cash. What happened was that Ms. Wu transferred the RMB 2.2 million from her Mainland China bank account to the Respondent's Mainland China bank account; followed by the Respondent's transfer of the same amount of money from his said account back to Ms. Wu's said account after conversion into Hong Kong dollars, i.e. about HK$2.6 million; then Ms. Wu wrote a cheque of the said HK$2.6 million to CGHK. All these transfers took place on the same day on 13 January 2012.

(3) Ms. Wu said in her evidence that before she turned to the Respondent for assistance, she had made inquiries with the bank and was given to understand that if the transfer were effected via official channels, it would be "very complicated". She did not further elaborate on this. We consider it is a matter of common sense that RMB 2.2 million is a significant amount of money and in order for Ms. Wu to transfer the said sum from Mainland China to Hong Kong, there are bound to be foreign exchange regulations which Ms. Wu had to observe and comply with. There would also be inquiries relating to the source of funds and purpose of transfer which she had to answer. In this connection, the Complainant submitted that the clear inference is that Ms. Wu had sought the Respondent's assistance to convert and transfer the RMB 2.2 million into Hong Kong dollars in order to circumvent the SAFE currency restrictions. On this particular point, no submission had been made by the Respondent in reply to the Complainant's such submission

whether in his written Reply or closing submissions.

(4) To get round the "very complicated" way of transferring the RMB 2.2 million, Ms. Wu chose to turn to the Respondent for assistance. She discussed the matter with the Respondent and using her words in the witness statement, she asked him to do her a "favour" "as a friend". Under cross-examination, however, she said it was not entirely accurate to describe the Respondent as a friend but he was rather her "professional agent" regarding the transfer. Judging from the label of "professional agent" and considering her evidence as a whole, particularly that Ms. Wu and the Respondent never had any private or personal relationship, we consider that Ms. Wu did not come to the Respondent for assistance because they were personal friends but rather that she placed her trust on the Respondent's professional capacity as a qualified accountant: The risk of the Respondent, as a professional accountant who had been engaged by CLH as the auditor for the past few years, absconding with her monies would be low. This was why Ms. Wu turned to the Respondent for assistance on the matter.

(5) We are fully aware that the transfer of the RMB 2.2 million was effected on 13 January 2012 which was 3 days after the Firm's resignation as the auditor of CLH. However, any suggestion that the Code would not apply to the Respondent by reason of his Firm's resignation as auditor of CLH would be futile because the Code applies to all professional accountants who are individual members of the HKICPA and the Respondent is at all material times a member of the HKICPA. Further, we entirely agree with Ms. Tong that the Firm's resignation did not prevent the Respondent from rendering professional services to CLH or Ms. Wu in his capacity as a professional accountant. When Ms. Wu requested the Respondent to transfer the RMB 2.2 million back to her in Hong Kong dollars and the Respondent agreed to and did carry out the transfer as told, there existed a professional and client relationship between the Respondent and Ms. Wu, in that the Respondent had, in his capacity of a professional accountant, provided assistance and

services to Ms. Wu by effecting the transfer in the way which Ms. Wu intended to avoid the "very complicated" procedure if the transaction was to be done via official channels. We consider that the assistance and services provided by the Respondent required his professional knowledge of the relevant foreign exchange regulations and the risks involved. Such assistance and services provided are within the scope of professional services as defined in the Code. For the purpose of the conversion and transfer of RMB 2.2 million into Hong Kong dollars, there is no doubt that the Respondent had rendered the said professional services to Ms. Wu in his capacity of a professional accountant and that the RMB 2.2 million transferred by Ms. Wu to the Respondent were "client monies" for the purposes of Section 270 of the Code. In this connection, we note that the expression "client monies" was not specifically defined under the Code but we consider that such expression should be construed purposively for the purposes of Section 270.

(6) According to Section 270.2 of the Code, a professional accountant in public practice entrusted with money or other assets belonging to others shall, inter alia, keep such assets separately from person or firm assets (Section 270.2(a)). Having accepted Ms. Wu's transfer of the RMB 2.2 million into his personal bank account, the Respondent should have separated Ms. Wu's monies from his own funds in the same account. Whilst Mr. Lai for the Respondent submitted that the Complainant failed to produce any evidence to show that the Respondent had failed to segregate Ms. Wu's funds from his funds, we consider that unless there is evidence to the contrary, the natural and reasonable inference would be that following Ms. Wu's said transfer into the Respondent's personal bank account, the said RMB 2.2 million would necessarily have been mixed together with the Respondent's own funds existed in the same account. If the Respondent had ever segregated Ms. Wu's funds from his own funds, it would have been easy for him to give evidence and say so. Despite having direct personal knowledge on this matter, the Respondent chose not to give

or produce any evidence whatsoever to rebut the Complainant's case. In the circumstances, it can be reasonably inferred against the Respondent on the basis of the available evidence that the Respondent had failed to comply with Section 270.2(a) by separating the assets belonging to Ms. Wu from his personal assets.

(7) Ms. Wu stated for the very first time in her oral evidence that the source of the RMB 2.2 million came from proceeds of her sale of certain properties in the Mainland China and that she had informed the Respondent about this. She never mentioned about this in her witness statement. In his written case and reply, it was never stated that the Respondent was told by Ms. Wu as to the source of funds. He never said if any inquiries had been made regarding the source of funds and whether he had considered the relevant legal and regulatory obligations. If the Respondent had been informed of the source of funds, he should have mentioned it in the correspondence with the Institute, his written Case and Reply. Be that as it may, even assuming that Ms. Wu had informed the Respondent as to the source of funds as suggested, we consider that it is still incumbent on the part of the Respondent to make appropriate inquiries as a professional accountant to confirm, for instance, that the RMB 2.2 million was not derived from illegal activities such as money laundering. Again, despite having direct personal knowledge of these matters, the Respondent had chosen not to give or produce any evidence whatsoever to show that he had made inquiries as to the source of funds and had considered the relevant legal and regulatory obligations. This is a matter which the Committee is entitled to take into account in deciding on the facts relevant to this Complaint. On the basis of the available evidence, it can be reasonably inferred that the Respondent had made no such inquiries and hence he is in contravention of Section 270.3 of the Code.

(8) For the sake of completeness, we consider that the voucher titled "結算

業務申請書" is clear evidence that the RMB 2.2 million was transferred from Ms. Wu's personal account to the Respondent's personal account. Whilst another voucher titled "支出証明單" bore the words "莊聯興往來款" and seemed to suggest that the source of Ms. Wu's RMB 2.2 million came from CLH, we consider no such inference can be safely drawn as there was no witness coming forward to explain matters such as who wrote the words "莊聯興往來款" on the voucher, when and under what circumstances those words were written; what exactly the words "莊聯興往來款" meant and who had purportedly signed on the voucher. In her evidence, Ms. Wu even denied having signed on it and claimed that the voucher was not genuine. In this respect, there was no other evidence adduced by the Complainant to rebut Ms. Wu's allegations. In all fairness, we consider that even assuming that the voucher was genuine, no weight should be given to this voucher titled "支出証明單".

In any event, by reason of what we have stated above the RMB 2.2 million transferred by Ms. Wu to the Respondent were client monies for the purpose of Section 270 of the Code. The duty is on the Respondent to segregate such funds from his personal assets and that he had failed to do so.

(9) Regarding the repayment of the Hong Kong dollar equivalent of the RMB 2.2. million by the Respondent to Ms. Wu, we note that there is no documentary proof in support. What we have is Ms. Wu's confirmation in her oral evidence that a sum of HK$2,699,386.50 being the Hong Kong dollar equivalent of the RMB 2.2 million was repaid to her by the Respondent and in turn she had issued a cheque, which was produced before us, in the same amount to CGHK. Whilst the cheque itself cannot be regarded as direct and solid evidence to show that the

Respondent had actually repaid Ms. Wu, the Complainant also had no other evidence to contradict Ms. Wu's evidence that such repayment had in fact been made. However, even if the Respondent had repaid Ms. Wu, his breaches under Sections 270.2(a) and 270.3 by failing to segregate client's assets from his personal assets and to make appropriate inquiries about the source of funds are still clearly established.

146. By reason of the above, the 6th Complaint is proved.

147. In the light of the Respondent's responses and defences since the stage of investigation and all the relevant circumstances of the case, we consider that this transaction between the Respondent and Ms. Wu was questionable. We would recommend the Institute to consider taking further appropriate action on the matter and consult opinions of relevant authorities as may be necessary.

7TH COMPLAINT

148. This Complaint relates to the Respondent's failure to maintain professional knowledge and skill at the level required to ensure that CLH received competent professional service based on current developments in practice, legislation and techniques, in breach of the Fundamental Principle of Professional Competence and Due Care under Section 100.4(c) of the Code (for the audit of 2010 Financial Statements) and Section 100.5(c) of the Code (for the audit of the 2011 Financial Statements). The Complainant urged the Committee to take into account the totality of the Respondent's failure and breaches of professional standards which are the subject of the 1st to 5th Complaints, in particular, the repeated and obvious omissions to undertake basic and necessary audit procedures and to obtain sufficient and appropriate audit evidence to enable him to draw reasonable conclusions on which to base his opinion contained in the auditor's reports on the 2010 and 2011 Financial Statements.

149. The Complainant submitted that:-

(1) The manner in which the Respondent conducted the audits in question demonstrates a lack of competence and due care that one would expect from a competent accountant, and a clear failure to maintain professional knowledge and skill at the level required to ensure that a client receives competent professional services.

(2) The Respondent has demonstrated a serious lack of understanding of his professional duties as an auditor as set out in the professional standards, and even the fundamental and basic legal requirements relating to the preparation and presentation of financial statements as required under the Ordinance, with which any competent auditor ought to be familiar.

(3) The Respondent's lack of competence is fortified by the various evolving defences which he has raised in these proceedings in response to the Complaints, which are plainly untenable, and go further to show that he has failed to maintain professional knowledge and skill necessary for the purpose of rendering competent professional service to CLH.

150. On the other hand, the Respondent submitted, inter alia, that whether the 7th Complaint is made out depends on whether the Committee's determination of the 1st – 5th Complaints and the Respondent repeats the submissions already made. We have already decided that the 1st – 5th Complaints are made out. We do not accept the Respondent's defences in response to each of the above Complaints.

151. Further, the Respondent submits that all the stakeholders of CLH were made aware of CLH's adoption of Section 141D of the Ordinance, the Impairment Provision and CLH's taking out of the banking facilities. None of them have been misled and their knowledge is attributed to CLH. Thus, according to the Respondent, it cannot be said that CLH has not received

the requisite quality of services. However, as stated above, whether any shareholders were misled is no valid answer to the Complaints above and that only goes to mitigation of sanctions.

152. The Respondent also submitted that the 6th Complaint is clearly unconnected to the Respondent's provision of services to CLH and that the audits in question took place almost a decade ago and during this period the Respondent had not been subject to any other disciplinary proceedings. This shows that the Respondent is not incompetent in delivering his professional services. We do not agree.

153. By reason of the Respondent's non-compliance with the professional standards relevant to the 1st, 3rd and 4th Complaints, we agree with the Complainant's submissions that the Respondent's work demonstrated his incompetence and failure to advise CLH properly and that the Respondent had failed to maintain professional knowledge and skill at the level required to ensure that CLH received competent professional services based on current developments in practice, legislation and techniques, in breach of the Fundamental Principle of Professional Competence and Due Care under Sections 100.4(c) and 100.5(c) of the Code. In the premises, the 7th Complaint is proved.

Conclusion and Orders

154. By reason of the above, we find the Respondent guilty of the 1st, 3rd, 4th, 6th and 7th Complaints. The alternative complaints, namely the 2nd and 5th Complaints shall remain on file.

Directions

155. The Committee makes the following directions:

(1) the Complainant shall file and serve a written submission on sanctions and costs within 14 days of the service of this Decision; and

(2) the Respondent shall file and serve a written submission on sanctions and costs within 14 days of service of the Complainant's said written submission under paragraph (1).

Ms. POON, Suk Ying, Debora
Chairperson

Ms. LAM, Po Ling, Pearl
Member

Mr. CHAN, Stephen
Member

Mr. KAN, Siu Lun, Philip
Member

Ms. LAW, Elizabeth
Member

Ms. Sara Tong and Ms. Esther Mak, Counsel instructed by solicitors Messrs. MinterEllison LLP, for the Complainant

Mr. Adrian Lai, Counsel instructed by solicitors Messrs. Yung & Au, for the Respondent

Proceedings No. D-12-0734-C

IN THE MATTER OF

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

BETWEEN

Registrar of the Hong Kong Institute of
Certified Public Accountants COMPLAINANT

AND

Mr. Law Fei Shing (A15863) RESPONDENT

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

Members: Ms. POON, Suk Ying, Debora (Chairperson)
Mr. CHAN, Stephen
Ms. LAM, Po Ling, Pearl
Mr. KAN, Siu Lun, Philip
Ms. LAW, Elizabeth

Dates of Hearing: 25 and 26 January 2021 and 1 February 2021
Date of Decision: 3 August 2021
Date of Order: 3 December 2021

ORDER

Section A – INTRODUCTION

1. The complaints against Mr. LAW Fei Shing ("**the Respondent**") in this case related to, inter alia, breaches of professional standards in the audits of the 2010 and 2011 financial statements of a Hong Kong company known as Chong Luen Hing Garments Limited ("**CLH**").

2. The Respondent is the sole proprietor of F. S. Law & Co. ("**the Firm**") which was the auditor of CLH for the financial years ended 31 March 2009, 31 March 2010 and 31 March 2011.

3. At all material times, CLH had three shareholders, namely, Ms. WU Wing Che Deven ("**Ms. Wu**"), Mr. Lee Kwong On ("**Mr. Lee**") and Mr. Johnny Alan Vorzimer. They held 60%, 20% and 20% shares of CLH respectively. Ms. Wu and Mr. Lee were the only directors of CLH.

4. CLH held 100% ownership interest in a Mainland company known as Foshan Shunde Mao Nian Garments Limited (佛山市順德區茂年製衣有限公司) ("**the Factory**") which was established in the People's Republic of China.

5. On 13 November 2009, 22 November 2010 and 10 January 2012, the Firm issued auditor's reports signed by the Respondent on CLH's financial statements for the years ended 31 March 2009, 31 March 2010 and 31 March 2011 ("**the 2009 Financial Statements**", "**the 2010 Financial Statements**" and "**the 2011 Financial Statements**") respectively. The complaints in these proceedings only concerned with the 2010 and 2011 Financial Statements.

6. There were 7 complaints against the Respondent. In essence:-

   (1) The 1st and 2nd Complaints relate to the Respondent's concurrence with CLH's adoption of Section 141D of the Companies Ordinance (Cap. 32) ("**the Ordinance**") and the Small and Medium-sized Entity Financial Reporting Framework and Financial Reporting Standard ("**SME-FRF**") for preparing the 2010 and 2011 Financial Statements when CLH was not qualified to do so. The 1st and 2nd Complaints are in the alternative, in that:-

(a) the 1st Complaint relates to the Respondent's failure to obtain sufficient audit evidence to substantiate CLH's adoption of Section 141D and the SME-FRF, in breach of HKSA 250.19 (for the audit of the 2010 Financial Statements) and HKSA 250.13 (for the audit of the 2011 Financial Statements); and

(b) the 2nd Complaint relates to the Respondent's failure to prepare sufficient and appropriate audit documentation for his concurrence with CLH's adoption of Section 141D and the SME-FRF, in breach of HKSA 230.2 (for the audit of the 2010 Financial Statements) and HKSA 230.7 (for the audit of the 2011 Financial Statements).

(2) The 3rd Complaint relates to the Respondent's failure to qualify his opinion on the 2010 and 2011 Financial Statements concerning a scope limitation in verifying the accumulated provision for impairment loss in respect of the investment in the Factory in the sum of HK$10,875,000 ("**the Impairment Provision**"), in breach of HKSA 701.18.

(3) The 4th and 5th Complaints relate to the Respondent's concurrence with the non-disclosure in the 2011 Financial Statements of securities given by CLH for banking facilities granted to CLH Group (HK) Limited ("**CGHK**"), a company in which Ms. Wu held a controlling interest. The 4th and 5th Complaints are in the alternative:-

(a) the 4th Complaint relates to the Respondent's failure to obtain sufficient appropriate audit evidence to substantiate CLH's non-compliance with disclosure requirements under Section 161B of the Ordinance, in breach of HKSA 250.13; and

(b) the 5th Complaint relates to the Respondent's failure to prepare sufficient and appropriate audit documentation for his concurrence with CLH's non-disclosure, in breach of HKSA 230.7.

(4) The 6th Complaint relates to the Respondent's failure to segregate monies received from Ms. Wu on 13 January 2012 and to make appropriate inquiries on the source of funds to ensure compliance with relevant laws and regulations, in breach of Section 270 of the Code of Ethics for Professional Accountants ("**the Code**"); and

(5) The 7th Complaint relates to the Respondent's failure to maintain professional knowledge and skill at the level required to ensure that CLH received competent professional service based on current developments in practice, legislation and techniques, in breach of Section 100.4(e) (for the audit of the 2010 Financial Statements) and 100.5(c) (for the audit of the 2011 Financial Statements) of the Code.

7. Following the substantive hearing and having considered all the submissions and evidence presented by the parties, the Disciplinary Committee ("**the Committee**") found the 1st, 3rd, 4th, 6th and 7th Complaints proved as against the Respondent and the alternative complaints, namely, the 2nd and 5th Complaints shall remain on file.

8. The Committee's findings of fact and reasons are set out in the Decision dated 3 August 2021 ("**the Decision**"). This decision on sanctions and costs should be read together with the Decision.

9. Pursuant to the Committee's directions, the Registrar of the Hong Kong Institute of Certified Public Accountants ("**the Complainant**") provided their written submissions on sanctions and costs on 17 August 2021 and 2nd written submissions on 14 September 2021 whereas the Respondent provided his written submissions on 3 September 2021 and 2nd written submissions on 24 September 2021 respectively.

Section B – SANCTIONS

10. The Committee has a wide discretion in determining sanctions under Section 35 of the PAO. According to Section 4 of the Guideline to Disciplinary Committee for Determining Disciplinary Orders ("**the Guideline**"), the Committee is

recommended to take the following 3-step approach in determining a disciplinary order:-

(1) Determine the seriousness of the offence (See Section 5);

(2) Determine the appropriate sanctions based on case severity **before** considering other factors (See Section 6); and

(3) Consider impact of other factors on sanctions (i.e. past similar cases, aggravating and/or mitigating factors) in determining a disciplinary order (See Section 7).

I. Seriousness of Offences involved

11. Pursuant to Section 5 of the Guideline, the Committee should consider the full circumstances of each case before determining what sanctions should be imposed. A list of considerations is set out under Section 5.2 (1) and (2) to assist the Committee in reviewing the circumstances of the case and determining seriousness of the breach. It is further stipulated under Section 5.3 that the seriousness of disciplinary offences could be increased by some features set out thereunder.

12. It is the Complainant's submissions that the Respondent's case falls within the "very serious" category. The Complainant's submissions are three-folded:-

(1) First, the offences in the present case should be considered "very serious" in the light of the nature of each of the failures and/or offences and the relative significance of the standards or regulations breached. In this connection, the Complainant highlighted in their written submissions the relevant circumstances of the case and submitted that:-

(a) the Respondent had demonstrated a serious lack of understanding of his professional duties as an auditor as set out in the professional standards and even the fundamental and basic legal requirements relating to the preparation and presentation of financial statements required under the

Ordinance, with which any competent auditor ought to be familiar;

(b) the Respondent's lack of professional competence is fortified by the various evolving defences which he has raised in the proceedings and those defences were found by the Committee as plainly untenable;

(c) the proven breaches by the Respondent in the 1st, 3rd and 4th Complaints accumulated in the 7th Complaint against the Respondent, namely, that he had failed to maintain professional knowledge and skill at the level required to ensure that CLH received competent professional service based on current development and practice, legislation and techniques, in breach of Section 100.4(e) (for the audit of the 2010 Financial Statements) and 100.5(c) (for the audit of the 2011 Financial Statements) of the Code. Professional competence is a Fundamental Principle under the Code. The Respondent's breach in this respect is in any view very serious;

(d) the Respondent also failed to comply with his ethical duties in respect of the receipt of client monies in breach of Section 270 of the Code (6th Complaint). It is self-evidently important for certified public accountants to segregate client monies from their personal assets and to make appropriate inquiries into the source of funds; and

(e) as such, the sanctions to be imposed should reflect the fact that there were **multiple breaches of basic and fundamental technical professional standards** across various audit areas, which could have a **material impact on the accuracy and reliability of the 2010 and 2011 Financial Statements**, and also breaches of **fundamental ethical principles** that all certified public accountants are required to comply with.

(2) Second, the sanctions should also reflect the fact that the complaints involved non-compliance of multiple professional standards over two audits, meaning that they were not isolated events but were recurring (Guideline Sections 5.2(1)(j) and 5.3(a)).

(3) Third, the Respondent's lack of professional competence and failure to comply with the Code in respect of client monies could undermine public confidence in the standards of the profession and have a detrimental effect of the reputation of the profession (Guideline Sections 5.2(1)(g), (i) and 5.3(f)). It is paramount that the sanction imposed adequately reflects that breaches of professional standards will not be condoned, and the sanctions imposed should provide a deterrence against the deficiencies in order to maintain and promote public confidence in the profession.

13. In his Written Submissions, the Respondent submitted that the breaches should not be considered "very serious". In this connection, the following points should be highlighted:-

(1) The 1st, 3rd and 4th Complaints were concerned with non-compliance with technical standards imposed by the Companies Ordinance and/or accounting standards. They are regarded as technical breaches.

(2) The reasons leading to the breaches were primarily caused by differences in understanding the relevant legal and/or accounting standards. The fact that the Respondent's interpretation not being accepted is not by itself elevated as "a serious lack of understanding of his professional duties (or competence)".

(3) None of the Complaints were concerned with breach of trust or confidence by the Respondent.

(4) The Respondent has not received any benefits, pecuniary or otherwise, from the breaches.

(5) The Respondent disagrees with the Complainant that there have been ethical issues involved in the breaches. For the 6th Complaint, though it was found to have made out, the salient features are that it did not involve any abuse of trust and confidence. Instead, Ms. Wu was willing to give evidence to support the Respondent's case.

(6) There is no evidence that the Company or its shareholders had suffered loss as a result of the breaches. Mr. Lee, being the original complainant, knew full well of the true state of affairs of the Company and the Factory; and the other two shareholders did not consider their own interest being affected by the Respondent's services. The saga was caused by the shareholders' dispute which had nothing to do with the Respondent's carrying out of the statutory audits.

(7) With respect to the breaches found to have been made out, a great extent of culpability was attributed to Mr. Lee (the original complainant) who had been in control of the Factory and yet obstructing in providing the Factory's financials, resulting in no consolidated accounts having been prepared.

(8) The level of public interest involved was minimal. The Company concerned was not a public company, and there is no evidence that members of the general or investing public have suffered loss as a result of the breaches.

(9) Since the level of public interest involved was minimal, the breaches realistically would not cause damage to the reputation of the profession or undermine the public confidence in the profession.

(10) The Respondent disagrees with the Complainant's superficial submissions that the breaches had been recurring. Those breaches were isolated in nature.

14. Accordingly, the Respondent submits that the breaches concerned fall somewhere between "moderately serious" and "serious" categories, but not the "very serious" one.

15. Having considered the submissions of both parties and all the circumstances of the case, the Committee is of the view that the Respondent's breaches fall within the "very serious" category. In reaching our conclusion, we have considered all the relevant matters including the following:-

(1) We consider that the Respondent had demonstrated a serious lack of

understanding of (a) the professional standards required of him as an auditor, (b) the Code required of him as a certified public accountant, and (c) the fundamental and basic legal requirements relating to the preparation and presentation of financial statements in accordance with the Ordinance. These are matters, in our view, which any competent auditor and certified public accountant should be familiar with. In this connection, it would be useful to revisit the nature and seriousness of the subject matter of the Complaints which were proved against the Respondent:-

1st Complaint

(a) So far as the 1st Complaint is concerned, the Respondent had failed to obtain sufficient appropriate audit evidence to support his concurrence with CLH's adoption of Section 141D of the Ordinance and the SME-FRF in preparing the 2010 and 2011 Financial Statements, in breach of HKSA 250.19 (for the audit of the 2010 Financial Statements) and HKSA 250.13 (for the audit of the 2011 Financial Statements).

(b) As supported by the available evidence before the Committee, CLH held 100% ownership in the Factory at the material times and the Factory was deemed to be a subsidiary of CLH by virtue of the clear wordings of Section 2(4)(a) of the Ordinance. As such, CLH was not qualified to rely on Section 141D to adopt the SME-FRF in preparing the 2010 and 2011 Financial Statements but the Respondent had concurred with CLH's adoption of Section 141D and the SME-FRF in preparing its financial statements. The Respondent has thus failed or neglected to observe, maintain or otherwise apply the professional standard HKSA 250 in his audits of both the 2010 and 2011 Financial Statements. In other words, the Respondent's such failure or neglect was not an isolated incident. It did spread for two consecutive audit years.

(c) The Respondent then sought to rely on HKAS 27 and argued that the Factory was not a subsidiary of CLH by reason that CLH had no control over the Factory. As detailed in our Decision, we rejected the Respondent's argument as the definition of "subsidiary" in any accounting

standards cannot override the statutory definition of "subsidiary" under Section 2(4) of the Ordinance; and the concept of "control" under HKAS 27 is irrelevant in determining whether a company is a "subsidiary" under Section 141D and whether the SME-FRF is applicable. As such, the Respondent's evidence from Ms. Wu and Mr. Chen concerning the alleged loss of control by CLH over the Factory as well as the report compiled by Mr. Chen are irrelevant. For the sake of completeness, we have nevertheless dealt with the evidence of Ms. Wu and Mr. Chen. We considered the Respondent's claim of loss of control by CLH over the Factory is both unmeritorious and unsubstantiated by sufficient evidence.

(d) More importantly, the Respondent's claim of loss of control by CLH over the Factory by reason of HKAS 27 is squarely contradicted by the information contained in the 2010 and 2011 Financial Statements where he expressly acknowledged that the Factory was a subsidiary (See paragraph 41 of the Decision).

(e) We have also dealt with the various ex post facto arguments raised by the Respondent in answer to the 1st Complaint (See paragraphs 42 – 46 of the Decision). We rejected those defences as they were untenable and in any event not recorded or supported by any contemporaneous audit documentation. Further, those defences which evolved over time actually displayed a lack of professional competence and proper understanding of the professional standards required of him as an auditor.

(f) We have no hesitation to reject the Respondent's submissions that the 1st Complaint merely concerned technical breach and that the breach was primarily caused by differences in understanding the relevant legal and/or accounting standards. As mentioned hereinabove, CLH was clearly not qualified to rely on Section 141D of the Ordinance to adopt the SME-FRF in preparing the 2010 and 2011 Financial Statements. The statutory requirements under Section 141D and the professional standard laid down in HKSA250 are clear and not open to interpretation by individual auditors. The Respondent's failure to obtain sufficient appropriate audit evidence to

support his concurrence with CLH's adoption of Section 141D and the SME-FRF in the two said Financial Statements is by no means technical. It reflected the Respondent's serious lack of competence and understanding of professional standards required of him as an auditor.

3rd Complaint

(a) The 3rd Complaint concerns the Respondent's failure in both the 2010 and 2011 Financial Statements to express a qualified opinion relating to the scope limitation in assessing the Impairment Provision, in breach of HKSA 701.18. In essence, the Respondent was engaged as the auditor of CLH since 2009. In the 2009 Auditor's Report, the Respondent gave his qualified opinion regarding the underlying value of investment as follows: "... in absence of audited accounts of the subsidiary, we are unable to ascertain the underlying value of the Investment although an aggregate impairment loss of the investment amount to HK$10,875,000 have been provided". The term "impairment loss" or "impairment provision" was introduced by the Respondent in 2009 and not by the previous auditor. Whilst the sum of HK$10,875,000 being the aggregate amortization cost of investment carried forward from 2008 was newly labelled by the Respondent as "accumulated provision for impairment loss" 2009, no explanation as to such change of accounting treatment was proffered. It was only stated that there was reclassification of certain comparative figures (at paragraph 25 of the Notes to the 2009 Financial Statements).

(b) In the 2010 Auditor's Report, though the "accumulated provision for impairment loss" still remained, the Respondent did not issue any qualified opinion in respect of the underlying value of the investment as he did in the 2009 Auditor's Report. The impairment provision of HK$10,875,000 remained the same for the financial years 2009, 2010 and 2011 but the Respondent did not qualify his opinion regarding the Impairment Provision after 2009. In the Audit Working Papers, the Respondent expressly noted that there was a scope limitation regarding his audit work in assessing the appropriateness of the Impairment Provision: In the Audit Working Papers for the 2010 Financial Statements, it was

stated that the Respondent could not obtain any accounts, management accounts and other relevant information of the Factory. Due to the absence of information, the Respondent could not do any valuation test of the investment of the Factory and the recoverable amount of the investment cannot be determined. Yet, the Respondent considered that as the Factory kept supplying goods to CLH continuously, he accepted the directors' view to maintain the amount of Impairment Provision made by the former auditor. In the Audit Working Papers for the 2011 Financial Statements, similar remarks were made. We considered that the lack of financial information and accounts of the Factory has clearly presented a scope limitation in the Respondent's audit work for assessing the Impairment Provision. Such limitation in audit scope relating to a significant amount in the 2010 and 2011 Financial Statements should have been duly reflected in the relevant auditor's reports as a qualification. The Respondent's failure to express a qualified opinion concerning the said limitation of scope is a clear breach of HKSA 701.18. It is also noted that the Respondent's such failure was not an isolated mistake as it involved two consecutive audit years.

(c) The Respondent's other defences raised in answer to the 3rd Complaint are also without merit. In particular, the Respondent's contention that there was a potential sale of the Factory at about HK$4 million which might prove the Factory's fair value less cost to sell was not evidenced by any contemporaneous documents or recorded anywhere in the Audit Working Papers. His explanation that no prejudice was actually caused to any shareholder is no answer to the question as to whether he has breached any professional standards. Further, the Respondent had all along recognized the need to ascertain the recoverable amount for the purpose of making a proper assessment of the Impairment Provision. It was thus only bizarre for him to raise a new defence saying that there was no need to assess the recoverable amount.

(d) Again, we have no hesitation in rejecting the Respondent's submission that the 3rd Complaint concerned only with technical breach and the reasons

leading to the breach was mainly due to differences in understanding the relevant legal and/or accounting standards. As mentioned hereinabove, the lack of financial information and accounts of the Factory has clearly presented a scope limitation in the Respondent's audit work for assessing the Impairment Provision. The Respondent should have expressed a qualified opinion (as he did in 2009) on the 2010 and 2011 Financial Statements. The failure to do so demonstrated a lack of competence on the part of the Respondent as an auditor and a lack of understanding as to the professional standards which the Respondent has to duly comply with, maintain and observe. It cannot be said that the breach was merely technical. The requirements laid down in HKSA 701.18 are drafted in clear terms and are not open to interpretation and application by individual auditors to suit their own convenience.

4th Complaint

(a) The 4th Complaint concerns the Respondent's failure in respect of the 2011 Financial Statements to substantiate CLH's compliance with Section 161B of the Ordinance and his concurrence with CLH's non-disclosure of securities given by CLH for banking facilities granted to CGHK (a company in which Ms. Wu held a controlling interest), in breach of HKSA 250.13. The failure to disclose the Charges in question was in direct contravention to Section 161B of the Ordinance. Suffice to say, there was nothing in the Audit Working Papers to show that the Respondent had obtained sufficient appropriate audit evidence to prove that CLH had duly complied with Section 161B.

(b) Again, we reject the Respondent's submission that his breach under the 4th Complaint was merely a technical breach and that the reasons leading to the breach was primarily caused by difference in understanding or interpretation of the relevant legal and/or accounting standards. The Respondent's breach of HKSA 250.13 clearly demonstrated his lack of professional competence and understanding of the professional standards required of him as an auditor. We do not accept the Respondent's submission that his breach was merely caused by a different understanding

of the relevant professional standards.

6th Complaint

(a) Regarding the 6th Complaint, we found that the Respondent had failed to segregate the RMB 2.2 million received from Ms. Wu on 13 January 2012 and to make appropriate inquiries on the source of the funds, thereby in breach of Section 270 of the Code. We take the view that the Respondent's such breach of his ethical duties under Section 270 of the Code again demonstrated a lack of professional competence and proper understanding of the professional standards required of him as a certified public accountant. The Respondent's breach under the 6th Complaint would undermine public confidence in the standards of the profession and have a detrimental effect on the reputation of the profession (See Guideline Sections 5.2(1)(g) and (i), 5.3(d) and (f)). Whilst the Respondent had not received any benefits, pecuniary or otherwise, out of his dealing with Ms. Wu, this does not avail the Respondent because the fact remained that the Respondent had breached professional ethics by failing to segregate client's monies from his own monies and to make proper inquiries as to the source of funds in question. In fact, we have already stated in the Decision that the dealing between the Respondent and Ms. Wu was questionable. We found the breach serious and have asked the Institute to see if the case should be referred to other relevant authorities for follow-up actions.

7th Complaint

(a) By reason of the Respondent's non-compliance with the professional standards relevant to the 1st, 3rd and 4th Complaints, we considered that the 7th Complaint is proved. In essence, the Respondent's work demonstrated his incompetence and failure to advise CLH properly and he had failed to maintain professional knowledge and skill at the level required to ensure that CLH received competent professional services based on current developments in practice, legislation and techniques, in breach of the Fundamental Principle of Professional Competence and Due Care under Sections 100(e) and 100.5(c) of the Code.

(2) We have carefully considered all the Respondent's other submissions on the seriousness of the breaches including that (a) there was no breach of trust or confidence by the Respondent; (b) there was no actual loss suffered by the shareholders or CLH and (c) the level of public interest involved was minimal. However, taking into account of all the circumstances of the case and the submissions from both parties, we are of the view that the breaches involved in the present case are "very serious" in nature.

II. Appropriate Sanctions

16. Having decided that the breaches in the present case are "very serious", we turn to Section 6 of the Guideline which provides that the starting points for sanctions includes:-
    (1) Reprimand; and/or
    (2) Financial penalty; and/or
    (3) Cancellation of practising certificate and not re-issued for at least 1 year; and/or
    (4) Temporary or permanent removal from the register; and/or
    (5) Payment of costs and incidentals.

17. In this connection, a reprimand is the minimum sanction that should be handed down (§3.2(3) of the Guideline). As regards the quantum of any financial penalty, it should normally reflect the seriousness of the misconduct which is a matter for the Committee. Under Section 35(1)(c) of the PAO, the maximum penalty which can be imposed for each complaint under a complaint letter is HK$500,000. As for cancellation of practising certificate and removal from register, the Institute would normally recommend a cancellation of a practising certificate or removal from register where the Institute considers that a respondent's conduct calls into question his/her professional competence or integrity; and such an order is necessary for protection of the public.

18. Having regard to the seriousness of the breaches herein and all the relevant circumstances of the case, we are of the view that the Respondent should be reprimanded and ordered to pay financial penalty in the range of HK$100,000 to

HK$200,000 to sufficiently reflect the severity of the breaches herein. Further, the Respondent's practising certificate should be cancelled and not be re-issued for a period in the range of 12 to 24 months. Since costs should follow the event, we consider that there is no reason why the Respondent should not bear the Complainant's costs and expenses of and incidental to the proceedings (which included the costs and expenses of the Committee).

III. Other matters to be taken into account

Mitigating Factors

19. The Committee should consider if there are mitigating and/or aggravating factors.

20. The Respondent, aged 62, has a clear disciplinary record. The Respondent asked the Committee to consider various mitigating factors which included:-

(1) The breaches were spent as they took place back in early 2010s and have never recurred;

(2) The Respondent has taken remedial actions after the breaches to improve his professional knowledge and competence in discharging his duties as a member of the accountancy profession: He consistently brings himself up-to-date with respect to knowledge of the professional standards, and he regularly attends seminars and workshops and always complies with the CPD requirement;

(3) In the most recent practice review, the Quality Assurance Department of the HKICPA opined that the action plan of the Respondent's firm demonstrated the Practice's commitment to improve work quality and comply with professional standards;

(4) The prosecution of the present disciplinary proceedings was brought about by the highly unusual background e.g. complaints filed by Mr. Lee who knew full well the financial affairs of the Company out of grudge against Ms. Wu, and the Respondent being left to deal with the aftermath on his own when the disputing parties had settled their disputes;

(5) The Respondent had been practising as a sole proprietor for a long time and his firm admitted another partner in about 2017. The firm is of a small scale and its clients were predominantly consisted of small companies with no investing public involved;

(6) The Respondent is suffering from age-related health conditions (but no specific information or details were given);

(7) The Respondent was under immense pressure due to the present proceedings and is now exposed to serious sanction against his professional life and reputation; and substantial financial exposure due to the Complainant's claim for costs; and

(8) Various mitigating letters were submitted on behalf of the Respondent to show that the Respondent is a person of integrity and willing to contribute to the community.

21. We have duly considered the mitigating factors and the letters submitted on behalf of the Respondent. There can be no dispute that the Respondent is of clear disciplinary record and has never been subjected to disciplinary proceedings in his practice for no less than 21 years. The breaches herein are dated in the 2010s and there are no new breaches committed by the Respondent. As supported by the mitigating letters, he is of previous good character.

Aggravating Factors

22. There are, however, as the Complainant submits, various aggravating factors which the Committee should take into account:-

(1) The Respondent did not show any remorse. As of today, the Respondent is still trying to shift the blame to Mr. Lee. This demonstrated the Respondent's lack of remorse and responsibility on the matter.

(2) The Respondent had deliberately adopted delaying tactics which resulted in substantial delay to the proceedings. In particular:-

(a) By a letter dated 5 September 2012, Mr. Lee complained to the Institute regarding the Respondent's audits of the 2009 – 2011 Financial Statements and he claimed to be misled as to the financial position of CLH and the Factory. After the Institute's year-long investigation, the proceedings were commenced in September 2014. During the investigation, the Respondent confirmed through his legal representatives that the audit working papers he provided were complete. The Respondent also made comments and representations in response to Mr. Lee's complaints.

(b) The present proceedings had been significantly delayed by the Respondent's conduct and various unmeritorious applications. As a result, it has taken more than 6 years for the matter to be heard before the Committee. In particular, the present proceedings were delayed for almost 5 years as a result of the Respondent's two unsuccessful applications for leave to commence judicial review:-

(i) The Respondent applied for leave to commence judicial review against the decision made by the Council of the Institute ("the Council") to refer Mr. Lee's complaint to the Committee (HCAL 132/2014, 2 February 2015). Such application was refused by the Court of First Instance and the Respondent's subsequent application for leave to appeal all the way to the Court of Final Appeal was also refused (HCMP 748/2015, 21 April 2016 and 20 October 2016 and FAMV 50 of 2016 by way of paper disposal dated 29 June 2017).

(ii) When the proceedings resumed over two years later in June 2017, the Respondent filed his Respondent's Case but shortly afterwards he applied for leave to commence a second judicial review on 27 April 2018. Such second application was again refused by the Court of First Instance (HCAL 750 of 2018, 26 November 2018 and [2018] HKCFI 2592) and the Respondent's subsequent appeal to the Court of Appeal was dismissed on 13 June 2019 ([2019] 4

HKLRD 225). In the Court of Appeal's judgment, it was stated that "the **significant and unnecessary delay is predominantly caused by [the Respondent's] two consecutive unsuccessful leave applications to apply for judicial review** regarding various intermediate and procedural decisions made by the institute and the Disciplinary Committee. This is clearly unsatisfactory as further demonstrated by the fact that the applicant took out the present application not long after the first unsuccessful leave application, thereby further interrupted the progress of the disciplinary proceedings again after already a long delay." (§§39 – 42 of the Judgment, emphasis added).

(c) The proceedings were then further delayed when the Respondent through adducing expert evidence on accounting and auditing standards referred for the first time to copies of some audit planning memos and audit issue memos ("**the Memos**") which were not part of the Audit Working Papers provided by the Respondent to the Institute and were never referred to in the Respondent's Case and Reply. The Memos were only provided to the Complainant on 16 October 2019, that is, 5 years after the commencement of the proceedings.

(d) Thereafter, upon the Respondent's application on 13 January 2020, the Committee granted leave to the Respondent to rely on the Memos and directed, inter alia, that the Respondent should file a witness statement to address the provenance and authenticity of the Memos. The Respondent then sought to defer the filing of the said witness statement on 21 February 2020 and 4 March 2020 but ultimately he withdrew his application to adduce the Memos on 11 March 2020. Though the Committee exceptionally granted additional time to the Respondent to file such witness statement, no witness statement was filed. Hence, the Memos were expunged from evidence.

(e) On 15 January 2021, the Respondent applied for an adjournment of the hearing which was due to commence on 18 January 2021 for medical

reasons. At the hearing on 18 January 2021, counsel for the Respondent informed the Committee that the Respondent's legal team were only instructed to apply for an adjournment and that if the application for adjournment was refused, they would not attend the substantive hearing. Eventually, the Respondent's application was granted and the hearing was adjourned to 25 January 2021.

(3) The Respondent's defences changed and evolved over time and this demonstrated a lack of candour on the part of the Respondent in responding to his professional governing body. As evidenced by his manner in defending these proceedings, there was an obvious lack of understanding on the part of the Respondent as to the standards required of him as an auditor.

23. In response to the Complainant's above submissions, the Respondent submitted, inter alia, that:-

(1) The Respondent should not be penalized for invoking his constitutional right to take the matter to judicial review. In any event, the Complainant has been properly compensated by costs following the outcome of the judicial review proceedings and as such the Respondent should not be doubly jeopardized by a more serious sanction;

(2) The Respondent explained that his application to adduce the Memos was withdrawn because his intended engagement of a replacement accounting expert in place of the deceased expert was strongly opposed by the Complainant and that the replacement expert was unable to finish his report within a short time frame. Though the Committee subsequently granted extra time for the Respondent to produce a new report, the replacement expert was already released by the Respondent and the release was irreversible.

(3) The Respondent denied having played delaying tactic in adjourning the hearing on 18 January 2021. He submitted that his application for adjournment was supported by medical evidence which was not challenged by the Complainant.

(4) Lastly, the Respondent contended that the defences he advanced were mainly offering different interpretations and analyses on the legal and/or accounting standards. Those defences were raised on the same set of facts and evidence and did not cause additional time and costs to be incurred.

24. Having considered the parties' submissions, we are of the view that there are aggravating factors in the present case which we should take into account in deciding what orders of sanction should be imposed.

25. First of all, the Respondent's submissions that he is the scapegoat out of the grudges between Mr. Lee and Ms. Wu and that some of the breaches were merely technical showed clearly that the Respondent had limited remorse. Afterall, the 1st, 3rd, 4th, 6th and 7th Complaints were found proved against the Respondent out of his own deeds. He must therefore bear the consequences instead of attributing the blame to Mr. Lee. Further, so far as the 6th Complaint is concerned, we have already stated clearly in the Decision that the Respondent had breached professional ethics by failing to segregate a client's monies with his own monies and to make inquiries as to the source of funds. We consider that the breach is serious and have asked, in the Decision, the HKICPA to see if the case should be referred to other authorities for further follow up actions.

26. Second, the present proceedings were delayed for almost 5 years as a result of the Respondent's two unmeritorious applications for leave to commence judicial review. As pointed out by the Court of Appeal, the significant and unnecessary delay was predominantly caused by the Respondent's two consecutive unsuccessful leave applications to apply for judicial review regarding various intermediate and procedural decisions made by the Institute and the Committee (See [2019] 4 HKLRD 225 at §§39 – 42). Whilst the Respondent was perfectly entitled to exercise his constitutional right to apply for judicial review, we cannot lose sight of the fact that the present proceedings were indeed delayed for almost 5 years as a result and that the Respondent's conduct in pursuing unmeritorious and vexatious applications for leave to apply for judicial review and appeal all the way to the Court of Final Appeal are matters which we are fully entitled to take

into account.

27. Likewise, the Respondent's conduct in attempting to adduce the Memos 5 years after commencement of the proceedings thereby causing further delay to the proceedings is also far from satisfactory. Suffice to say, the Committee has endeavoured to balance the interests of all parties and to accommodate the Respondent's need to file a replacement expert report within reasonable time. Extra time was granted to the Respondent for filing such report and it was the Respondent who decided to withdraw his application to adduce the Memos as evidence.

28. Further, the Respondent's urgent application on 15 January 2021 to adjourn the hearing scheduled to be heard three days afterwards on 18 and 19 January 2021 was another instance whereby the proceedings were further delayed. The application was, according to the Respondent, necessitated by medical reasons. On the first day of the scheduled hearing on 18 January 2021, the Respondent did not attend the hearing and was only represented by his counsel and solicitors. The legal team of the Respondent informed the Committee that they only had instructions to apply for the adjournment on behalf of the Respondent and that they would not attend the hearing any further if the application for adjournment was refused. According to the medical evidence provided to the Committee, the Respondent would be admitted to the hospital urgently for an operation to be performed on 18 January 2021. As such, he would be unable to attend the hearing on 18 and 19 January 2021. The medical proof submitted to us included a letter issued by the Respondent's doctor and an admission form of the hospital indicating that the Respondent was admitted thereto at 18:10 hours on 17 January 2021. Needless to say, it would be highly undesirable in the eyes of justice and fairness if the substantive hearing were to proceed in the absence of not only the Respondent but also his legal representatives. With great reluctance, the Committee adjourned the hearing to 25 January 2021 and directed the Respondent to, inter alia, serve a medical report from his treating doctor and an affirmation setting out matters including a chronology setting out the Respondent's medical conditions and the timing of him giving instructions to his solicitors and counsel regarding the application for adjournment.

29. Lastly, we have already found that various defences raised by the Respondent changed and evolved over time. It demonstrated the lack of candour on the part of the Respondent in responding to his professional governing body. It does not make any sense for the Respondent to say that the various defences were mainly advanced to offer different interpretations and analyses on the legal and/or accounting standards. As mentioned hereinabove, the professional standards required of the Respondent as an auditor and a certified public accountant were laid down in clear terms and not open for individual auditors or certified public accountants to cherry pick different interpretations to suit their convenience. It also defies common sense and logic for the Respondent to introduce defences just to offer different interpretations or analyses on the legal or accounting standards when such defences were without merit or that they actually contradicted the Respondent's stated case and evidence.

30. We do not agree with the Respondent's submission that the various defences were raised on the same set of facts and evidence and thus it did not cause additional time and costs to be incurred. As noted in our Decision, some of the Respondent's defences were no longer actively pursued in his Written Closing Submissions. However, the Respondent's counsel verbally informed the Committee that he had no instruction to abandon any of the points or defences raised before. In the circumstances, the Committee had no choice but to deal with each and every point or defence raised by the Respondent though it appeared clearly that the Respondent was no longer relying on some of the points in his Closing Submissions. The Respondent's conduct in defending the Complaints in this way would also be taken into account by the Committee.

Past Cases

31. The Committee notes that it is not bound by the decisions reached by a previous committee. Each case turns on its own facts. It is for the Committee to determine the appropriate penalty in the light of the specific facts and circumstances of each case. That said, the Complainant has referred to three past decisions with similar features to the present case, namely, (1) D-19-1460P, (2) D-17-1278F and (3) D-17-1232F:-

(1) D-19-1460P is a case where the four complaints against the respondent were all found proven on the basis of his own admission. The case related to the respondent's breaches of multiple professional standards in respect of two audit engagements, his failure to maintain an adequate quality control system in his practice and to comply with the fundamental principle of professional competence and due care under the Code. The Disciplinary Committee ordered that (1) the respondent be reprimanded, (2) a practising certificate shall not be issued to him for 18 months; and (3) the respondent do pay a penalty of HK$50,000.

According to the Respondent, however, this case should not be relied upon because the Committee therein did not articulate the basis upon which the sanctions were arrived and it only stated that all relevant factors have been considered.

(2) D-17-1278F is a case where the 1st respondent denied all three complaints against him but he chose not to appear at the substantive hearing. He was found to have breached multiple professional standards in his audit of a listed company, failed to comply with the fundamental principle of professional competence under the Code, failed to ensure that the engagement quality control reviewer appointed was independent of the audit team; and failed to discuss significant matters with the said reviewer. The Disciplinary Committee in the case noted (at §29(2)(a)), amongst other things, that the auditing irregularity in question was not a particularly serious mistake on its own but the manner in which the respondent had chosen to defend that mistake demonstrated an obvious lack of understanding of the requirements of the relevant accounting standards. This was not the first time the respondent was found to have fallen below professional standards in a listed company audit. The Disciplinary Committee ordered that (1) the respondent be reprimanded; (2) a practising certificate shall not be issued to the respondent for a period of 2 years; and (3) the respondent do pay a penalty of HK$50,000.

The Respondent argued that this case is distinguishable as various factors were

highlighted to justify a more severe penalty, namely: (1) the respondent had previous conviction records; (2) the company was a listed company which affected the interest of the investing public; (3) the reputation of the profession was at stake; and (4) there was a continuing lack of professional competence on the part of the respondent. The Respondent submitted that none of these factors are present in his case.

(3) D-17-1232F is a case where the respondents admitted all the complaints against them and did not dispute the facts. In particular, the 1st respondent was found to have breached multiple professional standards in respect of the audit of a listed company over two consecutive financial years and had failed to comply with the fundamental principle of professional competence under the Code. The Disciplinary Committee ordered that (1) the 1st respondent be reprimanded; (2) a practising certificate shall not be issued to the 1st respondent for a period of 36 months; and (3) the 1st respondent do pay a penalty in the sum of HK$150,000.

The Respondent argued that this case is also distinguishable as the company was a listed company and thus it was important to maintain public confidence in the profession.

32. The Respondent submitted that the following cases showed that only cases with exceptionally serious aggravating features warrant a severe suspension of practising certificate for a long period of time:-

(1) D-16-1182F is a case where the respondents have committed multiple breaches in auditing a listed company. They were suspended from practice for 6 – 9 months.

(2) D-16-1208P is a case where the respondent had committed multiple breaches and he was only suspended from practice for 6 months because (a) he had taken remedial actions after the breaches, (b) the scale of operation of his practice was small and (c) his clients were companies of tiny size.

(3) D-14-0935C is a case where the respondent had committed multiple breaches in auditing 5 companies. There had been serious and flagrant breaches of the core principle of independence or apparent independence of auditors. Yet, in the light of the respondent's age, health and pressure in dealing with the disciplinary proceedings, he was only suspended from practice for 6 months.

(4) D-15-1102P is a case where the respondent had committed multiple breaches and he had knowingly submitted materially false or misleading statements. He was suspended from practice for one year.

(5) D-15-1100H is a case where the respondent had committed multiple breaches in four consecutive years. The respondent paid minimal regard to the then pending civil and criminal investigation against the company's controller. The respondent was suspended from practice for one year.

(6) D-16-1139F is a case where the respondent committed multiple breaches in auditing a listed company. The respondent had previous convictions and one of which resulted in an order of removal. The case proved against him involved dishonesty or fraud. He was suspended from practice for one year.

33. In the light of the above cases, the Respondent submitted that long suspension is warranted only for cases with exceptionally aggravating features e.g. providing misleading information to the Disciplinary Committee, breaches involving dishonesty, fraud or criminal element; and without such features a suspension of less than one year would generally be regarded as a sufficient and proportionate measure to reflect the gravity of cases even in cases involving multiple breaches and listed companies.

34. In reply, the Complainant submitted that all the cases cited by the Respondent above were admitted cases where the respondents were thus entitled to a significant discount as to sanctions to reflect their remorse and insight into their mistakes.

35. As mentioned above, we are aware that the Committee is not bound by previous

decisions made by previous Committees. Each case is decided on its own facts. It is the duty of the Committee to decide on the order of sanctions having regard to the specific facts and circumstances of the case.

Orders as to Sanctions

36. We have considered the proposed orders as to sanctions made by the Complainant and the Respondent in their respective Written Submissions. Having regard to the matters detailed hereinabove including the very serious nature of the offences herein, the delay caused by the Respondent, his conduct throughout the proceedings, his evolving and inherently inconsistent defences and all the relevant circumstances of the case, we are of the view that the following orders should be made:-

(1) **Reprimand** – The Respondent be reprimanded under Section 35(1)(b) of the Professional Accountants Ordinance, Cap. 50 ("**PAO**");

(2) **Financial penalty** – The Respondent do pay a penalty at **HK$160,000** under Section 35(1)(c) of the PAO; and

(3) **Cancellation of practising certificate** – The practising certificate of the Respondent be cancelled under Section 35(1)(da) of the PAO and it shall take effect on the 42nd day from the date of this Order; and a practising certificate shall not be issued to the Respondent for a period of **15 months** under Section 35(1)(db) of the PAO.

Orders as to Costs

37. Costs will follow the event. The Respondent acknowledged expressly in his Written Submissions that he is obliged to pay costs and expenses incidental to the disciplinary proceedings. The Complainant submits that the Respondent should pay the costs and expenses of and incidental to the proceedings of the Complainant (including costs and expenses of the Committee) under Section 35(1)(iii) of the PAO in the sum of **HK$4,943,123** (for which HK$4,331,237 is the Complainant's costs and HK$611,886 is the Committee's costs). The Respondent submits that he does not object to the quantum with respect to the costs incurred by the

Committee in the sum of HK$611,886 but he objects to the excessive amount claimed by the Complainant and asked for a detailed bill of costs, followed by the Respondent submitting his list of objections.

38. In their submissions, the Complainant submitted that the costs and expenses incurred were reasonably and necessarily incurred. Further, the Committee should impose an enhanced costs order against the Respondent given his obstructive conduct throughout the proceedings, the long delay he caused, substantial wasted costs were incurred as a result of the Complainant's delaying tactic and repeated change of stance; the constant shifting of defences; and the need to instruct external counsel to represent the Complainant in the light of the Respondent's uncooperative and obstructive attitude. In reply, the Respondent argued, inter alia, that any enhanced costs order would not be justified in the circumstances and that the Respondent should only bear costs that are reasonably and necessarily incurred.

39. We have carefully considered the submissions from both the Complainant and the Respondent on the issue of costs as well as all the relevant circumstances of the present case. We agree with the Complainant that an enhanced costs order against the Respondent is appropriate in the light of the Respondent's conduct in the case, the delay involved and the very serious nature of the offences herein. We take the view that the Respondent should bear the Complainant's costs and expenses of and incidental to the proceedings in full.

40. Pursuant to §74 of the Guidelines for the Chairman and the Committee on Administering the Committee Proceedings Rules, "**rather than conducting as in-depth forensic examination of costs incurred as takes place at a court taxation hearing, the preferable approach is for the Committee to require the parties to submit a brief schedule** setting out their costs in respect of the proceedings and then, after hearing **brief submissions** from the parties as to the appropriate quantum of costs, makes a summary assessment of the amount payable. The process is similar to the **"gross sum" assessment** model sometimes used by courts and is intended to **minimise the administrative burden** associated with determining costs. A draft form of schedule to be submitted by the parties is

attached as annex 6." (emphasis added).

41. In our view, the Complainant's Statement of Costs dated 17 August 2021 has already contained more detail than is required under Annex 6 of the said Guidelines. Sufficient details have been included in the Complainant's Statement of Costs for the purposes of assessment. Having reviewed the said Statement of Costs, we are inclined to accept that the Complainant's costs of and incidental to the proceedings were reasonably and necessarily incurred. We do not consider it necessary for the Complainant to provide a detailed breakdown of costs as requested by the Respondent. Accordingly, we order the Respondent to pay the costs and expenses of and incidental to the proceedings of the Complainant including the costs and expenses of the Committee in the sum of **HK$4,943,123**.

Respondent's application to stay the publication of the decisions pending appeal

42. Last but not least, the Respondent sought to apply to stay the publication of the Decision pending appeal. In this connection, the Complainant has already confirmed in their Written Submissions that in the light of the statutory policy underpinning Section 38(2) of the PAO and the case of Registrar of Hong Kong Institute of Certified Public Accountants v X [2017] 3 HKLRD 541, the Decision (including the decision on sanction and costs) will not be published until the expiry of the appeal period or if an appeal is lodged by the Respondent within the appeal period, the final disposal of the appeal. Accordingly, there is no need for the us to make any order for stay as requested by the Respondent.

Ms. POON, Suk Ying, Debora
Chairperson

Ms. LAM, Po Ling, Pearl
Member

Mr. CHAN, Stephen
Member

Mr. KAN, Siu Lun, Philip
Member

Ms. LAW, Elizabeth
Member