

IN THE MATTER OF

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

BETWEEN

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

AND

Mr. Andrew David Ross FIRST
Membership No. A01858 RESPONDENT

Mr. Fok Wai Ming SECOND
Membership No. A14447 RESPONDENT

Baker Tilly Hong Kong Limited THIRD
Corporate Practice No. M0154 RESPONDENT

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

Members: Mr. Wong Wing Yan Kenneth (Chairman)

Mr. Lee Tsung Wah Jonathan

Mr. Wan Chuck Fan David

Ms. Leung Chi Ying Kathy

Mr. Espina Anthony Joseph

ORDER & REASONS FOR DECISION

1. This is a complaint made by the Registrar of the Hong Kong Institute of Certified Public Accountants (the "**Institute**") against Mr. Andrew David Ross, certified public accountant (practising) (the "**First Respondent**" or "**Ross**"), Mr. Fok Wai Ming, certified public accountant (practising) (the "**Second Respondent**" or "**Fok**"), and Baker Tilly Hong Kong Limited, a corporate practice (the "**Third Respondent**" or "**BTHK**"). Section 34(1)(a)(vi) of the Professional Accountants Ordinance ("**PAO**") applied to the Respondents.
2. The Complaint as set out in a letter dated 6 October 2016 (the "**Complaint**") are as follows:-

BACKGROUND

- (1) Century Ginwa Retail Holdings Limited (formerly known as China Golden Development Holdings Limited)("Company") was incorporated in Bermuda and its shares are listed on the Main Board of the Stock Exchange of Hong Kong (Stock code: 00162).
- (2) The financial statements of the Company and its subsidiaries ("Group") for the years ended 31 December 2008 ("2008 Financial Statements") and 31 December 2009 ("2009 Financial Statements")(collectively "Financial Statements") were stated to have been prepared in accordance with the Hong Kong Financial Reporting Standards ("HKFRS") issued by the Hong Kong Institute of Certified Public Accountants .
- (3) BTHK was appointed as auditor of the Company. Ross was the director responsible who issued the auditor's reports on behalf of BTHK for the 2008 Financial Statements and 2009 Financial Statements on 24 April 2009 and 20 April 2010 respectively. The auditor's reports stated that the audit for the years was conducted in accordance with the Hong Kong Standards on Auditing ("HKSA") and gave a true and fair view on the Financial Statements.
- (4) Although Fok, whose position was director before leaving BTHK, did not sign the auditor's reports on the Financial Statements, he was substantially involved in the audits of the Financial Statements based on the totality of facts available.
- (5) The Group's financial statements for the year ended 31 December 2010, which was audited by another practice, retrospectively adjusted to correct certain prior year errors.
- (6) On 22 March 2013, the Council of the Financial Reporting Council ("FRC") directed the Audit Investigation Board ("AIB") to investigate possible auditing irregularity in relation to the Financial Statements.
- (7) In carrying out its investigation, the AIB found non-compliances with financial reporting standards and auditing irregularities in relation to the recognition and /or measurement of the following areas:
 - (i) Assets and liabilities relating to the acquisition of a subsidiary in year 2008;
 - (ii) Impairment loss on goodwill for year 2008;
 - (iii) Revenue transactions relating to customer loyalty program for year 2009;
 - (iv) Depreciation of certain leasehold improvements for year 2009;
 - (v) Provision for social insurance as at years ended 2008 and 2009; and
 - (vi) Provision for contingent rentals as at year ended 2009.
- (8) In their representations to the FRC, BTHK asserts that they had performed adequate audit procedures based on the information provided by the Company; exercised their professional judgment in concurring the Company management's accounting treatments and did not admit that the audits on the Financial Statements contained any audit deficiencies as alleged in the AIB report.
- (9) BTHK submitted to the FRC that Ross was only the Engagement Quality Control Reviewer ("EQCR") for the audits despite he was the one who issued

the auditor's reports for the Financial Statements. It was argued that Ross was the executive director who signed the auditor's reports after he performed high-level review as an EQCR. BTHK suggested that though Fok was not an executive director of BTHK, he was assigned to work in the capacity of an engagement director.

- (10) In August 2013, Fok resigned from BTHK in his position as a director. He abstained from commenting on the findings of the AIB on the basis that he was never the engagement director or the EQCR of the audits .
- (11) On 21 September 2015, the FRC referred to the Institute a report of the AIB dated 24 August 2015 to the Institute pursuant to section 9(f) of the FRC Ordinance, Cap.588 .

SUMMARY OF PRINCIPAL ISSUES

In respect of First Complaint

- (12) In the Financial Statements, the Company failed to:
 - (a) recognize and measure identifiable assets acquired and liabilities assumed at their fair value arising from the Company's acquisition of a subsidiary in accordance with paragraphs 36, 37, 45 and B16 under Appendix B of HKFRS 3 "Business Combinations", paragraphs 12 of HKAS 38 "Intangible Assets" and paragraph AG64 under Appendix A of HKAS 39 "Financial instruments: Recognition and Measurement";
 - (b) conduct proper impairment test of goodwill, in accordance with paragraphs 91 to 93 of HKAS 36 "Impairment of Assets";
 - (c) recognize sales as multiple revenue transactions under the customer loyalty program, in accordance with Hong Kong (IFRIC) Interpretation 13 "Customer Loyalty Programmes";
 - (d) depreciate leasehold improvements within the lease term, in accordance with paragraph 56 of HKAS 16 "Property, Plant and Equipment";
 - (e) calculate correctly the provision for social insurance; and
 - (f) make adequate provision of contingent rent, in accordance with paragraph 25 of HKAS 17 "Leases".
- (13) The associated financial effects of the above non-compliances were considered material to the Financial Statements.
- (14) In carrying out the audits of the Financial Statements, BTHK was found to have failed to comply with the following HKSA's:
 - (a) Paragraphs 9 and 16 of HKSA 230 "Audit Documentation";
 - (b) Paragraphs 12 to 14 of HKSA 320 "Audit Materiality";
 - (c) Paragraphs 2 of HKSA 500 "Audit Evidence";

- (d) Paragraphs 12 and 12e of HKSA 520 "Analytical Procedures";
 - (e) Paragraphs 8 and 10 of HKSA 540 "Audit of Accounting Estimates";
 - (f) Paragraphs 37 and 50 of HKSA 545 "Auditing Fair Value Measurements and Disclosures";
 - (g) Paragraphs 2, 12 and 15 of HKSA 620 "Using the Work of an Expert"; and
 - (h) Paragraphs 11 and 13 of the HKSA 700 "The Independent Auditor's Report on a Complete Set of General Purpose Financial Statements".
- (15) In their responses to the Institute, BTHK maintained that they had performed adequate audit procedures based on the best, latest information available or provided by the Company; that they had exercised its professional judgment in concurring with the Company management's accounting treatments; and that they did not admit that the audits on the Financial Statements contained any audit deficiencies as alleged in the AIB report.
- (16) The Institute concurred with the AIB report and considered that the working papers show apparent lack of adequate audit procedures and documentation to support BTHK's unqualified opinion in the above audit areas.

In respect of Second Complaint against Ross

- (17) In responding to the Institute's enquiry, BTHK denied that Ross was the engagement director of the audits. It was asserted that Ross acted as the EQCR who performed high level tasks, such as reviews and sign-off of the auditor's reports for the Financial Statements on behalf of BTHK. They asserted that Fok was in substance the engagement director and that Ross was simply the signing director for the engagement.
- (18) Such denial is inconsistent with and contradicts the fact that Ross was clearly designated as the engagement director in the audit planning memorandum for the 2009 Financial Statements, that he had signed as the "Director-in-charge" in the relevant engagement letter entered between BTHK and the client dated 6 January 2009, that he reviewed the audit working papers and signed the auditor's reports for the Financial Statements as the director responsible.
- (19) With regard to the signing of auditor's reports, HKSA 700 states that, "The auditor's report also identifies the director responsible for the performance of the audit engagement contemplated by such report, and states his/her full name as appearing in his/her practising certificate and the practising certificate number". The auditor's report for each of the Financial Statements stated the full name and the practising certificate number of Ross.
- (20) If Ross was not the engagement director, he should not have signed the auditors' report as such conduct would amount to a breach of Rule 8 of the CPRR.
- (21) There is no evidence to support the suggestion that Ross was appointed as, and simply so acted, as the EQCR of these engagements.
- (22) In any event, it is clear that Ross played a substantive role in the engagements.

- (23) Accordingly, Ross failed to act diligently in accordance with section 100.4(c) as elaborated in section 130.1 of the then Code of Ethics for Professional Accountants ("COE").

In respect of Third Complaint against Fok

- (24) Fok was the senior audit team member for both audit engagements.
- (25) Whilst Fok maintained that he was not the engagement director of both years' audits, it is evident that he played a significant role and had substantial involvement in the audits. Fok did not comment on BTHK's non-compliance with the auditing standards but claimed that he worked under the direct supervision of Ross who would review, approve and reject his audit work.
- (26) From the working papers it is clear that Fok did not ensure (a) that sufficient evidence was obtained and (b) that documentation adequately reflected that appropriate audit procedures had been done. Clearly, his conduct fell short of his duties as a key member in the audit engagement. Consequently, Fok failed to act diligently in accordance with section 100.4(c) as elaborated in section 130.1 of the COE.

In respect of Fourth Complaint

- (27) Paragraphs 36, 38 and 39 of HKSA 220 Quality Control for Audits of Historical Financial Information requires the engagement partner (director) for audits of listed companies to ensure appointment of an EQCR, discuss significant audit matters with the EQCR; and issue the auditor's report after the completion of the engagement quality control review.
- (28) In spite of Ross's assertion that he acted as the EQCR, BTHK's working papers for both 2008 and 2009 audits indicated no evidence that any engagement quality control review had been performed or that any EQCR had even been appointed. As identified in §19 above, Ross had held himself out as the director in charge/responsible for the engagement.
- (29) As the engagement director of both years' audits, Ross would have failed to comply with HKSA 220.

In respect of Fifth Complaint (In the Alternative to the Fourth Complaint)

- (30) Even if Ross was the EQCR as asserted, he would have failed to comply with paragraphs 38 and 39 of HKSA 220 since an EQCR is required to carry out an objective evaluation of significant judgments made by the engagement team and conclusions reached in formulating the auditor's report. There is no evidence or documentation showing any objective evaluation had been performed by Ross.

In respect of Sixth Complaint

- (31) Paragraph 3, 42 and 60 of HKSQC1 (effective as of 15 June 2005) and paragraphs 30, 32, 35, and 42 of HKSQC1 (effective as of 15 December 2009) require a practice to have a system of quality control designed to provide it with

reasonable assurance that the practice and its personnel comply with professional standards, and that reports issued by the practice or engagement partners/directors are appropriate in the circumstances. Accordingly, the practice should clearly assign responsibility for each engagement to an engagement partner/director and require for appropriate engagement an engagement quality control review be conducted.

- (32) Based on the denials of both Fok and Ross that they were the engagement director, there would be no individual assuming the responsibility as the director responsible for the auditor's reports for the Financial Statements. The absence of a clearly designated engagement director raises serious doubt as to whether BTHK's system of quality control could have provided any reasonable assurance that the practice and its personnel would comply with professional standards or that the auditor's reports issued would be appropriate.

THE COMPLAINTS

First Complaint

- (33) Section 34(1)(a)(vi) of the PAO applies to BTHK in that, as the auditor for the Financial Statements, they failed or neglected to observe, maintain or otherwise apply any or all of the following professional standards:

- (a) Paragraphs 9 and 16 of HKSA 230;
- (b) paragraphs 12 to 14 of HKSA 320;
- (c) Paragraph 2 of HKSA 500;
- (d) Paragraphs 12 and 12e of HKSA 520;
- (e) Paragraphs 8 and 10 of HKSA 540;
- (f) Paragraphs 37 and 50 of HKSA 545;
- (g) Paragraphs 2, 12 and 15 of HKSA 620; and
- (h) Paragraphs 11 and 13 of HKSA 700

Second Complaint

- (34) Section 34(1)(a)(vi) of the PAO applies to Ross in that, non-compliances with eight professional standards in two-year audits show that he failed to act diligently in accordance with section 100.4(c) as elaborated in section 130.1 of the COE.

Third Complaint

- (35) Section 34(1)(a)(vi) of the PAO applies to Fok in that, non-compliances with eight professional standards in two-year audits show that he failed to act diligently in accordance with section 100.4(c) as elaborated in section 130.1 of the COE.

Fourth Complaint

- (36) Section 34(1)(a)(vi) of the PAO applies to Ross in that he issued the auditor's reports for the Financial Statements as director responsible for the audit, he failed or neglected to observe, maintain or otherwise apply paragraphs 36, 38 and 39 of HKSA 220 because he had failed to ensure appointment of an independent EQCR and ensure that an objective engagement quality review had

been done for the audits.

Fifth Complaint (In the Alternative to the Fourth Complaint)

- (37) Alternatively, section 34(1)(a)(vi) of the PAO applies to Ross in that, as EQCR of the audits of the Financial Statements, he failed or neglected to observe, maintain or otherwise apply paragraphs 38 and 39 of HKSA 220 because he had failed to carry out an objective engagement quality control review.

Sixth Complaint

- (38) Section 34(1)(a)(vi) of the PAO applies to BTHK in that they had failed or neglected to observe, maintain or otherwise apply HKSQC1 because there was inadequate policies and procedures to ensure the clear assignment of responsibility for the audit engagement of the Company to an engagement director and appointment of an EQCR.

The Proceedings

3. The Notice of Commencement of Proceedings was issued to the parties on 6 June 2017.
4. The Complainant filed the Complainant's Case on 1 August 2017.
5. On 4 August 2017, the First and Third Respondent wrote to the Disciplinary Committee and stated that they would admit the complaint against them. On 22 August 2017, the Complainant suggested to the Committee that
 - (a) the steps as set out in paragraphs 17 to 30 of the Disciplinary Committee Proceedings Rules ("**Rules**") be waived with respect to the First, Second, Fifth and Sixth Complaints of the Complaint Letter and that the admitted complaints can be disposed of on the basis of the admission made; and
 - (b) the Complainant and the First and Third Respondents to make written submissions on sanctions and costs under paragraph 31 of the Rules after the Disciplinary Committee's determination of the complaint against the Second Respondent.
6. The Committee approved the above proposal.
7. On 26 September 2017, the Second Respondent wrote to the Disciplinary Committee and stated that he would admit the complaint against him.
8. In light of the admission by all the Respondents, the Chairman directed that parties needed not file cases and replies and the oral hearing originally scheduled was vacated. Parties were directed to make submissions on sanctions and costs.
9. The Complainant and the Respondents provided their written submissions on sanction and costs on 26 October 2017 and 9 November 2017 respectively.

10. In considering the proper order to be made in this case, the Disciplinary Committee has had regard to all the aforesaid matters, including the particulars in support of the Complaints and the Respondents' conduct throughout the proceedings, and the respective written submissions of the Complainant and the Respondents. This Committee has taken note of the following:

(1) In so far as the Third Respondent is concerned:

- (a) The First Complaint. The Third Respondent admitted this Complaint, which concerns the failure or neglect to observe, maintain or otherwise apply eight auditing standards in respect of six audit areas which are listed in paragraphs 2 (12) – (14) above. We agree with the Complainant's submission that the Third Respondent's quality control system was clearly not sufficiently robust to identify and prevent the multiple non-compliances with the auditing standards identified, and that the Third Respondent should have ensured that there was adequate system of quality control that could provide reasonable assurance that the practice and its personnel would comply with professional standards or that the auditor's reports issues would be appropriate.
- (b) The Sixth Complaint. The Third Respondent admitted this Complaint, which concerns the practice's inadequate policies and procedures to ensure a clear assignment of responsibility for audit engagements in respect of the engagement director and appointment of an EQCR, in breach of HKSQC I. The Third Respondent's practice at the relevant time was confusing, in that although there was a senior director to sign on auditor's report, in fact there was another engagement director who actually took charge of the audit work. We agree with the Complainant's submissions that this confusing practice led to subsequent denials of both the Second and Third Respondents that they were the engagement director for the 2008 and 2009 audits, and that the absence of a clearly responsible engagement director could have caused the deficiencies identified in this case. We however note, and have taken into account, that the said confusing signing practice is no longer used by the Third Respondent.

(2) In so far as the First Respondent is concerned:

- (a) The First Complaint. The First Respondent was the director who signed on behalf of the Third Respondent the auditor's reports for the Financial Statements. Therefore, we agree with the Complainant's submission that he was the director responsible for the audits under HKSA 700 and as such should be held responsible for the breach of the auditing standards identified under this Complaint.
- (b) The Second Complaint. The First Respondent admitted this Complaint. In addition to signing on the auditor's reports, he was also the designated engagement director in the engagement letter and in the audit planning memorandum. Nonetheless, the audit working papers show that he played a minimum role in the audit works, and that it was really the Second Respondent who was the director doing the audit works.

(c) The Fifth Complaint. The First Respondent admitted this Complaint. Whilst he acted as the EQCR in the 2008 and 2009 audits, there was no documentary evidence showing that he had carried out an objective engagement quality control review in accordance with HKSA 220. This failure led to the serious consequence, i.e. the deficiencies in the six audit areas identified under the First Complaint. Had the review been done, the risk of the audit failures should at least have been lowered.

(3) In so far as the Second Respondent is concerned:

(a) The Third Complaint. The Second Respondent admitted this Complaint. Although he denied that he was the engagement director nor the EQCR, the evidence clearly shows that he played a key and leading role in the 2008 and 2009 audits. He supervised and checked the work performed by the audit team members. We agree with the Complainant's submission that primarily, the audit failures in this case were caused by the lack of diligence by the audit team to carry out adequate audit procedures and documentation on significant areas which were material to the Financial Statements, and the number of deficiencies identified demonstrates that the level of supervision and checking performed by the Second Respondent as the leader of the audit team fell below the level of competency and due care as expected of a CPA. We also agree with the Complainant's submission that the effects of such deficiencies were significant as the auditors failed to identify material misstatements in the Financial Statements which would have affected the investors of the listed company.

11. In light of the above matters, having considered sanctions that are commensurate with the deficiencies identified in the Complaints, the seriousness of the case, the objective of maintaining the public reputation of the profession, the culpability of each Respondent and the relevant audit fees received, and the submissions respectively made by the Complainant and the Respondents, the Disciplinary Committee orders that:-

- (a) all the Respondents be reprimanded under Section 35(1)(b) of the PAO;
- (b) the Third Respondent pay a penalty of HK\$250,000 under Section 35(1)(c) of the PAO;
- (c) the First Respondent pay a penalty of HK\$100,000 under Section 35(1)(c) of the PAO;
- (d) the Second Respondent pay a penalty of HK\$100,000 under Section 35(1)(c) of the PAO;

12. Since it was the conduct of the Respondents which gave rise to the current proceedings, we take the view that they should pay the costs and expenses of the proceedings, and as submitted by the Complainant, since the admission from the Second Respondent was received only after the Complainant's Case was filed, the

costs incurred by the Complainant to prepare its Case should be paid by the Second Respondent alone. In addition, as these proceedings were instituted as a result of an investigation under the Financial Reporting Council Ordinance, the Respondents should also pay to the FRC the costs and expenses in relation to the investigation incurred by the FRC. Accordingly, we order that:

- (a) the Respondents do pay the costs and expenses of and incidental to the proceedings of the Complainant in the sum of HK\$124,448.30 (being the aggregate of items B(i), C, D ("Photocopies - General") and E of the Statement of Costs, Appendix 4 to the Complainant's Submission on Sanctions dated 26 October 2017) under Section 35(1)(iii) of the PAO. The said sum shall be shared equally by the Respondents; and
- (b) the Second Respondent do pay the costs and expenses of the Complainant's Case in respect of the Second Respondent in the sum of HK\$14,912 (being the aggregate of items B(ii) and D ("Photocopies – Complainant's Case in respect of Second Respondent")) under Section 35(1)(iii) of the PAO.

Dated 5 January 2018