

IN THE MATTER OF

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

BETWEEN

The Practice Review Committee of the Hong Kong
Institute of Certified Public Accountants

COMPLAINANT

AND

Mr. CHIK, Wing Kan, Peter
Membership No. A13807

RESPONDENT

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

Members: Mr. LIM Kian Leng, Malcolm (Chairman)

Ms. LAI, Nadine

Ms. LEE, Fu Fan

Mr. CHAN, Wai Man, Raymond

Mr. YEUNG, Chi Wai, Edwin

ORDER AND REASONS FOR DECISION

1. This is a complaint made by the Practice Review Committee (“**PRC**”) of the Hong Kong Institute of Certified Public Accountants (the “**Institute**”) against Mr. CHIK, Wing Kan, Peter, certified public accountant (the “**Respondent**”). Sections 34(1)(a)(vi) and 34(1)(a)(viii) of the PAO apply to the Respondent.
2. The particulars of the Complaint as set out in a letter from the Executive Director on behalf of the PRC dated 3 May 2019 (the “**Complaint**”) are set out below.

Background

3. The Respondent is a sole proprietor of PCW CPA Limited (corporate practice no. S0593) (the "**Practice**"). He is responsible for the Practice's quality control system and the quality of its audit engagements.
4. A first practice review was conducted on the Practice and the practice reviewer ("**Reviewer**") reviewed the following two audit engagements:
 - (i) Client M, a private entity, for the year ended 31 March 2017. The relevant auditor's report was issued on 13 November 2017.
 - (ii) Client C, a private entity, for the year ended 31 December 2016. The relevant auditor's report was issued on 19 August 2017.
5. The Reviewer found a number of deficiencies in the Practice's quality control system and audit engagements. In addition, the Respondent was found to have provided false and/or misleading answers in the 2016 practice review self-assessment questionnaire ("**EQS**") and "Audit Health Screening" checklist which were submitted to the Reviewer prior to the practice review.
6. A copy of the Reviewer's report dated 20 September 2018 outlining the practice review findings and the Respondent's responses to the dated draft report was referred to. In his response, the Respondent did not dispute the facts and observations made by the Reviewer.
7. The PRC considered that the deficiencies identified showed a serious lack of due care and regard to the audit quality and demonstrated professional misconduct by the Respondent. Moreover, the incorrect reporting in the EQS and "Audit Health Screening" checklist raised PRC's concern about the integrity of the Respondent. The PRC therefore decided to raise a complaint against the Respondent.
8. Further copies of the working papers in relation to Client M and Client C were provided by the Respondent. The Respondent confirmed that they represented the complete documentation for the audit engagements.

The Complaints

First Complaint

9. Section 34(1)(a)(vi) of the PAO applies to the Respondent for having failed or neglected to

observe, maintain or otherwise apply a professional standard for his failure to maintain an adequate quality control system.

Second Complaint

10. Section 34(1)(a)(vi) of the PAO applies to the Respondent in that he had failed or neglected to observe, maintain or otherwise apply a professional standard in respect of the false and/or misleading answers he provided in the 2016 EQS and the Audit Health Screening checklist.

Third Complaint

11. Section 34(1)(a)(vi) of the PAO applies to the Respondent in that he had failed or neglected to observe, maintain or otherwise apply a professional standard in respect of his audit of Client M for the year ended 31 March 2017.

Fourth Complaint

12. Section 34(1)(a)(vi) of the PAO applies to the Respondent in that he had failed or neglected to observe, maintain or otherwise apply a professional standard in respect of his audit of Client C for the year ended 31 December 2016.

Fifth Complaint

13. Section 34(1)(a)(viii) of the PAO applies to the Respondent in that he has been guilty of professional misconduct as a result of his failure to comply with multiple professional standards.

Facts and circumstances in support of the Complaints

Complaint 1

14. Hong Kong Standard on Quality Control 1 "*Quality Control for Firms that Perform Audits and Reviews of Financial Statements, and Other Assurance and Related Services Engagements*" ("**HKSQC 1**") requires all firms of professional accountants to establish and maintain an adequate system of quality control which meets the requirements under the standard.

15. The Practice failed to maintain an adequate system of quality control which meets the HKSQC 1 requirements in respect of the following elements:
- (i) Ethical requirements
 - (ii) Human resources
 - (iii) Monitoring
 - (iv) Engagement performance

Ethical requirements, human resources and monitoring process

16. The Practice did not establish any policies and procedures nor develop a quality control manual to govern its conduct and its personnel. In particular, there were no policies and procedures to require :
- (i) the Practice and its personnel to comply with ethical requirements, in accordance with paragraph 20 of HKSQC 1;
 - (ii) it had sufficient personnel with the competence and capabilities to perform engagements and to enable the Practice to issue reports that were appropriate, in accordance with paragraph 29 of HKSQC 1; and
 - (iii) a monitoring review process on the Practice's system of quality control had been maintained, in accordance with paragraph 48 of HKSQC 1.

Engagement performance

17. Paragraph 32 of HKSQC 1 requires a practice to establish policies and procedures designed to provide it with reasonable assurance that engagements are performed in accordance with professional standards.
18. The Practice failed to comply with this requirement because for Clients M and C, the Practice did not carry out adequate audit procedures in accordance with the following Hong Kong Standards on Auditing ("HKSA"):
- (i) Obtain an understanding of the entities' internal controls relevant to the audits; evaluate the design of those controls to determine whether they have been properly implemented in the period under audit in accordance with HKSA 315 (Revised) "*Identifying and Assessing the Risks of Material Misstatement through Understanding the Entity and Its Environment*".

- (ii) Design and perform audit procedures in response to the assessed risks of material misstatements in accordance with HKSA 330 *"The Auditor's Responses to Assessed Risks"*.
 - (iii) Perform audit procedures, including journal entry testing to address the risks of management override of controls, in accordance with HKSA 240 *"The Auditor's Responsibilities Relating to Fraud in an Audit of Financial Statements"*.
 - (iv) Determine materiality and performance materiality as required by HKSA 320 *"Materiality in Planning and Performing an Audit"*.
 - (v) Obtain an understanding of the legal and regulatory framework applicable to the entity and evaluate whether the entity complied with law and regulations that affect the financial statements in accordance with HKSA 250 *"Consideration of Laws and Regulations in an Audit of Financial Statements"*.
 - (vi) Design and perform analytical procedures to assess whether the financial statements were consistent with the auditor's understanding of the entity in accordance with HKSA 520 *"Analytical Procedures"*.
 - (vii) Obtain sufficient appropriate audit evidence regarding the appropriateness of management's use of the going concern assumption in the preparation of the financial statements and evaluate the management's assessment of the entity's ability to continue as a going concern, in accordance with HKSA 570 (Revised) *"Going Concern"*.
 - (viii) Design an appropriate basis for determining sample size and selecting samples for audit tests in accordance with HKSA 530 *"Audit Sampling"*.
19. The number of non-compliances with professional standards in the Respondent's audits demonstrates that he did not establish effective policies and procedures in the Practice to ensure that the audit reports issued were appropriate, in accordance with HKSQC 1.
20. As HKSQC 1 is a professional standard under the PAO, section 34(1)(a)(vi) applies to the Respondent.

Complaint 2

21. The fundamental principle of integrity under sections 100.5(a), 110.1 and 110.2 of the Code of Ethics for Professional Accountants ("**COE**") requires a professional accountant to be straightforward and not knowingly be associated with information which contains false or misleading statements; or information furnished recklessly.
22. Prior to the practice review visit, the Respondent submitted a completed Audit Health Screening Checklist ("**Checklist**") in which the Practice had said "Yes" to having performed and documented audit procedures as required under HKSA's 240, 250, 315, 320, 330, 520 and 570 for all its audit engagements.
23. As indicated in paragraph 18 above, the Reviewer found no evidence that the Practice had carried out the relevant audit procedures for the two engagements (Clients M and C) that were selected for review.
24. In addition, the Reviewer discovered that certain answers provided by the Respondent in the 2016 EQS were also incorrect. For example, the EQS reported that:
 - (i) the Practice had implemented quality control policies and procedures and had retained documentation to provide evidence of the operation of each element of the system of quality control;
 - (ii) a monitoring review, including a review of implementation of firm's quality control policies and procedures and a review of completed audit engagement files, was completed during the period from 1 April 2015 to 31 March 2016 and the results had been documented; and
 - (iii) the Practice's audit methodology and procedures had been updated to take into account the latest requirements of HKSA's and other professional standards.
25. However, this was untrue. In his submission, the Respondent stated that the misstatements in the Checklist and EQS were due to a misunderstanding of the reporting requirements.
26. The Respondent does not dispute that his audits of Clients M and C did not comply with the auditing standards. Therefore, the answers in the Checklist were false and/or misleading.
27. In addition, the Respondent does not deny that there were no quality control policies and procedures, and no monitoring review having been performed by the Practice. Therefore, the answers in the EQS were also false and/or misleading.

28. In the circumstance, the Respondent had knowingly or recklessly submitted the false/misleading answers in the EQS and Checklist, in breach of sections 100.5(a), 110.1 and 110.2 of the COE.
29. As COE is a professional standard referred to in the PAO, section 34(1)(a)(vi) applies to the Respondent in this respect.

Complaint 3

30. The fundamental principle of Professional Competence and Due Care under sections 100.5(c) and 130.1 of the COE requires a professional accountant to maintain professional knowledge and skill at the level required to ensure that clients receive competent professional services and act diligently in accordance with applicable technical and professional standards.
31. The Reviewer found a number of breaches of Hong Kong Standard on Auditing in the Respondent's audit of Client M, which is a company engaged in the business of engineering contractors.

Breach of HKSA 210 and PN 900

32. The financial statements of Client M were stated to have been prepared in accordance with the Hong Kong Small and Medium-sized Entity Financial Reporting Standard ("**SME-FRS**") issued by the Institute.
33. According to paragraph 22 of SME-FRS, an entity is qualified for reporting its financial statements under SME-FRS if it satisfies certain criteria, amongst other things, relating to the size of the entity prescribed in the Hong Kong Companies Ordinance (Cap. 622) ("**CO**"). A private entity is qualified for reporting under SME-FRS if it does not exceed any two of the following conditions:
 - Total annual revenue of HK\$100 million
 - Total assets of HK\$100 million at the end of the reporting period
 - 100 employees
34. The working papers of Client M for the year ended 31 March 2017 showed that Client M had total revenue of HK\$194 million (over HK\$100 million) and total assets of HK\$76 million (below HK\$100 million). There was no information about the number of employees of Client M in the working papers. Therefore, it was uncertain whether Client M was

qualified for preparing its financial statements under SME-FRS.

35. Paragraph 6(a) of HKSA 210 "*Agreeing the Terms of Audit Engagements*" requires an auditor to determine whether the financial reporting framework applied in the financial statements is acceptable. Paragraph 11 of Practice Note 900 (Revised) "*Audit of Financial Statements Prepared in Accordance with the Small and Medium-Sized Entity Financial Reporting Standard*" ("**PN 900**") requires an auditor to obtain sufficient appropriate audit evidence for determining whether an entity with financial statements prepared under SME-FRS could fulfil the prescribed criteria under the CO.
36. The working papers did not show that the Respondent had carried out any audit procedures to assess whether Client M had fulfilled the qualifying criteria for reporting under SME-FRS. As such, the Respondent failed to comply with paragraph 6(a) of HKSA 210 and paragraph 11 of PN 900.

Breach of HKSA 500

37. Paragraph 6 of HKSA 500 "*Audit Evidence*" requires an auditor to design and perform audit procedures that are appropriate in the circumstances for the purpose of obtaining sufficient appropriate audit evidence.
38. The audit working papers of Client M did not show that adequate audit procedures had been carried out for the purpose of obtaining sufficient appropriate audit evidence in respect of the following accounts which are material to the financial statements.

- (i) Secured bank loans of HK\$21,007,882

The working papers showed that bank loans of HK\$20,091,843 were classified under non-current liabilities and bank loans of HK\$916,039 were classified under current liabilities at the reporting date. The working papers show no evidence of audit work performed to assess whether the classification of the bank loans reported in the financial statements was appropriate.

- (ii) Accounts receivable of HK\$17,435,886

The auditor had circularized confirmation request to a major customer of Client M to confirm a receivable balance of HK\$17,121,051. In its reply, the customer confirmed an amount which was HK\$9 million less than that of Client M's records.

The audit documentation shows that the auditor accepted the management's explanation that the difference of HK\$9 million was due to the timing difference in recording the transactions without any evidence of having done any work to verify the management's assertion. The auditor did not perform adequate audit procedures to ascertain whether the reported account receivables and sales were overstated.

(iii) Amount due from an associate of HK\$22,101,142

No impairment assessment on the amount due from an associate was carried out to ascertain the valuation of the balance at the year end date.

(iv) Revenue of HK\$194,000,111

The audit documentation shows that the auditor had performed substantive tests on revenue by checking the recorded amounts with the sales invoices. There was no evidence that the auditor had performed further audit procedures to ascertain that the basis of revenue recognition was appropriate.

39. The Respondent did not dispute the Reviewer's findings. The above failures by the Respondent to perform adequate audit procedures to substantiate the multiple accounts which are material to the financial statements demonstrate that he did not carry out the audit of Client M with the level of professional competence and due care to ensure compliance with auditing standards, in breach of sections 100.5(c) and 130.1 of the COE.

40. As COE is a professional standard referred to in the PAO, section 34(1)(a)(vi) applies to the Respondent in this respect.

Complaint 4

41. The Reviewer also found a number of breaches of HKSA's in the Respondent's audit of Client C demonstrating that the Respondent failed to carry out the audit with the expected level of professional competence and due care. Client C is a company engaged in the trading of electronic components.

Breach of HKSA 500

42. The auditor's report issued by the Respondent for Client C stated that the audit was conducted in accordance with HKSA's issued by the Institute.

43. The audit working papers showed that the auditor did not carry out adequate procedures to obtain sufficient appropriate audit evidence in respect of the following accounts which are material to the financial statements:

(i) Trade creditors of HK\$34,159,057

The auditor had performed alternative procedures for some of the confirmations where he did not receive a reply he only checked against the supplier invoices. However, it was noted that certain invoices had been amended by Client C without explanation. There was no evidence of any work done to investigate the cause of the changes so as to ascertain the reliability of the amended invoices. Further, the Respondent did not perform alternative work for two confirmations where no replies were forthcoming.

In his submission, the Respondent did not dispute the findings. He stated that he would perform adequate and effective procedures in this respect.

(ii) Trade debtors of HK\$45,701,616

There was no evidence of any alternative procedures done to obtain relevant and reliable audit evidence on the confirmations where no replies were forthcoming. Also, there was no impairment assessment performed to ascertain the valuation of the balances at the reporting date.

In his submission, the Respondent did not dispute the findings. He stated that he would perform adequate and effective procedures in this respect.

(iii) Stocks of HK\$23,019,724

The audit documentation shows that Client C had identified obsolete stocks but no provision was made on the obsolete items. In accepting this treatment, there was no evidence that the auditor had assessed (i) the financial impact of these obsolete stocks; and (ii) whether stock provision was required so as to ensure that stocks were stated at the lower of costs and net realizable value at the year end date.

There was no evidence that the auditor had performed any procedures to investigate the cause and assess the financial impact of the differences identified between the

quantities stated in the stock list and identified in the stock count.

There was also no evidence of audit work done to ascertain the existence and valuation of stocks which were kept at overseas warehouses at the end of the reporting period.

In his submission, the Respondent stated that he would perform adequate audit procedures to address the Reviewer's findings.

- (iv) Amount due from a related party of HK\$20,131,690 and amount due to a related party of HK\$25,287,639

No audit work was performed to consider the payment terms and the appropriateness of the classification and disclosures in the financial statements.

- (v) Prepayment of HK\$9,757,382

No audit work was performed on the prepayment account to assure the existence and valuation of the balance at year end date.

- (vi) Turnover and cost of sales of HK\$110,353,536 and HK\$73,386,301 respectively

There was no evidence that audit procedures had been carried out to check the delivery documents to ensure that turnover/purchase was properly recognized upon transfer of risks and rewards of goods sold/received.

Breach of HKSA 220

- 44. Paragraph 12 of HKSA 220 "*Quality Control for an Audit of Financial Statements*" ("**HKSA 200**") requires that an audit engagement partner should be satisfied that appropriate procedures regarding the acceptance and continuance of client relationships and audit engagements have been followed. This includes determining whether the engagement team is competent to perform the audit engagement and has the necessary capabilities, including time and resources.
- 45. In response to the practice review's findings, the Respondent explained that a number of findings were identified in Client C because the audit team had a tight reporting deadlines for completing the audit. The accounting records of Client C were only made available to

them one month before the reporting deadline.

46. The significant findings in Client C and the Respondent's response indicated that when deciding whether to accept the engagement, the Respondent did not carry out adequate assessment of whether the Practice had sufficient time and resources to handle the audit of Client C, in accordance with paragraph 12 of HKSA 220.
47. The above failures demonstrated that the Respondent had not maintained professional knowledge and skill at the level required to ensure that clients received competent professional services; and/or acted diligently in accordance with applicable professional standards when providing professional services, in breach of sections 100.5(c) and 130.1 of the COE.
48. As the COE has been a professional standard referred to in the PAO, section 34(1)(a)(vi) applies to the Respondent.

Complaint 5

49. The Respondent has been a practising member since 1999. In 2014, the Institute issued a reminder to all practising members that the PRC would take robust actions against practices for failure to take appropriate actions to prevent common deficiencies frequently communicated to practising members from occurring in their practice. The reminder described five defined areas of deficiencies and called for practices to implement adequate procedures to address the relevant requirements and failure to do so would constitute serious professional misconduct.
50. The Reviewer's findings above show that the Respondent failed and/or neglected to take heed of the Institute's advice in that his Practice did not comply with four out of the five defined areas of deficiencies described in the reminder. In addition, the vast number of deficiencies found in the quality control policies and procedures and audits of Client M and Client C, including those concerning basic audit requirements, pointed to the serious lack of professional competence and due care on the part of the Respondent when carrying out audits.
51. In addition, the false/misleading information submitted by the Respondent in the EQS and the Audit Health Screening checklist had raised concerns on the professional conduct and integrity of the Respondent.
52. The above multiple and serious failures as explained in Complaints 1 to 4 demonstrate a

blatant disregard by the Respondent to the requirements under the professional standards and the fundamental principles under the COE, and amount to professional misconduct.

The Submissions

53. The Complainant submits that nature and severity of these failures demonstrate a serious neglect by the Respondent to comply with the Institute's ethical requirements and professional standards. Even though the Respondent had made early admission of liability, it should not diminish the seriousness of the case. The Complainant considers that the appropriate sanctions should be a reprimand, penalty of an amount not less than HK\$50,000 and cancellation of the Respondent's practising certificate and an order that it should not be issued to the Respondent for at least 18 months.
54. The Respondent does not dispute any of the facts and circumstances in support of the complaints. However, he argues that the Practice employs audit staff with up to 30 years of experience and he took over the practice only since 2014. He also argues that he took the earliest opportunity to admit the Complaints, and he pleads for leniency on sanctions to be imposed so as to minimize the adverse impact on his clients. He is willing to pay the costs of the Complainant and these proceedings.
55. In considering the appropriate sanctions, the Disciplinary Committee needs to first determine the severity of the complaints. Parts 5.2 and 5.3 of the Guideline to Disciplinary Committee for Determining Disciplinary Orders ("**the Guideline**") sets out the considerations that are aimed to assist the Disciplinary Committee in determining the seriousness of the breach. For example:
 - (1) Nature and circumstances of the breach, such as:
 - (a) nature of failure and/or offence
 - (b) relative significance of the standard or regulation breached
 - (c) whether the breach could undermine confidence in the standards of the profession
 - (d) whether the breach involved ethical issues
 - (e) whether the breach may damage the reputation of the profession
 - (f) whether the breach was isolated or recurring
 - (2) Conduct of the respondent, e.g. whether the offence committed was intentional or

deliberate, or occurred as a result of carelessness or recklessness.

- (3) The seriousness of the offences could be increased by, e.g. recklessness or blatant disregard for regulatory requirements or principles, nature and impact of the breach, and/or detrimental effect on reputation of and confidence in the profession.
56. The Disciplinary Committee agrees with the Complainant that the Respondent's conduct shows serious disregard for regulatory requirements, raises doubt on his professional competence and integrity, and would have detrimental effect on the confidence in the profession. Even though the Respondent had made early admission of liability, it should not diminish the seriousness of the case. We note the Respondent's early admission of the Complaint which led to the saving of costs.
57. Notwithstanding that the Respondent has stated that he has taken steps to update, improve and rectify the quality control for his Practice and that similar breaches would not occur in the future, the Respondent has not stated the exact steps that have been taken.

The Order

58. In considering the appropriate order to be made, the Disciplinary Committee has taken into account the facts of the case, the Submissions by the Complainant and the Respondent including the submissions on sanctions and costs and mitigating circumstances.
59. The Disciplinary Committee ORDERS that:-
- (a) the Respondent be reprimanded under section 35(1)(b) of the PAO;
 - (b) the Respondent pay a penalty of HK\$50,000 under section 35(1)(c) of the PAO;
 - (c) the practising certificate issued to the Respondent be cancelled on the 42nd day from the date of this order under section 35(1)(da) of the PAO;
 - (d) a practising certificate shall not be issued to the Respondent for a period of 15 months from the date that the Respondent's practising certificate is cancelled under subparagraph (c) above under section 35(1)(db) of the PAO; and
 - (e) the Respondent do pay the costs and expenses of and incidental to the proceedings of the Complainant in the sum of HK\$41,802 under section 35(1)(iii) of the PAO.

Dated 23 December 2019

Mr. LIM Kian Leng, Malcolm
Chairman

Ms. LAI, Nadine
Member

Mr. CHAN, Wai Man, Raymond
Member

Ms. LEE, Fu Fan
Member

Mr. YEUNG, Chi Wai, Edwin
Member