

IN THE MATTER OF

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

BETWEEN

The Registrar of the Hong Kong Institute  
of Certified Public Accountants

COMPLAINANT

AND

Kwok Kam Piu (A16997)

RESPONDENT

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

Members: Mr. DAWES Victor (Chairman)  
Ms. LO Fung Yee, Daphne  
Ms. YANG Elizabeth Ling  
Miss FUNG Suet Ngan, Gladys  
Mr. SHEN Ka Yip, Timothy

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### ORDER AND REASONS FOR DECISION

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1. This is a complaint made by the Registrar (the “**Complainant**”) of the Hong Kong Institute of Certified Public Accountants (the “**Institute**”) against Kwok Kam Piu, a practising certified public accountant (the “**Respondent**”).
2. The particulars of the Complaint as set out in a letter from the Registrar to the Council of the Institute dated 28 April 2020 (the “**Complaint**”) are as follows:

### BACKGROUND

- (1) In 2017, the Respondent was appointed as the auditor of King Honour Holdings Limited (“**Company**”), the principal activity of which was property investment holding. He issued an unmodified auditor’s report on the Company’s financial statements for the year ended 30 April 2017 (“**2017 FS**”) on 29 December 2017, and on the Company’s financial statements for the year ended 30 April 2018 (“**2018 FS**”) on 20

September 2018. The two sets of financial statements were prepared in accordance with SME-FRS<sup>1</sup>. The audits were conducted in accordance with HKSA<sup>2</sup> and with reference to PN 900 (Revised)<sup>3</sup>.

- (2) A number of audit deficiencies were identified in respect of the Respondent's audits of the Company's 2017 FS and 2018 FS. As a result, four complaints have been raised.

## **THE COMPLAINTS**

### Complaint 1

- (3) Section 34(1)(a)(vi) of the PAO applies to the Respondent, in that he failed or neglected to observe, maintain or otherwise apply professional standards in relation to the amount due from a director in the audits of the financial statements of King Honour Holdings Limited for the years ended 30 April 2017 and 2018.

### Complaint 2

- (4) Section 34(1)(a)(vi) of the PAO applies to the Respondent, in that he failed or neglected to observe, maintain or otherwise apply professional standards in relation to (i) dividend paid, (ii) amount due to shareholders, and (iii) management fees paid in the audit of the financial statements of King Honour Holdings Limited for the year ended 30 April 2018.

### Complaint 3

- (5) Section 34(1)(a)(vi) of the PAO applies to the Respondent, in that he failed or neglected to observe, maintain or otherwise apply professional standards in relation to the maintenance of professional skepticism and/or properly respond to risks of material misstatements in the audits of the financial statements of King Honour Holdings Limited for the years ended 30 April 2017 and 30 April 2018.

### Complaint 4

- (6) Section 34(1)(a)(vi) of the PAO applies to the Respondent in that he failed or neglected to observe, maintain or otherwise apply a professional standard for his failure to maintain professional knowledge and skill at a level required, and act diligently and in accordance with applicable professional standards, to ensure his clients received competent professional services in relation to the 2017 and 2018 audits for King Honour Holdings Limited.

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<sup>1</sup> Hong Kong Small and Medium-sized Entity Financial Reporting Standard

<sup>2</sup> Hong Kong Standards on Auditing

<sup>3</sup> Practice Note 900 (Revised) *Audit of Financial Statements Prepared in Accordance with the Small and Medium-sized Entity Financial Reporting Standard*

## FACTS AND CIRCUMSTANCES IN SUPPORT OF THE COMPLAINT 1

- (7) The Company adopted a mode of operation under which a controlling shareholder-cum-director (“MD”) used his personal bank account to manage the Company’s receipts and disbursements. The net effect of those transactions was recorded as a “net movement” in the “Due from director” account in the Company’s books, which showed a year-end balance of HK\$2.3 million (receivable) in 2017 and HK\$3.2 million (receivable) in 2018.
- (8) In the 2017 and 2018 audits, the Respondent performed inadequate work with respect to the “Due from director” balances, which were above materiality, determined at 1% of net assets value of approximately HK\$40,000 for the 2017 audit and HK\$16,000 for the 2018 audit.
- (9) Based on the audit working papers, the procedures performed in 2017 were limited to casting and checking the balance to the ledger; whereas in the 2018 audit, the procedures performed were limited to casting and obtaining an audit confirmation from the MD confirming the year-end balance of the “Due from director” account.
- (10) Given the potential for management override by the MD over recording of the balance he owed the Company, a reasonable auditor would have been expected to perform additional testing. However, there is no evidence of any work performed on the validity of “net movement” amounting to HK\$291,098 in 2017 and HK\$891,354 in 2018, which represented the net effect of all transactions going through the MD’s personal bank account.
- (11) The Respondent submitted that he had checked the receipts to the MD’s personal bank book and the net movement, but there is no evidence of the performance of this purported procedure in the working papers. Further, a rather stable revenue stream from rental income would be expected based on the Company’s mode of operations. However, there is nothing in the audit working papers to suggest that the Respondent was alerted to a three-fold increase in the “net movement” amount in 2018. The audit working papers simply offer no trace of any procedures performed by the Respondent in respect of the “net movement” amounts in 2017 and 2018.
- (12) On the above basis, it is said that the Respondent failed to:
  - (a) perform adequate procedures to obtain sufficient appropriate evidence with respect to the accuracy of the due from director balance as recorded in the 2017 FS and 2018 FS, in breach of paragraph 6 of HKSA 500; and/or
  - (b) perform adequate risk assessment associated with related party relationships and transactions, in breach of paragraphs 18 and 19 of HKSA 550.

- (13) As HKSAs are professional standards referred to in the PAO, section 34(1)(a)(vi) applies to the Respondent in this respect.

## **FACTS AND CIRCUMSTANCES IN SUPPORT OF COMPLAINT 2**

### *Dividend paid*

- (14) A dividend paid of HK\$7.2 million was recorded in the 2018 FS. The 2018 working papers included a copy of the Company's resolution regarding the declaration of the dividend. A remark in the relevant working paper indicated that the dividends were "prepaid" by the MD to the shareholders on 20 May 2009, 17 January 2014 and 22 January 2015. Payment of the dividend was recorded by crediting the MD's due from director account and debiting equity.
- (15) The Respondent represented that he had verified the prepayments of the dividend by the MD by checking to the MD's personal bank account records. However, such audit procedure was not documented in the relevant audit working papers.
- (16) There is also no documentation in the audit working papers of audit confirmations requested or obtained from shareholders regarding their receipt of dividend payments from the MD. In his email dated 10 October 2019, the Respondent represented to the Institute that he was still waiting to receive the confirmations from the shareholders. Then in April 2020, the Respondent provided the confirmation replies from four shareholders, claiming that he had received two of those confirmations in August 2018 (before the auditor's report for the 2018 FS was signed off); and the other two in October 2019.
- (17) The Respondent explained that he had not referred to the two confirmations received in August 2018 because they were included in the old documents which were transferred from his home to the mini warehouse in January 2019; and he only retrieved them from the warehouse in October 2019. Further, the Respondent admitted that he omitted the procedure related to obtaining confirmations in the working papers.
- (18) Based on the above, with respect to the dividend paid which was a material amount in the 2018 FS, the Respondent failed to prepare adequate audit documentation in breach of paragraph 8 of HKSA 230.

### *Amount due to shareholders*

- (19) The 2018 FS included amounts due to shareholders totalling HK\$16.7 million, which arose out of reclassification of balances as stated in the 2017 FS. The working papers include a leadsheet showing audit confirmation request was made to five shareholders regarding their individual balances. Of the five confirmation requests, the Respondent

received three positive confirmations. One shareholder did not respond, while another returned the confirmation form without confirming his balance. For the latter two confirmations, the Respondent did not perform alternative procedures on the balances due to these two shareholders, e.g. by contacting the respective shareholders directly by other means to resolve the issue. The unconfirmed balances represented HK\$4.1 million (25%) of the total due to shareholders amount at 2018 year-end.

*Management fees paid*

- (20) The 2018 FS included a prior year adjustment (“PYA”) with respect to management fees paid of HK\$6 million. The fees were paid to the MD’s own company for services rendered to the Company from 2000 to 2017, which constituted related party transactions. Apart from obtaining a confirmation from the MD confirming the year-end balance due from him regarding his director’s account, the Respondent did not perform any procedures to verify the validity or existence of the management fees recorded in the PYA, e.g. checking to relevant contract/agreement and/or directors’ resolution.
- (21) The Respondent’s failure to properly identify the management fees paid as related party transactions was a breach of paragraphs 15, 18, and 21 of HKSA 550.
- (22) As a result of the deficiencies noted in (19) and (20) above, the Respondent failed to obtain sufficient appropriate audit evidence in accordance with paragraph 6 of HKSA 500 with respect to the amount due to shareholders and the management fees, both of which were material items, as recorded in the 2018 FS.
- (23) As HKSAs are professional standards referred to in the PAO, section 34(1)(a)(vi) applies to the Respondent in this respect.

**FACTS AND CIRCUMSTANCES IN SUPPORT OF COMPLAINT 3**

- (24) The breaches as set out in Complaints 1 and 2 above also pointed to the Respondent’s failure to adequately consider increased fraud risks arising from potential management override, as explained in paragraphs (25) to (27) below.
- (25) The Respondent documented in the 2017 working papers that there was little scope for management override. In the 2018 working papers, he noted the potential for management override given the MD’s role as the managing director and major shareholder. The Company’s mode of operations did not change in 2018, nor the MD’s role. Hence, the Respondent seemed to have reached inconsistent conclusions on his assessment of management override in 2017 and 2018 based on the same set of circumstances. The Respondent rightly pointed out the risk of management override in his 2018 audit. Therefore, his 2017 assessment

was not correct or appropriate. For both years, the Respondent did not identify significant fraud risk due to the “straightforward nature of client’s operations”.

- (26) Based on the above, the Respondent did not perform a proper fraud risk assessment in the 2017 and 2018 audits considering the following circumstances:
- (a) the “unusual” arrangement of the MD’s using his personal bank account for Company transactions;
  - (b) the lack of documentary evidence to support the MD’s “dividend prepayments” to shareholders in past years; and
  - (c) the lack of documentary evidence to support the validity of the management fees paid to the MD’s own company.
- (27) Under the circumstances, the conclusion of “no significant fraud risk” would be inappropriate in his 2017 and/or 2018 audits, and demonstrated the Respondent’s failure to:
- (a) maintain professional skepticism throughout the audit(s), recognizing the possibility that a material misstatement due to fraud could exist, in accordance with paragraph 12 of HKSA 240; and/or
  - (b) design and perform further audit procedures which nature, timing and extent were responsive to the assessed risks of material misstatement due to fraud at the assertion level, including risks of management override, in accordance with paragraphs 31 to 33 of HKSA 240.
- (28) As HKSAs are professional standards referred to in the PAO, section 34(1)(a)(vi) applies to the Respondent in this respect.

#### **FACTS AND CIRCUMSTANCES IN SUPPORT OF COMPLAINT 4**

- (29) Based on the above significant audit deficiencies as identified in Complaints 1 to 3, serious doubts exist in regards to whether the Respondent had maintained professional knowledge and skill at the level required to ensure that his clients received competent professional service; and acted diligently in accordance with applicable technical and professional standards when performing the audits, as required under the fundamental principle of Professional Competence and Due Care in sections 100.5(c) and 130.1 of the Code of Ethics for Professional Accountants (“Code”).
- (30) As the Code is a professional standard referred to in the PAO, section 34(1)(a)(vi) applies to the Respondent in this respect.

## **THE PROCEEDINGS**

3. By a letter signed by the parties dated 2 June 2020, the Respondent admitted the Complaint against him, and the parties requested that the steps set out in paragraphs 17 to 30 of the Disciplinary Committee Proceedings Rules (“**DCPR**”) be dispensed with.
4. The Disciplinary Committee agreed with the parties’ request to dispense with the steps set out in Rules 17 to 30 of the DCPR in light of the admission made by the Respondent, and directed the parties to make written submissions on sanctions and costs.
5. The complaints were all found proven on the basis of the admission made by the Respondent.
6. We have taken into account the personal circumstances of the Respondent that are set out in his submissions made on 24 August 2020. In short, the Respondent referred to the offer to conclude the matter by way of the Resolution by Agreement (“**RBA**”) procedure which was proposed to him on 13 December 2019 which provided for a public reprimand and payment of an administrative penalty of HK\$40,000 and the Institute’s costs of HK\$15,000. The Respondent suggested that the offer was not accepted by him by reason of his divorce, stress and unemployment. He also suggested that he was asked to admit material matters of fact in dispute which was subsequently revised. We were invited to take this matter into account.
7. He then suggested that in light of the deficiencies caused by insufficient documentation, he proposed a public reprimand and a payment of HK\$35,000.
8. We note the wide discretion given to us to determine the applicable sanctions under section 35 of the PAO. We accept the submissions of the Complainant that where there were multiple audit deficiencies which had occurred over 2 years of audit, the case falls within the “moderately serious” category as categorised in the Guideline to Disciplinary Committee for Determining Disciplinary Orders.
9. In considering the proper order to be made in this case, the Disciplinary Committee has had regard to all the aforesaid matters, including the particulars in support of the Complaint, the Respondent’s personal circumstances, and the conduct of the Complainant and the Respondent throughout the proceedings.

## **SANCTIONS AND COSTS**

10. The Disciplinary Committee **ORDERS** that:-
  - (a) the Respondent be reprimanded under section 35(1)(b) of the PAO;

- (b) the Respondent do pay a penalty of HK\$50,000 under section 35(1)(c) of the PAO; and
- (c) the Respondent do pay the costs and expenses of and incidental to the proceedings of the Complainant, including the costs of the Disciplinary Committee, in the sum of HK\$116,962 under section 35(1)(iii) of the PAO.

Dated the 20th day of November 2020

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Mr. DAWES Victor  
(Chairman)

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Ms. LO Fung Yee, Daphne  
(Member)

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Miss FUNG Suet Ngan, Gladys  
(Member)

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Ms. YANG Elizabeth Ling  
(Member)

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Mr. SHEN Ka Yip, Timothy  
(Member)