



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, a certified public accountant (practising) and a firm

(HONG KONG, 24 August 2018) A Disciplinary Committee of the Hong Kong Institute of Certified Public Accountants reprimanded Kwok Chee Tack, CPA (membership number F00769), Wong Kam Man, Kevin, CPA (practising) (membership number F01750) and Ernst & Young (firm number 0422) ("EY") on 18 July 2018 for their failure or neglect to observe, maintain or otherwise apply professional standards issued by the Institute. Further, the Committee ordered Kwok, Wong and EY to pay penalties of HK\$200,000, HK\$100,000 and HK\$400,000 respectively. In addition, the respondents were ordered to pay costs of the disciplinary proceedings in the sum of HK\$1,527,416.

During the years 1997 to 2002, EY was the reporting accountant of three companies for the listing of their shares in Hong Kong. The companies, which were under common ownership, were Gold Wo International Holdings Limited ("Gold Wo"), Fu Cheong International Holdings Limited ("Fu Cheong") and Yue Fung International Group Holding Limited ("Yue Fung").

EY was also the auditor of these companies. Wong was the engagement partner of the Gold Wo engagements and Kwok was the engagement partner of the Fu Cheong and Yue Fung engagements.

EY expressed unmodified opinions in the accountants' reports for the three companies. It also expressed unmodified auditor's opinions on the consolidated financial statements of Gold Wo and its subsidiaries for accounting periods ended in the years from 2000 to 2002, of Fu Cheong and its subsidiaries for accounting periods ended in the years 2000 and 2001, and of Yue Fung and its subsidiaries for accounting periods ended in the years from 1999 to 2002.

In response to the 2002 arrests of persons connected with the three companies, the Institute instigated three investigations under the Professional Accountants Ordinance (Cap. 50) ("PAO") into the conduct of the relevant CPAs and CPA practices in connection with the accountant's reports and audit engagements. The investigations were put on hold while the Independent Commission Against Corruption carried out criminal investigations into certain CPAs' involvement in fraudulent activities with regard to the three companies.

Relevant criminal proceedings were concluded in 2010. Various individuals, including some members of the companies' management, were found guilty of conspiring with others to defraud stakeholders by falsifying financial records and documents.

In 2010, the three Investigation Committees were reorganised into a single committee and the investigation proceeded. In November 2015, the Investigation Committee

submitted its reports to the Council of the Institute, noting that the respondents would have a case to answer.

In light of the findings set out in the reports of the Investigation Committee, complaints were lodged against the respondents under section 42C(1) of the PAO.

The Disciplinary Committee found, in relation to the Gold Wo engagements, that:

- (i) Wong and EY were in breach of Statement of Auditing Standards ("SAS") 100 *Objective and General Principles Governing an Audit of Financial Statements*, SAS 200 *Planning*, SAS 230 *Audit Documentation* and SAS 400 *Audit Evidence* for their deficient audit work in the areas of sales and receipts for sales, purchases and related cash disbursements, and long-term investments.
- (ii) Wong and EY were in breach of Statement 1.200 Professional Ethics – *Explanatory Foreword* and Statement 3.340 Auditing Guideline – *Prospectuses and the reporting accountant* for their failure to adequately review the preceding auditors' work for 1998 and 1999, to document the work performed as part of the review and to perform relevant analytical procedures.

The Committee found, in relation to the Fu Cheong engagements, that:

- (i) Kwok and EY were in breach of SAS 100, SAS 200, SAS 230 and SAS 400 for their deficient audit work in the areas of sales and receipts for sales, and purchases and related cash disbursements.
- (ii) Kwok and EY were in breach of Statement 1.200 Professional Ethics and Statement 3.340 Auditing Guideline for their failure to adequately review the preceding auditors' work for 1998 and 1999, to document the work performed as part of the review and to perform relevant analytical procedures.

The Committee found, in relation to the Yue Fung engagements, that Kwok and EY were in breach of SAS 230 and SAS 400 for their deficient audit work in the areas of sales and sales receipts.

Having taken into account the circumstances of the case, the Disciplinary Committee made the above order against the respondents under section 35(1) of the PAO.

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 more than 42,000 members and 18,000 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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香港會計師公會對一名會計師、一名執業會計師及一間會計師事務所作出紀律處分

(香港，二零一八年八月二十四日) 香港會計師公會轄下紀律委員會，於二零一八年七月十八日就會計師郭智達先生(會員編號：F00769)、執業會計師黃錦文先生(會員編號：F01750)及安永會計師事務所(「安永」，事務所編號：0422)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，對他們作出譴責。此外，紀律委員會命令郭先生、黃先生及安永分別須繳付罰款 200,000 港元、100,000 港元及 400,000 港元。三名答辯人另須繳付紀律程序費用共 1,527,416 港元。

在一九九七年至二零零二年期間，安永曾是三間在香港招股上市的公司的申報會計師。該三間公司分別為金禾國際控股有限公司(「金禾」)、富昌國際控股有限公司(「富昌」)及裕豐國際集團控股有限公司(「裕豐」)。三間公司屬相同所有權。

安永亦是該三間公司的核數師。黃先生是負責金禾項目的合夥人，而郭先生是負責富昌項目及裕豐項目的合夥人。

安永於該三間公司的會計師報告中發表了無保留意見。安永亦對金禾及其附屬公司二零零零年至二零零二年會計期間的綜合財務報表、富昌及其附屬公司二零零零年及二零零一年會計期間的綜合財務報表、以及裕豐及其附屬公司一九九九年至二零零二年會計期間的綜合財務報表發表了無保留的核數師意見。

鑑於該三間公司的一些關連人士於二零零二年被拘捕，公會根據香港法例第 50 章《專業會計師條例》(「PAO」)對上述會計師報告及審計項目中相關會計師及會計師事務所的行為展開三項調查。公會的調查及後因廉正公署對若干會計師涉及該三間公司的欺詐行為進行刑事調查而暫緩。

相關刑事程序於二零一零年完結。多名人士包括該等公司一些管理人員，被裁定串謀偽造財務記錄及文件以欺騙持份者的罪名成立。

於二零一零年，該三個調查委員會重組成一個委員會，並繼續進行調查。調查委員會於二零一五年十一月向公會理事會提交報告，指出答辯人須作出答辯。

基於調查委員會報告所列發現，調查委員會根據 PAO 第 42C(1)條對答辯人作出投訴。

紀律委員會就金禾項目裁定：

- (i) 黃先生及安永就銷售和收款、採購和相關現金支出，以及長期投資方面的審計工作不足，因而違反了 Statement of Auditing Standards (「SAS」) 100「Objective and General Principles Governing an Audit of Financial

Statements」、SAS 200「Planning」、SAS 230「Audit Documentation」及 SAS 400「Audit Evidence」。

- (ii) 黃先生及安永沒有充分審閱前任核數師就一九九八年及一九九九年度進行的工作、記錄有關的審閱及進行相關分析程序，因而違反了 Statement 1.200「Professional Ethics – Explanatory Foreword」及 Statement 3.340「Auditing Guideline – Prospectuses and the reporting accountant」。

紀律委員會就富昌項目裁定：

- (i) 郭先生及安永就銷售和收款、採購和相關現金支出方面的審計工作不足，因而違反了 SAS 100、SAS 200、SAS 230 及 SAS 400。
- (ii) 郭先生及安永沒有充分審閱前任核數師就一九九八年及一九九九年度進行的工作、記錄有關的審閱及進行相關分析程序，因此違反了 Statement 1.200「Professional Ethics」及 Statement 3.340「Auditing Guideline」。

紀律委員會就裕豐項目裁定郭先生及安永就銷售和收款方面的審計工作不足，因而違反了 SAS 230 及 SAS 400。

經考慮有關情況後，紀律委員會根據 PAO 第 35(1)條向答辯人作出上述命令。

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。公會會員超過 42,000 名，學生人數逾 18,000。

公會開辦專業資格課程，確保會計師的人職質素，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。

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IN THE MATTER OF

Complaints made under section 42C(1) of the Professional Accountants Ordinance (Cap. 50)

BETWEEN

An Investigation Committee of the Hong Kong Institute of Certified Public Accountants COMPLAINANT

AND

Mr. Kwok Chee Tack (F00769) 1st RESPONDENT
Mr. Wong Kam Man Kevin (F01750) 2nd RESPONDENT
Ernst & Young (0422) 3rd RESPONDENT

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

Members: Dr. WILSON Claire (Chairman)
Mr. LAM Sze Cay Kevin
Mr. LI Ka Fai David
Mr. ESPINA Anthony Joseph

ORDER & REASONS FOR DECISION

1. These are complaints made by an Investigation Committee of the Institute ("**Complainant**") against the Respondents under section 42C(1) of the Professional Accountants Ordinance (Cap. 50) ("**PAO**"). The disciplinary proceedings are:
 - (a) complaints against Mr. Kwok Chee Tack ("**Kwok**"), a certified public accountant (practising) and Ernst & Young ("**EY**"), a firm of certified public accountants (practising) relating to the audits of Yue Fung International Group Holding Limited ("**Yue Fung**") (case no. D-03-IC13Q);

- (b) complaints against Mr. Wong Kam Man Kevin ("**Wong**"), a certified public accountant (practising) and EY relating to the accountants' reports and audits of Gold Wo International Holdings Limited ("**Gold Wo**") (case no. D-03-IC14Q); and
 - (c) complaints against Kwok and EY relating to the accountants' reports and audits of Fu Cheong International Holdings Limited ("**Fu Cheong**") (case no. D-03-IC15Q).
2. The original complaints are set out in three complaint documents from the Complainant ("**Original Complaints**") which were transmitted to the Disciplinary Committee ("**Committee**") under cover of a letter dated 13 March 2017.
 3. On 28 November 2017, the Committee approved the parties' joint applications by letters dated 1 November 2017 to amend the Original Complaints to the amended complaints ("**Amended Complaints**") set out in the documents annexed to the parties' letters of 1 November 2017.
 4. The Amended Complaint for case no. D-03-IC13Q is as follows:
 - (1) Based on the Investigation Committee's observations of the audit evidence, they consider that Respondents failed to apply relevant auditing standards and guidelines in respect of sales and receipts for sales.
 - (2) After consideration, the Investigation Committee ("**IC**") has identified the following breaches in professional standards.

Complaint

- (3) With respect to sales and receipt for sales in the audits of 1999, 2000, 2001 and 2002, the Respondents did not comply with the following Statements on Auditing Standards ("**SAS**"):
 - (i) SAS 400 to obtain sufficient appropriate audit evidence to satisfy themselves that sales were fairly stated; and
 - (ii) SAS 230 to document the work performed or the judgment made on matters important to the audit opinions of the relevant financial statements.

Audit Evidence - Sales testing

- (4) IC considers that the Respondents' working papers did not contain sufficient evidence to indicate that Yue Fung had effective controls over the sales cycle and integrity of warehouse records. As a result, a reasonable auditor would have been alert of the potential risks of misstatement when planning and performing the audit.
- (5) Although the Respondents conducted various tests relating to the existence and quantity of sales, the audit evidence was not sufficient to substantiate shipments and related payments, which typically would be sourced from external parties.
- (6) Databank products constituted a significant portion of Yue Fung's sales and would, therefore, be subject to test work. However, proof of customer acknowledgement was rarely inspected and documents showing identity of customers settling sales receivables were not inspected for any of the databank product sales.
- (7) In respect of sales to PRC customers, the shipments were made by a local delivery service which did not provide proof of delivery. There was, however, inadequate evidence reflecting that the Respondents had evaluated the potential risks associated with this deviation from the standard practice and/or the legality of transactions which would have been subjected to the laws and rules of another jurisdiction.
- (8) The IC also considered that there was insufficient evidence to confirm that sales actually reflected the finished goods delivered to customers, since the Goods Delivery Notes ("GDNs") were not consistently used in sequential order and were not prepared for all sales transactions.
- (9) Furthermore, source documents that were generated by third parties showing delivery of goods to customers were inspected in less than 80% of the sales transaction samples selected.
- (10) Source documents pertaining to sales receipts, such as bank advice or cheque copies, were not inspected by the Respondents in the sales transaction testing, and direct audit evidence obtained did not adequately support that settlement was actually made by sales customers.

- (11) The working papers reflected a lack of evidence showing control over the accounts receivable circularization process and adequate testing of sales receipts. Furthermore, given the internal control deficiencies related to GDNs and the accounting records, the accuracy of total sales was questionable and the accounts receivable confirmations had limited evidential value in verifying the annual sales figures. A reasonable auditor would have been expected to gather additional evidence to ensure the sales were properly reflected in the financial statements.

Documentation

- (12) Even if Respondents conducted the necessary audit procedures which the IC considers lacking, the Respondents did not comply with SAS 230 in documenting the work performed or the judgment made on matters important to the audit opinions of the relevant financial statements.

5. The Amended Complaint for case no. D-03-IC14Q is as follows:

- (1) The Investigation Committee ("IC") determined that the Respondents failed to apply relevant auditing standards and guidelines in respect of the following key audit areas:
 - (a) Sales and receipts for sales;
 - (b) Purchases (cost of sales) and related cash disbursements; and
 - (c) Deposit for acquisition of long term investment and investment held for disposal.
- (2) The IC identified the following breaches in professional standards.

Complaint 1

- (3) With respect to the audit areas relating to (a) sales and receipts of sales and (b) purchases (cost of sales) and related cash disbursements in the audits of 2000, 2001 (7 months), 2001 and 2002, and (c) the deposit for acquisition of long term investment held for disposal in the 2002 audit, the Respondents did not comply with the following Statements on Auditing Standards ("**SAS**"):
 - (i) SAS 400 to obtain sufficient appropriate audit evidence to satisfy themselves that sales and purchases were fairly stated and that

- SSAP 20 had been applied in ascertaining disclosures of certain related party transactions;
- (ii) SAS 230 to document the work performed or the judgment made on matters important to the audit opinions of the relevant financial statements;
 - (iii) SAS 200 to plan the audit and SAS 300 in assessing risks related to the audits; and
 - (iv) SAS 100 to maintain an attitude of professional skepticism when planning and performing the audits.

Audit Evidence - Sales testing

- (4) The Respondents conducted various tests relating to the existence and quantity of sales including, inter alia, sales transaction testing, cash receipts testing, sales cut-off testing and circularization of accounts receivable (AR) balances. Although there were unusual findings noted by the Respondents in the test work performed in relation to the PRC sales¹, they considered the results of these tests satisfactory.
- (5) The results of the Respondents' test work showed there was insufficient evidence to support the recording of PRC sales, and that sales processing differed from the Respondents' understanding which was documented in the system audit working papers. The following points were identified by the Respondents:
 - (a) goods received were acknowledged by two agents instead of actual customers;
 - (b) PRC sales were not recorded in the AR sub-ledger;
 - (c) receipts of substantial portions of PRC sales were made in cash; and

¹ PRC sales were significant to Gold Wo's operations. Gold Wo entered into a processing arrangement with an external party to undertake the manufacturing function in the PRC. Under PRC law, mainland entities in the processing industry with no foreign trading rights cannot sell goods in the PRC domestic market. Accordingly, Gold Wo had to rely on certain PRC agents to handle the sales to its PRC customers. Proper testing should have included an assessment of the role and eligibility of the PRC agents as well as Gold Wo's compliance with PRC rules on exports, custom duties, and domestic sales tax obligations.

- (d) certain PRC sales were settled through the current account with Fu Chu Kan ("Fu"), the founder of Gold Wo, or through the inter-company current account.
- (6) The IC also determined that there was insufficient evidence to confirm that sales actually reflected finished goods delivered to the PRC customers, as the Goods Delivery Notices ("GDNs") were not pre-numbered and used in sequential order, nor were they prepared for all sales transactions.
- (7) The working papers reflected a lack of evidence showing control over the accounts receivable circularization process and consideration of related party disclosure requirements resulting from the sales that were recorded through an inter-company current account. Furthermore, although the audit team had obtained confirmations from Gold Wo's customers, accounts receivable confirmations would have limited evidential value in verifying the annual sales figures since the internal control deficiencies related to PRC sales.

Audit Evidence - Purchase testing

- (8) The Respondents conducted various tests relating to the purchase cycle including, inter alia, purchase transaction tests, cash payment tests, purchase cut-off tests and accounts payable circularization.
- (9) The results of the Respondent's test work showed there was insufficient evidence to support the recording of purchases of raw materials in the PRC that were handled by Fu. Such transactions were processed in a manner that differed from the other purchases transactions, as documented in the system working paper files. The following observations were noted by the Respondents:
 - (a) Suppliers' invoices on certain bank payments related to purchases of raw materials made by Fu on behalf of Gold Wo were unavailable for inspection;
 - (b) a significant portion of purchases were posted to the current account with Fu instead of AP sub-ledger in 2000; and
 - (c) Significant portion of payments were recorded in the current account with Fu in 2000 and 2001.

- (10) The IC concluded that additional audit evidence would be required to support that purchases were actually received by the warehouse. The Respondents should have followed up on why the Goods Receipts Notes ("GRNs") were not consistently pre-numbered and in sequential order and were not prepared for all purchase transactions.
- (11) Additionally, although the Respondents performed some work in response to their findings, the nature of these bank payments, which were paid through a director's account, should have prompted an auditor to make further enquiries to understand the reasonableness of and proper accounting for the payments.
- (12) The working papers reflected a lack of evidence showing control over the accounts payable circularization process and consideration of related party disclosure requirements resulting from the purchases that were recorded through an inter-company current account. Furthermore, although the audit team had obtained confirmations from Gold Wo's suppliers, given that the internal control deficiencies related to certain purchases, accounts payable confirmations would have limited evidential value in verifying the annual purchase figures.
- (13) The Respondents performed purchase transaction testing which consisted of inspecting bank statements and bank-in-slips. However, because these documents did not contain reference to a specific vendor, this increased the risks that the payment may not have been made for purchase transactions. Although the purchase transaction system remained the same across the years, in some years a smaller sample was selected for testing without sufficient justification.
- (14) Lastly, the Respondents' system audit working papers failed to clearly reflect that purchases were processed differently depending on whether they were classified as "HK Purchases" or "PRC Purchases."
- (15) The matters noted by the Respondents should have raised doubt over the accuracy of purchases recorded and prompted additional audit work. However, the Respondents did not make adequate enquiries to resolve issues related to the unusual transactions.

Audit Evidence - Analytical procedures

- (16) Analytical procedures should be performed near the end of the audit when auditors form an overall conclusion as to whether the financial statements are consistent with their understanding of the business.
- (17) The IC considered that the analytical review procedures had not been diligently conducted to obtain corroborating evidence to support the Respondents' understanding of the business. Specifically, the Respondents did not perform analytical review processes to compare Gold Wo's actual sales trends to relevant industry trends and related production trends. Furthermore, the Respondents accepted the management's explanation for changes in the overall gross profit margins from 1998 to 2002 without challenging its reasonableness.

Audit Evidence - Investments

- (18) As at 31 March 2002, the audited financial statements reflected a deposit for acquisition of long term investment of \$10 million and an investment with a disposal value of \$14 million. There were indications that the IPO share subscription proceeds may have funded the investments, which deviated from the intended use of the proceeds disclosed in the Prospectus.
- (19) The Respondents performed test work on the two investments and reviewed the relevant legal documents. However, from an auditing perspective there appears to be insufficient evidence of genuine existence of the investments, insufficient evidence to demonstrate that the funding source of the investments was not the application of IPO proceeds and inadequate explanation of the purpose of such investments.

Documentation

- (20) Even if the Respondents conducted the necessary audit procedures which the IC considers lacking, the Respondents did not comply with SAS 230 in documenting the work performed or the judgment made on matters important to the audit opinions of the relevant financial statements.

Audit Planning and Risks Assessment

- (21) Auditors are required to develop and document an overall audit plan and to assess audit risks in their planning and performance of an audit. There is

no evidence to demonstrate that the Respondents revised their overall audit plan as needed and/or gained proper understanding of the accounting systems and related internal controls.

- (22) In particular, there is no evidence to demonstrate that Respondents had performed the following:
- (a) identified and evaluated sufficient key controls applied by the Group to ensure that total sales and purchases were accurately reflected in the financial statements;
 - (b) conducted adequate procedures to address various internal control weaknesses;
 - (c) developed an appropriate plan that would consider the legality and financial flow of transactions regarding PRC sales; and
 - (d) considered additional audit procedures in light of the findings noted by the audit team during sales and purchase testing.
- (23) Furthermore, the working papers do not sufficiently reflect that the Respondents properly assessed known risks when determining the design and extent of substantive procedures.

Professional Skepticism

- (24) The IC determined that the Respondents should have exercised adequate professional skepticism in light of the following circumstances:
- (a) there were contract processing arrangements in the PRC with strict rules imposed on foreign manufacturers which needed to be scrutinised by the Respondents during the planning and execution of the audit;
 - (b) the current account of Fu reflected a high volume of fund movements and transactions with a related party in unusual situations which should have warranted the Respondent's to seek further understanding, further evaluation and documentation; and

- (c) the relatively late inclusion of the results of Top Executive in the course of Gold Wo's listing application, as it was a material contributor to the total profits of the Group.

Complaint 2

- (25) The Respondents failed to adequately review the preceding auditors' work for 1998 and 1999, to document the work performed as part of the review and to perform relevant analytical procedures in accordance with Statements 1.200 and 3.340 for the purpose of the Accountants' Report.
- (26) A reporting accountant is required to determine the extent to which they are able to rely on the audit work already performed by preceding auditors. However, the Respondents did not provide sufficient documentation as evidence that they had adequately evaluated the assurance work performed on the sales and purchases cycles by the prior year auditors. In addition, there is insufficient evidence to show that they had re-performed some of the assurance work on Top Executive, a subsidiary which comprised 57% of profits of the Group, to meet the profits threshold imposed by the Stock Exchange for listing applicants.
- (27) In particular, the IC considers that there were a number of risk factors related to the prior year audits. However, the files/documentation fail to reflect how the Respondents gained sufficient understanding of the risks to properly address potential consequences.

6. The Amended Complaint for case no. D-03-IC15Q is as follows:

- (1) The IC determined that the Respondents failed to apply relevant auditing standards and guidelines in respect of the following key audit areas:
 - (a) Sales and receipts for sales; and
 - (b) Purchases (cost of sales) and related cash disbursements.
- (2) The IC has identified the following breaches in professional standards:

Complaint 1

- (3) With respect to the audit areas relating to (a) sales and receipts of sales and (b) purchases (cost of sales) and related cash disbursements in the audits of 2000 and 2001 (9 months), the Respondents did not comply with the following Statements on Auditing Standards ("**SAS**"):
- (i) SAS 400 to obtain sufficient appropriate audit evidence to satisfy themselves that sales and purchases were fairly stated and that SSAP 20 had been applied in ascertaining disclosures of certain related party transactions;
 - (ii) SAS 230 to document the work performed or the judgments made on matters important to the audit opinions of the relevant financial statements;
 - (iii) SAS 200 to plan the audit and SAS 300 in assessing risks related to the audits; and
 - (iv) SAS 100 to maintain an attitude of professional skepticism when planning and performing the audits.

Audit Evidence - Sales testing

- (4) The Respondents conducted various tests relating to the existence and quantity of sales including, inter alia, sales transaction testing, cash receipts testing, sales cut-off testing and circularization of sales and accounts receivable balances. Although there were unusual factors noted by the Respondents in the test work performed in relation to sales settled by cash, they considered the results of these tests satisfactory.
- (5) Notwithstanding the fact that the Respondents performed audit procedures, there was insufficient audit evidence to determine whether the relevant receipts were indeed settlements made by sales customers, given that:
- (a) many of the cash receipts were firstly recorded in Fu Cheong's cash log book and then shown as "lump sum" deposits in bank statements or accounting records; and
 - (b) many of the cash receipts were not matched to specific invoice amounts and appears to have been allocated to customer accounts as cash receipts without matching invoices.

- (6) The IC also determined that there was insufficient evidence to confirm that sales actually reflected finished goods delivered to customers as the Goods Delivery Note ("GDNs") were not consistently used in sequential order nor were they prepared for all sales transactions.
- (7) The working papers reflected a lack of evidence showing control over the sales and accounts receivable circularization process and adequate testing of sales receipts. Furthermore, given the internal control deficiencies related to GDNs and the accounting records, the accuracy of total sales was questionable and a reasonable auditor would have been expected to gather additional evidence to ensure the transactions underlying "lump sum" payments were properly reflected in the financial statements.

Audit Evidence - Purchase testing

- (8) The Respondents conducted various tests relating to the purchase cycle including, inter alia, purchase transaction tests, cash payment tests, purchase cut-off tests and circularization of purchases and accounts payable. The Respondents noted some unusual findings when conducting their test work but considered the results satisfactory.
- (9) The results of the Respondents' work showed that there was insufficient evidence to support the recording of purchases from the PRC suppliers and subsequent payments. The following observations were noted by the Respondents for a significant portion of audit samples selected:
 - (a) invoice copies, suppliers' GDNs and purchase orders were not available for inspection;
 - (b) purchases were recorded based on suppliers' statements rather than actual source documents; and
 - (c) purchase payments were not consistently posted to the sub-ledger and/or supported by cheque copies.
- (10) The IC also concluded that the audit evidence gathered by the Respondents was insufficient to confirm that the purchases recorded were actually received by the warehouse. Results of test work was not sufficient to show that proper support was obtained for all purchase transactions selected or that proper control over source documents was maintained.

- (11) Additionally, the unusual nature of various payments by Fu Cheong should have prompted an auditor to make further enquiries to understand the reasonableness of and proper accounting for the payments, especially in light of the number of cash and lump sum settlements.
- (12) The working papers reflected a lack of evidence showing control over the purchase and accounts payable circularization process and consideration of related party disclosure requirements resulting from the cash purchase payments made by Ho Wing Cheong, one of Fu Cheong's founders. Furthermore, given that the internal control deficiencies related to certain purchases and the accounting records, the accuracy of total purchases was questionable and accounts payable confirmations would have limited evidential value in verifying the annual purchase figures.
- (13) Purchase transaction testing consisted of inspecting bank statements and bank-in-slips which did not contain reference to a specific vendor, thereby failing to mitigate the risk that the payment may not have been made for purchases.
- (14) Lastly, the Respondents' system audit working papers did not reflect the fact that purchases were processed differently, depending on whether they were classified as "HK Purchases" or "PRC Purchases."
- (15) The Respondents' findings should have raised doubt over the accuracy of purchases recorded and should have prompted extra test work. However, the Respondents did not make adequate enquiries to resolve issues related to these transactions.

Audit Evidence - Analytical procedures

- (16) Analytical procedures should be performed near the end of the audit when auditors form an overall conclusion as to whether the financial statements are consistent with their understanding of the business.
- (17) The IC determined that the analytical review procedures had not been diligently conducted to obtain corroborating evidence to support the Respondents' understanding of the business. Specifically, the Respondents did not perform analytical review processes to compare Fu Cheong's actual sales trends to relevant industry trends and related production trends. Furthermore, the Respondents accepted management's explanation for

changes in the overall gross profit margins from 1998 to 2001 without challenging its reasonableness.

Documentation

- (18) Even if the Respondents had conducted the necessary audit procedures which the IC considers lacking, the Respondents did not comply with SAS 230 in documenting the work performed or the judgment made on matters important to the audit opinions of the relevant financial statements.

Audit Planning and Risks Assessment

- (19) Auditors are required to develop and document an overall audit plan and to assess audit risks in their planning and performance of an audit. The available evidence does not demonstrate that the Respondents revised their overall audit plan as needed and/or gained proper understanding of the accounting systems and related internal controls.
- (20) In particular, there was no evidence to demonstrate that the Respondents had performed the following:
- (a) identified and evaluated sufficient key controls applied by the Group to ensure that total sales and purchases were accurately reflected in the financial statements;
 - (b) conducted adequate procedures to address various internal control weaknesses;
 - (c) developed an appropriate plan that would consider the commercial substance of the transfer of business to Fortune BVI and related complicating factors;
 - (d) considered additional audit procedures in light of the findings noted by the audit team during sales and purchase testing; and
 - (e) developed an overall audit plan for 2001 (9 months).
- (21) Furthermore, the working papers do not sufficiently reflect the fact that the Respondents properly assessed known risks when determining the design and extent of substantive procedures.

Professional Skepticism

- (22) The IC determined that the Respondents should have exercised adequate professional skepticism in light of the following:
- (a) treatment of cash sales receipts and purchases payments, and aggregate "lump sum" recording;
 - (b) the volume of purchase payments which were made through Ho; and
 - (c) lack of reliability of source documents inspected by the Respondents and the overall reliability of the accounting records.

Complaint 2

- (23) The Respondents failed to adequately review the preceding auditors' audit work for 1998 and 1999, to document the work performed as part of the review and to perform relevant analytical procedures in accordance with Statements 1.200 and 3.340 for the purpose of the Accountants' Report.
- (24) A reporting accountant is required to determine the extent to which he is able to rely on the audit work already performed by preceding auditors. However, the Respondents did not provide sufficient documentation to evidence that they had adequately evaluated the assurance work performed on the sales and purchases cycles by the prior year auditors. In addition, there is insufficient evidence showing how the prior year auditors dealt with significant changes in the principal activities of subsidiaries that recorded sales of the Group, in particular:
- (a) the activities of Fortune HK, which provided 100% of the Group sales in 1998, which subsequently ceased to operate and whose business was transferred to another subsidiary (Ford Reach) in November 1998 effective from 1 January 1999; and
 - (b) the subsequent transfer of assets and liabilities by Ford Reach to Fortune BVI in September 1999.
- (25) The IC determined that there were a number of risk factors relating to the prior year audits but there was insufficient audit documentation to reflect how the Respondents gained sufficient understanding of the risks to properly address potential consequences.

7. The Respondents have admitted the Amended Complaints against them. On 1 November 2017, the parties agreed that the steps set out in Rules 17 to 30 of the Disciplinary Committee Proceedings Rules ("DCPR") be dispensed with.
8. On 28 November 2017, the Committee agreed to the parties' joint applications to dispense with the steps set out in Rules 17 to 30 of the DCPR in light of the admissions of the Amended Complaints made by the Respondents and directed the parties to make written submissions on sanctions and costs.
9. The Complainant provided their submissions on sanctions and costs on 22 December 2017. EY provided their written submissions on sanctions and costs on 24 January 2018. Kwok and Wong provided their submissions on sanctions on 25 January 2018.
10. The Committee has considered the submissions made by the Complainant and Respondents.
11. In considering the order to be made in this case, the Committee has had regard to all the aforesaid matters, including the particulars in support of the Amended Complaints, and the conduct of the Complainant and Respondents throughout the proceedings.
12. The Complaints are found to be proven on the basis of the Respondents' admissions.
13. The Committee notes that it has wide discretion on the sanctions that may be imposed. Each matter is fact sensitive and the Committee is not bound by the decisions of previous Committees. Having considered all of the relevant facts, the Committee, in its determination of the level of financial penalty to be imposed, has taken into account the respective professional roles held by each of the Respondents.
14. The Committee has also considered EY's request that the Complainant should not be awarded the full amount of costs, and that costs should be reduced to a total of around HK\$1.2 million. After full consideration of further submissions made by both the Complainant and EY on the matter of costs the Committee could not find any basis to justify EY's request for the reduction of costs awarded.
15. The Committee orders that:-

- (a) all of the Respondents be reprimanded under section 35(1)(b) of the PAO;
- (b) Kwok do pay a penalty of HK\$200,000 under section 35(1)(c) of the PAO;
Wong do pay a penalty of HK\$100,000 under section 35(1)(c) of the PAO;
and EY do pay a penalty of HK\$400,000 under section 35(1)(c) of the PAO;
and
- (c) the Respondents do pay jointly and severally the costs and expenses of and incidental to the proceedings of the Complainant in the sum of HK\$1,527,416 under Section 35(1)(iii) of the PAO.

Dated the 18th day of July 2018

Dr. WILSON Claire (Chairman)

Mr. LI Ka Fai David

Mr. LAM Sze Cay Kevin

Mr. ESPINA Anthony Joseph