

CONSULTATION PAPER ON LEGISLATIVE PROPOSALS
TO ESTABLISH FINANCIAL REPORTING COUNCIL
Dated 16 September 2005

Submission

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1. When the clerk to the Bills Committee wrote to me for the Honorable Mandy Tam on 29 July 2005, my name was no longer on the Register of the HKICPA (myself serving a six month's removal). Any reader of this submission may bear in mind that I have never been negligent (this will be proved in due course) and that I am happy to submit my views in the matter.
2. The Consultation Paper contains all the background information to support it. I am however to present my view and to illustrate the efforts of the small practitioner to bring about the formation of the Financial Reporting Council. The small practitioners originally suggested it to be Accountants Authority.
3. Everything must start with Practice Review, then the collapse of Enron and the disintegration of Arthur Andersen with the development of capital market in Hong Kong in the background.

DEMUTUALISATION OF THE STOCK MARKET

4. When the barbarians attacked Hong Kong's currency and stock market, many people queried why outsiders knew our Achilles heel while our experts and regulators did not. We were lucky afterwards and everything is forgotten and forgiven.
5. In 2000, the greatest achievement of Hong Kong's Financial Secretary (now Sir Donald) is not the most welcome budget announced on 8th March 2000, but the unprecedented history making demutualization of the exchanges, abolishing the private club institutions into a government department, to make sure that there is no suppression of the minority and complete transparency of the control mechanism ----- making sure that the interest of the many will no longer be at the mercy of the few.
The same applies to the accounting profession.

THE PRACTICE REVIEW

6. In 1991 the Practice Review was introduced placing the Society at war with itself. The small practitioners are very displeased with it. Is there a case that the society appears to be continuing as a close shop and private club and a reform is necessary. In Hong Kong the practice review is described by many members as "fault finding" and has never been popular. Though its educational value cannot be denied if it is being

conducted on new practicing firms or firms seeking society's assistance. It is also described by the press "as picking a bone from an egg". No problem on small firms has ever been brought to our courts nor as subjects of public concern.

7. Even in United Kingdom, reforms were suggested to remove "a number of characteristics in the monitoring process that particularly irritate members.
8. It was felt a desirable thing to remove the disciplinary and investigative functions from the Hong Kong Society of Accountants. Government is now working towards that direction.
9. The small practitioners are of the view that certain functions should be administered by an Accountant Authority. Now it is the Financial Reporting Council. As such, the small practitioners, if I may say on their behalf, will welcome this piece of legislation. We are of the view that if the Society could not do it in the past and it, as a club, should not do it in future. The following show typical responses:
 - (a) Mr. Wu, senior partner of Ernst & Young, favours public intervention, (27/11/2002 Hong Kong Commercial Daily). Mr. David Sun also of Ernst & Young is the current President.
 - (b) S.C.M.P.: "The HKSA has been accused of lacking the will to penalize its members after 11 investigations into alleged accounting scandals in 1998 yielded no firm results."
 - (c) Shocking cowardice, using stolen documents & anonymous letters, the Court of Appeal said, "...In approaching this case it must be stated that there is a natural distaste for those who seek to convey information by anonymous letters. Those who hide behind anonymity in making complaints against others might legitimately be accused of cowardice..." A respectful professional society should act like one.

ENRON

10. August 2001 witnessed the height of the Enron/Andersen scandal and I was appealing before the Court of Appeal. I was anxious to assure their lordships that ENRON is different from Hong Kong and its accounting profession.
11. Enron is the 7th largest corporation in US sustaining a loss of US\$7.8 billion. Here, Andersen's relationship with Enron is beyond that of auditor and client. The last notorious case was the collapse of Barings, the oldest United Kingdom based investment bank (Loss US\$1.48 billion,

that is Pounds L1 billion.). Asian Wall Street Journal on 3 October 2001 said: "Liquidators of Barings said that Barings auditors had not done their jobs and were to blame for the collapse of Barings. KPMG is claiming L1 billion from Barings' auditors Coopers & Lybrand and Deloitte & Touche after out of court settlement failed.

12. The Enron scandal and the disintegration of Arthur Anderson made all eyes of the financial world to turn to the accounting profession --- looking for scape goat on corporate failures. In fact that is simply greed and "doing different things beyond auditing" that the courts came to the end conclusion.

THE WORKING OF THE DISCIPLINARY COMMITTEES AND THE CURRENT LAW AND THE VIEW OF THE COURT OF APPEAL JUDGES

13. The Court of Appeal (sitting under section 41 of the Ordinance) takes wrong view from the case of Tong Pun Wah vs HKSA where Godfrey J. said that he did not want to second guess what the peer committee decided. He simply did not want to interfere. If the Disciplinary Committee says "it is proved" and without giving reasons, one can doubt how can an accountant shows ground to appeal. If the Registrar says "not enough audit work", it may be also difficult to argue. This places the victim accountant at a very undesirable position. The Court of Appeal said that it is your peers who say you are wrong.
14. To remedy this situation and while the Financial Reporting Council is in place when the legislative proposal is approved, I am of the view that any accountant who is subject to the Disciplinary Committee hearing may choose to be heard by the Audit Investigation Board at his choice. A short amendment to the Professional Accountants Ordinance will be easy and sufficient.
15. Accountants who have been subject to practice review may choose to be investigated by the ICAC instead. You get a shocking answer if you ask them. They say "ICAC does not hate us. These people do!"
16. Financial Minister Hon. Ma Frederick pointed out in December 2002 that is the world trend for outside regulators to function as the profession's watchdogs.
17. My suggestion will give the aggrieved accountant one better option.

Appendix

begin a public relations program to con-

FIRM	AMOUNT PAID
Arthur Andersen	\$137,089,359
Peat Marwick Mitchell	19,400,000
Ernst & Whinney	6,020,500
Deloitte Haskins & Sells	4,997,585
Coopers & Lybrand	4,375,850
Price Waterhouse	3,500,000
Touche Ross	2,250,000
Arthur Young	1,490,000

Source: House Subcommittees on Oversight and Investigations

Big firm pays for fraud without admitting wrong; – small firms posting no public problems!

Andersen pays US\$110 million to settle fraud suit

Vol. 7: 4

Payment sets record, firm refuses to admit wrongdoing

Andersen, formally known as Arthur Andersen, has agreed to pay US\$110 million to shareholders of beleaguered appliance maker Sunbeam to settle a class action lawsuit.

It is the second largest paid by an accounting firm in a securities lawsuit. The record is US\$335 million paid by Ernst & Young to Cendant shareholders in 1999.

The suit was filed on behalf of investors who purchased Sunbeam stock between April 1997 and June 1998. It alleges Arthur Andersen

issued an "unqualified audit opinion" on Sunbeam's 1997 financial statements that had the effect of boosting the company's share price.

Sunbeam's share price once hovered around US\$ 53. But after the company was forced to restate its profits and losses for the six quarters before a change of management in 1998, it dived to US\$7 per share.

The suit also claims the accounting firm became reckless once the CEO of Sunbeam cut Arthur Andersen's fees from US\$ 1 million

to US\$ 700,000, squeezing the firm's profit margin to such a degree that it left them "little motivation ... to do the kind of full-scale audit required in 1997."

The accountants "knowingly or recklessly disregarded numerous red flags evidencing that [Sunbeam's] internal controls were virtually non-existent in critical areas and that certain financial data was inaccurate and unreliable," the suit alleges.

In February, Sunbeam filed for Chapter 11 bankruptcy protection.