

ORDER

other proceedings brought by or on behalf of the Board, or to which the Board is a party, and without admitting or denying the findings herein, except as to the Board's jurisdiction over them and the subject matter of these proceedings, which is admitted, Respondents consent to the entry of this Order Instituting Disciplinary Proceedings, Making Findings and Imposing Sanctions ("Order") as set forth below.³

III.

On the basis of Respondents' Offers, the Board finds⁴ that:

A. Respondents

1. KCC & Associates (a/k/a Chun C. Kwok, a/k/a Kwok & Company) is, and at all relevant times was, a sole proprietorship under the laws of the state of California and located in Los Angeles, California. KCC operates pursuant to Fictitious Name Permits issued to Kwok (FNP no. 2714 and FNP no. 2585). KCC is registered with the Board pursuant to Section 102 of the Act and PCAOB rules. At all relevant times KCC was the external auditor for the issuer identified below.

2. Chun Cho Kwok, 54, of Los Angeles, California is a certified public accountant licensed by the California Board of Accountancy (License No. 115816). At all relevant times, Kwok was the sole proprietor of KCC and served as the engagement partner on the audits discussed below. Kwok is an associated person of a registered public accounting firm as that term is defined in Section 2(a)(9) of the Act and PCAOB Rule 1001(p)(i).

³ The findings herein are made pursuant to Respondents' Offers and are not binding on any other persons or entities in this or any other proceeding.

⁴ The Board finds that Respondents' conduct described in this Order meets the conditions set out in Section 105(c)(5) of the Act, 15 U.S.C. § 7215(c)(5), which provides that certain sanctions may be imposed in the event of (1) intentional or knowing conduct, including reckless conduct, that results in a violation of the applicable statutory, regulatory, or professional standard; or (2) repeated instances of negligent conduct, each resulting in a violation of the applicable statutory, regulatory, or professional standard.



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B. Summary

3. This matter concerns Respondents' violations of PCAOB rules and standards in connection with the issuance of audit reports on the financial statements of San Lotus Holding, Inc. ("San Lotus") for the years ended December 31, 2013 and 2014. As detailed below, Respondents failed to exercise due professional care, including professional skepticism, and failed to obtain sufficient appropriate audit evidence, in connection with the audit of the December 31, 2013 financial statements of San Lotus ("2013 audit"), and the audit of the December 31, 2013 (restated) and December 31, 2014 financial statements of San Lotus ("2014 audit").

C. Respondents Violated PCAOB Rules and Standards

4. In connection with the preparation or issuance of any audit report, PCAOB rules require that a registered public accounting firm and its associated persons comply with the Board's auditing and related professional practice standards.⁵ An auditor may express an unqualified opinion on an issuer's financial statements only when the auditor has formed such an opinion on the basis of an audit performed in accordance with PCAOB standards.⁶ Those standards require among other things, that an auditor plan and perform the audit to obtain sufficient appropriate audit evidence to provide a reasonable basis for the auditor's opinion.⁷ PCAOB standards further require that an auditor exercise due professional care and professional skepticism in performing the audit.⁸

5. PCAOB standards require that the audit report state whether the financial statements are presented in conformity with generally accepted accounting principles ("GAAP").⁹ "Generally accepted accounting principles recognize the importance of

⁵ See PCAOB Rule 3100, *Compliance with Auditing and Related Professional Practice Standards*; PCAOB Rule 3200T, *Interim Auditing Standards*.

⁶ See AU § 508.07, *Reports on Audited Financial Statements*.

⁷ See Auditing Standard No. 15, *Audit Evidence* ("AS 15") at ¶ 4.

⁸ See AU § 150, *Generally Accepted Auditing Standards*, AU § 230, *Due Professional Care in the Performance of Work*.

⁹ See AU § 411, *The Meaning of Present Fairly in Conformity with Generally Accepted Accounting Principles*.

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reporting transactions and events in accordance with their substance. The auditor should consider whether the substance of transactions or events differs materially from their form."¹⁰

6. In the case of significant transactions that are outside the normal course of business for the entity, or that otherwise appear to be unusual given the auditor's understanding of the entity and its environment, PCAOB standards require the auditor to gain an understanding of the business rationale for such transactions and whether that rationale (or the lack thereof) suggests that the transactions may have been entered into to engage in fraudulent financial reporting or conceal misappropriation of assets.¹¹ In addition, where a risk of fraud is identified, the auditor is required by PCAOB standards to "perform substantive procedures, including tests of details, that are specifically responsive to the assessed fraud risks."¹²

7. As described below, Respondents failed to comply with PCAOB rules and standards in connection with the 2013 and 2014 audits of San Lotus.

Audit of San Lotus's 2013 Financial Statements

8. Kwok, as engagement partner, authorized the Firm's issuance of an audit report, dated March 21, 2014, expressing an unqualified audit opinion on San Lotus's financial statements for the year ended December 31, 2013. The report was included in San Lotus's Form 10-K filed with the Securities and Exchange Commission ("Commission") on April 7, 2014.

9. San Lotus reported in its 2013 Form 10-K that it had entered into three transactions to acquire land in Taiwan during 2013. As disclosed in the Forms 8-K and 8-K/A announcing each of the transactions, the sellers included San Lotus directors and

¹⁰ Id. ¶ 6.

¹¹ See AU § 316.66, *Consideration of Fraud in a Financial Statement Audit* (since superseded for audits of fiscal years beginning on or after December 15, 2014); see also Auditing Standard No. 13, *The Auditor's Responses to the Risks of Material Misstatement*, ("AS 13") ¶ 15(c).

¹² See AS 13 ¶ 13.

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officers, and/or business entities in which San Lotus shareholders held an ownership interest. San Lotus issued shares to the land sellers to pay for the transactions.¹³

10. In the first transaction, San Lotus acquired a land holding company, Da Ren International Development Inc. Da Ren's primary asset was a "qualified ownership" interest in land.¹⁴ After acquiring Da Ren in September 2013, San Lotus recorded that land on its year-end 2013 balance sheet as a fixed asset with a value of more than \$3.1 million. San Lotus's valuation of the land was based on a third-party appraisal conducted as of April 29, 2013.

11. In two other transactions, San Lotus agreed to purchase land in Xinpi Township and Miaoli County. Although San Lotus issued shares to the sellers in 2013 as consideration for the land, San Lotus disclosed that title for the underlying land parcels did not transfer to San Lotus in 2013. On its year-end 2013 financial statements, San Lotus recorded prepaid assets of \$8.6 million as a result of the Xinpi and Miaoli land transactions, based on appraised values of \$1.8 million for the land in Xinpi and \$6.8 million for the land in Miaoli.

12. The assets recorded from the three land transactions (\$11.7 million) represented 94% of total assets at year-end 2013. The appraisals on which the valuations of those assets were based—described in paragraphs 10 and 11 above—contained language indicating that they were only to be used as a reference for certain Taiwanese urban renewal-related purposes and could not be used as a reference for other appraisal purposes.

13. When planning the 2013 audit, Respondents identified the land transactions as significant, equity-based transactions, outside of the normal course of business with related parties. Respondents also identified a risk of material misstatement due to fraud related to the valuation of the land assets acquired. Respondents, however, failed to perform sufficient appropriate procedures to evaluate

¹³ On the date that each contract was signed: (1) San Lotus's Taiwanese subsidiary delivered a promissory note to the sellers for a cash purchase price that was based on an appraisal of the land asset; (2) San Lotus assumed the subsidiary's obligations under the promissory note; and (3) the sellers agreed to accept shares of San Lotus in satisfaction of the promissory note.

¹⁴ Da Ren's ownership of the land was qualified because the seller could, in certain circumstances, reclaim title to the land from Da Ren.

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the business rationale of the land transactions,¹⁵ or to plan and perform audit procedures that were specifically responsive to the assessed fraud risks of the land transaction.¹⁶ For example, Respondents failed to consider whether management may have been placing more emphasis on the need for a particular accounting treatment for the land transactions than on the underlying economics of the transactions.¹⁷ Respondents also failed to perform any procedures to evaluate whether it was appropriate under U.S. GAAP to record assets from the land transactions at appraised values and proceeded on the basis of a view that the use of the appraised values was appropriate.¹⁸

14. As a result, Respondents, failed to exercise due professional care, including professional skepticism,¹⁹ during the audit, and failed to obtain sufficient appropriate evidence to support the audit opinion they issued in connection with San Lotus's 2013 financial statements.²⁰

March 6, 2015 Form 8-K

15. Between October 2014 and January 2015, the staff of the Commission's Division of Corporation Finance sent a series of comment letters to San Lotus. The comment letters, among other things, raised questions concerning whether the recorded land assets should be valued at historical cost. Respondents reviewed those letters, as well as San Lotus's responses to those letters.

¹⁵ See AU § 316.66.

¹⁶ See AS 13 ¶ 13.

¹⁷ See AU § 316.67.

¹⁸ To audit the valuation of the land transactions, Respondents performed certain procedures prescribed by AU § 336, *Using the Work of a Specialist*. However, Respondents still failed to adequately perform the procedures required under AU § 336 to make use of the appraisals. In particular, Respondents failed to consider the appropriateness of using the appraisals as evidence of the value of the land assets for U.S. GAAP purposes, given the language limiting the use of the appraisals. See AU § 336.09(e).

¹⁹ See AU § 230; AS 13 ¶ 7.

²⁰ See AS 15 ¶¶ 4-6.



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16. On March 6, 2015, San Lotus disclosed in a Form 8-K that its previously filed 2013 financial statements should no longer be relied upon. Among other things, San Lotus stated in the Form 8-K that the 2013 financial statements "fail[ed] to properly reflect the value of each land purchased in 2013 . . . at its historical carrying value." San Lotus further announced that it intended to file restated financial statements as soon as practicable, and that it had discussed the matters in the Form 8-K with KCC.

Audit of San Lotus's 2013 (Restated) and 2014 Financial Statements

17. On March 30, 2015, San Lotus filed a Form 10-K with the Commission, containing San Lotus's 2013 (restated) financial statements and 2014 financial statements. Kwok, as engagement partner, authorized the Firm's issuance of an audit report, dated March 25, 2015, expressing an unqualified audit opinion on the financial statements, which was also included in the Form 10-K filed with the Commission.

18. In the 2013 (restated) financial statements, San Lotus reported \$4.9 million in assets related to the aforementioned land transactions (comprising 87% of total assets). This included \$1.8 million from the Xinpi land and \$3.1 from the Da Ren land transaction.²¹ In the 2014 financial statements, San Lotus reported \$2.9 million in assets relating to the Da Ren land transaction (comprising 79% of total assets).²² San Lotus continued to record the value of those assets based on the third-party appraisals conducted in 2013.²³

19. When planning the audit of the 2013 (restated) financial statements and the 2014 financial statements, Respondents again identified the land transactions as

²¹ No assets were reported from the Miaoli land transaction in either the 2013 (restated) or 2014 financial statements. San Lotus disclosed in the 2014 Form 10-K that those transactions had been "cancelled" in early 2015 because the "entire title to the [Miaoli land] has not been transferred."

²² No asset was reported for the Xinpi land transaction in the 2014 financial statements. In 2014, San Lotus returned the Xinpi land to one of the original sellers in exchange for the return of an equivalent number of San Lotus shares to the number of shares issued in the original transaction.

²³ The difference in the reported amount of the Da Ren land, from \$3.1 million on the 2013 (restated) financial statements to \$2.9 million on the 2014 financial statements, was due to the application of a different exchange rate for each balance sheet date.

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significant, equity-based transactions, outside of the normal course of business, with related parties. Respondents also again identified a risk of material misstatement due to fraud related to the valuation of the land assets acquired in the foregoing land transactions. Nevertheless, Respondents again failed to plan and to perform appropriate procedures to evaluate the business rationale of the land transactions, or to plan and perform audit procedures that were specifically responsive to the risks of fraud associated with those transactions.²⁴

20. Despite being aware of San Lotus's correspondence with the Commission's Division of Corporation Finance concerning the value of the land acquisitions, Respondents again failed to perform appropriate procedures to determine whether the assets from the Da Ren and Xinpi land transactions were properly recorded. Respondents failed to appropriately consider the disclosure in the March 6, 2015 Form 8-K, that previously filed financial statements should no longer be relied upon because San Lotus had failed to record the land it had purchased at historical carrying values. Respondents also failed to perform any procedures to evaluate whether it was appropriate under U.S. GAAP for San Lotus to continue to record assets from the Da Ren and Xinpi land transactions at appraised values.²⁵

21. Instead, Respondents continued to accept management's valuations of the land assets based on the appraisals, and failed to perform sufficient appropriate procedures to test those values. In particular, Respondents continued to use the appraisals as audit evidence supporting the value of the land assets.²⁶

22. As a result, Respondents failed to exercise due professional care, including professional skepticism,²⁷ during the audit, and failed to obtain sufficient appropriate evidence to support the audit opinion they issued in connection with San Lotus's 2013 (restated) and 2014 financial statements.²⁸

²⁴ See AS 13 ¶ 13.

²⁵ See Auditing Standard No. 14, *Evaluating Audit Results*, ("AS 14") ¶ 30.

²⁶ See AU § 336.09(e).

²⁷ See AU § 230; AS 13 ¶ 7.

²⁸ See AS 15 ¶¶ 4-6.

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IV.

In view of the foregoing, and to protect the interests of investors and further the public interest in the preparation of informative, accurate, and independent audit reports, the Board determines it appropriate to impose the sanctions agreed to in Respondents' Offers. Accordingly, it is hereby ORDERED that:

- A. Pursuant to Section 105(c)(4)(E) of the Act and PCAOB Rule 5300(a)(5), Chun Cho Kwok, CPA, and KCC & Associates (a/k/a Chun C. Kwok, a/k/a Kwok & Company) are hereby censured;
- B. Pursuant to Section 105(c)(4)(B) of the Act and PCAOB Rule 5300(a)(2), Chun Cho Kwok, CPA, is barred from being an associated person of a registered public accounting firm, as that term is defined in Section 2(a)(9) of the Act and PCAOB Rule 1001(p)(i);²⁹
- C. After two (2) years from the date of this Order, Chun Cho Kwok, CPA, may file a petition, pursuant to PCAOB Rule 5302(b), for Board consent to associate with a registered public accounting firm;
- D. Pursuant to Section 105(c)(4)(A) of the Act and PCAOB Rule 5300(a)(1), the registration of KCC & Associates (a/k/a Chun C. Kwok, a/k/a Kwok & Company) is revoked; and

²⁹ As a consequence of the bar, the provisions of Section 105(c)(7)(B) of the Act will apply with respect to Kwok. Section 105(c)(7)(B) provides: "It shall be unlawful for any person that is suspended or barred from being associated with a registered public accounting firm under this subsection willfully to become or remain associated with any issuer, broker, or dealer in an accountancy or a financial management capacity, and for any issuer, broker, or dealer that knew, or in the exercise of reasonable care should have known, of such suspension or bar, to permit such an association, without the consent of the Board or the Commission."

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- E. After two (2) years from the date of the Order, KCC & Associates (a/k/a Chun C. Kwok, a/k/a Kwok & Company) may reapply for registration by filing an application pursuant to PCAOB Rule 2101.

ISSUED BY THE BOARD.

/s/ Phoebe W. Brown

Phoebe W. Brown
Secretary

June 30, 2016