

SHINEWING

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Expanding beyond the border – opportunities and challenges

Why do companies choose to expand overseas? What are the challenges in completing an M&A project? This article will discuss these issues from the China related M&A transactions perspective.

Privacy issues associated with Smartphones

Have you ever lost your mobile phone? How panic are you when thinking of your personal data being stolen or exposed? Does it mean that there is no problem if you keep your mobile phone physically secured? We will discuss some of these issues and give you tips on the potential leakages.

Professional ethics in liquidation and insolvency (Part II)

We will continue the discussion from our last SAS e.Bulletin on the relevant issues relating to the recently updated code of professional ethics for professional work and conduct of insolvency professionals issued by the HKICPA.

New law on anti-money laundering and counter terrorist financing

The Anti-Money Laundering and Counter-Terrorist Financing (Financial Institutions) Ordinance (Cap. 615) has come into effect since 1 April 2012. This article will highlight some of the key provisions in this legislation.

Knowledge – History of Forensic Accounting

When did Forensic Accountants first appear in history?

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Expanding beyond the border – opportunities and challenges

By Peggie Wong, Director and June Siu, Vice President

Global M&A volume reached a total of US\$2.81 trillion in 2011, a record high since 2009. Against the backdrop of global uncertainties and financial instabilities in some European countries, China continued to be one of the most active M&A markets in the world. This is evidenced by the fact that, M&A activities in China doubled both in terms of volume and value in 2011, with cross-border deal flows accounted for half of the overall market activities.

In recent years, there is a growing number of Chinese companies looking to buy assets offshore, in particular in the energy and natural resources sector, and consumer products business that comes with a well-known brand. The US\$121 million acquisition of a stake in Greece-based jewellery and luxury goods retailer, Folli Follie Group, by Shanghai-based Fosun International is one of the noticeable transactions announced last year.

While we see there is an increasing trend of outbound investments, international investment interest in China also remained high in the last couple of years. Nonetheless, it is expected that inbound investment or M&A activities are going to slow down, as investors in developed countries such as USA, Japan and the EU will remain cautious in their overseas investments under the current economic environment.

Why think cross-border?

Each cross-border transaction is unique in its own right. Some clearly have the synergies with the acquirers' current business, while others have a less tangible link. We have summarised some of the key reasons below:

- Companies encounter pressure to compete with their global competitors in face of a sluggish domestic economy. They start to look abroad and are particularly interested in the growth potential of the China market.
- Companies are motivated to acquire more competitive foreign technology that can be transferred to the domestic market in anticipation of the increasing foreign competition. An example is the acquisition of Volvo by China-based Geely Motors in 2010. The acquisition enabled Geely to gain access to advanced automotive technologies, as well as own a well-established brand which enhances its competitiveness in both domestic and international markets.
- Companies are seeking a fast-track entry into a foreign market by acquiring established foreign operations.
- Companies are driven to expand through acquisitions to satisfy shareholder demands for higher returns, which cannot be as easily satisfied through organic growth.

- Companies are operating in stagnant or declining markets, and seek to operate in higher growth, adjacent markets.
- More PE/VCs exit through trade-sell or M&A instead of IPO due to poor performance of the world stock market in recent years. Related M&A deals in China doubled in 2011 and accounted for nearly 20% of total deal volume in that year.

Though political and economic uncertainties may cause some companies to halt their overseas investment plans, increasing competitive pressures and globalisation of local economies will continue to be major driving forces for cross-border M&A activities in China.

The challenges: When conducting M&As in China...

Despite the growing M&A activities in China, completing M&A transactions is always full of challenges and can be a daunting task. Here are some common issues that may arise:

- *Large gap between buyer's and seller's expectations on price and terms* – there is always a big price gap between buyer and seller, and it will take a long process to bridge and close the gap. Many Chinese owners also tend to be reluctant to hand over their management control. More often, some like to change the transaction terms at the very last minute.



- **The struggle for reliable and quality information in due diligence** – common issues include: hidden liabilities and exposures, unclear ownership of land and property, informal arrangements and related party transactions etc.
- **Integrity of the target's management** – certain widespread business practices in China may be unacceptable to foreign buyers, and non-compliant with their home country's regulations.
- **Legal and regulatory environment** - China's evolving legal system and rapidly changing regulatory environment can create uncertainty. Investors will need to invest more time and effort to conduct due diligence and evaluate the potential impact.
- **Integration issues** – e.g. cultural differences, tax and customs compliance issues, retention of key staff, remuneration structure differences etc.

We have seen many of these obstacles when negotiating and completing a transaction. Unless deal breakers are identified, deal issues and associated risks can usually be mitigated. Some common ways include: adding representations and warranties in sales and purchase agreements to minimise or even transfer the risks of contingent liabilities; discussing with the seller to ensure that banks will continue granting the existing facilities to the target company after the change of control, etc.



Some cases to share ...

Needless to say **due diligence** is a crucial step in a transaction. While some may think due diligence process on well-established or listed enterprises should be much more straightforward and easier to manage, it may not be always true. Our team has recently assisted a large state-owned mining enterprise in China to perform a financial due diligence in relation to its proposed merger with an overseas company. Despite the fact that only limited access to the financial information via a virtual data room was allowed, our work was finally concluded through leveraging our industry knowledge in the mining sector, good understanding of the regulatory system in both markets and our experience in handling cross-border deals.

Post-deal integration can be a complex process and will be particularly challenging when an unfamiliar business is being acquired. One of our clients, a leading UK garment trading company, faced these challenges after they acquired a production factory based in Dongguan. As they were not familiar with the commercial practices in China, they encountered operational problems, such as poor cash flow planning, unexpected investigation by the customs and tax authorities, and loss of key management.

The owner decided to engage our team to smooth out the integration process by supporting the acquired business' daily finance and accounting operations and ERP system implementation etc.

How to mitigate the risk, enhancing the chance to success...

A few points to bear in mind:

- **Deliberate planning** – drafting an M&A roadmap, understand the corporate value and strategy of the target business, look for synergy, hire or retain the right management team, etc.
- **Effective communication between the buyer and seller, and among different professional advisors involved** – as the timeframe of a transaction is usually tight, it is crucial to keep constant communication with parties involved and tackle immediately any issues that may arise.
- **Proper integration** – many M&A cases turn out to be a failure due to poor merger integration. It is important to watch for risks in the areas of synergy, organisational structure, corporate culture and people.

Not to mention that leveraging the skill and knowledge of experienced experts is one of the crucial elements to secure successful M&A transactions. If there is a need to bring in external resources and experts, it is better to do it sooner rather than later.

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Privacy issues associated with smartphones

By Matthew Chu, Senior Manager and Kenneth Lam, Assistant Manager



Smartphones are mobile phones built with internet connectivity on a mobile computer where additional functionality can be extended with a simple installation of an application (or better referred to as “Apps”). Statistical analysis reveals that 35% of mobile phone users in Hong Kong are smartphones users, being the third highest in Asia Pacific. While this number continues to grow at a significant rate, smartphones are now more than just making voice calls, reading and replying emails, or taking and sharing instant photos, more users use these for performing internet banking transactions.

To enjoy the convenience and advantages of using a smartphone, we need to store sensitive information on our devices for relevant functions to work seamlessly. These include basic telephone contacts, text messages (SMS) to services that require account name and password such as email and social networking site (e.g. Facebook and Twitter). Other personal data include a position locator (GPS of your location) and

possibly details of accounts and passwords for use with internet web browsers.

In this article, we will explore the privacy risks that come hand in hand with these newly evolved mobile phones, especially the associated risks when you lose your phones!

Losing a smartphone

Most users never “plan” to lose their mobile phones. With manufacturers’ sleekly design, mobile phones can be sneaked or lost without notice. Looking at this positively, it is a good excuse to purchase a brand new and smarter smartphone. However, your cost is absolutely more than the monetary value of the new phone; you are inevitably losing most of the data stored on your lost smartphone. Under a worst case scenario, a fraudster may now have access to the personal information being stored somewhere within your lost smartphone.

Be prepared for the worst in 15 minutes – help yourself, save your data and prevent them from potential leakage.

- **Set and use a screen lock**

A screen lock is the simplest way to protect your personal data and deter other person from prying your device (if the

password is not too easy to guess such as 1234 or 1111). Some smartphones require complicated passwords by extending the length of the password or passphrase that includes alpha-numeric characters and also symbols.

- **Enable automatic or remote data wiping**

To set up a rule to wipe (i.e. delete permanently) all data stored on the phone in case you lose your device. Simply configure your smartphone to erase all data automatically once a threshold is met, say wrong passwords are entered 10 times consecutively. For tech savvy users, the same can be achieved by sending a remote command by SMS to start the wiping process for lost device. However, if the device is switched off, the process will not start until it is being turned on again.

- **Back up your data regularly**

Number one of data security rule is to have a backup. A successful backup will minimise the loss of data. Smartphones can be backed up traditionally using a computer or with advances in cloud technology. Users can backup their data remotely to a cloud service, such as Apple iCloud, Dropbox or your favourite cloud service provider.



Deactivate SIM card and change online passwords

If you are unable to contact the person who currently gets hold of your phone, contact your mobile network operator to instantly deactivate the SIM card to prevent any further losses (financially or non-financially). Furthermore, do change your passwords for email accounts and websites as they may have been saved on your smartphone. This will prevent unauthorised access to your email and web services.

Mobile phone malware and virus

Mobile phones have evolved to become a sophisticated handheld computer. Unfortunately, in this new smartphone era, personal data stored on your smartphone may still end up leaking to third parties, even though you are able to keep your

phone physically secured. You may ask – How? Fraudsters would populate app distribution platforms (like App Store, Google Play and Ovi Store) with innocent-looking apps that contain malware or malicious software, and pertain them to be a game or a handy utility. Unknowingly, once the app is downloaded and installed, the malware can enable fraudsters to take control of the smartphone, allowing them to make calls, send and intercept SMS, download paid contents and even track your location using GPS.

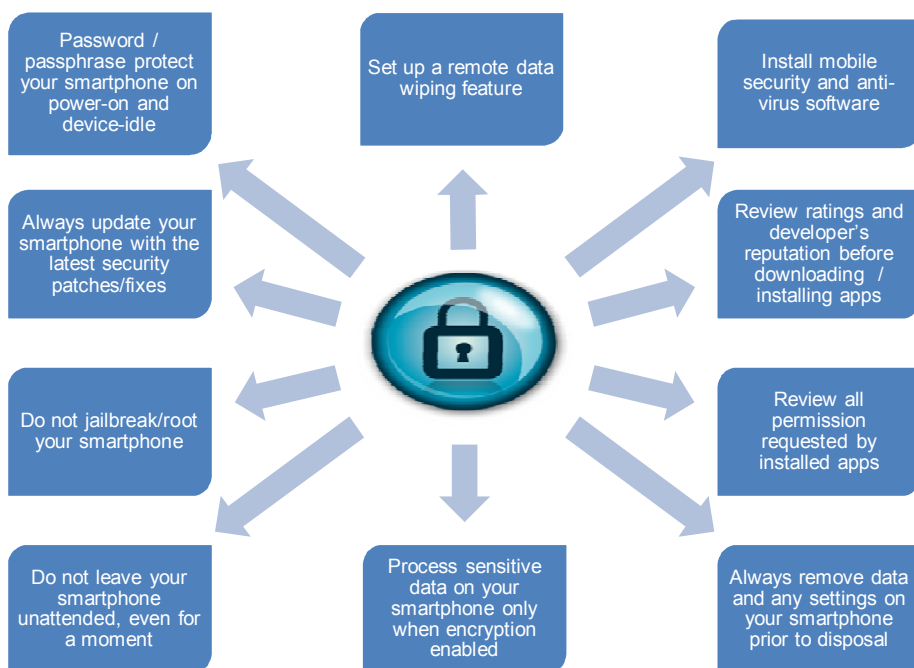
To minimise the threat of malware and viruses, you may consider installing an antivirus software for smartphones and do avoid jail-breaking if you have an iPhone or rooting if you have an Android device. This will minimise exposure of the potential loop holes on your smartphone, should

you otherwise choose to override the usage and access rights through jail-breaking or rooting.

Conclusion

Smartphones bring much convenience to us while at the same time raise concerns over privacy for personal data stored within. While protecting your data, it only takes a few simple steps to deter prying eyes. Simply spending a little time to set up a screen lock, an automatic or remote wiping rule and perform backup regularly, you are minimising your losses should an incident occur. Most importantly, be aware of personal data security at all times and keep your phone safe.

Tips roundup:
Personal data can be leaked when an unprotected smartphone is stolen or lost, or when the device is infected with malware. Here are some general tips for maintaining the security of your smartphone.



Professional Ethics in Liquidation and Insolvency (Part II)

By Terry Kan, Director

The Hong Kong Institute of Certified Public Accountants (HKICPA) has launched the new Section 500 on Professional Ethics in Liquidation and Insolvency, effective from 1 April 2012 (New Code). In Part I of this series, we have outlined the five core principles of this New Code and the areas of threats that Insolvency Practitioners (IP) should be aware of. Part II of this series will highlight the specific applications of the principles in different circumstances.

Specific applications of the New Code

The New Code provides the following specific circumstances which may assist an IP to evaluate threats and consider safeguards in insolvency engagements.

These circumstances are not exhaustive but are usual matters that IPs may encounter:

- Acceptance or non - acceptance of an appointment
- Professional and personal relationships
- Dealing with assets of the entity
- Obtaining specialist advice and services
- Fees and other types of remuneration
- Obtaining appointments
- Gifts and hospitality
- Record keeping

Acceptance or non-acceptance of an appointment

Prior to accepting an engagement, an IP should consider relevant laws, judicial authorities and court directions to ensure that the ethical principles are not compromised. Should there be any potential threat to the principles during the engagement, the IPs may consider safeguards such as consultation with another IP (inside or outside their practice), creditors' committee or professional bodies, changing the insolvency team members, setting clear internal procedures, termination of financial or business relationships or seeking court directions where appropriate.

If, however, no safeguards can be applied to remove or minimise the threats to an acceptable level, an IP should exercise professional judgment to decline or terminate such an appointment.

Multiple engagements in different entities within a group may give rise to tension if not conflicts due to significant professional and personal relationships with the entity. The New Code does not discourage multiple appointments if reasonable steps are taken to minimise potential conflicts and there are no actual / perceived conflicts which may impair the overall objectivity and integrity.

Professional competence and skills are addressed in the New Code. Accepting an engagement without the required skills and experience may render the IP and team members exposed to self-interest threat. Requisite skills and experience may vary in each case

and hence the New Code has provided some general guidelines for consideration.

Potential conflicts at the merger of practices may arise. For example, acting as agent to another IP should be prohibited unless the control of the conduct of the engagement and the professional competency are maintained. Nevertheless, there is no immediate concern to terminate engagements upon merger.

Professional and personal relationships

Professional and personal relationships between an IP and the engagement entity are modified as "Significant Professional Relationship", which covers extensive business and personal relationships that may lead to potential threats.

In brief, all stakeholders including shareholders, directors, business partners, parent and subsidiary companies with common control, debtors, creditors and close relative of the officers or parties with commercial relationships are all taken into account. Such relationship may extend to previous engagements and whether the fees are significant to the practice. Suggested safeguards may include disclosure of prior engagements, cutting the financial / business relationship or changing of the insolvency team. If threats exist but cannot be minimised i.e. "Significant Professional Relationship" or "Significant Personal Relationship" exists, an IP should decline such an engagement.



Dealing with the assets of an entity

To uphold objectivity, no staff members, agents or close relatives of an IP should purchase any assets of the engagement entity. The process of selling of assets should be transparent, understandable and readily identifiable to all third parties concerned. Proper asset valuation by third-party specialists before disposal may reduce or remove the threats entirely.

Obtaining specialist advice and services

When obtaining specialist advice and services, an IP should ensure that best value and service are obtained and such relationship with the specialist should be reviewed on a regular basis. In the selection of specialist, general reputation, expertise, resources and relevant professional and ethical standards of the service provider should be observed and evaluated, aiming to reduce familiarity threats and self-interest threats.

Fees and other types of remuneration

Referral fees or commissions in connection with the acceptance of an engagement should be avoided as it represents a significant threat to objectivity. However, fees paid on account for liquidation costs and expenses are excluded. IPs are reminded not to contravene provisions under the Prevention of Bribery Ordinance (PBO) (Cap 201). If in doubt, legal advice should be sought.

Obtaining appointments

Advertising or marketing activities that may lead to winning of engagements should be fair and

not misleading to the public, in particular when fee basis and the scope of work are provided. Section 250 of the Code "Marketing Professional Services" and Section 450 regarding "Practice Promotion" provide additional guidelines in conjunction with the New Code.

Gifts and hospitality

Gifts and hospitality may lead to self-interest or familiarity threats. Where significant or unacceptable threats are identified, after taking into consideration of all facts and circumstances and concluding that such an offer is NOT regarded "trivial and inconsequential" in the ordinary course of business, an IP should decline the offer. Relevant provisions in PBO (Cap 201) should be noted.

Record keeping

The New Code highlights the significance of record keeping for an IP to demonstrate that actions have been taken to identify and evaluate threats leading to a satisfactory conclusion. The objective test is to enable an independent third party to form a view of the work done based on the paper trail maintained by the IP.

Application of the New Framework to other specific situations

Part 3 of the New Code has modified specific situations previously set out in the past ethical code (Section 432), and divided them into two categories. Category A deals with situations not connected with previous or existing appointments. Category B provides examples relevant to previous or existing appointments.

Both categories are summarised on page 8 of this e.Bulletin for the ease of reference.

Conclusion

The New Code has transformed the old Code into a principle-based standard that all IPs and their insolvency team members are obliged to follow. Specific applications of the ethical principles under more detailed circumstances would make the standard more relevant and applicable to the increasingly complex business world. No doubt, the new ethical standard has accelerated the revamp of engagement procedural checklists or guidelines, in-house practice review procedures and continuous professional training as part of the necessary safeguards for IPs to deliver quality professional work and sustain good practices.

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Summary of application of the New Framework to other specific situations:

Category A appointment	Acceptable / decline engagement	Remarks
Following audit related work within prior 2 years	Decline	Except for Members' Voluntary Liquidation (MVL) or in relation to an insolvent scheme of arrangement in limited circumstances. Same consideration for any insolvency appointment where audit work was done for more than 2 years.
Close personal or business relationship with debenture holder	Decline	Decline in general where an IP holds a position in a financial institution (FI) which is a work provider to the IP. However, IP's general personal relationship as a retail customer of the FI will not count.
Following engagement as investigating accountant	Acceptable	Significant professional relationship would not normally arise except where the IP is involved in the entity's management.
Administrator, manager, adjudicator of a scheme of arrangement of an insolvent client	Decline	Except for the appointment as liquidator or provisional liquidator where the scheme assets and liabilities are significantly different from the assets and liabilities of the company that had previously been audited. Cautious on self-review threat.

Category B appointment	Acceptable / decline engagement	Remarks
Liquidator following appointment as receiver	Decline	Except for the previous appointment being as receiver by court or court approved.
Conversion from MVL into creditors' voluntary liquidation	Acceptable	If no significant professional relationship exists.
Trustee in bankruptcy following appointment of nominee of an Individual Voluntary Arrangement	Acceptable	Provided that unacceptable threat to compliance of fundamental principles does not exist.
Trustee of provident fund, schemes of companies in liquidation or receivership	Decline	Decline if IP is the liquidator, provisional liquidator or receiver.
Administrator, manager or adjudicator of a scheme of arrangement of an insolvent client	Acceptable	Subject to consideration of any unacceptable threats.

New legislation on anti-money laundering and counter terrorist financing

By Anita Hou, Partner

The Anti-Money Laundering and Counter-Terrorist Financing (Financial Institutions) Ordinance (Cap. 615) (AMLO) has come into effect since 1 April 2012. This legislation inter alia is enacted as a result of the evaluation of Hong Kong's progress on implementing the recommendations from the Financial Action Task Force (FATF) in 2007/08. Customer due diligence (CDD), record-keeping requirements and regulatory framework for remittance agents and money exchangers are some of the areas that Hong Kong needs to improve on.

Highlights of AMLO

The new legislation requires that financial institutions such as banks, securities firms, insurers, insurance agents and brokers, remittance agents and money exchangers must verify customer identity and keep a record of relevant customer details and transactions before:

- establishing a new business relationship; or
- making a remittance of HK\$8,000 or above or carrying out other transactions of HK\$120,000 or above for a customer without an account maintained in these financial institutions.

If customers fail to provide the required documents, financial institutions cannot open an account or carry out any transaction on their behalf.

FATF is an inter-governmental body whose purpose is the development and promotion of national and international policies to combat money laundering, the financing of terrorism and proliferation of weapons.

The AMLO inter alia provides for the imposition of requirements relating to CDD and record-keeping by the financial institutions, and provide for the powers of the relevant authorities to supervise the compliance with those requirements and other requirements under AMLO.

There are penalties, including imprisonment and fines, being introduced, should the financial institutions fail to meet the CDD requirements.

The Hong Kong Monetary Authority (HKMA), the Securities and Futures Commission (SFC), the Insurance Authority and the Customs and Excise Department are empowered as the respective relevant authorities to supervise compliance with the statutory requirements by the specified financial institutions.

A Review Tribunal is also set up to review specific decisions and to hear and determine any question or issue arising from or in connection with any review given under the specified provision of AMLO.

CDD requirements

The CDD requirements are, in fact, not substantially different from those being undertaken by banks in accordance with the current HKMA guidelines. Financial institutions may still rely on due diligence being undertaken by intermediaries until the grace period ending on 31 March 2015. Upon such expiry, financial institutions will be required to conduct CDD in accordance with the AMLO and the prevailing HKMA guidelines by themselves, which will undoubtedly increase the compliance

and administrative burden of the financial institutions.

Guidelines on the anti-money laundering (AML) and counter-terrorist financing (CTF) (Guidelines)

At least three sets of Guidelines have been issued in early 2012 by the respective regulatory authorities (including HKMA, SFC and Office of the Commissioner of Insurance) to provide general background and practical guidance for facilitating the relevant financial institutions and their senior management on designing and implementing their own policies, procedures and controls in the relevant operational areas so as to meet the relevant statutory and regulatory requirements.

How can SHINEWING SAS help

- Review existing AML / CTF measures (processes, controls and governance) and assess compliance with the AMLO and relevant regulatory guidelines.
- Conduct testing to help to assess operational effectiveness of the relevant AML / CTF measures
- Recommend practical and cost effective improvement measures, where required.

Conclusion

Management and compliance personnel should ensure that they are familiar with the changes and assess their existing procedures and controls so as to comply with the specific requirements and to improve the operation.

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Forensic & Investigation

Knowledge

History of Forensic Accounting – back to the time of ancient Egypt!

The existence of *Forensic Accounting* went back to the ancient Egyptian scribes who took care of all of the Pharaoh's assets. These scribes were known as the “eyes and ears of Pharaoh”. In around 1800, forensic accounting had its first day in court when an accountant was required to testify at a bankruptcy hearing. In around 1950, Mr. Maurice E. Peloubet developed the term “*Forensic Accounting*” in his essay “Forensic Accounting: Its Place In Today's Economy.” Hence, rather than a new practice, forensic accounting has long been part of the accounting profession.

Today's forensic accountants are involved in a wide variety of cases, both civil and criminal, from family

/ matrimonial disputes and commercial matters to a range of criminal investigations, which include business fraud, murder and anti-money laundering, where forensic accountants are engaged to trace the money trail and uncover where the source and application of funds is.

Forensic accounting has also been crucial in unravelling the corporate scandals of companies in both Hong Kong and elsewhere, such as Akai Holdings, Enron and Worldcom.



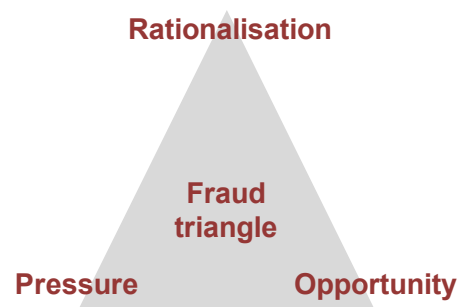
FAQs – Forensic and Investigation

Q: What is a Fraud Triangle?

A: The idea of “Fraud Triangle” was first identified by criminologist Dr. Donald Cressey in the 1950s which describes three factors that are presented in fraud:

- **Pressure (or motivation)** – the need for committing fraud (financial need, performance pressure etc.)
- **Rationalisation** – the mindset of the fraudster that justifies them to commit fraud
- **Opportunity** – the situation that enables fraud to occur (often when internal controls are weak or nonexistent)

According to the fraud triangle, all these three factors will normally be present for fraud to occur. If any one of the three elements is missing, fraud may not occur.



Q: What is an MD5 hash?

A: An MD5 (message digest) hash is a “fingerprint” of an electronic document or file. It is a string made up of 32 hexadecimal characters computed from the contents of the file with a ‘hashing’ algorithm. Files with identical contents always produce the same MD5 hash regardless of the filename.

Computer forensic examiners use MD5 to identify duplicate files, files of evidentiary value or to filter known files from the electronic evidence. Furthermore, an MD5 fingerprint can be used to verify that data hasn't been tampered with or altered since the evidence was collected so as to ensure its Integrity.



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Announcement – SAS Workshops

Forensic and Investigation series

More and more legal proceedings and investigations seek support from accounting firms for their forensic accounting and computer forensic expertise.

A series of workshops have been / will be run to explain the roles and capabilities of forensic accountants and computer forensic experts, through live demos, case studies and interactive discussions. Topics of the workshops are as follows:

- **Course 101 – The ABCs of Forensic Accounting and Computer Forensics, and beyond** - 6 Jun & 13 Jun 2012
- **Reading behind and beyond audited financial statements** - 27 Jun 2012
- **Deciphering “cooked books”** - 18 Jul 2012 (tentative)
- **Lifting the veil of phantom companies** - 8 Aug 2012 (tentative)

Details of the workshops and registration arrangements will be announced under separate emails.



News

- Alan Tang, head of SAS was invited jointly by **the World Bank, the International Development Law Organization and the PRC Supreme People’s Court** to deliver (as part of an international team of trainers) training for some 200 PRC Bankruptcy Judges from all over the PRC in Beidaihe (near Beijing) earlier in June 2012. **Topics covered include the role and functions of the administrator in the bankruptcy process and economic foundations of bankruptcy law.**
- Anita Hou and Matthew Chu, partner and senior manager of FIS, talked about **how forensic accountants crossover with computer forensic experts** in a seminar organised by SW Pearl on 1 June 2012.
- Members of SAS (Alan Tang, Anita Hou, and Terry Kan and Elisa Lui) were speakers in various **insolvency related** courses organised by the Hong Kong Institute of Certified Public Accountants from March to June 2012.

Feedback from readers is essential to our success. We welcome and value your comments or suggestions. Feel free to contact us for any questions as well.