

Fraud – Black lettered paragraphs

This agenda paper presents the black lettered paragraphs contained in the draft ED.

3. When planning and performing the audit to reduce audit risk to an acceptably low level the auditor should consider the risk of material misstatements in the financial statements resulting from fraud.

Professional skepticism

22. When conducting the audit, the auditor should that recognize the possibility that a material misstatement due to fraud could exist, regardless of any past experience with the entity and regardless of the auditor's belief about management's honesty and integrity.

Discussion Among the Audit Team

24. The members of the audit team should discuss the susceptibility of the entity's financial statements to material misstatement due to fraud.

Inquiries of Management

27. The auditor should make inquiries of management to obtain an understanding of:
 - (a) management's assessment of the risk that the financial statements may be materially misstated as a result of fraud;
 - (b) management's process for identifying and responding to the risks of fraud in the entity, including any specific fraud risks that management has identified or account balances or classes of transactions for which a risk of fraud may be likely to exist; and
 - (c) the internal control management has designed and implemented to mitigate specific fraud risks that management has identified, or that otherwise help to prevent, deter, and detect fraud, and to obtain an understanding of how management monitors internal control.
32. The auditor should make inquiries of management, and others within the entity, to determine whether they have knowledge of any fraud or suspected fraud affecting the entity or whether they are aware of any allegations of fraud or suspected fraud affecting the entity.

Inquiries of Those Charged with Governance

37. The auditor should makes inquiries of those charged with governance to obtain an understanding of how they exercise oversight of management's processes for identifying and responding to the risks of fraud in the entity and the internal control that management has established to mitigate these risks.

Risk Assessment Procedures

41. When obtaining an understanding of the entity and its environment, including its internal control, the auditor should consider whether the information obtained indicates that one or more fraud risks factors are present.

Assessing the Risk of Material Misstatement due to Fraud

49. The auditor should assess the risk of material misstatement due to fraud at the financial statement level, and at the assertion level for classes of transactions, account balances and disclosures.

Responding to the Risk of Material Misstatement due to Fraud

51. The auditor should determine overall responses to address the risk of material misstatement due to fraud at the financial statement level and should design and perform further audit procedures whose nature, timing and extent are responsive to the assessed risk of material misstatement at the assertion level.
61. To further respond to the risk of management override of controls, the auditor should design and perform audit procedures to:
- (a) Test the appropriateness of journal entries recorded in the general ledger and other adjustments made in the preparation of financial statements;
 - (b) Review accounting estimates for biases that could result in material misstatement due to fraud;
 - (c) Obtain an understanding of the business rationale of any transactions that the auditor becomes aware of that are outside of 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
68. The auditor should incorporate an element of unpredictability in the selection from year to year of auditing procedures to be performed.

Evaluation Audit Evidence

69. When the auditor identifies a misstatement, the auditor should consider whether such a misstatement may be indicative of fraud and if there is such an indication, the auditor should consider the implications of the misstatement in relation to other aspects of the audit, particularly the reliability of management representations.

Management Representations

73. The auditor should obtain written representations from management that:
- (a) It acknowledges its responsibility for design and implementation of internal control to prevent and detect fraud;
 - (b) It has disclosed to the auditor all significant facts relating to any frauds or suspected frauds known to management that may have affected the entity; and
 - (c) It has disclosed to the auditor the results of its assessment of the risk that the financial statements may be materially misstated as a result of fraud.

Communication with Management or Those Charged with Governance

76. If the auditor has identified a fraud or has obtained information that indicates that a fraud may exist, the auditor should communicate these matters to an appropriate level of management.

78. If the auditor has identified fraud involving senior management and fraud (whether caused by senior management or other employees) that results in a material misstatement in the financial statements the auditor should communicate these matters to those charged with governance.
79. The auditor should reach an understanding with those charged with governance regarding the nature and extent of communications with those charged with governance about fraud involving misappropriation of assets by a lower-level employee.

Communication to Regulatory and Enforcement Authorities

80. The auditor should make those charged with governance or management aware, as soon as practicable, and at the appropriate level of responsibility, of material weaknesses in the design and implementation of internal control to prevent fraud which may have come to the auditor's attention.

Auditor Unable to Continue the Engagement

84. If, as a result of a misstatement resulting from fraud or suspected fraud, the auditor encounters exceptional circumstances that bring into question the auditor's ability to continue performing the audit the auditor should:
 - (a) consider the professional and legal responsibilities applicable in the circumstances, including whether there is a requirement for the auditor to report to the person or persons who made the audit appointment or, in some cases, to regulatory authorities;
 - (b) consider the possibility of withdrawing from the engagement; and
 - (c) if the auditor withdraws:
 - i. discuss with the appropriate level of management and those charged with governance the auditor's withdrawal from the engagement and the reasons for the withdrawal; and
 - ii. consider whether there is a professional or legal requirement to report to the person or persons who made the audit appointment or, in some cases, to regulatory authorities, the auditor's withdrawal from the engagement and the reasons for the withdrawal.

Documentation

88. The auditor should document:
 - (a) The discussion among the audit team regarding the susceptibility of the entity's financial statements due to fraud, including how and when the discussion occurred, the audit team members who participated and the subject matter discussed;
 - (b) The results of the risk assessment of material misstatement due to fraud at the financial statement level and at the assertion level;
 - (c) The specific risk of material misstatement due to fraud and the overall responses to these risk at the financial statement level and the nature, timing and extent or the further audit procedures, the linkage of those procedures with the assessed risks at the assertion level and the results of the audit procedures;

- (d) The results of the audit procedures designed and performed to further respond to the risk of management override of controls;
- (e) The nature of the communications about fraud made to management, those charged with governance and others.