

THE FRAUD LENS – INTERACTIONS BETWEEN ISA 240 AND OTHER ISAs

This publication has been developed by the Fraud Task Force of the International Auditing and Assurance Standards Board (IAASB) to explain the relationship between and linkage of International Standards on Auditing (ISA) 240, The Auditor's Responsibilities Relating to Fraud in an Audit of Financial Statements and other ISAs when planning and performing an audit engagement.

This publication does not amend or override the ISAs, the texts of which alone are authoritative. The non-authoritative guidance is not meant to be exhaustiveⁱ and reading this publication is not a substitute for reading the ISAs.

International Standard on Auditing (ISA) 200,ⁱⁱ is the foundational standard that sets out the independent auditor's overall objectives when conducting an audit of financial statements in accordance with the ISAs and establishes the obligation of the auditor to comply with all the ISAs. The objectives in ISA 200 state that the auditor addresses material misstatements due to both **fraud and error** when conducting an audit to form and express an opinion and report on the financial statements.

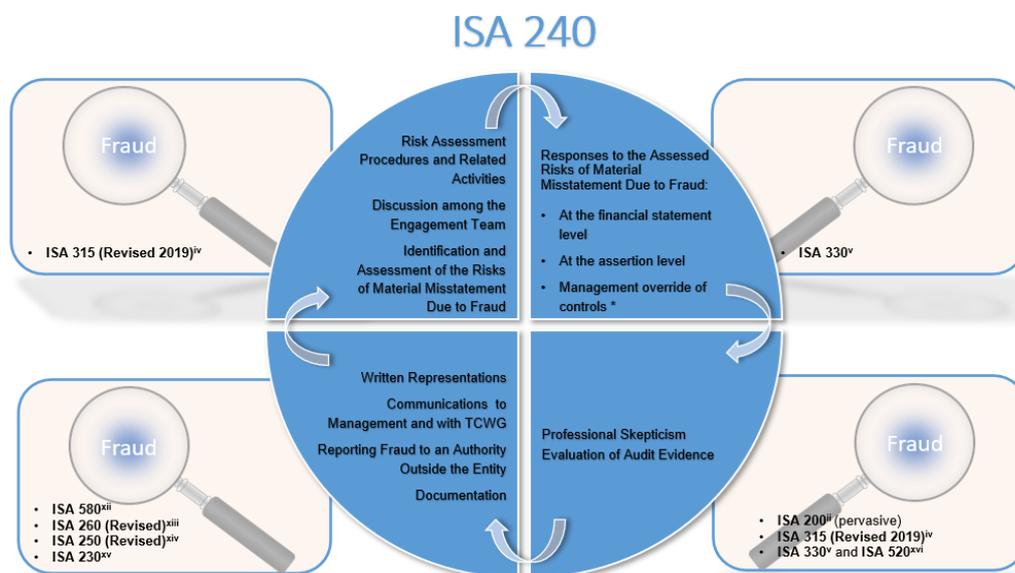
ISA 240 supplements ISA 200. ISA 240 deals with the auditor's responsibilities for fraud in an audit of financial statements and in doing so reinforces the continued use of the **fraud lens** throughout the audit engagement. ISA 240 also clarifies that the distinction between fraud and error is based on intent.ⁱⁱⁱ There is an additional emphasis on the importance of maintaining an attitude of professional skepticism which is especially relevant when identifying and assessing risks of material misstatement due to fraud and responding appropriately to the assessed risks due to fraud. These assessed fraud risks relate to those intentional misstatements that could arise either from fraudulent financial reporting, or the misappropriation of assets.

ISA 240 paragraph 11: The objectives of the auditor are:

- To **identify and assess the risks of material misstatement** of the financial statements due to fraud;
- To obtain **sufficient appropriate audit evidence** regarding the assessed risks of material misstatement due to fraud, through **designing and implementing appropriate responses**; and
- To **respond appropriately** to fraud or suspected fraud identified during the audit.

Relationship between ISA 240 and other ISAs. ISA 240

both expands on certain ISAs as well as provides fraud-specific audit procedures that complements the other ISAs. In doing so, ISA 240 broadly focuses on the auditor's **fraud lens** when planning and performing an audit of financial statements.



^{*} Includes specific audit procedures to address journal entries, biases in accounting estimates (ISA 540 (Revised)ⁱ), and significant transactions that are outside the normal course of business for the entity, or that otherwise appear to be unusual (including related party relationships and transactions in ISA 550ⁱⁱ).

ISA 240 expands on ISA 315 (Revised 2019)^{iv} and ISA 330^v. While other key standards address the core requirements for identifying and assessing the risks of material misstatement (ISA 315 (Revised 2019)) and responding to those risks of material misstatement (ISA 330), ISA 240^{vi} expands on how these standards are applied with a **fraud lens**.^{vii} In particular, in identifying and assessing the risks of material misstatement due to both fraud and error under ISA 315 (Revised 2019), the auditor takes into account the inherent risk factors, which includes the susceptibility to misstatement due to management bias or other fraud risk factors.^{viii}

The emphasis in ISA 240 on risk identification and assessment and responding to those risks of material misstatement through a more substantial work effort when there is a risk of material misstatement due to fraud, highlights the importance of obtaining an understanding of the entity and its environment and the entity's system of internal control with a **fraud lens**. Key aspects that underpin the auditor's consideration of the potential risks of material misstatement due to fraud include the entity's culture (including tone at the top), as well as the environment in which the entity operates.

ISA 240 paragraph 27: Assessed risks of material misstatement due to fraud are treated as **significant risks**

Purposeful engagement team discussions on these key aspects, as well as other matters or areas that have been identified as being susceptible to possible misstatement due to fraud, will help all engagement team members apply the **fraud lens** in undertaking their work.

In addition to designing and implementing overall responses to address the assessed risks of material misstatement due to fraud at the financial statement level, the auditor is also required to design and perform further audit procedures that are responsive to the assessed risks of material misstatement due to fraud at the assertion level. In doing so, the auditor may, when applying the **fraud lens**, change the nature, timing and extent of the further audit procedures in order to be responsive to the assessed fraud risks. For example, the auditor may amend the timing of the further audit procedures performed to incorporate additional elements of unpredictability or assign engagement team members who have more experience or have the necessary specialized skills or knowledge to address changes to the nature of the further audit procedures performed.

ISA 240 includes fraud-specific audit procedures. ISA 240 includes certain requirements that provide the auditor with the necessary **fraud lens** when executing audit procedures that are responsive to risks related to management override of controls and to address specific aspects of other ISAs. These fraud-related audit procedures are intended to be embedded throughout the audit process. The requirement in ISA 240^{ix} to review accounting estimates for biases and evaluate whether the circumstances producing the bias, if any, represents a risk of material misstatement due to fraud is an example of a fraud-related procedure that is to be performed in conjunction with addressing the requirements in ISA 540 (Revised)^x.

Linkage of other ISAs to ISA 240. Other relevant topic or subject-matter specific ISAs have explicit references to ISA 240. The fraud-specific requirements in other ISAs serve to focus the auditor's work effort on the identification and assessment of the risks of material misstatement due to fraud and the responses to address the assessed fraud risks. For example, ISA 550^{xi} includes requirements to meet the following stated objective, "to obtain an understanding of related party relationships and transactions sufficient to be able to recognize fraud risk factors, if any, arising from related party relationships and transactions that are relevant to the identification and assessment of the risks of material misstatement due to fraud." In this instance ISA 550 expands upon how ISA 240, ISA 315 (Revised 2019) and ISA 330 are to be applied in relation to risks of material misstatement associated with related party relationships and transactions.

Understand the interdependencies. A clear understanding of the relationship between and linkage of ISA 240 and the other ISAs will assist the auditor to enhance audit execution when applying a **fraud lens**. This will in turn fulfil the auditor's responsibilities under ISA 240 and other ISAs that contain the broader requirements for an audit.

Endnotes

- i While certain ISA requirements and application and other explanatory material are highlighted, this non-authoritative guidance does not cover all of the ISA provisions that are relevant to the auditor's responsibilities relating to fraud in an audit of financial statements that are effective as of [April 2022].
- ii ISA 200, *Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with International Standards on Auditing*
- iii ISA 240, paragraphs 2, 3 and 12(a)
- iv ISA 315 (Revised 2019), *Identifying and Assessing the Risks of Material Misstatement*
- v ISA 330, *The Auditor's Responses to Assessed Risks*
- vi ISA 240 as amended for the conforming and consequential amendments resulting from the approval of ISA 315 (Revised 2019)
- vii ISA 240, paragraph 1
- viii ISA 315 (Revised 2019), paragraphs 19(c) and 31(a)
- ix ISA 240, paragraph 33(b)
- x ISA 540 (Revised), *Auditing Accounting Estimates and Related Disclosures*
- xi ISA 550, *Related Parties*
- xii ISA 580, *Written Representations*
- xiii ISA 260 (Revised), *Communication with Those Charged With Governance*
- xiv ISA 250 (Revised), *Consideration of Laws and Regulations in an Audit of Financial Statements*
- xv ISA 230, *Audit Documentation*
- xvi ISA 520, *Analytical Procedures*

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