

# Agenda Item 2–B

## Proposed ISA 240 (Revised), *The Auditor’s Responsibilities Relating to Fraud in an Audit of Financial Statements* – Summary of Significant Deliberations and Changes

This paper summarizes the Fraud Task Force’s (Fraud TF) significant deliberations and changes, where applicable, that have been made to proposed ISA 240 (Revised)<sup>1</sup> (proposed standard) since the September 2023 IAASB meeting, as reflected in **Agenda Item 2–A**. In certain instances, this Agenda Item may include an explanation of why a change was not made based on feedback received. Unless otherwise indicated, references to “paragraph(s)” within this agenda item refer to paragraph(s) within proposed ISA 240 (Revised).

*Icon(s):*



Indicates that a conforming or consequential amendment is being proposed to the IAASB’s pronouncements as reflected in **Agenda Item 2–C**.



Denotes the numbering of a paragraph in the version of the proposed standard presented to the Board for the September 2023 IAASB Meeting as the proposed standard has been renumbered.

Reference	Significant Changes and the Rationale for Those Changes
<b>Introduction</b>	
<i>Introductory Material</i>	<p><i>Introductory Material</i></p> <ul style="list-style-type: none"> <li>Based on comments from the Board in September 2023, the Fraud TF considered adding a description of public interest objectives associated with the proposed standard to the introductory paragraphs. The Task Force decided not to because it would be challenging to describe those objectives concisely in the introductory paragraphs as required by Drafting Guideline 6.3.4 of Complexity, Understandability, Scalability and Proportionality Drafting Principles and Guidelines (CUSP Principles and Guidelines). Nevertheless, the Fraud TF agreed to include a description of those objectives in the explanatory memorandum.</li> </ul>
<b>Paragraph 3</b>	<i>Introductory Material</i>

<sup>1</sup> Proposed International Standard on Auditing (ISA) 240 (Revised), *The Auditor’s Responsibilities Relating to Fraud in an Audit of Financial Statements*

Reference	Significant Changes and the Rationale for Those Changes
	<ul style="list-style-type: none"> <li>Paragraph 3 was enhanced to include a sentence from extant ISA 240,<sup>2</sup> paragraph 4 which elaborates on how oversight from Those Charged with Governance (TCWG) contributes to the creation and maintenance of a culture of honesty and ethical behavior.</li> </ul>
<b>Paragraph 7</b>	<p><i>Application Material</i></p> <ul style="list-style-type: none"> <li>Paragraph A7. The Fraud TF changed the examples because: <ul style="list-style-type: none"> <li>The first example did not address the identification by the auditor of fraud or suspected fraud but, rather, the identification and assessment of a risk of material misstatement due to fraud.</li> <li>The second example stated that the auditor had identified the misappropriation of assets (i.e., which is a legal determination) while, as described in this ISA, auditors do not make a legal determination of whether fraud has occurred.</li> </ul> </li> <li>Paragraph A10. The Board asked the Fraud TF to clarify whether all instances of fraud or suspected fraud that are identified during the audit are subject to the fraud or suspected fraud requirements in paragraphs 54–58. Refer to section <i>I-C – Fraud or Suspected Fraud</i> in <b>Agenda Item 2</b> for more information on this matter.</li> </ul>
<b>Paragraph 11</b>	<p><i>Introductory Material</i></p> <ul style="list-style-type: none"> <li>The Fraud TF considered a recommendation to move this paragraph to the application material to further deemphasize the impact of the inherent limitations of an audit pertaining to fraud. The Fraud TF reaffirmed its prior decision to retain the paragraph in the introductory material because the paragraph adds context about why the proposed standard has different requirements for management fraud (e.g., management override of controls, communication requirements that vary depending on what level of management perpetrated the fraud).</li> </ul>
<b>Paragraphs 12–13</b>	<p><i>Introductory Material</i></p> <ul style="list-style-type: none"> <li>Paragraph 12B <b>←S</b> was moved to the application material (paragraph A15) to respond to a concern that the paragraph did not have a sufficiently robust fraud lens perspective on a requirement which exists in another</li> </ul>

<sup>2</sup> ISA 240, *The Auditor's Responsibilities Relating to Fraud in an Audit of Financial Statements*

Reference	Significant Changes and the Rationale for Those Changes
	ISA (i.e., ISA 220 (Revised)), <sup>3</sup> paragraph 14).
<b>Paragraph 14</b>	<p><i>Introductory Material</i></p> <ul style="list-style-type: none"> <li>The Fraud TF was asked to consider including a statement in paragraph 14 that indicates that the only auditing standard auditors apply when they identify fraud or suspected fraud is ISA 240. The Fraud TF reaffirmed its decision that there may be additional responsibilities under law, regulation or relevant ethical requirements that may apply when the auditor identifies fraud or suspected fraud that go beyond this and other ISAs, including ISA 250 (Revised),<sup>4</sup> and that, accordingly, it is not appropriate to state that only ISA 240 applies.</li> </ul> <p><i>Application Material</i></p> <ul style="list-style-type: none"> <li>Paragraph A17: The Fraud TF was also asked to clarify how the identification by the auditor of third-party fraud or suspected fraud interacts with paragraph 14. The Fraud TF added paragraph A17 which clarifies that the identification by the auditors of third-party fraud or suspected fraud which affects the entity may also give rise to additional responsibilities for the auditor law, regulation or relevant ethical requirements.</li> </ul>
<b>Definitions</b>	
<b>Paragraph 18(a)</b>	<p><i>Application Material</i></p> <ul style="list-style-type: none"> <li>Paragraph A19: To improve the overall flow of the standard, the Fraud TF presented this paragraph as the first paragraph of this section.</li> <li>Paragraph A20: To address comments from the Board, the Fraud TF clarified that corruption, bribery and money laundering are distinct concepts in law or regulation, however, they may be fraudulent acts. The Fraud TF also clarified that the examples illustrate “corruption involving fraud,” “bribery to conceal fraud,” and “money laundering to facilitate fraud.”</li> <li>Paragraph A22: The Fraud TF moved the boxed examples to paragraph A52. The Fraud TF believes that the examples would be more useful as application material to requirement addressing third-party fraud (i.e.,</li> </ul>

<sup>3</sup> ISA 220 (Revised), *Quality Management for an Audit of Financial Statements*

<sup>4</sup> ISA 250 (Revised), *Consideration of Laws and Regulations in an Audit of Financial Statements*

Reference	Significant Changes and the Rationale for Those Changes
	for the engagement team discussion to include an exchange of ideas about fraud risk factors, including how assets of the entity could be misappropriated by third parties).
<b>Paragraph 18(b)</b>	<p><b>Fraud Risk Factors</b></p> <p><i>Application Material</i></p> <ul style="list-style-type: none"> <li>Paragraph A24: The Fraud TF enhanced the application material on fraud risk factors by adding a reference to <b>Appendix 1</b>.</li> </ul>
<b>Requirements</b>	
<b>Professional Skepticism</b>	
<b>Paragraph 19</b>	<p><i>Requirement and Application Material</i></p> <ul style="list-style-type: none"> <li>The Fraud TF was asked to redeliberate its decision to delete the following: <ul style="list-style-type: none"> <li>The clause in paragraph 19: "..., notwithstanding the auditor's past experience of the honesty and integrity of the entity's management those charged with governance (TCWG)"; and</li> <li>Paragraph A24 <b>←S</b>: <i>Although the auditor cannot be expected to disregard past experience of the perceived honesty and integrity of the entity's management and those charged with governance, the auditor's professional skepticism is particularly important in considering the risks of material misstatement due to fraud because there may have been changes in circumstances.</i></li> </ul> </li> <li>The Fraud TF reaffirmed its decision to delete the material because: <ul style="list-style-type: none"> <li>Revisions to the requirements and application material are proposed by the Fraud TF with a view that the revisions should be based on the application of a fraud lens; and</li> <li>Retaining that material might serve to undermine the exercise of professional skepticism in audits of longer standing audit clients.</li> </ul> </li> </ul>

Reference	Significant Changes and the Rationale for Those Changes
Paragraph 20	<p><i>Requirement and Application Material</i></p> <ul style="list-style-type: none"> <li>The matters deliberated and decisions reached by the Fraud TF are described in <b>Agenda Item 2</b>. Refer to section <i>I-A – Professional Skepticism – Authenticity of Records and Documents</i> in <b>Agenda Item 2</b>.</li> </ul>
Paragraph 21 ←S	<p><i>Requirement</i></p> <ul style="list-style-type: none"> <li>After further deliberation, the Fraud TF proposes to delete the paragraph to respond to concerns raised about the value proposition of that paragraph and its consistency with the CUSP Principles and Guidelines. The paragraph had been introduced to act as a signpost to direct auditors to the fraud or suspected fraud requirements in paragraphs 54-58 (S → paragraphs 54–63), when auditors identify instances of fraud or suspected fraud. Nevertheless, the Fraud TF acknowledges that a signpost is not likely required because audit platforms are increasingly digital which, in turn, direct auditors to the applicable requirements depending on the circumstances, including, for example, when fraud or suspected fraud is identified.</li> </ul>
<b>Engagement Resources</b>	
Paragraph 22	<p><i>Application Material</i></p> <ul style="list-style-type: none"> <li>Paragraph A34, lead-in: The Fraud TF replaced "IT experts" with "other experts" to broaden the range of possible experts that may be involved in the audit engagement when addressing fraud. The Fraud TF made similar changes to other paragraphs. Also, the Fraud TF made changes to the examples, to address the concern of conflating fraud with non-compliance with laws and regulations, by emphasizing the fraudulent aspects of the non-compliance with laws and regulations. In addition, the Fraud TF deleted the example in the fifth bullet point, which was perceived to raise more questions than provide guidance.</li> <li>Paragraph A36: The Fraud TF added a 'fraud lens' by linking the examples cited in the parentheses to the significant risk related to management override of controls.</li> </ul>
<b>Engagement Performance</b>	
Paragraphs 23–24	<p><i>Requirement</i></p>

Reference	Significant Changes and the Rationale for Those Changes
	<ul style="list-style-type: none"> <li>The Fraud TF reaffirmed its position to keep the requirements in paragraphs 23–24 separate because the consideration of the matters referred to in paragraph 24 feeds into the required "determination" in paragraph 23 (e.g., the risks of material misstatement due to fraud in paragraph 23(b) is driven by matters laid out in paragraphs 24(a)–24(c)).</li> </ul>
<b>Risk Assessment Procedures and Related Activities</b>	
<b>Paragraph 26</b>	<p><i>Application Material</i></p> <ul style="list-style-type: none"> <li><b>S→</b> Paragraph A45: The Fraud TF deleted this paragraph as it was duplicating paragraph 1 of the proposed standard. Paragraph 1 states that the requirements and guidance in the proposed standard refer to, or expand on, the application of other relevant ISAs and highlights ISA 315 (Revised 2019)<sup>5</sup> as one of the standards it refers to or expands on.</li> </ul>
<b>Paragraph 28</b>	<p><i>Application Material</i></p> <ul style="list-style-type: none"> <li>Paragraph A47: The Fraud TF made changes to align the application material with paragraph 14 of ISA 540 (Revised).<sup>6</sup></li> </ul>
<b>Paragraph 29</b>	<p><i>Requirement</i></p> <ul style="list-style-type: none"> <li>Paragraph 29(a)(ii)(a): The Fraud TF deleted the reference to "third parties" because auditors may not necessarily have a view of the incentives or pressures on third parties to commit fraud, particularly third parties that are unknown.</li> <li>Paragraph 29(a)(ii)(c): The Fraud TF clarified that the requirement relates to an exchange of ideas about fraud risk factors regarding how assets of the entity could be misappropriated by different individuals such as management, TCWG, employees or third parties. This change aligns the construct of the requirement with paragraph 29(a)(ii)(b).</li> </ul>

<sup>5</sup> ISA 315 (Revised 2019), *Identifying and Assessing the Risks of Material Misstatement*

<sup>6</sup> ISA 540 (Revised), *Auditing Accounting Estimates and Related Disclosures*

Reference	Significant Changes and the Rationale for Those Changes
	<ul style="list-style-type: none"> <li>Paragraph 29(b)(ii): The Fraud TF made changes to align the requirement with paragraph 7, which indicates that suspected fraud includes allegations of fraud that come to the auditor's attention during the course of the audit.</li> </ul> <p><i>Application Material</i></p> <ul style="list-style-type: none"> <li>Paragraph A48: The Fraud TF deleted the first sentence of the application material as it was repeating what is required by ISA 220 (Revised), paragraph 14.</li> <li>Paragraph A52: The Fraud TF deleted the fourth bullet point as it was perceived to be conflating fraud with non-compliance with laws and regulations. Further, the Fraud TF added that the exchange of ideas during an engagement team discussion may include whether the entity has third party relationships that give rise to a fraud risk factor, or a risk of third-party fraud. This bullet point was added to add a hook for the boxed examples that were moved from paragraph A22. The Fraud TF also modified the boxed examples to illustrate that a fraud risk factor may be identified in the risk identification and assessment, or during the audit.</li> </ul>
<b>Paragraph 30</b>	<p><i>Requirement</i></p> <ul style="list-style-type: none"> <li>The Fraud TF reaffirmed its decision to retain this requirement because deleting it makes the proposed standard less robust than extant ISA 240. The Fraud TF noted that paragraph 30 is the equivalent of paragraph 15 in extant ISA 240.</li> </ul>
<b>Paragraph 31</b>	<p><i>Application Material</i></p> <ul style="list-style-type: none"> <li>Paragraph A54: The Fraud TF deleted the second example as it was perceived not to have a 'fraud lens.'</li> </ul>
<b>Obtaining an Understanding of the Entity and Its Environment, the Applicable Financial Reporting Framework and the Entity's System of Internal Control</b>	
<b>Paragraph 33</b>	<p><i>Application Material</i></p> <ul style="list-style-type: none"> <li>Paragraphs A62 and A63: The Fraud TF made changes to address the concern of conflating fraud with non-compliance with laws and regulations.</li> </ul>
<b>Paragraphs 34–36</b>	<p><i>Requirement</i></p>

Reference	Significant Changes and the Rationale for Those Changes
	<ul style="list-style-type: none"> <li>Paragraph 34(a): The Fraud TF made changes to align the requirement with paragraph 21(a)(i) of ISA 315 (Revised 2019).</li> <li>Paragraphs 34(d)(i), 35(b)(i) and 36(b): The Fraud TF made changes to clarify that the intended outcome of the inquiries of TCWG, management, individuals within the internal audit function, and other appropriate individuals within the entity are about allegations of fraud in the context of the entity and not in the context of the auditor (also see related description in paragraph 7).</li> </ul>
<b>Paragraph 37</b>	<p><i>Requirement</i></p> <ul style="list-style-type: none"> <li>Paragraph 35(b)(i): The Fraud TF made changes to align the requirement with paragraph 25(a)(i)(a) of ISA 315 (Revised 2019).</li> </ul> <p><i>Application Material</i></p> <ul style="list-style-type: none"> <li>Paragraph A97: The Fraud TF emphasized in the application material addressing the auditor’s understanding of the entity’s information system and communication, that the auditor may assign individuals with specialized skills and knowledge, such as forensic and IT experts, or more experienced individuals to the engagement.</li> </ul>
<b>Paragraphs 38–39</b>	<p><i>Requirement and Application Material</i></p> <ul style="list-style-type: none"> <li>Paragraphs 38–39: For more information about the key deliberations and recommendations relating to these requirements, refer to <i>Section I-B</i> in <b>Agenda Item 2</b>.</li> <li>Paragraphs 38(a)–38(b) and A100–A101: The Fraud TF clarified that the requirements relate to controls “designed” to prevent or detect fraud.</li> <li>Paragraph A102, lead in: The Fraud TF clarified that the boxed examples are examples of general IT controls that may address the risks arising from the use of IT and may also be relevant to the prevention or detection of fraud.</li> </ul>
<b>Identifying and Assessing the Risks of Material Misstatement due to Fraud</b>	
<b>Paragraph 40</b>	<i>Requirement</i>



Reference	Significant Changes and the Rationale for Those Changes
	<ul style="list-style-type: none"> <li>Paragraph 40(b): The Fraud TF made changes to align the requirement with paragraph 26(d) of ISA 315 (Revised 2019).</li> </ul>
<b>Paragraph 41</b>	<p><i>Requirement</i></p> <ul style="list-style-type: none"> <li>To avoid broadening the requirement to include all fraud risk factors, the Fraud TF deleted the reference to the word "any" within the requirement to clarify that the auditor only needs to take into account related fraud risk factors.</li> </ul> <p><i>Application Material</i></p> <ul style="list-style-type: none"> <li>Paragraph A112: The Fraud TF clarified that the auditor may conclude that there are no risks of material misstatement due to fraud relating to revenue recognition in the case where no fraud risk factors are present or when the fraud risk factors are not significant.</li> </ul>
<b>Responses to the Assessed Risks of Material Misstatement Due to Fraud</b>	
<b>Paragraph 47</b>	<p><i>Application Material</i></p> <ul style="list-style-type: none"> <li>Paragraph A122: The Fraud TF deleted the last part of the third bullet point to make the matter more general as it was noted that this example was too specific.</li> <li>Paragraph A123: The Fraud TF updated the example in response to Board comments that it was substantially a repeat of the guidance provided in the lead into paragraph A123. The changes were also made in response to comments that differences may occur, and that it happens in practice relatively frequently.</li> <li>Paragraph <b>S→</b> A124: The Fraud TF deleted this paragraph because it did not have a fraud lens and was only describing requirements in ISA 505.<sup>7</sup></li> </ul>
<b>Paragraph 53</b>	<i>Application Material</i>

<sup>7</sup> ISA 505, *External Confirmations*

Reference	Significant Changes and the Rationale for Those Changes
	<ul style="list-style-type: none"> <li>Paragraph A143: The Fraud TF deleted the fifth indicator that may suggest that significant transactions that are outside the normal course of business for the entity as cryptocurrency may become a more prevalent form of payment in the future.</li> </ul>
<b>Fraud or Suspected Fraud</b>	
<b>Paragraphs 54 – 58</b>	<p><i>Requirements and Application Material</i></p> <ul style="list-style-type: none"> <li>For more information about the significant deliberations and changes to this section, refer to section <i>I-C – Fraud or Suspected Fraud</i> in <b>Agenda Item 2</b>.</li> </ul>
<b>Communications with Management and Those Charged with Governance</b>	
<b>Paragraph 66</b>	<p><i>Application Material</i></p> <ul style="list-style-type: none"> <li>Paragraph A187: The Fraud TF aligned the first sentence of the application material with the requirement in paragraph 66.</li> </ul>
<b>Appendices</b>	
<b>Appendices 1–4</b>	<ul style="list-style-type: none"> <li>The Fraud TF clarified, enhanced or deleted certain examples in response to the Board's offline written comments.</li> </ul>
<b>Conforming and Consequential Amendments</b>	
<b>ISA 200</b>	<ul style="list-style-type: none"> <li>For more information about the key deliberations and recommendations relating to the consequential amendments to paragraph A24 of ISA 200,<sup>8</sup> refer to section <i>I-A – Professional Skepticism – Authenticity of Records and Documents</i> in <b>Agenda Item 2</b>.</li> </ul>

<sup>8</sup> ISA 200, *Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with International Standards on Auditing*