

Agenda Item H.4

For Reference

Please note: This is the IAASB Fraud Issues Paper that was discussed by the Board at the June 2023 IAASB quarterly meeting (Agenda Item 3). This paper is provided to the IAASB CAG Representatives in September 2023 for reference purposes. Other June 2023 Fraud Agenda Items, as summarized below, may be accessed through the IAASB's [Meeting Page](#).

Proposed ISA 240 (Revised), *The Auditor's Responsibilities Relating to Fraud in an Audit of Financial Statements* – Issues

Objectives:

The objectives of the IAASB discussion in June 2023 are to obtain the Board's input on the Fraud Task Force's (Fraud TF):

- Key proposed changes in ISA 240¹ that are intended to promote consistent practice and change auditor behavior – see **Section I** of this Agenda Item and the:
 - Related paragraphs in **Agenda Item 3–A**.
 - Proposed conforming and consequential amendments specific to ISA 700 (Revised), *Forming an Opinion and Reporting on Financial Statements* and ISA 701, *Communicating Key Audit Matters in the Independent Auditor's Report*, arising from the changes to proposed ISA 240 (Revised) addressing transparency in the auditor's report in **Agenda 3–C**.
- Other significant changes made since December 2022 – see **Section II** of this Agenda Item and the related paragraphs in **Agenda Item 3–A**. The explanation of significant changes in **Agenda Item 3–B** provides additional detail as to the rationale for changes made in **Agenda Item 3–A**.

Approach to the Board Discussion:

The Fraud TF Chair will go through the draft of proposed ISA 240 (Revised) presented in **Agenda Item 3–A**, by section or sub-section, and the proposed conforming and consequential amendments in **Agenda Item 3–C**. **Section III** of this Agenda Item specifies the two matters for the IAASB's consideration as the Fraud TF Chair 'walks' the Board through the proposed standard in plenary session. As part of the 'walk through', the Fraud TF Chair will highlight, and Board members may wish to specifically address, the key proposed and other significant changes discussed in **Sections I and II** of this Agenda Item.

Introduction

1. Changes to ISA 240, based on the proposed actions in the [project proposal](#), were previously discussed with the Board at the [March](#), [June](#), [September](#) and [December](#) 2022 IAASB meetings.
2. At the December 2022 IAASB meeting, the Fraud TF presented to the Board its views, recommendations and drafting for two topics: (a) fraud and suspected fraud; and (b) transparency in the auditor's report. In addition, the IAASB was presented with the changes considered and made by the Fraud TF to the drafting paragraphs of proposed ISA 240 (Revised) in response to Board feedback for the topics that were deliberated at the June and September 2022 IAASB meetings.

¹ International Standard on Auditing (ISA) 240, *The Auditor's Responsibilities Relating to Fraud in an Audit of Financial Statements*

3. The IAASB broadly supported the Fraud TF proposals and provided specific comments for the topics discussed to be considered further in the development of proposed ISA 240 (Revised). The approved December 2022 IAASB meeting minutes are available on the *IAASB Quarterly Board Meeting – December 5-9, 2022* [webpage](#).
4. This paper sets out the:
 - **Section I** – Key proposed changes in ISA 240 aimed at promoting consistent practice and changing auditor behavior.
 - **Section II** – Significant changes to proposed ISA 240 (Revised).
 - **Section III** – Matters for the IAASB’s consideration.
 - **Section IV** – Way forward.

Materials Presented—Appendices and Other Agenda Items Accompanying This Paper

5. This Agenda Item includes the following appendices, other agenda items and supplemental material:

Appendix 1	Fraud TF Members and Update on Activities Since the December 2022 IAASB Meeting
Appendix 2	Mapping of Key Changes in Proposed ISA 240 (Revised) to Relevant Paragraphs in Agenda Item 3–A
Agenda Item 3–A	Proposed ISA 240 (Revised), <i>The Auditor’s Responsibilities Relating to Fraud in an Audit of Financial Statements</i> – Marked from December 2022
Agenda Item 3–B	Explanation of Significant Changes
Agenda Item 3–C	Conforming and Consequential Amendments Arising from Proposed ISA 240 (Revised) * For ISA 700 (Revised) and ISA 701 only
Agenda Item 3–D (Supplemental)	Examples of Key Audit Matters that Relate to Fraud
Agenda Item 3–E (Supplemental)	Comparison of Proposed ISA 240 (Revised) with Extant ISA 240, <i>The Auditor’s Responsibilities Relating to Fraud in an Audit of Financial Statements</i>
Agenda Item 3–F (Supplemental)	Mapping of Key Changes in Proposed ISA 240 (Revised) to the Actions and Objectives in the Project Proposal that Support the Public Interest
Agenda Item 3–G (Supplemental)	Proposed ISA 240 (Revised), <i>The Auditor’s Responsibilities Relating to Fraud in an Audit of Financial Statements</i> – Clean Version

Ongoing Engagement with Others

6. Project specific outreach since the December 2022 IAASB meeting included the following:
- January 2023 – The Fraud TF Chair and members, and IAASB Staff met with representatives from the American Institute of Certified Public Accountants (AICPA) and the AICPA's Auditing Standards Board. At the meeting, the AICPA provided an update of their research initiative aimed at gathering perspectives and insights relevant to enhancing transparency in the auditor's report. This included sharing an overview of interview summaries from 26 US-based users and preparers that among others included aspects relevant to enhancing transparency about fraud.
 - March 2023 – The Fraud TF Chair provided representatives from the IAASB Consultative Advisory Group (CAG) with an update on the progress of the fraud project. Specifically, the IAASB CAG was consulted on certain of the proposals² being put forward to revise ISA 240 as the Fraud TF continued to progress its work in advance of the June 2023 IAASB meeting.
7. In addition, the topic of fraud was specifically addressed in meetings with the following stakeholders during this period as part of the general outreach program:
- December 2022 – Participation at meeting of the International Association of Insurance Supervisors (IAIS), Accounting and Auditing Working Group – By Videoconference (Seidenstein, Botha)
 - February 2023 – Meeting with Leadership and Technical Staff of the Institute of Chartered Accountants in England and Wales (ICAEW) – By Videoconference (Seidenstein, Botha)
 - March 2023 – Participation at meeting of the International Forum of Independent Audit Regulators' (IFIAR) Standards Coordination Working Group – Madrid, Spain (Seidenstein, Botha)
 - April 2023 – Joint IAASB / IESBA³ participation as panelists at the 2023 IFIAR Plenary Meeting – Washington DC (Seidenstein, Dias)
 - May 2023 – Presentation at the Forum of Firms, Audit Quality Event with Latin America and Caribbean Region Members – Sao Paulo, Brazil (Botha)

Coordination with IESBA, IAASB Task Forces, Consultation Groups, and Other Experts

IESBA

8. In May 2023, the IAASB Staff and Fraud TF Chair met twice with the IESBA Staff and Liaison Board Member to request their input on the Fraud TF's initial views and recommendations regarding the linkage between proposed ISA 240 (Revised) and the IESBA Code.⁴ The IESBA Staff and Liaison Board Member were also asked to perform a high-level review of proposed ISA 240 (Revised) to identify any relevant ethical considerations or matters pertaining to fraud, in addition to those

² The IAASB CAG was consulted on the Fraud TF's proposals on the following topics: (a) professional skepticism; (b) journal entries; (c) audit documentation; (d) identifying and assessing risks of material misstatement due to fraud; (e) fraud or suspected fraud; and (f) transparency in the auditor's report on fraud.

³ International Ethics Standards Board for Accountants (IESBA)

⁴ IESBA's *International Code of Ethics for Professional Accountants (including International Independence Standards)* (IESBA Code)

proposed by the Fraud TF. The IAASB Staff and Fraud TF Chair subsequently updated the IESBA Staff and Liaison Board Member on the Fraud TF's deliberations specific to relevant ethical requirements and linkages to the IESBA Code

9. In developing the Fraud TF's initial views and recommendations, the Fraud TF primarily focused on:
- The *Revisions to the Code to Promote the Role and Mindset Expected of Professional Accountants*, issued in October 2020 ; and
 - Instances within the IESBA Code (Parts 1 and 3) where there is a reference to fraud, suspected fraud, or alleged fraud, including terms associated with fraud, such as bribery, corruption, money laundering, cybercrime and terrorist financing and the related impact of third-party fraud on the responsibilities of professional accountants in public practice.⁵
10. In summary, the Fraud TF:
- Endeavored to include, where applicable, targeted references to the relevant ethical requirements covered by the IESBA Code's *Fundamental Principles*. In doing so, the Fraud TF proposed to either add or enhance application material in proposed ISA 240 (Revised) as it relates to relevant ethical requirements or insert a footnote reference to the relevant sections in the IESBA Code (and specific paragraphs where possible).
 - Considered comments and suggestions from the IESBA Staff and Liaison Board Member on the linkages between proposed ISA 240 (Revised) and the IESBA Code.
11. The outcome of the coordination with IESBA to date is reflected in the relevant proposals in **Agenda Item 3–A**. Further the IAASB Fraud TF Chair will be presenting the proposals to the IESBA Board as part of the IAASB-IESBA coordination update at the June 2023 IESBA meeting.

IAASB Task Forces and Consultation Groups

12. Since the approval of the project proposal, coordination activities with IAASB Task Forces and Consultation Groups included:
- Going Concern Task Force: Consideration of the various proposals outlined in the Exposure Draft of Proposed ISA 570 (Revised 202X), *Going Concern* (ED-570), including the references to ISA 240 and fraud risk factor(s), and, where applicable, of adopting a consistent approach to address certain proposed actions that impact both the fraud and going concern projects.
 - Audit Reporting Consultation Group (ARCG): Consultation on their input on the use of fraud related key audit matters (KAMs) and the related proposed changes to the auditor's responsibilities in the auditor's report.
 - Technology Consultation Group (TCG): Consultation on their input on proposals regarding the incorporation of technology-related application material.

Other Experts

13. The Fraud TF has benefitted from the input of the following two experts:

⁵ In performing this analysis, it was noted that the relationship between proposed ISA 240 (Revised), ISA 250 (Revised), and Non-compliance with Laws and Regulations (NOCLAR) under the IESBA Code will be addressed as part of non-authoritative guidance at the conclusion of the project.

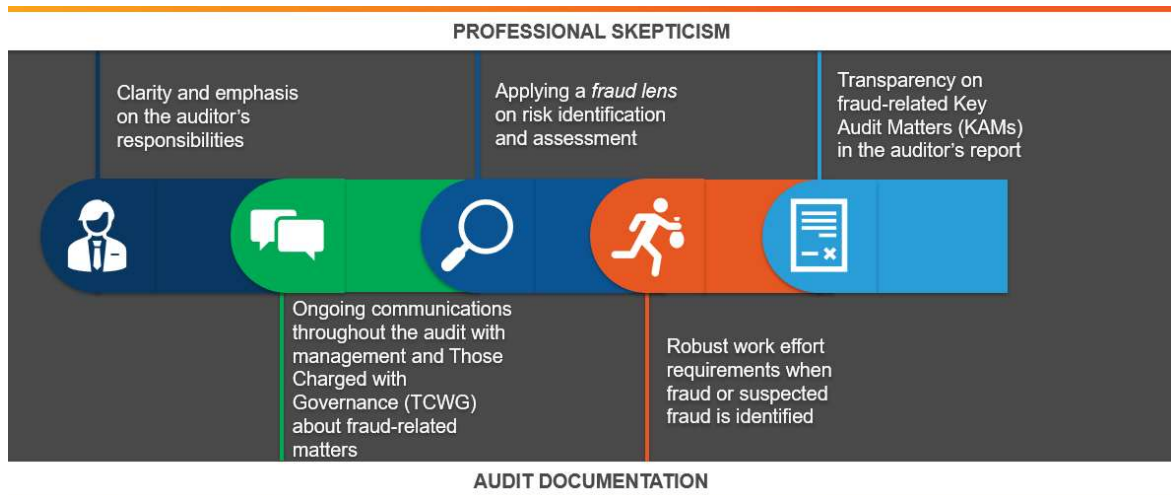
- Mike Savage, Partner at EY Canada LLP and a member of the EY Global Forensics Leadership Team – Mike focused on the importance and benefits of having a forensic specialist as a member of the engagement team (depending on the facts and circumstances of the audit engagement), and the expertise that may be leveraged throughout the audit engagement.
- Sandy Herrygers, Partner at Deloitte & Touche LLP and the Global Assurance Leader – Sandy provided practical insights and current perspectives into the use of technology when performing work related to fraud in an audit of financial statements.

Addressing the Standard-Setting Actions Included in the Project Proposal

14. In developing the revisions to proposed ISA 240 (Revised), the Fraud TF remained focused on the standard-setting actions envisaged by the project proposal and considered the qualitative standard-setting characteristics⁶ as criteria to assess the proposed standard's responsiveness to the public interest. **Agenda Item 3–F** provides a table that compares the Fraud TF proposals to date to address the standard-setting actions of the project proposal.

Section I – Key Proposed Changes in ISA 240 Aimed at Promoting Consistent Practice and Changing Auditor Behavior

15. The diagram and the related sections below depict and describe what the Fraud TF believes to be the seven most important proposed changes addressing the key issues identified in the project proposal, that will drive consistency in practice and change in auditor behavior, specifically: **auditor's responsibilities, professional skepticism, communications with management and those charged with governance (TCWG), risk identification and assessment, fraud or suspected fraud, transparency in the auditor's report and documentation.** These proposed changes cover new topics to be discussed with the Board at the June 2023 meeting and topics previously discussed at the March, June, September and December 2022 meetings.



A. Clarity and Emphasis on the Auditor's Responsibilities (Introduction) *(Previously Discussed with the IAASB)*

⁶ See paragraph 26 of the project proposal and the Public Interest Framework (PIF) included in the Monitoring Group report *Strengthening the International Audit and Ethics Standard-Setting System*.

Fraud Project Proposal – Key Issues and Proposed Actions

16. The project proposal included proposed actions to address key issues related to the auditor's responsibilities (see key issue in paragraphs 19(a)(i)–19(a)(ii) and proposed action A.1 in paragraph 25 of the project proposal for the revision of ISA 240).

Previous IAASB Discussions

17. The Board discussed this topic at the June 2022 IAASB meeting. The Fraud TF restructured the Introduction section to:
- Clarify and emphasize the auditor's responsibilities regarding fraud in an audit of financial statements.
 - Reduce the ambiguity between the inherent limitations of an audit and the auditor's responsibilities for fraud in an audit of financial statements.
18. As part of this restructuring, the Fraud TF:
- Placed the auditor's responsibilities prior to the description of inherent limitations of an audit. The auditor's responsibilities were drafted with a focus on the *fraud lens*. This reordering sets the tone for a clear and affirmative articulation of the auditor's responsibilities specific to fraud at the outset of the standard (see paragraphs 2 and A1, 3, 9–11 and A12 in **Agenda Item 3–A**).
 - Clarified that the auditor's responsibilities include communicating and reporting about matters related to fraud as required by proposed ISA 240 (Revised) (see paragraph 2(b) in **Agenda Item 3–A**).
 - Introduced the "Key Concepts in this ISA" section, which explains the underlying concepts in the standard such as the characteristics of fraud, inherent limitations, professional skepticism and professional judgment, and noncompliance with laws and regulations (see paragraphs 4–13 and A2–A15 in **Agenda Item 3–A**).
 - Relocated part of the auditor's responsibilities relating to the inherent limitations of the audit under the sub-heading "Inherent Limitations." By doing so, the auditor's responsibilities are more succinct and unencumbered by language that may be perceived to diminish the auditor's responsibilities (see paragraphs 9–11 and A12 in **Agenda Item 3–A**).
19. In addition to the explanation about the responsibilities of others in the financial reporting ecosystem in the introductory section (see paragraph 3 in Agenda Item 3–A), the Fraud TF has endeavored to enhance the proposed standard by including application material that focuses on how the practices of certain stakeholders may assist in mitigating the risk of misstatement due to fraud in the financial statements. For example, management may place a strong emphasis on fraud prevention by implementing a fraud risk management program (see paragraph A74 in **Agenda Item 3–A**).

B. Professional Skepticism (*New Topic to be Discussed with the IAASB*)

Fraud Project Proposal – Key Issues and Proposed Actions

20. The project proposal included proposed actions to address key issues related to professional skepticism (see key issue in paragraph 19(g)(i) and proposed action C.25 in paragraph 25 of the project proposal for the revision of ISA 240).

Fraud TF's Initial Views and Recommendations

21. The Fraud TF discussed the overall approach to professional skepticism given the ongoing efforts of the IAASB to appropriately emphasize the importance of maintaining professional skepticism. The discussion was informed by:
- The views of IAASB CAG Representatives encouraging clarity around the auditor's considerations in maintaining professional skepticism throughout the audit (i.e., when performing work relating to fraud in an audit of financial statements).
 - The perspectives of an IAASB CAG Representative that the IAASB's approach to professional skepticism should be reconsidered given the importance for the auditor to maintain professional skepticism throughout the audit, rather than emphasizing professional skepticism separately in each subject-matter standard.
22. The Fraud TF believes that it remains appropriate to highlight the importance of maintaining professional skepticism especially in the context of emphasizing the *fraud lens*. The Fraud TF proposes to retain the extant section on Professional Skepticism in proposed ISA 240 (Revised) with a focus on remaining alert throughout the audit engagement for information about fraud, suspected fraud, or alleged fraud.
23. The inclusion of paragraph 12 in **Agenda Item 3–A** is intended to highlight to the auditor (a) the importance of professional skepticism when performing audit procedures (as noted by the reference to ISA 200⁷) and (b) the interrelationship between professional skepticism and professional judgment. This is similar to the approach taken in recently issued or proposed ISAs, in particular paragraph 7 of ISA 220 (Revised),⁸ paragraph 3 of ISA 315 (Revised 2019),⁹ and paragraph 9 of ISA 600 (Revised).¹⁰
24. When referencing the proposed action in the project proposal, the Fraud TF considered the enhancements that have already been made in:
- Paragraphs 7 and A33–A36 of ISA 220 (Revised) emphasizing the importance of professional skepticism at the engagement level, and the maintenance of professional skepticism among the engagement team members throughout the audit engagement; and
 - Paragraph 13 of ISA 315 (Revised 2019) that states “[t]he auditor shall design and perform risk assessment procedures in a manner that is not biased towards obtaining audit evidence that may be corroborative or towards excluding audit evidence that may be contradictory.”

The Fraud TF is of the view that to repeat the requirements in proposed ISA 240 (Revised) is not appropriate as the suite of ISAs apply in their entirety. Instead, the Fraud TF believes that where appropriate, the linkages to relevant ISAs should be strengthened by the use of footnotes.

⁷ ISA 200, *Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with International Standards on Auditing*

⁸ ISA 220 (Revised), *Quality Management for an Audit of Financial Statements*

⁹ ISA 315 (Revised 2019), *Identifying and Assessing the Risks of Material Misstatement*

¹⁰ ISA 600 (Revised), *Special Considerations-Audits of Group Financial Statements (Including the Work of Component Auditors)*

25. In addressing the first bullet¹¹ of the proposed action, the Fraud TF proposed a requirement that addresses auditor bias when designing and performing audit procedures to respond to an assessed risk of material misstatement due to fraud (see paragraph 43 in **Agenda Item 3–A**). This is consistent with the approach adopted in paragraph 18 of ED-570.
26. In approaching the changes to paragraphs 18 and 19 in **Agenda Item 3–A**, the Fraud TF is of the view that it is important to retain an emphasis on a neutral mindset and outline the responsibilities as it relates to the authentication of records or documents with respect to:
- Maintaining professional skepticism – the essential material was removed as it is contrary to the Complexity Understandability Scalability and Proportionality (CUSP) Drafting Principles and Guideline to retain such material as part of the requirements. Paragraph A24 in **Agenda Item 3–A** addresses the matter of the auditor's past experience with the *perceived* honesty and integrity of the entity's management and TCWG. The Fraud TF believes that this change obviates the necessity to repeat the essential material in the application material. Application material was added to highlight the importance of unconscious bias, and how bias may impede the exercise of professional skepticism.
 - Authentication of a record or document – the Fraud TF referenced paragraph A9–1 of ISA (UK) 240¹² and incorporated examples of circumstances that may indicate that a document is not authentic. The Fraud TF leveraged paragraph A56 of proposed ISA 500 (Revised), *Audit Evidence* to explain the attribute of authenticity.
27. The Fraud TF also recognizes the importance of the auditor remaining alert, especially when performing audit procedures related to fraud. The requirement to remain alert is included, among other ISAs, in paragraph 16 of ISA 250 (Revised),¹³ paragraph 15 of ISA 550,¹⁴ paragraph 15 of ISA 720 (Revised),¹⁵ and paragraph 13 of ED-570. The Fraud TF believes it is appropriate to include a similar requirement (see paragraph 20 in **Agenda Item 3–A**) and highlight in the application material those circumstances e.g., especially near the end of the audit, when it may be necessary for the auditor to have a heightened sense of awareness when performing audit procedures to address the risks of material misstatement due to fraud.
28. The second bullet of the proposed action focuses on the “ramp up” of procedures when fraud is identified or suspected in the application material – this element of the proposed action is addressed by paragraph 21 in **Agenda Item 3–A** requiring the auditor to perform the procedures in the *Fraud or Suspected Fraud* section of proposed ISA 240 (Revised).

C. Ongoing Communications Throughout the Audit with Management and TCWG About Fraud Related Matters *(Previously Discussed with the IAASB)*

Fraud Project Proposal – Key Issues and Proposed Actions

¹¹ Proposed action C.25 in paragraph 25 of the project proposal, bullet 1 “...enhancing requirements and application material in ISA 240 for the auditor to design and perform procedures that is not biased towards obtaining audit evidence that may be corroborative or towards excluding evidence that may be contradictory.”

¹² ISA (UK) 240 (Revised May 2021), *The Auditor's Responsibilities Relating to Fraud in an Audit of Financial Statements*

¹³ ISA 250 (Revised), *Consideration of Laws and Regulations in an Audit of Financial Statements*

¹⁴ ISA 550, *Related Parties*

¹⁵ ISA 720 (Revised), *The Auditor's Responsibilities Relating to Other Information*

29. The project proposal included proposed actions to address key issues related to communication with TCWG (see key issue in paragraph 19(h)(i) and proposed action D.27 in paragraph 25 of the project proposal for the revision of ISA 240).

Previous IAASB Discussions

30. The Board discussed this topic at the March and June 2022 IAASB meetings. The ongoing nature of communications with management and TCWG about fraud related matters is embodied in all stages of the audit as reflected in both requirements and application material throughout the standard. These communication requirements are not meant to be applied in a linear fashion but are intended to reflect the iterative nature of an audit.
31. The choice of verbs used in the requirements such as “communicate,” “discuss,” or “inquire” (and variations thereof) signal the work effort the auditor is intended to apply to comply with the requirement. Matters related to fraud are intended to be communicated with appropriate parties in the circumstances, which may be parties other than management and TCWG such as individuals within the internal audit function (if the function exists). This is intended to be a robust two-way and open dialogue with active participation by all parties. In certain circumstances, the auditor may be required to report to an appropriate authority. This may or may not involve two-way communication and is likely dependent on the nature of the communication required by the applicable law, regulation or relevant ethical requirements.
32. Proposed ISA 240 (Revised) includes:
- A new overarching requirement to **communicate** with management and TCWG matters related to fraud at appropriate times throughout the audit engagement (see paragraphs 25 and A40–A44 in **Agenda Item 3–A**).
 - A combination of new, enhanced or extant requirements to make **inquiries** of TCWG, management, appropriate individuals within the internal audit function (if the function exists) and other appropriate individuals within the entity about certain fraud related matters, when obtaining an understanding of the entity and its environment, the applicable financial reporting framework and the entity’s system of internal control (see paragraphs 31(c), 31(d) and A70–A73, 32(b) and A84–A86, 33(b) and A88–A89 in **Agenda Item 3–A**).
 - If the auditor determines that the financial statements are materially misstated due to fraud, a new requirement to **discuss** with the appropriate level of management that is at least one level above those involved, and TCWG, the matter and an approach to further investigate the matter. (see paragraph 62(b) in **Agenda Item 3–A**).
 - An extant requirement to **discuss** with the appropriate level of management and TCWG the auditor’s withdrawal from the engagement and the reasons for the withdrawal (see paragraph 65(c)(i) in **Agenda Item 3–A**).
 - Extant requirements to **communicate** with management and TCWG when fraud or suspected fraud is identified (see paragraphs 71–73 and A190–A195 in **Agenda Item 3–A**).
 - An extant requirement to **report** to appropriate authorities outside the entity, including regulatory and enforcement authorities, when fraud or suspected fraud is identified (see paragraphs 74 and A196–A200 in **Agenda Item 3–A**).
 - Requirements that provide clear signposting when fraud or suspected fraud has been identified

for the communications with management and TCWG in paragraph 54(b) in **Agenda Item 3–A** and the reporting to an appropriate authority outside the entity, including regulatory and enforcement authorities, in paragraph 54(c) in **Agenda Item 3–A**.

D. Applying a *Fraud Lens* on Risk Identification and Assessment (*Previously Discussed with the IAASB*)

Fraud Project Proposal – Key Issues and Proposed Actions

33. The project proposal included proposed actions to address key issues related to identifying and assessing the risks of material misstatement due to fraud (see key issue in paragraph 19(b)(i) and proposed action B.4 in paragraph 25 of the project proposal for the revision of ISA 240).

Previous IAASB Discussions

34. This topic was discussed more broadly by the Board at the March 2022 IAASB meeting and then specifically as it related to *Obtaining an Understanding of the Entity and Its Environment, the Applicable Financial Reporting Framework and the Entity’s System of Internal Control* at the June, September and December 2022 IAASB meetings.
35. In developing the proposed changes relating to risk identification and assessment, the Board was mindful of maintaining the balance between what ISA 315 (Revised 2019) and proposed ISA 240 (Revised) address, respectively. Given that ISA 315 (Revised 2019) focuses on the broad requirements relating to risk identification and assessment, it was agreed that proposed ISA 240 (Revised) would only need to explain how to undertake those procedures with a *fraud lens*.
36. Accordingly, the Fraud TF:
- Made substantive changes in proposed ISA 240 (Revised) and only with the *fraud lens*, when referring to, or expanding on, the application of the requirements in ISA 315 (Revised 2019). In making such changes, the Board provided direction for the Fraud TF not to duplicate nor repeat requirements from ISA 315 (Revised 2019) especially when enhancing or developing related application and other explanatory material in proposed ISA 240 (Revised).
 - Restructured proposed ISA 240 (Revised) to follow a similar structure as ISA 315 (Revised 2019), which helps demonstrate the integrated relationship between the two standards. This action synchronizes any changes made in proposed ISA 240 (Revised), and thereby, helps auditors better connect the considerations on fraud with the foundational requirements in ISA 315 (Revised 2019).
37. The Board supported the restructuring of the relevant sections in proposed ISA 240 (Revised) and agreed that the appropriate *fraud lens* was applied when referring to, or expanding on, what is already required in ISA 315 (Revised 2019) with minimal duplication noted. The Board also supported maintaining Appendix 1 on fraud risk factors in proposed ISA 240 (Revised).
38. The Fraud TF focused on emphasizing the importance of the auditor’s understanding of the entity and its environment, the applicable financial reporting framework and the entity’s system of internal control and leveraging such understanding when identifying and assessing risks of material misstatement due to fraud. The Fraud TF believes that the nature of the understanding underpins the fraud related work performed by the auditor.
39. After the December 2022 meeting, the Fraud TF further enhanced the section that builds on ISA 315

(Revised 2019) based on comments received from the Board and based discussions within the Task Force. The most notable change is that the Fraud TF added a new requirement that applies a *fraud lens* on the information system and communication component of the system of internal control. The Fraud TF is of the view that obtaining an understanding of how journal entries are initiated, processed and corrected and how the information system ensures the completeness of journal entries is important given the heightened risk of fraud related to journal entries and the focus of this standard on journal entries.

40. Applying a *fraud lens* in risk identification and assessment is a continual and iterative process. Proposed changes to make fraud risk identification and assessment more robust in proposed ISA 240 (Revised) are intended to focus on incentives/pressures, opportunities, and attitudes/rationalizations for fraud (i.e., fraud risk factors), including those arising from the entity's tone at the top and performance measures.

E. Robust Work Effort Requirements When Fraud or Suspected Fraud Is Identified (*Previously Discussed with the IAASB*)

Fraud Project Proposal – Key Issues and Proposed Actions

41. The project proposal included proposed actions to address key issues related to when fraud is identified or suspected (see key issue in paragraph 19(f)(v) and proposed action B.17 in paragraph 25 of the project proposal for the revision of ISA 240).

Previous IAASB Discussions

42. In December 2022, the IAASB discussed the overall approach when fraud or suspected fraud is identified. The Fraud TF also developed a flowchart and related scenarios intended to assist the Board in understanding the proposed approach and direction taken by the Fraud TF when fraud or suspected fraud is identified. The Board supported the direction taken by the Fraud TF, including that the requirements and application material reside in a separate section of proposed ISA 240 (Revised) (see the approved minutes of the December 2022 IAASB meeting).
43. The Board observed that fraud or suspected fraud may be identified by parties other than the auditor. The Fraud TF concurs with the observation, and consequently throughout proposed ISA 240 (Revised) the wording, where appropriate, is neutral in terms of who specifically identified the fraud or suspected fraud. Irrespective, once the fraud or suspected fraud has been identified, the auditor is required to respond appropriately in accordance with paragraphs 54-63 in **Agenda Item 3–A**. This responsibility is clearly established at the outset of the proposed standard in paragraph 21 in **Agenda Item 3–A**.

Fraud TF's Deliberations and Proposals

44. In developing the proposals, the Fraud TF believes that once fraud or suspected fraud is identified the engagement partner has a responsibility to obtain a thorough understanding of the nature, timing and extent of the fraud related matter i.e., a "pencils-down approach" before determining how to respond (see paragraph 54 in **Agenda Item 3–A**).
45. The application material outlines the appropriate actions the engagement partner may take when obtaining the understanding of the fraud or suspected fraud. The actions taken are intended to be scalable to address the facts and circumstances. For example:

- The auditor may, depending on a preliminary understanding, determine to continue with other aspects of the audit engagement if the fraud or suspected fraud is believed to be inconsequential or otherwise limited in nature. Alternatively, if it is anticipated that the fraud or suspected fraud is pervasive and the integrity of management is in question, then the auditor may determine that no further audit work may be performed until the matter is satisfactorily resolved.
- The actions taken to obtain an understanding related to an immaterial misappropriation of assets, may be less extensive, than the courses of action taken when a component auditor communicates that there is suspected fraud at a component to the group auditor.

The Fraud TF believes that once the in-depth understanding is obtained that this information will inform whether the auditor is required to perform additional risk assessment procedures or revise the identification and assessment of the risks of material misstatement due to fraud in accordance with ISA 315 (Revised 2019). The Fraud TF is of the view that there are certain required additional audit procedures that will need to be performed, irrespective of whether (or not) there are changes resulting from revisions to the risk assessment, such as determining if control deficiencies related to the prevention or detection of fraud exist.

46. Using the flowchart presented to the Board in December 2022, the Fraud TF further developed its drafting proposals with respect to:
- The required responses if the auditor identifies a misstatement due to fraud (see paragraph 60 in **Agenda Item 3–A**).
 - How to determine whether identified misstatements due to fraud are material when considering the nature of the circumstances (qualitative or quantitative) giving rise to the misstatements (see paragraph 61 in **Agenda Item 3–A**).
 - The required responses if the auditor determines that the financial statements are materially misstated (see paragraph 62 in **Agenda Item 3–A**).
 - Circumstances where the auditor is unable to obtain sufficient appropriate audit evidence as it relates to a material misstatement due to fraud (see paragraph 63 in **Agenda Item 3–A**).

F. Transparency on Fraud Related KAMs in the Auditor's Report (*Previously Discussed with the IAASB*)

Fraud Project Proposal – Key Issues and Proposed Actions

47. The project proposal included proposed actions to address key issues related to transparency in the auditor's report on fraud (see key issue in paragraph 19(h)(ii) and proposed action B.27 in paragraph 25 of the project proposal for the revision of ISA 240).

Previous IAASB Discussions

48. In its December 2022 meeting, the Board agreed with the Fraud TF's proposal to:
- Use a filter for communicating about risks of material misstatement relating to fraud that is similar to the filter used to communicate KAMs.
 - Include the communication of fraud related KAMs in the Key Audit Matters section of the auditor's report.

49. The Board was of the view that proposed ISA 240 (Revised) should not include a requirement to communicate in the auditor's report identified significant deficiencies in internal control that are relevant to the prevention and detection of fraud.
50. In its December 2022 meeting, the Board also provided direction on the following matters:
- Explore whether the same filtering mechanism could be used to communicate KAMs and fraud related KAMs.
 - Draft the requirements in proposed ISA 240 (Revised) in such a manner that they drive the auditor to include entity-specific information and avoid the use of boilerplate language.
 - Clarify how the auditor should communicate a matter that is determined to be both a KAM (as determined by ISA 701) and a fraud related KAM (as determined by proposed ISA 240 (Revised)).

Fraud TF's Deliberations and Proposals on Way Forward

51. During the February and May 2023 Fraud TF meetings, the Fraud TF discussed how to address the matters raised by the Board in December 2022. In general, the Fraud TF was of the view that proposed ISA 240 (Revised) should leverage ISA 701. Therefore, the Fraud TF used ISA 701 as a foundational standard to develop the requirements and application material as it relates to transparency in the auditor's report.
52. Given the interest of users of the financial statements in fraud related matters, the Fraud TF's goal was to develop requirements and application material that drive the auditor to communicate in the auditor's report fraud related KAMs. It is anticipated that this will be achieved by:
- Enhancing the auditor's work effort when performing audit procedures to address fraud in an audit of financial statements which will in turn result in an increased number of fraud related matters that are communicated with those charged with governance, and
 - Expanding on ISA 701 to strengthen the requirements for the auditor to report fraud related KAMs.

Clarifying the Link to ISA 701

53. To clarify the link with ISA 701, the Fraud TF used the phrase "In applying ISA 701" and only included requirements for matters that the auditor should *take into account* in addition to the requirements included in ISA 701. With respect to application material, the Fraud TF reviewed ISA 701 and included relevant paragraphs in proposed ISA 240 (Revised) and applied a *fraud lens* to these paragraphs.
54. With respect to the filtering mechanism, the Fraud TF proposes to have the same filtering mechanism for communicating fraud related KAMs as for communicating KAMs (see paragraphs 66 and 67 in **Agenda Item 3–A**). The Fraud TF identified three areas in applying the *fraud lens* to ISA 701 that the auditor is required to *take into account* in determining which matters required significant auditor attention:
- Significant risks of material misstatement due to fraud;
 - The identification of fraud or suspected fraud; and
 - The identification of deficiencies in internal control that are relevant to the prevention and detection of fraud.

55. These matters are not deemed to be a checklist as the Fraud TF recognizes that there may be other fraud related matters that require significant auditor attention and may be of relevance in making the auditor's determination. This circumstance is also highlighted in the application material (see paragraph A177 in **Agenda Item 3–A**).
56. The Fraud TF focused on steering the auditor to include entity-specific information and avoid the use of boilerplate language by:
- Encouraging the use of entity-specific information. This was accomplished by including application material that highlights the importance of relating KAMs directly to the specific circumstances of the entity as that may help to minimize the potential that such descriptions become overly standardized and less useful over time (e.g., see paragraph A182 in **Agenda Item 3–A**).
 - Aligning the requirements with ISA 701. The [Auditor Reporting Post Implementation Review](#) showed that KAMs are valued and, generally, include entity-specific information and avoid the use of boilerplate language. By leveraging the requirements in ISA 701, the Fraud TF is of the view that the same will hold true for fraud related KAMs.

Encouraging Auditor's to Communicate Fraud Related KAMs

57. As noted above, given the interest of users of the financial statements in fraud related matters, and the objective of the project to “enhance transparency on fraud related procedures where appropriate, including strengthening reporting requirements in ISA 240 and other relevant ISAs,” the goal of the Fraud TF was to develop requirements and application material that drive the auditor to communicate fraud related KAMs. In doing so, the intention is to encourage communication, based on the audit procedures performed, of at least one fraud related KAM. These fraud related KAMs would be communicated in extension of the KAMs communicated under ISA 701.
58. To achieve the Fraud TF's goal, the Fraud TF added application material that provides a very strong steer to communicate fraud related KAMs in the auditor's report. For example:
- Paragraph A174 in **Agenda Item 3–A** states that “fraud related matters often are matters that require significant auditor attention.” The CUSP Drafting Principles and Guidelines, Appendix 1, provides an overview of the terms used in the ISAs to describe the likelihood of occurrence. ‘Often’ is labeled as the term with the second highest likelihood of occurrence, after ordinarily.
 - Paragraph A179 in **Agenda Item 3–A** states that fraud related matters that required significant auditor attention “ordinarily are matters of most significance in the audit of the financial statements of the current period and therefore are key audit matters.” The CUSP Drafting Principles and Guidelines, Appendix 1, labels ‘ordinarily’ as the term with the highest likelihood of occurrence.
59. In addition, the Fraud TF proposes, as a conforming and consequential amendment, to enhance paragraph A21 from ISA 701. This paragraph states, depending on their nature, the presumed fraud risk of revenue recognition and management override of controls may not require significant auditor attention, and therefore would not be considered in the auditor's determination of KAMs. The Fraud TF is of the view that this application material may have driven auditors not to communicate fraud related KAMs (see **Agenda Item 3–C**). Instead, the Fraud TF aligned the wording with paragraph A177 in **Agenda Item 3–A**.

Significant Deficiencies

60. In response to the Board's decision not to include a requirement in proposed ISA 240 (Revised) to communicate in the auditor's report identified significant deficiencies in internal control that are relevant to the prevention and detection of fraud, the Fraud TF removed the related requirement in proposed ISA 240 (Revised).
61. Given the addition of the identification of deficiencies in internal control that are relevant to the prevention and detection of fraud in the auditor's determination of which matters required significant auditor attention (see paragraph 66 in **Agenda Item 3–A**), the Fraud TF is of the view that deficiencies in internal control that are relevant to the prevention and detection of fraud will be more often communicated in the auditor's report than currently is the case.

*Conforming and Consequential Amendments Arising from Proposed ISA 240 (Revised)*¹⁶ (see **Agenda Item 3–C**)

62. The Fraud TF believes that in order for the Board to provide the feedback necessary to advance the proposals to address transparency in the auditor's report, the conforming and consequential amendments should be presented such that the Board has an overview of all the fraud related changes that would impact the auditor's report. Consequently, an initial draft of the conforming and consequential amendments impacting ISA 700 (Revised) and ISA 701 has been prepared. See **Agenda Item 3–B** for an explanation of the significant changes made to ISA 700 (Revised) and ISA 701.

Examples of Key Audit Matters Including Fraud Risks (see **Agenda Item 3–D (Supplemental)**)

63. At the December 2022 meeting, the Board directed the Fraud TF to clarify how the auditor should communicate a matter that is determined to be both a KAM (as determined by ISA 701) and a fraud related KAM (as determined by proposed ISA 240 (Revised)). It was noted that the illustrations provided for the December 2022 meeting did not clearly result in the different KAMs being disclosed. In addition to enhancing the requirements and application material in proposed ISA 240 (Revised) Staff developed three examples leveraging facts and circumstances outlined in publicly available auditor's reports (see **Agenda Item 3–D (Supplemental)**).

G. Audit Documentation (*New Topic to be Discussed with the IAASB*)

Fraud Project Proposal – Key Issues and Proposed Actions

64. The project proposal included proposed actions to address key issues related to audit documentation (see key issue in paragraph 19(f)(ix) and proposed action B.21 in paragraph 25 of the project proposal for the revision of ISA 240).

Fraud TF's Initial Views and Recommendations

65. The Fraud TF discussed enhancing the audit documentation requirements, which included requiring specific aspects of the auditor's work related to fraud to be included in the audit documentation. In developing the proposals, the Fraud TF built on the foundational standard ISA 230,¹⁷ as well as

¹⁶ For ISA 700 (Revised) and ISA 701 only.

¹⁷ ISA 230, *Audit Documentation*

expanded on the requirements in ISA 315 (Revised 2019) and ISA 330.¹⁸

66. In approaching the *Documentation* section in proposed ISA 240 (Revised), the Fraud TF referenced the layout of recently issued ISAs, specifically ISA 315 (Revised 2019) and ISA 600 (Revised) and the section was reformatted accordingly.
67. In addition, the Fraud TF reviewed the requirements in proposed ISA 240 (Revised) and included a documentation requirement where appropriate after giving due consideration to the fact that the audit work being documented relates to procedures to address the susceptibility of the financial statements to material misstatement due to fraud e.g., a documentation requirement was added with respect to the work performed relating to fraud or suspected fraud identified by the auditor (see paragraph 75 in **Agenda Item 3–A**).

Section II – Explanation of Significant Changes to Proposed ISA 240 (Revised)

68. **Agenda Item 3–A** includes a first full draft of proposed ISA 240 (Revised). **Agenda Item 3–B** provides an explanation of the significant changes considered and proposed by the Fraud TF and may be helpful when understanding the thinking of the Fraud TF when developing the proposals outlined in **Agenda Item 3–A** and **Agenda Item 3–C**.
69. In developing the changes, the Fraud TF considered:
- Comments provided in December 2022, by the Board during the plenary session, and any comments of a non-substantive nature provided to IAASB Staff directly (i.e., 'off-line comments').
 - Comments provided by IAASB CAG Representatives.
 - Relevant proposals in ED-570 in order to adopt a consistent approach in addressing certain proposed actions that impact both the fraud and going concern projects.
 - Input from the IESBA Staff and Liaison Board Member regarding the linkage between proposed ISA 240 (Revised) and the IESBA Code.
 - Input from the ARCG regarding the usage of fraud related KAMs and the proposed changes to the auditor's responsibilities in the auditor's report related to fraud.
 - Input from the TCG regarding the incorporation of technology-related application material.

Section III – Matters for the IAASB Consideration

70. The following are the two matters the Fraud TF would like the Board to consider when providing input on the materials presented.

The Board is requested to provide its views:

1. Regarding the Fraud TF's proposed changes as outlined in **Agenda Item 3–A** and **Agenda Item 3–C**.
2. As to whether there are any other matters the Fraud TF should consider in order to promote consistent practice and change auditor behavior when performing work related to fraud in an audit

¹⁸ ISA 330, *The Auditor's Responses to Assessed Risks*

of financial statement.

Section IV – Way Forward

71. Following the June 2023 IAASB meeting, and based on the Board's feedback, the Fraud TF intends to continue to discuss the issues as well as to align and refine the drafting for the proposed standard. An updated draft of proposed ISA 240 (Revised), together with all the proposed conforming and consequential amendments to other relevant ISAs, will be presented to the Board for further deliberation at the September 2023 meeting.
72. The IAASB Staff and the Fraud TF remain committed to continue the dialogue and collaboration with the IESBA Staff and Liaison Board Member as it relates to relevant ethical requirements and the linkage to the IESBA Code with respect to fraud related matters. In addition, the Fraud TF will continue to liaise with other IAASB task forces, working groups and consultation groups as needed, as well as other stakeholders in the financial reporting ecosystem as deemed necessary.
73. In December 2023, the Fraud TF intends to present to the Board an exposure draft of proposed ISA 240 (Revised) for approval.

Appendix 1

Fraud TF Members and Update on Activities Since the December 2022 IAASB Meeting

Fraud TF Members

1. The Fraud TF consists of the following members:
 - Julie Corden, Chair
 - William Edge
 - Josephine Jackson
 - Sachiko Kai
 - Diane Larsen
2. Information about the project can be found [here](#).

Fraud TF Activities

3. Since December 2022, the Fraud TF held 1 virtual meeting and 4 physical meetings over seven days.

Appendix 2

Mapping of Key Changes in Proposed ISA 240 (Revised) to Relevant Paragraphs in Agenda Item 3–A

The requirements and application material that underpin the seven key proposed changes in ISA 240 outlined in **Section I** are, in many instances, dispersed throughout the proposed standard. The tables below are intended to provide an overview of the paragraphs that address each of the key proposed changes that are aimed at promoting consistent practice and changing auditor behavior.

A. Clarity and Emphasis on the Auditor’s Responsibilities (Previously Discussed with the IAASB)

Relevant Paragraphs in Agenda Item 3–A		
Subheading	Requirement	Application Material
Responsibilities of the Auditor, Management and Those Charged with Governance		
<i>Responsibilities of the Auditor</i>	Para. 2	Para. A1
<i>Responsibilities of Management and Those Charged with Governance</i>	Para. 3	–
<i>Characteristics of Fraud</i>	Paras. 4–8	Paras. A2–A11
<ul style="list-style-type: none"> Fraud or Suspected Fraud 	Paras. 6–7	Para. A7–A10
<ul style="list-style-type: none"> Nature of the Circumstances Giving Rise to the Fraud and the Identified Misstatements 	Para. 8	Para. A11
<i>Inherent Limitations</i>	Paras. 9–11	Para. A12
<i>Professional Skepticism and Professional Judgment</i>	Para. 12	Paras. A13–A14
<i>Non-Compliance with Laws and Regulations</i>	Para. 13	Para. A15

B. Professional Skepticism (New Topic to be Discussed with the IAASB)

Relevant Paragraphs in Agenda Item 3–A		
Subheading	Requirement	Application Material
<i>Professional Skepticism and Professional Judgment</i> (Note: Within the Introduction, under Key Concepts in this ISA)	Para. 12	Paras. A13–A14

Relevant Paragraphs in Agenda Item 3–A		
Subheading	Requirement	Application Material
Professional Skepticism (Note: Within the Requirements)	Para. 18	Paras. A23–A26
	Para. 19	Paras. A27–A28
	Para. 20	Paras. A29–A30B
	Para. 21	–
(Note: Elsewhere within application material of the standard)	–	Paras. A9, A86, A116 and A139

C. Ongoing Communications Throughout the Audit with Management and TCWG About Fraud Related Matters *(Previously Discussed with the IAASB)*

Relevant Paragraphs in Agenda Item 3–A		
Subheading	Requirement	Application Material
Ongoing Nature of Communications with Management and Those Charged with Governance	Para. 25	Paras. A40–A44
<i>Understanding the Components of the Entity's System of Internal Control</i>		
Control Environment		
• [Effectiveness of oversight by TCWG]	–	Paras. A68
• [Inquiries of management]	Para. 31(c)	–
• [Inquiries of TCWG]	Para. 31(d)	Paras. A70–A73
The Entity's Risk Assessment Process		
• [Inquiries of management and of other appropriate individuals within the entity]	Para. 32(b)	Paras. A84–A86
The Entity's Process to Monitor the System of Internal Control		
• [Inquiries of appropriate individuals within the internal audit function (if the function exists)]	Para. 33(b)	Paras. A88–A89

Relevant Paragraphs in Agenda Item 3–A		
Subheading	Requirement	Application Material
Fraud or Suspected Fraud	Paras. 54(b)–54(c)	Para. A154
	Para. 62(b)	–
Auditor Unable to Continue the Engagement	Para. 65(c)(i)	–
Communications with Management and Those Charged with Governance	Paras. 71–73	Paras. A190–A195
Reporting to an Appropriate Authority Outside the Entity	Para. 74	Paras. A196–A200

D. Applying a *Fraud Lens* on Risk Identification and Assessment (*Previously Discussed with the IAASB*)

Relevant Paragraphs in Agenda Item 3–A		
Subheading	Requirement	Application Material
Risk Assessment Procedures and Related Activities	Para. 26	Paras. A45–A46
<i>Information from Other Sources</i>	Para. 27	Paras. A47–A48
<i>Retrospective Review of the Outcome of Previous Significant Accounting Estimates</i>	Para. 28	–
<i>Engagement Team Discussion</i>	Para. 29	Paras. A49–A52
<i>Understanding the Entity and Its Environment, and the Applicable Financial Reporting Framework</i>	Para. 30	Paras. A54–A62
<i>Understanding the Components of the Entity’s System of Internal Control</i>		
• Control Environment	Para. 31	Paras. A63–A73
• The Entity’s Risk Assessment Process	Para. 32	Paras. A74–A86
• The Entity’s Process to Monitor the System of Internal Control	Para. 33	Paras. A87–A89
• The Information System and Communication	Para. 34	Paras. A90–A92

• Control Activities	Para. 35	Paras. A93–A94
<i>Control Deficiencies Within the Entity’s System of Internal Control</i>	Para. 26	Para. A95
Identifying and Assessing the Risks of Material Misstatement due to Fraud		
<i>Evaluation of Fraud Risk Factors</i>	Para. 37	Paras. A96–A99
<i>Evaluating the Audit Evidence Obtained from the Risk Assessment Procedures</i>		
• Inquiries of Management and Inconsistent Responses	Para. 38	–
• Analytical Procedures Performed and Unusual or Unexpected Relationships Identified	Para. 39	Para. A100
<i>Identifying and Assessing the Risks of Material Misstatement Due to Fraud</i>	Para. 40	Paras. A101–A105
Presumption of the Risks of Material Misstatement Due to Fraud in Revenue Recognition	Para. 41	Paras. A106–A111
Significant Risk Related to Management Override of Controls	Para. 42	Paras. A112

E. Robust Work Effort Requirements When Fraud or Suspected Fraud Is Identified (*Previously Discussed with the IAASB*)

Relevant Paragraphs in Agenda Item 3–A		
Subheading	Requirement	Application Material
Fraud or Suspected Fraud (Note: Within the Introduction, under Key Concepts in this ISA)	Paras. 6–7	Para. A7–A10
Fraud or Suspected Fraud (Note: Within the Requirements)	Para. 54	Paras. A148–A155
	Para. 57	Para. A156
	Para. 59	Paras. A157–A157A
	Para. 60	Paras. A158–A159

Relevant Paragraphs in Agenda Item 3–A		
Subheading	Requirement	Application Material
	Para. 61	Paras. A160–A161
	Para. 62	–
	Para. 63	–

F. Transparency on Fraud Related KAMs in the Auditor’s Report (*Previously Discussed with the IAASB*)

Relevant Paragraphs in Agenda Item 3–A		
Subheading	Requirement	Application Material
<i>Determining Key Audit Matters</i>	Para. 66	Paras. A171–A177
	Para. 67	Paras. A178–A179
<i>Communicating Fraud Related Key Audit Matters</i>	Para. 68	Paras. A181–A183
	Para. 69	Paras. A184–A187A

G. Audit Documentation (*New Topic to be Discussed with the IAASB*)

Relevant Paragraphs in Agenda Item 3–A		
Subheading	Requirement	Application Material
Documentation	Para. 75	Para. A201
(Note: Elsewhere within application material of the standard)	–	Para. A111