

Fraud in an Audit of Financial Statements

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IAASB CAG Meeting
September 13, 2023
Agenda Item H.1

Approach to Revising ISA 240

Proposed ISA 240 (Revised)



Considering the qualitative standard-setting characteristics within the **Public Interest Framework**



Addressing the proposed actions in the **Fraud Project Proposal**



Expanding, through applying the *fraud lens*, on the requirements of certain **Foundational Standards**, including ISA 200, ISA 220 (Revised), ISA 315 (Revised 2019), and ISA 330; as well as leveraging the **Reporting Mechanism** in ISA 701



Following the conventions in the **CUSP Drafting Principles and Guidelines**

Promoting Consistent Practice and Changing Auditor Behavior

PROFESSIONAL SKEPTICISM

Clarity and emphasis
on the auditor's
responsibilities

Applying a *fraud lens*
on risk identification
and assessment

Transparency on Key
Audit Matters (KAMs)
related to fraud in the
auditor's report



Ongoing communications
throughout the audit with
management and TCWG
about fraud-related
matters

Robust work effort
requirements if fraud
or suspected fraud is
identified

AUDIT DOCUMENTATION

Professional Skepticism



Highlighting the interrelationship between professional skepticism and professional judgment



Maintaining professional skepticism throughout the audit



Further investigating the authenticity of a record or document when conditions are identified that indicate they may not be



Remaining alert throughout the audit for information about fraud or suspected, including allegations of fraud



Designing and performing audit procedures in a manner that is not biased towards obtaining corroborative or contradictory audit evidence

Clarity and Emphasis on the Auditor's Responsibilities



Responsibilities

- Auditor
- Management and TCWG



Key Concepts

- Fraud or suspected fraud
- Circumstances giving rise to fraud and the identified misstatements
- Inherent limitations



Relationship with Other ISAs, including ISA 250 (Revised), *Consideration of Laws and Regulations in an Audit of Financial Statements*

Ongoing Communications with Management and TCWG



Overarching requirement to communicate with management and TCWG matters related to fraud at appropriate times throughout the audit engagement

New



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

Enhanced



If the auditor identifies fraud or suspected fraud, a requirement to make inquiries about the matter and the process to investigate the matter with an appropriate level of management that is at least one level above those involved, and TCWG

New



Requirement to discuss with the appropriate level of management and TCWG the auditor's withdrawal from the engagement and the reasons for the withdrawal

Extant



Requirements to communicate with management and TCWG, if fraud or suspected fraud is identified

Extant



Requirement to report to appropriate authorities outside the entity, including regulatory and enforcement authorities, if fraud or suspected fraud is identified

Extant



Clear signposting for required communications with management and TCWG and reporting to an appropriate authority outside the entity, including regulatory and enforcement authorities, if fraud or suspected fraud is identified

New

Applying a *Fraud Lens* on Risk Identification and Assessment



Applying the appropriate *fraud lens* when referring to, or expanding on, what is already required in ISA 315 (Revised 2019)



Obtain an Understanding of the Entity and Its Environment, the Applicable Financial Reporting Framework, and the Entity's System of Internal Control



Fraud Risk Factors
Incentives, Pressures, or Opportunities to Commit Fraud
Risks of Material Misstatement (RoMMs) Due to Fraud

Robust Work Effort if Fraud or Suspected Fraud Is Identified

*When fraud or suspected fraud is identified, the **engagement partner***

- Obtains an understanding of the fraud or suspected fraud in order to determine the effect on the audit engagement
- Communicates with management and TCWG, as required
- Reports to an appropriate authority outside the entity, as required

*Linkages to ISA 315
(Revised 2019) and ISA 330*

Based on the understanding obtained, the auditor determines whether to:

- Perform additional risk identification and assessment procedures; or
- Design and perform further audit procedures to respond to RoMMs due to fraud.

Additional audit procedures to address the identified fraud or suspected fraud

- Make inquiries about the matter and entity's process to investigate the matter
- Evaluate the entity's process to investigate the matter
- Determine if control deficiencies exist relating to the identified fraud or suspected fraud
- Determine additional responsibilities under law, regulation or relevant ethical requirement
- If applicable, consider impact on other engagements

Robust Work Effort if Fraud or Suspected Fraud Is Identified



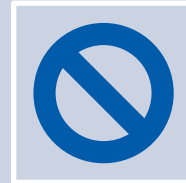
Required responses if the auditor identifies a misstatement due to fraud



Determining whether identified misstatements due to fraud are material when considering the nature of the circumstances (qualitative or quantitative) giving rise to the misstatements



Required responses if the auditor determines that the financial statements are materially misstated



Addressing circumstances where the auditor is unable to obtain sufficient appropriate audit evidence as it relates to a material misstatement due to fraud

Transparency on Key Audit Matters Related to Fraud in the Auditor's Report

Determining KAMs

- ***In applying ISA 701***, the auditor determines, from the matters related to fraud communicated with TCWG, those matters that required **significant auditor attention***
 - In making the determination, the auditor takes the following into account:
 - Significant risk of material misstatements due to fraud.
 - The identification of fraud or suspected fraud.
 - The identification of deficiencies in internal control that are relevant to the prevention and detection of fraud.
- ***In applying ISA 701***, the auditor determines which of the matters related to fraud were of **most significance in the audit** of the financial statements of the current period and therefore are KAMs

Principle Used

Refer to, or expand on, ISA 701, *Communicating Key Audit Matters in the Independent Auditor's Report*

Communicating KAMs Related to Fraud

- ***In applying ISA 701***, in the KAMs section of the auditor's report, the auditor uses an appropriate subheading that clearly describes that the matter relates to fraud
- ***In applying ISA 701***, if the auditor determines that there are no KAMs related to fraud to communicate, the auditor includes a statement to this effect in the KAMs section of the auditor's report

* It is expected that matters related to fraud communicated with TCWG will require significant auditor attention

Audit Documentation

Key elements of the auditor's understanding,* the sources of information from which the auditor's understanding was obtained, and the risk assessment procedures performed.

New

The matters discussed discussion among the engagement team regarding the susceptibility of the entity's financial statements to material misstatement due to fraud.

Enhanced

The identified and assessed risks of material misstatement at the financial statement level and at the assertion level, and the rationale for the significant judgments made

Enhanced

Fraud or suspected fraud identified, the results of audit procedures performed, the significant professional judgments made, and the conclusions reached

New

The results of the audit procedures performed to address the risk of management override of controls, the significant professional judgments made, and the conclusions reached.

Enhanced

Matters related to communications about fraud with management, TCWG, regulatory and enforcement authorities, and others, including how management, including how management, and where applicable, TCWG have responded to the matters

Enhanced

If the auditor has concluded that the presumption that a RoMM due to fraud related to revenue recognition is not applicable in the circumstances of the engagement, the reasons for that conclusion

Extant

* Understanding of the entity and its environment, the applicable financial reporting framework, and the entity's system of internal control

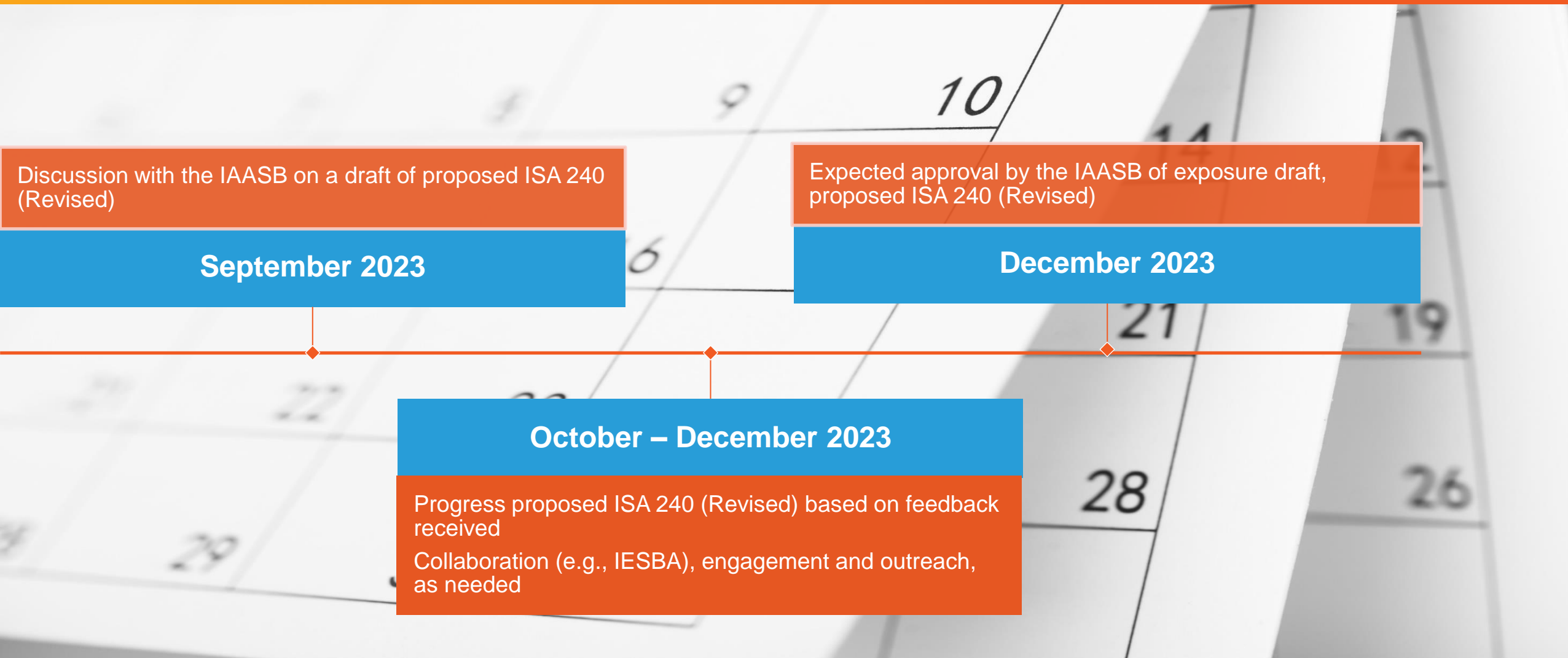
Matters for IAASB CAG Consideration

1. Representatives are asked for their views on the proposed changes presented in **Agenda Item H.2** relating to
 - (a) Clarity and emphasis on the auditor's responsibilities
 - (b) Applying fraud lens on risk identification and assessment
 - (c) Robust work effort requirements if fraud or suspected fraud is identified
 - (d) Transparency on KAMs related to fraud in the auditor's report

Matters for IAASB CAG Consideration

2. Representatives are asked whether there are any other matters in **Agenda Item H.2** that the Fraud TF should consider as it finalizes the enhancements to proposed ISA 240 (Revised) in December 2023

Way Forward





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