

Sustainability Assurance – Fraud

This Agenda Item includes the analysis of comments received on Question 19 in the Explanatory Memorandum to ED-5000,¹ and the related Staff views and recommendations.

Background

1. Stakeholders encouraged the IAASB to give appropriate consideration to the topic of fraud (including “greenwashing”) in ED-5000. It was noted that the reporting of sustainability information, and the system of internal control related to sustainability matters and preparation of the sustainability information, are continuing to develop and in many cases are less mature than for historical financial information. This may increase the susceptibility of the sustainability information to misstatements due to fraud, particularly when there are pressures for management to meet publicly announced targets or goals.
2. The IAASB recognized the importance of the practitioner’s consideration of the risks of material misstatement due to fraud and responding appropriately to actual or suspected fraud identified during the engagement. Therefore, ED-5000 has numerous references to fraud throughout the requirements and application material. The IAASB also discussed the importance of continued coordination with IESBA on the topics of fraud and non-compliance with laws and regulations.

What We Asked

3. Question 19 asked respondents:

Do you agree that ED-5000 appropriately addresses the topic of fraud (including “greenwashing”) by focusing on the susceptibility of the sustainability information to material misstatement, whether due to fraud or error? If not, what suggestions do you have for increasing the focus on fraud and why?

125 of 143 respondents provided a response to question 19, including all four Monitoring Group (MG) members.

See **Agenda Item 2-H.5** for further details on the overall responses and **Agenda Item 2-I.5** for comments received.

What We Heard

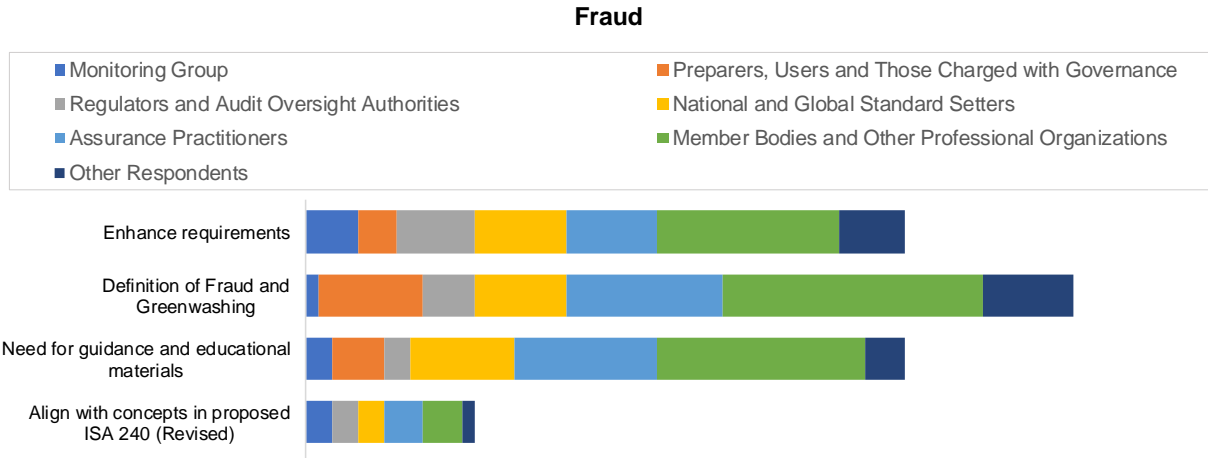
Highlights

- Support for ED-5000 appropriately addressing the topic of fraud (including “greenwashing”).
- Calls for enhancing the definition of, or requirements relating to, fraud.
- Various comments regarding “greenwashing.”

¹ Proposed International Standard on Sustainability Assurance (ISSA) 5000, *General Requirements for Sustainability Assurance Engagements, and Proposed Conforming and Consequential Amendments to Other IAASB Standards*.

- Calls for alignment with the concepts in proposed ISA 240 (Revised).²

4. The chart below shows a breakdown of the respondents' comments to question 19 by theme and stakeholder group.



Monitoring Group Comments

5. Two of the MG members were of the view that ED-5000 appropriately addresses the topic of fraud (including “greenwashing”), and all four MG members had comments or suggestions, including:
- A “stand back” requirement for the assurance practitioner to consider evidence obtained on a holistic basis for fraud or management bias;
 - Clarification of “greenwashing” in the final standard;
 - The need for more specific guidance and examples on the topic of fraud in the context of sustainability reporting;
 - Aligning with proposed ISA 240 (Revised); and
 - Addressing fraud in a single section of the standard

Other Respondents' Comments

6. Respondents generally agreed that ED-5000 appropriately addresses the topic of fraud (including “greenwashing”) and had comments or suggestions that fell into the key themes summarized below.

Enhance Requirements

7. Respondents encouraged the IAASB to include more specific requirements related to fraud in proposed ISSA 5000. Principal suggestions included additional requirements relating to:
- Management override of controls. Some of these respondents noted the need for a presumed fraud risk for the risk of management override of controls, and related requirements, similar to ISA 240 (Revised).

² Proposed International Standard on Auditing 240 (Revised), *The Auditor's Responsibilities Relating to Fraud in an Audit of Financial Statements*

- (b) A “stand back” requirement for the assurance practitioner to consider evidence obtained on a holistic basis.
- (c) Non-compliance with laws and regulations.

Definition of Fraud and the Term “Greenwashing”

- 8. Even though fraud is defined in ED-5000, several respondents noted that ED-5000 could be enhanced by defining fraud and describing its characteristics in the context of sustainability reporting to facilitate consistent understanding.
- 9. Respondents had various comments regarding “greenwashing” including:
 - (a) Use of the term in the proposed standard

Respondents that commented on this point generally supported the fact that the term “greenwashing” is not used in ED-5000, noting that “greenwashing” may have different definitions in various jurisdictions and the concept may evolve.
 - (b) Clarification or definition of “greenwashing” needed

A few respondents noted that “greenwashing” should be clearly defined or there should be clarity in the use of the term. Moreover, some respondents commented that greenwashing can be both intentional and unintentional and was only fraudulent in nature when it was intentional.
 - (c) Additional requirements

Several respondents suggested additional requirements to address the risk of greenwashing. For example, one MG member and two other respondents suggested a “stand back” in relation to “greenwashing.”
 - (d) Additional guidance

Some respondents suggested additional guidance, including intentional and non-intentional aspects, as this will be difficult to distinguish in practice and practitioners will need practical guidance.

Need for Guidance and Educational Materials

- 10. Respondents had various comments on the need for more specific guidance and examples on the topic of fraud in the context of sustainability reporting, either through additional application material in proposed ISSA 5000 or other guidance. Specific areas noted by respondents included management override of controls, estimates and forward-looking information, and management bias. A few other respondents suggested developing educational materials for users.

Align with Concepts in Proposed ISA 240 (Revised)

- 11. Some respondents suggested that the IAASB consider aligning ED-5000 with the current project to revise ISA 240 (Revised). A specific area to consider noted by some respondents related to the authenticity of records and documents.

Other Matters

12. Other matters related to fraud noted by respondents included the following:

- (a) Construct of fraud-related provisions: A few respondents recommended including an additional single section in the proposed standard or an appendix that could cross-reference to all fraud-related requirements and related application material to give the fraud topic more prominence.
- (b) Separate standard for fraud: A few respondents suggested that the IAASB consider whether there is a need for a separate and more detailed standard addressing fraud within the ISSA suite of standards.
- (c) Reporting: Comments related to the assurance report will be considered in the analysis of Question 21 (see **Agenda Item 2-G**).

Observations from the Survey

The survey asked respondents whether they agree that ED-5000 appropriately addresses the topic of fraud (including "greenwashing") by focusing on the susceptibility of the sustainability information to material misstatement, whether due to fraud or error.

Survey respondents that agreed included similar points as comment letter respondents, such as suggesting that the IAASB consider developing a separate ISSA on fraud in the medium term, or enhance fraud-related provisions in the proposed standard (e.g., by including the risk of management override of controls).

Some survey respondents were undecided, noting that ED-5000 needed more content, including that a more extensive process should be established to address greenwashing and fraud in a limited assurance engagement.

Survey respondents that disagreed had various comments including the following:

- The response to fraud is not adequate.
- Need to differentiate "fraud" and "greenwashing" or define "greenwashing" and clarify if "greenwashing" is in scope of ED-5000 or not.
- The competency/expertise of the sustainability assurance providers need to be verified and disclosed.
- Additional focus on omitted information.
- More clarity in the assurance report on what is being assured and the report should include a description of fraud-related procedures and the conclusions from those procedures.

SATF Views and Recommendations

Enhance Requirements or Definition

Management Override of Controls

Relevant Paragraphs in Agenda Item 2-A.1 and 2-A.2		
Introduction and Requirements	Application Material	Related Definitions
110AR, 135AAR	A355AR, A397AR	-

13. The SATF's view is that given the maturity of internal controls for sustainability reporting is behind that of financial reporting, the risk of management override of controls is elevated in sustainability assurance engagements.
14. The SATF is proposing a new requirement in the risk assessment section of proposed ISSA 5000 (see paragraph 110AR of **Agenda Item 2-A.1**) based on ISA 240 and ED-240³ and consistent with the proposed ISSA 5000 principle of the spectrum of risk.
15. The SATF is also proposing a new requirement under the Responding to Risks of Material Misstatement section in proposed ISSA 5000 (see paragraph 135AAR of **Agenda Item 2-A.1**) based on ISA 240 and ED-240. Because the relevant requirements in extant ISA 240 and ED-240 relate to journal entries and other adjustments, the requirement in paragraph 135AAR has been changed to relate to the entity's process for assembling the sustainability information. A new application material paragraph A397AR has also been added to provide other procedures in response to the risk of management override.
16. The new requirements related to management override of controls are only relevant to reasonable assurance engagements. Extending the requirements to limited assurance engagements would require the practitioner to obtain an understanding of the control activities component, which would be inconsistent with the IAASB position that the practitioner is not required to obtain an understanding of *all* of the components of the entity's internal control in a limited assurance engagement, and is not required to evaluate the design of controls and determine whether they have been implemented unless the practitioner plans to obtain evidence by testing the operating effectiveness of controls.

"Stand Back" Requirement

Relevant Paragraphs in Agenda Item 2-A.1 and 2-A.2		
Introduction and Requirements	Application Material	Related Definitions
163		-

17. The SATF discussed the calls for a "stand back" requirement in proposed ISSA 5000 for the practitioner to consider evidence obtained on a holistic basis, noting that similar calls were raised

³ *Proposed International Standard on Auditing 240 (Revised), The Auditor's Responsibilities Relating to Fraud in an Audit of Financial Statements and Proposed Conforming and Consequential Amendments to Other ISAs (ED-240)*

during the ED-5000 global roundtable events during the exposure period. The SATF did not support a separate requirement for a fraud “stand back” in proposed ISSA 5000 over the sustainability information as a whole due to the wide-ranging nature of sustainability information. The SATF also noted that this decision was consistent with the Board’s decision not to include a “stand back” in ED-240. However, the SATF revised paragraph 163 of **Agenda Item 2-A.1** to clarify that the practitioner is required to conclude about whether the sustainability information is free from material misstatement, whether due to fraud or error.

Non-compliance with Laws and Regulations

Relevant Paragraphs in Agenda Item 2-A.1 and 2-A.2		
Introduction and Requirements	Application Material	Related Definitions
117A	A370A	-

18. Respondents recommended that paragraphs 20 and 21 of ISA 250⁴ be included to provide more context for the requirement in paragraph 118 of **Agenda Item 2-A.1**, which is based on paragraph 22 of ISA 250 and relates to procedures when non-compliance with laws and regulation is identified or suspected. Respondents noted that doing so would further enable the requirements to be consistently and appropriately applied.
19. The SATF’s view is that the above requirements from ISA 250 are addressed in other parts of proposed ISSA 5000. Paragraphs 62 and A137 of **Agenda Item 2-A.1 and 2-A.2**, respectively, address the communications of significant matters with management or those charged with governance (TCWG), including the communication of identified or suspected fraud or non-compliance with law or regulation (NOCLAR). Paragraphs 165 and A456 address the circumstances when the practitioner is unable to obtain sufficient appropriate evidence.
20. The SATF noted, however, that there is no explicit requirement in proposed ISSA 5000 for the practitioner to communicate instances of suspected fraud or NOCLAR to management or TCWG. Therefore, the SATF is proposing the addition of a requirement leveraged from the first sentence of paragraph 20 of ISA 250 (see paragraph 117A of **Agenda Item 2-A.1**)
21. The SATF noted that some relevant ethical requirements may require the practitioner to consider communicating instances of suspected non-compliance with law or regulation with the financial statement auditor and added application material paragraph A370A to acknowledge this point.

Definition of Fraud and the Term “Greenwashing”

Relevant Paragraphs in Agenda Item 2-A.1 and 2-A.2		
Introduction and Requirements	Application Material	Related Definitions
-	-	A24A, A24B

⁴ International Standard on Auditing 250 (Revised), *Consideration of Laws and Regulations in an Audit of Financial Statements*

22. Fraud is defined in proposed ISSA 5000 in the same way as in ISA 240 (Revised) and ISAE 3410,⁵ and is not exclusively a financial reporting concept. The definition is broad enough to encompass all intentional actions by management and TCWG to obtain an unjust or illegal advantage and clear enough not to include unintentional management bias. Therefore, the SATF is of the view that the definition of fraud is appropriate for sustainability assurance engagements.
23. Although no changes are proposed to the definition of fraud, the SATF is proposing additional application material (see paragraphs A24A and A24B of **Agenda Item 2-A.2**) that refers to management bias and intentional misstatements (leveraged from paragraphs 36 and A136 of ISA 540 (Revised)⁶) and provides links to the examples of fraud in other application material paragraphs.
24. The SATF notes that there were mixed views from respondents on the inclusion of a description or definition of “greenwashing” in proposed ISSA 5000. Some respondents commented that defining greenwashing or using the term in the standard would not be appropriate as the term is understood to mean different things to different stakeholder groups and jurisdictions.
25. Accordingly, the SATF is proposing no change to the position in ED-5000, i.e., no definition, description or requirements related to “greenwashing.” Terms such as “greenwashing” and “greenhushing” and their relationship with fraud and management bias may be better explained in educational materials, similar to the IESBA Staff publication, issued in October 2022, highlighting the relevance and applicability of the Code in addressing “greenwashing.”⁷

Need for Guidance and Educational Materials

26. Additional guidance or examples on specific topics related to fraud, such as management override of controls, management bias, or “greenwashing,” can be considered in the development of the first time implementation guidance or other non-authoritative guidance.

Align with Concepts in Proposed ISA 240 (Revised)

27. The SATF and Board considered the developments in the IAASB Fraud project during the development of ED-5000. The SATF also considered ED-240 when responding to the respondent comments on ED-5000.
28. The public consultation for ED-240 will close on June 5, 2024, after which the Fraud Task Force will review the comments received and the proposals in ED-240 may be modified based on the comments. With the timeline for the finalization and approval of proposed ISSA 5000 preceding that of proposed ISA 240 (Revised), the SATF will continue to coordinate with the Fraud Task Force on the material leveraged from ED-240.

Other Matters

Separate Section or Appendix for Fraud

29. As noted in the EM, the SATF’s view is that referring to fraud throughout the requirements and application material recognizes the importance of the practitioner’s consideration of the risks of

⁵ ISAE 3410, *Assurance Engagements on Greenhouse Gas Statements*

⁶ ISA 540 (Revised), *Auditing Accounting Estimates and Related Disclosures*

⁷ <https://www.ethicsboard.org/publications/ethics-considerations-sustainability-reporting>

material misstatement due to fraud and responding appropriately to actual or suspected fraud identified during the engagement. The SATF is also concerned that including a single section that deals with fraud may lead to the consideration of the risks of material misstatement due to fraud becoming a “tick box” exercise and may not encourage practitioners to maintain professional skepticism throughout the assurance engagement.

Separate Standard for Fraud

30. Respondent suggestions for the development of separate standards within the ISSA suite, for topics such as fraud and estimates and forward-looking information, will be further considered by the Board as part of the discussion of future work plans.

Matters for IAASB Consideration

1. The IAASB is asked for its views on the SATF’s recommendations and proposed revisions to ED-5000, as described above.