

Fraud – Question 4

4. Does ED-240 establish robust work effort requirements and application material to address circumstances when instances of fraud or suspected fraud are identified in the audit?

Q01 Agree

1. Monitoring Group

International Organization of Securities Commission

Yes, we agree ED-240 establishes robust work effort requirements and application material to address circumstances when instances of fraud or suspected fraud are identified in the audit.

2. Investors and Analysts

Eumedion

Agree (with no further comments)

3. Regulators and Audit Oversight Authorities

Financial Reporting Council – United Kingdom

Agree (with no further comments)

Securities and Exchange Commission of Brazil

Agree (with no further comments)

4. Jurisdictional and National Auditing Standard Setters

Instituto Mexicano de Contadores Publicos

Agree (with no further comments)

5. Accounting Firms

RSM International

Agree (with no further comments)

MNP

Agree (with no further comments)

SRA

Agree (with no further comments)

6. Public Sector Organizations

Provincial Auditor Saskatchewan

Yes, ED-240 establishes robust work effort requirements and application material to address when instances of fraud or suspected fraud are identified in the audit.

Office of the Auditor General of Canada

Agree (with no further comments)

Office of the Auditor General of Ontario

We agree with the proposed requirements.

7. Member Bodies and Other Professional Organizations

Malaysian Institute of Certified Public Accountants

Agree (with no further comments)

Chartered Accountants Ireland

Agree (with no further comments)

Virginia Society of Certified Public Accountants

Agree (with no further comments)

Federation of Accounting Professions of Thailand

Agree (with no further comments)

Institute of Chartered Accountants of Ghana

Agree (with no further comments)

Malta Institute of Accountants

Agree (with no further comments)

Botswana Institute of Chartered Accountants

Agree (with no further comments)

Institute of Certified Public Accountants of Rwanda

Agree, with comments below

And the robust work effort appears explicit

Instituto Nacional de Contadores Públicos de Colombia

Agree (with no further comments)

9. Individuals and Others

Albert Bosch

Agree (with no further comments)

Moises Gonzalez Mercado

Agree (with no further comments)

2 Agree with comments

2. Investors and Analysts

Corporate Reporting Users' Forum

Agree, with comments below

We agree that the Paragraph 55 of ED-240 clarifies the auditor's response to address the fraud or suspected fraud when they are identified. We expect the auditor's actions required in the Paragraph 55 to work effectively, including:

(a) in Paragraph 55: to make inquiries about the matter with a level of management that is at least one level above those involved and, when appropriate in the circumstances, make inquiries about the matter with those charged with governance;

(d) in Paragraph 55: to determine whether control deficiencies exist, including significant deficiencies in internal control related to the prevention or detection of fraud, relating to the identified fraud or suspected fraud. We also support Paragraph 25 to require the auditor to communicate with management and those charged with governance matters related to fraud at appropriate times throughout the audit engagement.

3. Regulators and Audit Oversight Authorities

Canadian Public Accountability Board

Overall comments

CPAB is supportive of the positive steps that the IAASB has taken to improve the audit procedures related to fraud in an audit of financial statements. We performed fraud thematic reviews in 2019 and 2021, the results of which, included in communications issued in 2020 and 2022, support our comments in this letter. We agree more robust requirements are needed to promote consistent behaviour and facilitate effective identification and assessment of risks of material misstatement due to fraud and to reinforce the importance of auditors exercising professional skepticism in fraud-related audit procedures throughout the audit. In addition, we support the proposed changes to the communication of key audit matters related to fraud.

We are supportive of the IAASB's work to improve the audit procedures related to fraud in an audit of financial statements. We encourage the IAASB to consider the specific matters highlighted in this letter to support more consistent application of the standard.

Botswana Accountancy Oversight Authority

Agree, with comments below

Yes, the work effort requirements and applications material in ED-240 is robust. The requirements and application material detail the audit procedures that the Auditor has to perform when, the Auditor; identifies fraud or suspects fraud, identifies misstatement due to fraud, determines that financial statements are materially misstated due to fraud and also the relevant standard to consider when the Auditor is unable to conclude whether the financial statements are materially misstated as a result of fraud.

Independent Regulatory Board for Auditors – South Africa

Agree, with comments below

We agree that ED-240 sets robust work effort requirements, but we have concerns about the applicability of the requirements to different fraud or suspected fraud scenarios.

Our response to question one, specifically the comment made in 2.7, highlights that there are various ways in which information that is indicative of fraud or suspected fraud can come to the auditor's attention. As it relates to the requirements to respond to Fraud or Suspected Fraud, ED-240 does not:

Differentiate between the auditors' required response to confirmed fraud versus suspected fraud and does not consider how this may differ depending on the source of the information.

We acknowledge the explanations about the Scalability of the Fraud or Suspected Fraud Requirements. However, ED-240 can benefit from further enhancements related to the applicability of the required procedures in different circumstances. For example:

For confirmed fraud:

May auditors rely on internal investigation reports, or is an independent investigation by the auditor necessary?

How does the auditor evaluate whether the remedial actions are appropriate?

For suspected fraud:

What should auditors do if inquiries do not yield further information and management takes no action?

Is there a requirement for auditors to engage an investigator or expert to assess the need for an investigation?

Address how the auditor must respond to suspected fraud under investigation.

An ongoing investigation can significantly delay the finalisation of an audit and therefore the issue of the financial statements due to uncertainties related to suspected fraud. This delay may not be in the public interest. For ongoing investigations, we question:

Whether the auditor can conclude the audit (assuming this is also allowed legally)?

What intermediate actions the auditor must take in the public interest to be able to finalise the audit and allow for the issue of the financial statements?

How the auditor would bring to the attention of the users of the financial statements the fact that a suspected fraud investigation is ongoing if the audit is finalised, and the financial statements are issued before the finalisation of the fraud investigation.

Address how the auditor must respond when management or those charged with governance are suspected of fraud.

Assuming the auditor is unable to obtain further information, and therefore unable to perform the procedures in paragraphs 56 – 59, we question:

Is it sufficient for auditors to seek legal advice and consider withdrawal, or are there minimum procedures to follow / complete first?

How does the auditor comply with the requirements in ED-240 paragraph 60, such as the requirement to identify a misstatement and communicate with the appropriate level of management and those charged with governance about the auditor's withdrawal from the engagement and the reasons for the withdrawal?

Address how the auditor must respond when, under circumstances of suspected management or those charged with governance involvement in fraud, the auditor is requested to resign as auditor.

We recommend that the IAASB provides clearer distinctions and guidance for auditors facing different fraud scenarios, including those involving management and those charged with governance. The IAASB may take into consideration developing a flow chart to direct the auditor's response to fraud or suspected fraud.

Additionally, we propose enhancing the clarity of the auditor's responsibilities related to determining whether control deficiencies exist in paragraph 55(d).

We propose moving the requirement in paragraph 55(d) down and incorporating it into paragraph 58, i.e., creating a paragraph 58(c), because practically it may only be possible to identify significant deficiencies in internal control related to the prevention or detection of fraud after the auditor has determined that the financial statements are materially misstated due to fraud.

Differentiation between the applicability of requirements to different fraud or suspected fraud scenarios.

4. Jurisdictional and National Auditing Standard Setters

Japanese Institute of Certified Public Accountants

Agree, with comments below

We agree that ED-240 establishes robust work effort requirements and application material to address circumstances when instances of fraud or suspected fraud are identified in the audit.

However, we propose the IAASB consider the following points.

Paragraphs 55(c) and A151 use the term "remediation measures," while the last example in paragraph A41 and Appendix 1 use the similar term "remedial action(s)." In addition, in the extant International Standards on Quality Management (ISQM) and International Standards on Auditing (ISA), "remedial action(s)" is often used (e.g., ISQM 1, paragraph 42; ISA 250, paragraph A25; ISA 265, paragraph A1) and "remedial measures" is not used. We believe that the term "remedial action(s)" should be used throughout the standard if it is intended to mean the same thing.

The lead-in of paragraph 55 and paragraph 55(a) through (c) use the term "the matter" to refer to identified fraud or suspected fraud, but paragraph 55(d) uses the term "identified fraud or suspected fraud" and the terminologies are not consistently used. It may cause a misunderstanding that the meaning of the term in paragraph 55(d) is different from others. Therefore, if they are intended to mean the same thing, the wording should be consistent.

Paragraph 55(d) requires the auditor to determine whether control deficiencies exist, including significant deficiencies in internal control related to the identified fraud or suspected fraud. However, paragraph 55 is the first requirement that applies in all circumstances if the auditor identifies fraud or suspected fraud. As a consequence, we believe that it may be difficult to determine whether an identified deficiency in internal control is a significant deficiency at the stage of obtaining an understanding of identified fraud or suspected fraud in accordance with paragraph 55. Therefore, we propose to delete the reference to "significant deficiencies in internal control" from paragraph 55(d) and make a reference in paragraph A150 to ISA 265 which requires the auditor to determine whether there is a significant deficiency in internal control. Please see below for details.

"55. If the auditor identifies fraud or suspected fraud, the auditor shall obtain an understanding of the matter in order to determine the effect on the audit engagement. In doing so, the auditor shall: (Ref: Para. A146–A151)..."

(d) Determine whether control deficiencies exist, including significant deficiencies in internal control related to the prevention or detection of fraud, relating to the identified fraud or suspected fraud..."

"A150. If the auditor has identified one or more control deficiencies, ISA 265 requires the auditor to determine whether, individually or in combination, the deficiencies constitute a significant deficiency provides requirements and guidance about the auditor's communication of significant deficiencies in internal control identified during the audit to those charged with governance. Examples of matters that the auditor considers in determining whether a deficiency or combination of deficiencies in internal control constitutes a significant deficiency include:"

Compagnie Nationale des Commissaires aux Comptes and Conseil Supérieur de l'Ordre des Experts-Comptables

Agree, with comments below

Paragraph 55 of the ED states that: If the auditor identifies fraud or suspected fraud, the auditor shall obtain an understanding of the matter in order to determine the effect on the audit engagement. In doing so, the auditor shall: (Ref: Para. A146–A151)

- (a) Make inquiries about the matter with a level of management that is at least one level above those involved and, when appropriate in the circumstances, make inquiries about the matter with those charged with governance.
- (b) If the entity has a process to investigate the matter, evaluate whether it is appropriate in the circumstances.
- (c) If the entity has implemented remediation measures to respond to the matter, evaluate whether they are appropriate in the circumstances; and
- (d) Determine whether control deficiencies exist, including significant deficiencies in internal control related to the prevention or detection of fraud, relating to the identified fraud or suspected fraud.

This paragraph needs to be clarified regarding the meaning of “If the auditor identifies fraud or suspected fraud”. Does it mean that all these requirements are applicable when the auditor identifies a fraud that was not previously identified by Management or when any fraud comes to his/her attention?

Requirements and work effort when a fraud is identified should be different depending on:

whether the fraud was previously identified by Management or not,

whether the fraud was committed by a third party or by someone inside the entity’s organization,

whether the fraud has a material impact on the financial statements or not.

By differentiating the treatment of identified fraud depending on the circumstances of their discovery and occurrence, the auditor would be able to adapt its work effort to focus on the most “serious” frauds. In the simplest cases such as a fraud committed by a third-party, already identified by Management and without significant impact on the financial statement, the auditor would not deploy the full set of procedures required in paragraph 55, (a), (b), (c), (d).

Finally, the auditor could be explicitly authorized to adopt a “grouped” approach to address frauds of the same type and with the same potential impact on the financial statements such as all petty theft committed by third parties (e.g. shoplifters in the retail industry).

New Zealand Auditing and Assurance Standards Board of the External Reporting Board

Agree, with comments below

While we agree that the auditor needs to obtain an understanding of the identified or suspected fraud in order to determine the impact on the audit we are concerned with the practicality and scalability of the requirement in paragraph 55 as drafted.

As defined, suspected fraud includes allegations of fraud that have come to the auditor’s attention. If an entity that has a whistleblower program, and receives hundreds of allegations of fraud, is the auditor expected to obtain an understanding of every incidence reported?

The role of the auditor is to obtain reasonable assurance that the financial statements are free from material misstatement whether due to fraud or error. Lack of any reference to materiality considerations in applying paragraph 55 may lead the auditor to spend significant time investigating matters that are clearly inconsequential to the audit.

Saudi Organization for Chartered and Professional Accountants

Agree, with comments below

Austrian Chamber of Tax Advisors and Public Accountants

Agree, with comments below

We suggest that the link to IAS 260 should be more clearly established and not just by revising a table attached to ISA 260 and to add language that the means and ways of communicating should follow the guidance provided in ISA 260.

We noted that the application material in A189 includes a reference to IAS 250 revised, which is not included in the earlier section of the application material. It may therefore be misleading, as it suggests that ISA 250 revised may only be applicable to reporting to an appropriate authority outside the entity, while ISA 250, dealing with considerations of law and regulations in the audit of financial statements is of course also applicable to reporting to management and TCWG. We suggest to clarify this by including a brief reference to ISA 250 also in the application guidance sections A182 to A187. Also, footnote 90 should include a reference to para. 29 of ISA 250 revised is this the underlying ISA and not only the application material included in ISA 250 revised paragraphs A28 through A34.

Also, we noted that the distinction between alleged, suspected, and actual (when proven) fraud does not appear to be sufficiently clear and therefore the consequences attached to such a distinction may be ambiguous.

Hong Kong Institute of Certified Public Accountants

Agree, with comments below

ED-240.55 requires that the auditor shall obtain an understanding of the matter in relation to the identified fraud or suspected fraud in order to determine the effect on the audit engagement. In doing so, the auditor shall perform ED-240.55(a) to (d). Apart from ED-240.55(a) which requires the auditor to make inquiries about the matter, the requirements set out in ED-240.55(b) to (d) go beyond simply to “obtain an understanding of the matter” as stated in ED-240.55. ED-240.55(b) to (d) require the auditor to determine whether control deficiencies exist, and evaluate whether the entity’s process to investigate the matter and whether the remediation measures are appropriate if the entity has such process and remediation measures are in place. Therefore, we recommend that the IAASB clarify the requirements in ED-240.55 and the circumstances under which ED-240.55(b) to (d) would be carried out.

In addition, additional guidance on the implementation of the procedure outlined in ED-240.56(b), which states “If applicable, consider the impact on other engagements, including audit engagements from prior years.” would be helpful, such as clarification on the nature of considerations and the timeframe (i.e. number of years) to be taken into account. Notably, for new audit clients, there is no similar requirement set out in ISA 510, Initial Audit Engagements —Opening Balances. We would suggest that the IAASB provide guidance in ED-240.56(b) or application material on its expected implementation of the required procedure.

Auditing and Assurance Standards Board Canada

Agree, with comments below

While we support the requirements and application material for providing a framework for auditors to address circumstances when instances of fraud or suspected fraud are identified, we have some comments relevant to this question in our response to Question 1 and Question 8 as noted below.

Auditors' responsibilities regarding non-material fraud

Refer to our response under Question 1.

Inquires when fraud or suspected fraud is identified

Refer to our response under Question 8.

Other suggestions:

Through our outreach and detailed review of the proposed revisions, we have identified a suggestion that can improve the clarity and understandability of ED-240.

First-time implementation guidance

Consider first-time implementation guidance to highlight what is new compared to extant in this section as there are new requirements, relocated existing requirements, the elevation of existing application material to requirements, and enhanced application material.

We found the following references to non-material fraud or suspected fraud outside of ED-240:

The "Public Interest Issues Table—Mapping of Key Changes Proposed in ED-240 to the Actions and Objectives in the Project Proposal that Support the Public Interest" states that the requirements "apply to all instances of fraud or suspected fraud identified by the auditor, irrespective of materiality, and that the auditor is required to apply some or all of those requirements before determining the implications of the fraud or suspected fraud on the audit, including whether it is inconsequential."

Paragraph 56 of the IAASB's Explanatory Memo, also states "for all instances of fraud or suspected fraud identified by the auditor, ED-240 requires the auditor to apply at least some of the fraud or suspected fraud requirements that are applicable in the circumstances to determine the effect on the audit engagement."

We agree with the IAASB's statements above that all instances of fraud or suspected fraud are in scope of ED-240. However, our outreach indicated different interpretations of whether a threshold is applied to paragraphs 55-59. Interpretations varied as follows:

Some believe paragraphs 55-59 do not apply to inconsequential frauds even though the standard does not define inconsequential fraud.

For example, a coffee shop, where management is aware of inconsequential fraud with cashiers giving free coffee to their friends. In this example, management knows about the fraud or suspected fraud but does not further investigate the matter or implement additional controls to prevent a reoccurrence as they accept this level of inconsequential fraud as a cost of business.

Others interpret paragraphs 55-59 as applicable to all frauds, including non-material and inconsequential frauds, as cumulatively it may indicate a broader issue.

We acknowledge and support that paragraph A152 includes an example of inconsequential fraud and as part of the engagement partner's determination, the engagement team continues with other aspects of the audit engagement while management of the entity is resolving the matter.

Given the differing interpretations of the scope of paragraph 55, we believe there is a risk that paragraphs 55-59 in practice will be applied inconsistently across engagements.

Suggest:

Adding application material to paragraph 55 to explicitly state that it applies to all instances of fraud or suspected fraud identified by the auditor, irrespective of materiality. As we believe the proposals in paragraphs 56-59 appropriately build on the understanding obtained in paragraph 55.

Nordic Federation of Public Accountants

Agree, with comments below

Overall, we support including more explicit requirements on how to address identified fraud situations. We also support emphasizing the involvement of the engagement partner.

However, paragraph 55 in ED-240 together with its application material, for example paragraph 55 (a) and A147, gives the impression that focus is on fraud committed by lower level of management or staff. These situations are relevant but fraud involving top management or even TCWG are the kind of frauds that more often might lead to material misstatements of the financial statements and eventually cause corporate failures. These situations are not sufficiently addressed in the standard. The requirements in paragraphs 57-58 could be enhanced in this respect.

Also, paragraph 55 addresses "fraud or suspected fraud". According to the definitions in paragraphs 6 and 7, this includes the entire spectrum from actual fraud to all kinds of fraud allegations. The starting point that triggers actions is therefore set very low and we question whether this is reasonable and appropriate. In our view at least clearly trivial allegations and inconsequential suspicions of fraud should be excluded. The auditor should be allowed to apply some professional judgment. The way the paragraph is drafted it also includes non-material fraud and non-material suspected fraud, which contributes to a lack of clarity about the auditor's responsibilities (see paragraph 18 of the EM).

Instituto de Auditoria Independente do Brasil

Agree, with comments below

Besides we acknowledge that is a matter of professional judgment, the extent of the audit procedures to be performed by the auditor when fraud is identified and when there is 'only' a suspected fraud could be enhanced with further examples of situations in the application material. Also, in determining whether identified misstatements due to fraud are material, we have noted that ED-240 requires the auditor to consider the nature of the qualitative or quantitative circumstances giving rise to the misstatement and conclude accordingly. However, the impact of communicating fraud risks to the public especially when it was not possible to conclude as it is required in paragraph 59 of ED-240 can be challenging and could generate additional responsibilities to auditors. Therefore, the need to evaluate this communication should be highlighted in the expected outcomes of the performed procedures.

Scalability

Para. 55-56 might be unnecessarily onerous in certain circumstances. Paragraph 55 is not clear if the requirement is related solely to instances of fraud or suspected fraud discovered by the auditor or all instances

of fraud or suspected fraud, including those identified by the auditor and those identified by others such as management. In addition, sometimes the auditor may be able to conclude that a fraud is an isolated occurrence and clearly quantitatively and qualitative immaterial not necessarily performing all the procedures as required in Para. 55-56.

Para. 56 seem to be unduly onerous to require the engagement partner such requirement specially when the partner is the group engagement partner. We suggest that the requirement be modified to clarify that the engagement partner “take responsibility” to such determinations. Then, we recommend changing “determine whether” to “take responsibility for the determination as to whether”

ED requires the auditor to perform procedures in response to allegations of fraud. However, the application of all the requirements at Para. 55-59 to “all” allegations does not seem appropriate in all circumstances

Royal Dutch Institute of Chartered Accountants

Agree, with comments below

Positive remarks:

We support the proposed new requirement to obtain an understanding of the fraud or suspected fraud. We consider this an improvement that makes explicit what is implied in the extant ISA (among other things, par. 36, 37, 41, 42, 44, which topics are included in the ED-240).

Also, this aligns with the role of the engagement partner and key engagement team members in the engagement team discussion in par. 29.

The application material enhances the various related topics.

Constructive critical remark:

We suggest IAASB consider a requirement in par. 55 to involve forensic expertise within or outside the engagement team in case of fraud, suspected fraud or indications of fraud. Further, we suggest IAASB offer an explanatory paragraph that may assist auditors in this regard.

We also suggest to include which considerations to make when evaluating the appropriateness of the remedial action plan.

5. Accounting Firms

BDO International

Agree, with comments below

We agree that ED-240 includes robust work effort requirements and application material to address instances of fraud or suspected fraud, especially in the following areas:

Having an explicit requirement in paragraph 55 for the auditor to obtain an understanding of the fraud or suspected fraud in order to increase the consistency and quality of work done by auditors in these situations.

The requirement in paragraph 56 for the engagement partner to determine the effect of the fraud or suspected fraud on the audit reinforces the partner involvement requirements laid out in paragraph 31 of ISQM 1.

Depending on the nature of the fraud or suspected fraud, some of the fraud or suspected fraud requirements may not be applicable. This will allow for effective scalability in applying the revised standard in practice.

PriceWaterhouseCoopers

Agree, with comments below

We agree in principle that ED-240 establishes robust work effort requirements addressing circumstances when instances of fraud or suspected fraud are identified in the audit. The proposed new requirements are useful additions to the standard. They appropriately reinforce the overall responsibility of management for taking action to identify and respond to fraud while recognising the auditor needs to also evaluate the appropriateness and further implications, if any, of those actions. These changes help address a perceived gap in ISA 240 and help to ensure the auditor “closes the loop” on identified or suspected fraud matters.

Furthermore, we support the proposed requirement for the engagement partner to exercise professional judgment in determining what further actions are appropriate in the circumstances, based on their understanding of the fraud or suspected fraud and how management has responded. This approach ensures appropriate scalability, allowing for flexibility in audits of entities of varying size and complexity, recognising that the response to individual instances of fraud or suspected fraud may require unique actions specific to the particular audit. Importantly, the reference to identified or suspected fraud in paragraph 55 includes both matters that are directly identified by the auditor when performing audit procedures, as well as matters that the auditor has become aware of through inquiries of management, those charged with governance, or others (which includes matters that may have been captured and addressed by an entity’s whistleblower program or other reporting mechanism). The auditor’s understanding of these matters appropriately includes whether and, if so, how management and those charged with governance have responded to the matter (including any process to investigate and remediate the matter). Management’s conclusions about the potential effects on the financial statements may also inform the auditor in determining the nature and extent of further work necessary to obtain evidence about whether the financial statements are materially misstated due to fraud.

Our primary observation on this set of requirements relates to paragraph 55(d). The auditor is required to “determine whether control deficiencies exist, including significant deficiencies in internal control related to the prevention or detection of fraud, relating to the identified fraud or suspected fraud.” The auditor may not have performed testing of the operating effectiveness of internal controls as part of the audit. Therefore, while we agree that the auditor’s inquiries may lead to a suspicion, possibly even a strong one, that one or more controls may not have been implemented or have operated effectively, we question whether the auditor will have a sufficient evidential basis for making a “determination” in accordance with this requirement. While we support the sentiment of the requirement, we ask the Board to reconsider how it is articulated and to reflect on the varying nature of work that an auditor may have undertaken when responding to assessed risks of misstatement in accordance with ISA 330.

We also have a concern that some of the application material in support of the requirements can be interpreted as inconsistent with the principle described in paragraph 6 that the auditor is only concerned with fraud or suspected fraud that could give rise to material misstatement of the financial statements. For example, we suggest the following amendments:

Paragraph A7, example 2: referring to:

“.....possible recurring misappropriation of high-value products from the entity’s warehouse”

Paragraph A147, example 1: it is unclear as to the relevance of referring to “an employee who does not have a significant role or authority in the entity” when referring to misappropriation of assets. This could be implied as suggesting that this is unlikely to be a situation that may give rise to material misstatement of the financial

statements. We suggest altering the example, to align with the suggestion on paragraph A7 and instead refer to:

“...evidence that indicated assets may have been misappropriated by an employee who does not have a significant role or authority in the entity the warehouse manager by overriding relevant controls.”

Certain other facts in the example would need to be adjusted to reflect this change.

Paragraph A148, example 1: we suggest making clear that the allegations were such that this could result in a material misstatement of the financial statements due to fraud as, given the other facts explained in the example, the auditor would not be expected to follow up all spurious claims made against an entity by disgruntled employees. We recommend amending to state:

“New, persuasive, allegations of fraud were made...”. We also suggest not referring to prior allegations as this seems technically not relevant to the situation, and instead just stating: “Since the entity’s policies and procedures were followed and prior the allegations of a similar nature had been investigated and were determined to be without merit. Therefore, management...”

Moore Global Network

Agree, with comments below

We do agree that the ED does establish the work efforts required and the application materials are well received.

However, we believe that Paragraph 55 would be more useful, and scalable if it were to include a step at an early stage of the process to obtain an understanding of the matter, a note on determining whether the fraud or suspected fraud is quantitatively or qualitatively material before continuing, to limit the work that needs to be performed on non-material fraud.

Deloitte

Agree, with comments below

We agree that ED-240 appropriately establishes robust work effort requirements and application material to address circumstances when instances of fraud or suspected fraud are identified in the audit; however, we have the following recommendations to improve the clarity of ED-240:

We are supportive of the IAASB’s proposal, as outlined in paragraph 55 of ED-240, which states that “If the auditor identifies fraud or suspected fraud, the auditor shall obtain an understanding of the matter in order to determine the effect on the audit engagement.” This emphasizes the importance of auditors responding to such matters comprehensively, based on the understanding of the matters identified. However, paragraph 55 as written may be construed differently by readers, as it does not clarify if the requirement is related solely to instances of fraud or suspected fraud discovered by the auditor or all instances of fraud or suspected fraud, including those identified by the auditor and those identified by others such as management.

Our interpretation is that this paragraph is meant to encompass all instances of fraud or suspected fraud regardless of the party who identified the matter. If this is the case, we are concerned that paragraph 55, as currently drafted, may be too prescriptive for practical application to every identified fraud or suspected fraud, requiring the auditor to execute each step as an audit procedure for each instance rather than a consideration based on the understanding the auditor obtained of the matter. This is concerning when the fraud or suspected fraud is identified by management, as this may result in duplicative efforts by the auditors to understand the

matter. This could give rise to scalability and feasibility issues when the auditor needs to determine the course of action in each instance of fraud or suspected fraud.

Consequently, we recommend the IAASB move items (b) through (d) in paragraph 55 of ED-240 to a new requirement paragraph that follows the auditor obtaining an understanding of the identified fraud or suspected fraud. This would allow scalability and auditor judgment in applying audit procedures for those instances of fraud or suspected fraud that may reasonably pose a risk of material misstatement in the financial statement due to fraud, aligning with the objective of paragraph 17(a). Also, this will focus the auditor's attention to those matters that are important to the financial statement versus matters that are clearly inconsequential and do not warrant significant auditor attention (for example, customer theft in a retail environment). Accordingly, we recommend the following edits:

Paragraph 55: If the auditor identifies, or otherwise becomes aware of, fraud or suspected fraud, the auditor shall obtain an understanding of the matter by making inquiries about the matter and management's associated response with a level of management that is at least one level above those involved and, when appropriate in the circumstances, make inquiries about the matter with those charged with governance in order to determine the effect on the audit engagement. In doing so, the auditor shall:

- (a) Make inquiries about the matter with a level of management that is at least one level above those involved and, when appropriate in the circumstances, make inquiries about the matter with those charged with governance;
- (b) If the entity has a process to investigate the matter, evaluate whether it is appropriate in the circumstances;
- (c) If the entity has implemented remediation measures to respond to the matter, evaluate whether they are appropriate in the circumstances; and
- (d) Determine whether control deficiencies exist, including significant deficiencies in internal control related to the prevention or detection of fraud, relating to the identified fraud or suspected fraud.

Paragraph 55.A: If, after obtaining an understanding of an identified fraud or suspected fraud, including the associated entity response, the matter is deemed to be more than inconsequential to the audit, the auditor shall:

- (a) If the entity has a process to investigate the matter, evaluate whether it is appropriate in the circumstance;
- (b) If the entity has implemented remediation measures to respond to the matter, evaluate whether they are appropriate in the circumstances; and
- (c) Determine whether control deficiencies exist, including significant deficiencies in internal control related to the prevention or detection of fraud, relating to the identified fraud or suspected fraud.

Paragraph A149 is intended to provide guidance on how to evaluate the appropriateness of the entity's process to investigate and remediate the fraud or suspected fraud to which an auditor has become aware. The application material is focused on providing guidance on the remediation element; however, there is no guidance on how to evaluate the sufficiency of an investigation. We recommend the IAASB provide guidance on matters to consider when evaluating the appropriateness of the entity's process to investigate, for example, when an independent investigation would be expected

versus an internal investigation, among other matters.

We are concerned that paragraph 56(a) may be impractical, especially related to group audits, given that the current wording requires the engagement partner to determine everything provided in this paragraph. There

will be engagements whereby it will be impossible for the engagement partner to directly perform certain of the actions without needing assistance from other engagement team members. For example, paragraph 56(a)(iii) requires the engagement partner to determine whether there are additional responsibilities under law, regulation or relevant ethical requirements about the entity's non-compliance with laws and regulations. If the entity's non-compliance with a law or regulation is in another jurisdiction whereby a component auditor is assisting the engagement partner, the engagement partner would need that component auditor's involvement to assist in making this determination. Accordingly, we recommend the following edits to paragraph 56(a) of ED-240:

Paragraph 56: "Based on the understanding obtained in accordance with paragraph 55, the engagement partner shall: (Ref: Para. A152–A153)

Take responsibility for the determination as to Determine whether:"

We are also concerned with paragraph 56(b), which requires an auditor to, as applicable, consider the impact of identified fraud or suspected fraud on other engagements, including audit engagements from prior years. ISA 510 does not include similar requirements to consider prior engagements. In addition, there are certain jurisdictions that do not permit restatements of financial statements. Such requirement in ED-240 fails to provide context on the extent of other engagements one needs to consider or the nature of what one needs to consider for other engagements. Accordingly, we recommend the IAASB remove paragraph 56(b) from ED-240.

CohnReznick

Agree, with comments below

We believe ED-240 establishes robust work effort requirements and application material for the circumstances when instances of fraud or suspected fraud are identified in the audit. We believe the examples in the application material will be helpful in promoting a consistent understanding of the auditor's requirements with respect to fraud which may be referenced/cited to others, including audit clients, when describing the auditor's work effort. Often, there is a lot of sensitivity when a fraud has been identified or suspected, even for low-level third-party fraud. By having examples in the proposed standard, auditors will be able to point to the application material during their discussions with management and those charged with governance in explaining their professional obligations.

Ernst & Young Global

Auditors' required procedures related to fraud or suspected fraud

We do not believe it is practical for the auditor to perform all the required procedures proposed in ED-240 for all instances of fraud or suspected fraud, including those that are clearly inconsequential, such as minor instances of misappropriation of assets by employees or customers. We suggest that the requirements be bifurcated to require an initial understanding of the fraud or suspected fraud, through inquiries, in all instances. We then believe it would be more realistic to require further procedures by the auditor only when the auditor determines the fraud or suspected fraud has the potential to be more than clearly inconsequential and warrants further understanding and possible actions.

Agree, with comments below

We believe that ED-240 is a substantial improvement over extant ISA 240 related to establishing robust work effort requirements and application material to address circumstances when instances of fraud or suspected fraud are identified in the audit. However, we do not believe it is practical for the auditor to perform all the

required procedures in paragraph 55 of ED-240 for all instances of fraud or suspected fraud, including those that are clearly inconsequential. We also do not believe there are sufficient parameters and guidance for the auditor's response to third-party fraud.

Requirements related to identified or suspected fraud

We agree with paragraph 56 of the EM that for all instances of fraud or suspected fraud, it is necessary for the auditor to apply "at least some of the fraud or suspected fraud requirements that are applicable in the circumstances to determine the effect on the audit engagement" because in many cases, the materiality of a matter identified may not be truly understood without obtaining further information about the instance of fraud or suspected fraud.

However, we believe ED-240 should be clearer about which procedures are necessary in all cases as we do not believe that scalability has been clearly introduced. We are concerned that the requirements in paragraph 55 of ED-240 could result in unnecessary work effort and documentation by the auditor on matters that are clearly inconsequential. This is especially the case for large, complex entities that may have numerous whistleblower allegations, or for any entity where there could be misappropriation of assets involving the theft of an entity's assets that is perpetrated by employees (or customers) in relatively small and immaterial amounts (as is often the case for misappropriation of assets as acknowledged in paragraph A6 of ED-240).

Therefore, we suggest that paragraph 55 of ED-240 be bifurcated to require an initial understanding of the fraud or suspected fraud through inquiries in all instances. We then believe it would be more realistic to require the procedures in paragraph 55(b)–(d) of ED-240 only when the auditor determines the fraud or suspected fraud is more than clearly inconsequential and warrants further understanding.

We also note that paragraph A152 of ED-240 includes an example that states that "based on an understanding of the suspected fraud, the engagement partner believed the suspected fraud was inconsequential because it was limited to the misappropriation of immaterial assets by employees. Consequently, the engagement partner determined to continue with other aspects of the audit engagement while the matter was being resolved by management of the entity." This example supports our recommendation to limit the initial understanding of the matter to inquiries about the nature and circumstances of the matter in order to determine if further procedures by the auditor are necessary (i.e., to determine whether the matter is more than clearly inconsequential).

Paragraph 14 of ED-240 clearly states that fraud constitutes an instance of non-compliance with laws and regulations. It is therefore important for the procedures related to responding to identified or suspected fraud in ED-240 to be interoperable with the requirements of Section 360 of the IESBA Code such that there are not implementation issues for those auditors that need to comply with both the ISAs and IESBA Code. In particular, we refer to the following requirements with which ED-240 could be closer aligned (emphasis added):

360.7 A2 A professional accountant who encounters or is made aware of matters that are clearly inconsequential is not required to comply with this section. Whether a matter is clearly inconsequential is to be judged with respect to its nature and its impact, financial or otherwise, on the client, its stakeholders and the general public.

R360.10 If a professional accountant engaged to perform an audit of financial statements becomes aware of information concerning non-compliance or suspected non-compliance, the accountant shall obtain an understanding of the matter. This understanding shall include the nature of the non-compliance or suspected non-compliance and the circumstances in which it has occurred or might occur.

R360.19 The professional accountant shall assess the appropriateness of the response of management and, where applicable, those charged with governance.

Given our comments above to bifurcate the requirement and better align the procedures in ED-240 with the IESBA Code, we suggest the following revisions to paragraph 55 of ED-240:

55. If the auditor identifies fraud or suspected fraud, the auditor shall:

(a) Obtain an understanding of the nature and circumstances of the matter in order to determine the effect on the audit engagement. In doing so, the auditor shall: including making (a) Make inquiries about the matter with a level of management that is at least one level above those involved and, when appropriate in the circumstances, make making inquiries about the matter with those charged with governance.;

(b) If the matter is determined to be more than clearly inconsequential, obtain a further understanding of the matter to determine the effect on the audit engagement, including:

(i) If the entity has a process to investigate the matter, evaluate whether management's response to the matter it is appropriate in the circumstances;

(ii) If the entity has implemented remediation measures to respond to the matter, evaluate whether they are appropriate in the circumstances; and

(iii) Determine whether control deficiencies exist, including significant deficiencies in internal control related to the prevention or detection of fraud, relating to the identified fraud or suspected fraud.

Responding to third-party fraud

Our responses to Q1 and Q3 suggests needed clarifications to provide the right context for explaining the auditor's responsibilities for each category of third-party fraud, which include external parties known to the entity and unknown to the entity, as well as how the nature of the auditor's response to third-party fraud differs from risks of fraud internal to the entity.

We are particularly concerned that, as the standard is currently written, it would seem that all cyber breaches are considered fraud. However, all cyber breaches do not result in misappropriation of assets or fraudulent financial reporting, nor do they always affect the entity's non-compliance with laws and regulations. We therefore suggest a clearer distinction is needed between cyber breaches and fraud and the circumstances in which cyber breaches require a response from the auditor.

For each category of third-party fraud, we recommend clarifications are made to the requirements and guidance of ED-240 so that appropriate distinctions are made in the threshold for, and nature of, the auditor's required response. In our view, such clarifications could include that:

Fraud or suspected fraud involving a related party should always require further procedures by the auditor to respond to the matter (i.e., such instances of fraud are always "more than clearly inconsequential").

For known third parties, a threshold of "more than clearly inconsequential" applies, as suggested in our revised paragraph 55(b) above.

For cyber breaches, the auditor obtains an understanding sufficient to determine the possible effect on the financial statements and also to consider whether the event constitutes fraud for the purposes of ED-240 (for which clarifying guidance is needed), as well as any implications for the entity's compliance with laws and regulations (e.g., required reporting to authorities or other required disclosures). When appropriate conditions are met, which need to be more clearly defined, the auditor is required to respond to the matter in accordance with paragraph 55(b).

Application material related to the requirements for identified or suspected fraud

To help the auditor in determining when the procedures in our proposed paragraph 55(b) would be required, we suggest that the IAASB add supporting application material, for example:

Guidance could be added to explain that determining whether a matter is more than clearly inconsequential, involves evaluating its nature and its impact to the financial statements. In addition, an instance of fraud or suspected fraud is likely “more than clearly inconsequential” when it:

Involves management, or employees who have significant roles in internal control

Causes the auditor to doubt the integrity of management or those charged with governance

Involves related parties

Guidance could be added that suggests that instances of identified fraud or suspected fraud involving misappropriation of assets (that do not involve the parties listed above) may be determined to be “clearly inconsequential” after completing the initial understanding required by our proposed paragraph 55(a). This would eliminate the need for the auditor to spend time further understanding and documenting matters, for example, related to employees stealing immaterial amounts of office supplies or using a company vehicle for personal use. On the other hand, instances of identified fraud or suspected fraud involving fraudulent financial reporting may need further understanding in all instances.

We suggest re-positioning the procedures suggested in paragraph A146 of ED-240 as procedures that the auditor would perform in response to our proposed paragraph 55(b). This would avoid, implying that procedures such as involving an auditor’s expert, inspecting whistleblower files or making inquiries of legal counsel or internal audit would be necessary for every instance of identified or suspected fraud.

We also urge the IAASB to challenge the examples provided in paragraphs A147, A148 and A152 of ED-240 that are illustrating the extent of the understanding required by paragraph 55 of ED-240. We do not believe these examples fully reflect the requirements in paragraph 55 of ED-240 and suggest that the IAASB either specifically state as part of the example which requirements the example is illustrating or create one comprehensive example (possibly combining the partial examples provided) to more accurately illustrate the procedures required by paragraph 55 of ED-240. We believe these examples, as proposed, contradict the requirements in ED-240 and will cause confusion as auditor’s attempt to reconcile the examples with the requirements in ED-240. Specifically:

The examples in paragraph A147 are illustrating the “extent of the understanding of the fraud or suspected fraud”, however, the examples only seem to be illustrating the requirement in paragraph 55(a), and not the requirements in paragraph 55(b)–(d) (i.e., there is no illustration of how the auditor evaluated the entity’s process, evaluated the remediation measures or determined whether control deficiencies exist).

The second example in paragraph A147 illustrates that changes were made to the overall group audit strategy and group audit plan, which goes beyond illustrating the extent of the understanding of the fraud or suspected fraud (as indicated in the lead-in to the examples). This is also misleading as the other procedures required by paragraph 56 are not addressed in the example.

We do not believe the examples in paragraph A152 effectively illustrate what is required by paragraph 56, which is the requirement for the engagement partner to determine whether to perform further audit procedures. In our view, they only illustrate when an auditor would continue working versus ceasing the audit work. We suggest that the IAASB provide guidance and examples that more closely align with the requirements in paragraph 56 (examples of relevant additional risk assessment procedures or further audit

procedures). We also suggest that in the second example, consideration is given as to whether the auditor is able to continue the engagement (i.e., include a reference to the requirement in paragraph 60).

We also recommend that further guidance and/or examples be added to ED-240 on how the auditor's understanding can

be performed for larger entities with mature whistle-blower programs and developed processes for responding to allegations of fraud. As paragraph 55 requires procedures to be performed for all identified or suspected fraud, we believe it is essential that the IAASB provides guidance on the auditor's responsibility to complete the procedures in paragraph 55 when there are large volumes of whistleblower files, tips or complaints that allege fraud. This could be in the form of a "scalability" application material paragraph. For larger entities, our experience is that categorization of the allegations may be applied, and assessments done by category. Having to assess each of them separately, and document that assessment separately, would be impractical when applying the procedures required in paragraph 55.

Finally, we are struggling with how the application material in paragraph A149 of ED-240 provides guidance for evaluating the appropriateness of the entity's process to investigate a fraud or suspected fraud. Rather, the considerations focus on the auditor's understanding of the entity's process to remediate the fraud or suspected fraud (i.e., how management responded to any misstatements, how management responded to the fraud, how management addressed control deficiencies and the outcomes of the process). We nevertheless support the guidance because it is consistent with our recommended revision above to paragraph 55(b) to require the auditor to understand whether management's response to the matter is appropriate. If the IAASB decides to retain the requirement for the auditor to evaluate the entity's process to investigate the matter, we suggest that the IAASB include application material to better explain how the auditor would do that, which could include the auditor considering the objectivity and competence of those investigating the matter.

Evaluation of whether the financial statements are materially misstated

We suggest that the requirements in paragraphs 58 and 59 of ED-240 be merged as we believe the required procedures would be the same whether the financial statements are materially misstated, or whether the auditor is unable to conclude whether the financial statements are materially misstated.

58. If the auditor determines that the financial statements are materially misstated due to fraud or the auditor is unable to conclude whether the financial statements are materially misstated due to fraud, the auditor shall:

(a) Determine the implications for the audit and the auditor's opinion on the financial statements in accordance with ISA 705 (Revised); and

(b) If appropriate, obtain advice from legal counsel.

59. If the auditor is unable to conclude whether the financial statements are materially misstated as a result of fraud, the auditor shall determine the implications for the audit or the auditor's opinion on the financial statements in accordance with ISA 705 (Revised).

Communications with management and those charged with governance

Paragraph 67 of ED-240 that addresses required communication with those charged with governance about identified or suspected fraud has not been revised from extant ISA 240, as it continues to limit communication of fraud to only those matters involving management, employees who have significant roles in internal control, and others where fraud results in a material misstatement of the financial statements. We believe this

requirement should be better linked to paragraph 55 of ED-240 as communications with those charged with governance may be needed to obtain the required understanding of a fraud or suspected fraud.

In addition, the communication requirement in paragraph 67 of ED-240 does not align with either the communication requirement for instances of non-compliance with laws and regulation in ISA 250 (Revised) or the ED-240 proposed changes to the auditor's report. We point out the following inconsistencies that require revisions either in ED-240 or as conforming changes to other ISAs:

The requirement in paragraph 67 of ED-240 only requires communication with those charged with governance in certain situations, while the proposed amendments to paragraph 40 of ISA 700 includes a statement in the auditor's report that the auditor communicates any identified fraud or suspected fraud to those charged with governance.

Because fraud is defined to be a matter involving non-compliance with laws and regulations, instances of identified or suspected fraud would also seem to be subject to paragraph 23 of ISA 250 (Revised), which requires communication with those charged with governance other than when the matters are clearly inconsequential, which is not consistent with the scope of communications required by paragraph 67 of ED-240 or the scope of communications described in the auditor's report.

We suggest that the IAASB align the scope of required communications with those charged with governance in ED-240 about identified and suspected fraud to the current communication requirement in ISA 250 (Revised) to communicate matters unless they are clearly inconsequential. We also suggest conforming changes to the proposed description of the auditor's communication responsibilities for fraud in the auditor's report.

Finally, we suggest that the IAASB consider providing a link between paragraphs A183 of ED-240 that describes communication with management about instances of fraud and the new requirement in paragraph 55 of ED-240 for the auditor to make inquiries of management about instances of fraud or suspected fraud as part of obtaining an understanding of the matter, as these communications may occur concurrently.

KPMG International

Agree, with comments below

We are supportive of the enhancements to ED-240 in this area, which we believe will drive a robust work effort. In particular, we are supportive of the inclusion of the separate section, entitled "fraud or suspected fraud", to address such instances of fraud or suspected fraud, which we consider would give this part of the audit greater prominence, as well as the explicit requirements for the auditor to first understand the matter, including the entity's process to investigate and remediate, if any. Whilst certain of these requirements are implicit in the extant standard, we believe these enhancements will provide greater clarity and drive greater consistency and a more focused auditor response.

However, we have certain concerns and make recommendations to further clarify/enhance the requirements in this area, as we set out below.

Scalability Considerations

We have concerns and recommendations in relation to the scalability of the requirements at paragraph 55-56 to situations where a fraud or suspected fraud is not considered material. Whilst we note that paragraphs 57-59 are inherently scalable, as well as including specific reference to materiality determinations (from both a quantitative and qualitative perspective), we believe the requirements at paragraph 55-56 may be unnecessarily onerous in certain circumstances, for example:

In respect of audits of larger and more complex entities, including large group audits, as well as audits of entities with operations in multiple locations, e.g., retail entities, where multiple non-material frauds may occur across the entity/group, paragraph 55 appears to require the engagement team to obtain a detailed understanding of every instance of a fraud in order to determine the effect on the audit engagement. Paragraph 56 also requires the (group) engagement partner to consider each and every instance of fraud.

We recommend that additional application material be developed to enable these two requirements to be more scalable. For example, the auditor could be permitted to group frauds that are similar in nature together when performing the procedures in paragraphs 55 and 56, and perform the procedures on selected items within the group to obtain sufficient understanding in order to determine the effects on the audit engagement.

Additionally, where the auditor has determined that such frauds do not involve senior management, the auditor may consider establishing a filter mechanism, such as size thresholds, to determine whether they are required to perform all the procedures required by paragraphs 55-56.

We think it would also be useful to recognize that there may also be circumstances where the auditor may be able to conclude that a fraud is an isolated instance and clearly quantitatively and qualitatively immaterial without performing all of the procedures required in paragraphs 55 and 56. Therefore, it would be useful to acknowledge that the auditor can exercise professional judgment in determining whether all of the procedures in paragraphs 55 and 56 are necessary to make the determinations;

Paragraph 56 of ED-240 explicitly requires the engagement partner to determine, based on the understanding in accordance with paragraph 55, whether to perform additional risk assessment procedures and to design and perform further audit procedures to appropriately respond to the risks of material misstatement due to fraud. In certain circumstances, e.g., when auditing a large group, it may be unduly onerous to require the (group) engagement partner to fulfil this requirement. Accordingly, we suggest that the requirement be modified for the engagement partner to “take responsibility” for these determinations, to enable appropriate involvement of others within the engagement team;

We note that Paragraph 7 states that “suspected fraud includes allegations of fraud that come to the auditor’s attention during the course of the audit”, and related application material at A10 states that “allegations of fraud by another party involving the entity are treated by the auditor as suspected fraud once the allegations have come to the auditor’s attention” and “the auditor performs audit procedures in accordance with paragraphs 55–59 to address the suspected fraud”. Whilst we agree that instances of fraud/suspected fraud may be identified as a result of such allegations initially, e.g., allegations made via an entity’s whistleblowing hotline, we believe that the allegations captured may be broad and application of all the requirements at paragraphs 55-59 to all such allegations would not be appropriate in all circumstances. For example, the procedures applicable to respond to a serious allegation also appear to be required to respond to a complaint that the auditor may relatively quickly determine was baseless (such as a complaint made via a whistleblowing hotline by a single disgruntled former employee, which the entity has investigated and determined to be clearly without merit, which ED-240 itself discusses in the first example at paragraph A148).

Accordingly, we recommend that, based on the audit procedures performed in accordance with paragraph 55(a), if the auditor evaluates that management’s process to investigate the matter is appropriate in the circumstances, and that management’s assessment of the allegation of fraud by another party involving the entity is baseless, then it is no longer a suspected fraud and paragraph 55 parts (c), and (d), and paragraph 56, are no longer applicable;

We welcome the reference in the application material, at paragraph A146, to the involvement of an auditor’s expert, such as a forensics expert. To further enhance this material, and recognising that this is likely to be

applicable in the context of an audit of a larger and more complex entity, we recommend that the guidance focus on more specific matters that the expert may assist with, such as in evaluating whether the entity's investigation process is appropriate, and their remediation measures effective, as well as whether (significant) control deficiencies exist.

Additionally, and as we highlight in our response to Question 1, fraud is distinguished from error as it involves intent, however, it may be challenging for auditors to determine whether intent is, in fact, present. We recommend that this be discussed in the application material in respect of understanding the fraud/suspected fraud, and further guidance be

provided as to how the auditor may approach making this determination, which may require the involvement of an expert, such as a forensics or legal expert.

We believe there is a lack of clarity regarding the applicability of paragraph 66. We note that both paragraphs 55 and 66 state "if the auditor identifies fraud or suspected fraud, the auditor shall...". In respect of paragraph 55, we believe that the requirements would apply to all instances of fraud, whether identified by the auditor directly, or identified by management and communicated to the auditor, as, irrespective of the origin of the identification, the auditor would need to understand the matter further to determine the effect on the audit engagement. However, in respect of paragraph 66, we do not consider it necessary or appropriate for the auditor to communicate fraud or suspected fraud already identified by the entity to management and TCWG, and instead believe this requirement should focus only on those frauds or suspected frauds identified by the auditor directly. We recommend that the IAASB clarify this, to avoid unnecessarily onerous communication requirements being placed on the auditor, and to avoid undermining the impact of such communications with unnecessary information that management and TCWG are already aware of.

Structure and Flow of the Proposed Standard

We also set out certain concerns and recommendations in relation to the proposed structure and flow of the standard in Appendix 1 to this response.

7. Member Bodies and Other Professional Organizations

Federación Argentina de Consejos Profesionales de Cs. Económicas

Answer 4: We consider that the requirements established when cases of fraud or suspected fraud are identified in the audit are appropriate.

The application material in particular has tripled with respect to the current ISA 240, being able to find important details for the development of the audit

Korean Institute of Certified Public Accountants

Agree, with comments below

The KICPA agrees that the ED establishes robust work effort requirements and application material to address circumstances when instances of 'fraud or suspected fraud' are identified in the audit.

Paragraph 57 of the ED describes the actions the auditor shall take when the auditor identifies a material misstatement due to fraud. However, the procedures outlined under (b)/(c) of the same paragraph are considered to be necessary when 'fraud or suspected fraud' is identified, even if the auditor doesn't identify a misstatement due to fraud.

(b) Determine the implications of the misstatement in relation to other aspects of the audit, including when the auditor has reason to believe that management is involved; and

(c) Reconsider the reliability of management's representations and audit evidence previously obtained when the circumstances or conditions giving rise to the misstatement indicate possible collusion involving employees, management or third parties

The KICPA hopes that clearer explanation is provided with regard to the above.

Chartered Accountants Australia and New Zealand and the Association of Chartered Certified Accountants

Agree, with comments below

While we agree that ED-240 establishes robust work effort requirements and application material to address circumstances when instances of fraud or suspected fraud are identified in the audit, we suggest that the following areas should be further clarified:

While we understand that fraud may be qualitatively material, the current drafting of paragraph 55 seems to capture even inconsequential instances of fraud without any reference to materiality. We therefore suggest further clarification here.

According to paragraph 7 suspected fraud includes allegations of fraud that come to the auditor's attention during the course of the audit, however, the application material seems to consider all allegations as suspected fraud even if they are weak in nature. We therefore suggest adding some examples to further clarify the work effort depending on the circumstances.

Institute of Chartered Accountants of Jamaica

Agree, with comments below

Several of the clauses of the exposure draft introduce additional work effort for the external auditor. This will have significant cost implications for audit clients and audit firms. Therefore, there will need to be appropriate guidance to help the external auditor achieve the right cost/benefit balance in planning the audit response.

Institute of Singapore Chartered Accountants

Agree, with comments below

Determining the effects of fraud on the audit

This would be challenging in situations where fraud is perpetuated by senior management or personnel who play a significant role in internal control. More guidance is needed on assessing the effects in such situations, for example, whether a controls reliance strategy is still appropriate.

In addition, while paragraph 55 requires the auditor to evaluate management's process and remedial actions in response to the fraud or suspected fraud, where applicable, it would be difficult for the auditor to determine the effects on the audit if these are not in place. More guidance on how the auditor's assessment would be affected in the absence of management's process and actions would be helpful.

Accountancy Europe

Agree, with comments below

As per paragraph 7, which impacts the understanding of the proposed definition, suspected fraud includes allegations which may be unjustified or clearly superficial. This is too onerous and will lead to impracticalities.

There needs to be a clear distinction between persuasive allegations and possibly vexatious allegations. A good first step for any auditor, when faced with a suspected fraud or an allegation, would be to obtain an

understanding of the matter by, for instance, reviewing relevant whistleblower files and inquiring individual(s) responsible for the entity's whistleblowing program.

We understand that paragraphs 55-59 are conditional requirements applicable to cases where the auditor identifies an instance of fraud or suspected fraud. The implications of such an identification will be different if the management had not been aware of the instance prior to the auditor's identification. In such cases, the auditor should consider if this is an indicator of a significant internal control deficiency and consider the need to revise their risk assessment. This distinction is not recognised in ED-ISA 240.

Chamber of Auditors of the Czech Republic

Agree, with comments below

We propose to add to A 158 an example when a manager-owner commits fraud.

ASEAN Federation of Accountants

Agree, with comments below

Also, it would be challenging in situations where fraud is perpetuated by senior management or personnel who play a significant role in internal control. More guidance is needed in assessing the effects in such situations, for example, whether a controls reliance strategy is still appropriate. Also,

more guidance on how the auditor's assessment would be affected in the absence of management's process and actions would be important.

International Federation of Accountants

Agree, with comments below

The work effort requirements and application guidance are robust, but there are a few challenges we raise. The wording of proposals in ED-240 could do more to clarify the difference between suspected fraud and alleged fraud. The difference can be significant as baseless allegations may be more commonplace in some jurisdictions and in some sectors, although we acknowledge some work would still be appropriate if these allegations could have a significant impact. Clarifying terminology and approach to remove any confusion in this area could be beneficial for users.

The public interest table (B.19) clarifies that "the fraud or suspected fraud requirements in paragraphs 55–59 apply to all instances of fraud or suspected fraud identified by the auditor, irrespective of materiality, and that the auditor is required to apply some or all of those requirements before determining the implications of the fraud or suspected fraud on the audit, including whether it is inconsequential." Ultimately, the expectations in this area remain unclear with regards to the level of enquiries and work that need to be conducted in relation to non-material fraud.

Internal consistency in terminology within standards is an area where we often receive feedback that improvements would be helpful. There are some examples where wording in the requirements and associated application guidance in this area may create issues. Specifically, Paragraph 55(c) and A151 use the expression "remediation measures", while the third example in A41 and Appendix 1 use the similar expression "remedial action(s)". In addition, in the current International Standards of Quality Management (ISQMs) and International Standards on Auditing (ISAs), "remedial action (s)" is often used (for example, ISQM 1 paragraph 42, ISA 250 paragraph A25, ISA 265 paragraph A1, etc.) and "remedial measures" is not used. It is not clear whether there is any intended difference between these terms, but we presume the lack of clarity means that

this is not the case. If this is correct, then it would be useful to align terminology with the existing expression "remedial action (s)."

Similarly, in Paragraph 55 (a) through (c), the expression "the matter" is used to refer to the identified fraud or suspected fraud, but in Paragraph 55 (d), "identified fraud or suspected fraud" is used. Again, it would be useful to harmonize the expressions if they are intended to have the exact same meaning. The presence of inconsistent terms can create ambiguity which may pose challenges for both users of the English version of the standard and for translations.

Finally, as fraud in one entity can sometimes also result in fraud at a counterparty, it may be useful to flag to auditors that communication with the auditor of that counterparty in relation to potential fraud could be appropriate in certain circumstances. We note that legislation or other requirements may prevent this in certain jurisdictions and instances, so any mandated requirement for communication would be inappropriate, but situations can be envisioned where such communication would be in the public interest.

CPA Ontario Small and Medium Practices Advisory Committee

Agree, with comments below

The EM explains that ED-240 significantly expands the requirements and guidance on how auditors should respond when fraud or suspected fraud is detected. This includes determining the implications for the audit and the necessary modifications to the audit approach. This section underscores the need for auditors to reassess the risk assessment and modify the nature, timing, and extent of further audit procedures to respond adequately to the identified risks.

Section 1-E (Paragraph 35) discusses the ongoing nature of communications with management and those charged with governance about fraud-related findings. It emphasizes the importance of clear and timely communication to ensure that those responsible for governance are fully aware of the issues and can take appropriate actions.

Paragraphs 55–59 provide detailed requirements for the auditor's actions upon the identification or suspicion of fraud. This includes assessing the implications of the fraud on the audit, evaluating whether the fraud indicates a significant deficiency in the entity's internal control, and considering the effect on the reliability of management's representations.

Paragraphs 66–69 outline the requirements for communicating about fraud with the appropriate level of management and with those charged with governance. The standard specifies that auditors should inform the appropriate level of management at least one level above those involved in the fraud, and, where fraud involves senior management, the auditor should report the matter directly to those charged with governance.

Together, these sections ensure that auditors are equipped with clear guidelines to adequately address and respond to fraud or suspected fraud. The standards aim to enhance the auditor's ability to perform diligent and responsive audit procedures, ensuring that all relevant parties are appropriately informed and that the integrity of the audit process is maintained.

Institute of Certified Public Accountants of Uganda

Agree, with comments below

We believe that the ED-240 establishes robust work effort and application material to address the circumstances when instances of fraud or suspected fraud are identified in the audit.

However, we recommend that Paragraph 56 of ED-240 be amended to require the engagement partner to take responsibility for the performance of additional risk assessment procedures and for the design and performance of further audit procedures in response to the risks of material misstatement due to fraud.

Asociacion Interamericana de Contabilidad

Agree, with comments below

We believe that the requirements established when cases of fraud or suspected identified fraud in the audit are Adequate. We found an adequate amount of material application in the draft.

Yes, ED-240 establishes robust work effort requirements and provides detailed application material to address circumstances when instances of fraud or suspected identified fraud in the audit. The document reinforces the need for auditors to take concrete actions and adequately document their findings and responses to the detection of indications of fraud. It states that auditors should adjust their audit procedures and consider the implication of fraud findings on the rest of the audit, ensuring that responses are commensurate with the risks identified. In addition, ED- 240 guides auditors on how to communicate effectively fraud issues to management and those charged with corporate governance, highlighting the importance of transparency and collaboration to mitigate the effects of detected fraud. It also provides guidance on reconsidering the risk assessment and the need to review related areas that may be affected.

Pan-African Federation of Accountants

Agree, with comments below

We agree that ED-240 establishes robust work effort requirements, however, some stakeholders have raised concerns about their applicability to different fraud or suspected fraud scenarios. Specifically:

ED-240 doesn't differentiate between the auditors' required response to confirmed fraud versus suspected fraud and doesn't consider how this may differ depending on the source of the information.

While the explanations in paragraphs 54 – 57 of the Explanatory Memorandum is acknowledged, we believe that ED-240 can benefit from further enhancements, using the requirement in ED-240 paragraph 55 as an example.

For confirmed fraud:

May auditors rely on internal investigation reports, or is an independent investigation necessary?

How does the auditor evaluate whether the remedial actions are appropriate?

For suspected fraud:

What should auditors do if inquiries do not yield further information and management takes no action?

Is there a requirement for auditors to engage an investigator or expert to assess the need for an investigation?

ED-240 doesn't address how the auditor must respond to suspected fraud under investigation.

An ongoing investigation can significantly delay the financial statements due to uncertainties related to suspected fraud, which is not in the public interest. For ongoing investigations, we question:

Whether the auditor can conclude the audit (assuming this is also allowed legally)?

What intermediate actions the auditor must take in the public interest?

ED-240 doesn't address how the auditor must respond when they suspect management or those charged with governance of fraud.

Assuming the auditor is unable to obtain further information, and therefore unable to perform the procedures in paragraphs 56 – 59, we question:

Is it sufficient for auditors to seek legal advice and consider withdrawal, or are there minimum procedures to follow / complete first?

How does the auditor comply with the requirements in ED-240 paragraph 60, such as the requirement to identify a misstatement and communicate with the appropriate level of management and those charged with governance about the auditor's withdrawal from the engagement and the reasons for the withdrawal.

ED-240 doesn't address how the auditor must respond when, under circumstances of suspected management or those charged with governance involvement in fraud, the auditor is requested to resign as auditor.

We recommend that the IAASB provides clearer distinctions and guidance for auditors facing different fraud scenarios, including those involving management and governance. The IAASB may take into consideration developing a flow chart to direct the auditor's response to fraud or suspected fraud.

Malaysian Institute of Accountants - Auditing and Assurance Standards Board

Agree, with comments below

8. Academics

University of KwaZulu-Natal

Agree, with comments below

Paragraphs 6-8 of ED should be referenced as these paragraphs are part of fraud identification.

Accounting and Finance Association of Australia and New Zealand

Agree, with comments below

We agree that ED-240 establishes more robust work effort requirements, but there is an opportunity to enhance application and other explanatory material to improve auditors' understanding of, and response to, fraud or suspected fraud.

Research suggests that managers may have a preference for fraudulent activity that involves omission rather than commission (Hamilton and Smith 2021). Concerningly, this same research also highlights that auditors may perceive omissions as being less serious than commissions. Relatedly, auditors apply less scepticism to excuses for an omission (i.e., a management contention that the omission was unintended) (Hamilton et al. 2024). Paragraph A3 in ED-240 notes the prospect of omissions giving rise to intentional misstatements. We believe that this should be supplemented by expanding paragraph A152 to reinforce that the requirements in paragraph 56 are unaffected by whether the fraud or suspected fraud is characterised by commission or omission.

Hamilton, E.L., and Smith, J.L. 2021. Error or Fraud? The effect of omissions on management's fraud strategies and auditors' evaluations of identified misstatements. *The Accounting Review* Vol.96, No.1, pp.225-249.

Hamilton, E.L., Smith, J.L., and Carlisle, M. 2024. Explaining away intentional misstatements: Do management-provided excuses decrease auditor skepticism?. Auditing: A Journal of Practice & Theory Vol.43 No.1, pp.151-166.

9. Individuals and Others

John Keyser

Agree, with comments below

The new proposed requirement in paragraph 55 is appropriate and, I believe, reflects something that most firms are (or should) already be doing. If the auditor becomes aware of fraud or suspected fraud, I don't know how they could conclude that the financial statements are free of material misstatement without having first met the proposed paragraph 55 requirement.

I strongly agree with the guidance in application paragraph A150 and A151 that an entity's failure to investigate fraud or suspected fraud is indicative of a significant deficiency in internal control.

Ataf Noor Ali Chartered Accountants

R4: Yes.

The reasons for our agreement follows:

4.1 There is now an explicit requirement for an understanding of fraud or suspected fraud. This requires the auditors to make inquiries, evaluate if appropriate where an entity has a process in place to investigate such matter and remedial measures, determine further significant control deficiencies (in the internal control related to the identified fraud and error) exists.

4.11 Explanatory Memorandum paragraph 51 refers to ED240 para 55 (b)-(c): elements of the auditor's understanding. The said reference is not correct. The term 'elements of auditor's understanding' is used with reference to ED240 para 33-38.

4.2 First responsibility of the engagement partner is missing: to provide audit engagement resources to complete the task as in ISQM1. Other three responsibilities of the engagement partner are clear: perform additional risk assessment procedures, design and perform further audit procedures, comply with the additional responsibilities under the law and regulations of the jurisdiction.

4.3 We normally have a difficult time in making management understand why we need a list of changes in the HR. 'What it has to do with the audit?' we often hear. Keep in mind that employees who play a role in perpetuating a fraud may proceed to exit swiftly during the period. Changes in the workforce may leave a trail of incomplete information or obstacles in accessing information. Guidance? ED240 mentions it not.

Colin Semotiuk

Agree, with comments below

Yes, ED-240 appropriately provides requirements and application material when fraud or suspected fraud is identified. This material is appropriately included in ED-240 as it is not overly cumbersome and does not logically fit into other ISAs.

3 Neither agree nor disagree

2. Investors and Analysts

CFA Institute

Neither agree/disagree, but see comments below

See our overall comments in Part A regarding our uncertainty in evaluating whether the proposed changes in ED-240 address shortcomings in existing practice as revealed by recent frauds.

3. Regulators and Audit Oversight Authorities

Committee of European Auditing Oversight Bodies

Given the continuing evolving nature of technology and its importance in many audits, the language in paragraph A36 should be amended to state that the engagement partner would usually be expected to consider expertise in IT systems etc when determining if the engagement team have the necessary competence and capabilities.

In paragraph A147 it would be helpful to include the use of forensic expertise in the second example.

The intent of the examples in paragraph A148 is unclear as the question of what the auditor needs to do in response to such investigations by the entity remains unanswered, such as for example evaluating the expert hired by the entity (as required in ISA 500, paragraph 8).

Additionally, legal privilege could be applicable in investigations by clients, when performed by a lawyer. It would be helpful to give guidance on what an auditor should do with these reports.

In paragraph A152, the IAASB should replace the word ‘believed’ in the first example. Auditors have to perform procedures to determine that the suspected fraud was not material, no management was involved etc. It is not sufficient for an engagement partner to “believe” a suspected fraud to be inconsequential without performing further audit procedures.

Paragraph 14 states that “fraud constitutes an instance of non-compliance with laws and regulations” (NOCLAR). This may also apply the other way around as NOCLAR could also be fraud. This is not clear in the current versions of ED 240 and ISA 250. We urge the IAASB to make amendments and add additional explanations in the final version of ED 240 on this subject to make it clearer. Language such as: ‘Because of the nature of some instances of non-compliance with laws and regulations, they meet the definition of fraud (refer to the definition in paragraph 18a), such as corruption, money laundering and breach of competition law (cartel)’ could be used.

Use of specialists

While ED 240 includes additional material on the use of specialists, it should be made clear that the use of a specialist does not reduce the auditor’s responsibility for the audit. The auditor remains responsible for forming and expressing the audit opinion. In addition, it is important for auditors to be clear on the expertise that they expect from that specialist and the link with the audit engagement. Discussing the need for a specialist’s involvement with TCWG may prove beneficial.

Engagement quality review (EQR)

Additional quality control review procedures focused on the engagement team’s responsibilities relating to fraud should be considered for all engagements where an EQR is required. In particular, the engagement quality reviewer should be required to review the reasons used to conclude that the presumed fraud risk related to revenue recognition has been rebutted.

Communications with TCWG and other parties

Communicating more information to TCWG, including audit committees, and to other authorities allows the entity to take remediation measures in relation to fraud on a timely basis. For example, for PIE audits in the European Union, when an auditor suspects or has reasonable grounds to suspect that irregularities including fraud with regard to the financial statements of the audited entity, may occur or may have occurred, the auditor is required to inform the audited entity and invite it to investigate the matter and take appropriate measures to deal with such irregularities in the future. Where the audited entity does not investigate the matter, the auditor is required to inform the authorities responsible for

investigating such irregularities (for example regulatory and/or enforcement authorities). Those provisions should be fully integrated in the ISAs.

In the same vein, in such circumstances, the IAASB should also consider requiring the auditor to assess whether the measures taken by management are appropriate and evaluate the impact on its relationship with the audited entity.

We urge the IAASB to also reword paragraph 70(d) regarding the documentation required when the presumption related to revenue recognition is “not applicable in the circumstances of the engagement”. It may be seen as an encouragement to auditors to rebut the presumption of fraud risks for all revenue streams in an audit. We suggest that this should be replaced by a requirement to document the analysis to be performed in paragraph 41 (determine which types of revenue exist, revenue transactions and relevant assertions that give rise to fraud risks, including any revenue types where the presumption has been rebutted and the reasons for that conclusion).

Paragraph 70(d) should also stress the need for the documentation to be sufficient to enable another practitioner to understand the rationale for the rebuttal as well as requiring

documentation to show that, where applicable, all the entity’s revenue streams have been considered. This would go some way towards addressing the issues identified in the CEAOB inspections findings database. Additionally, the IAASB should consider including application material to provide guidance for auditors on the documentation that would be appropriate in such cases e.g. engagement team discussions, discussions with technical experts, experience in previous audits and no changes to the revenue streams, internal controls or key client personnel in this area.

Written representations

The statement in paragraph A180 of ED 240 that “although written representations are an important source of audit evidence, they do not provide sufficient appropriate audit evidence on their own about any of the matters with which they deal” should be moved to the requirements section as it is integral to the auditor’s use of written representations. A corresponding amendment should also be made to ISA 580.

Irish Auditing & Accounting Supervisory Authority

Neither agree/disagree, but see comments below

Given the continuing evolving nature of technology and its importance in many audits, the language in paragraph A36 should be amended to state that the engagement partner would usually be expected to consider expertise in IT systems etc when determining if the engagement team have the necessary competence and capabilities.

In paragraph A147 it would be helpful to include the use of forensic expertise in the second example.

The intent of the examples in paragraph A148 is unclear as the question of what the auditor needs to do in response to such investigations by the entity remains unanswered, such as for example evaluating the expert

hired by the entity (as required in ISA 500, paragraph 8). Additionally, legal privilege could be applicable in investigations by clients, when performed by a lawyer. It would be helpful to give guidance on what an auditor should do with these reports.

In paragraph A152, the IAASB should replace the word ‘believed’ in the first example. Auditors have to perform procedures to determine that the suspected fraud was not material, management was not involved etc. It is not sufficient for an engagement partner to “believe” a suspected fraud is inconsequential without performing further audit procedures.

Use of specialists

While ED 240 includes additional material on the use of specialists, it should be made clear that the use of a specialist does not reduce the auditor’s responsibility for the audit. The auditor remains responsible for forming and expressing the audit opinion. In addition, it is important for auditors to be clear on the expertise that they expect from a specialist and the link with the audit engagement. Discussing the need for a specialist’s involvement with TCWG may prove beneficial.

Engagement quality review (EQR)

Additional engagement quality review procedures focused on the engagement team’s responsibilities relating to fraud should be considered for all engagements where an EQR is required. In particular, the engagement quality reviewer should be required to review the reasons used to conclude that the presumed fraud risk related to revenue recognition has been rebutted.

Communications with TCWG and other parties

Communicating more information to TCWG, including audit committees, and to other authorities allows the entity to take remediation measures on a timely basis. For example, for PIE audits in the European Union, when an auditor suspects or has reasonable grounds to suspect that irregularities including fraud with regard to the financial statements of the audited entity, may occur or may have occurred, the auditor is required to inform the audited entity and invite it to investigate the matter and take appropriate measures to deal with such irregularities in the future. Where the audited entity does not investigate the matter, the auditor is required to inform the authorities responsible for investigating such irregularities (Article 7 of Regulation 537/2014/EU). These provisions should be integrated in the ISAs.

The IAASB should also consider requiring the auditor to assess whether the measures taken by management are appropriate and evaluate the impact on its relationship with the audited entity.

Written representations

The statement in paragraph A180 of ED 240 that “although written representations are an important source of audit evidence, they do not provide sufficient appropriate audit evidence on their own about any of the matters with which they deal” should be moved to the requirements section as it is integral to the auditor’s use of written representations. A corresponding amendment should also be made to ISA 580.

European Securities and Markets Authority

For ESMA, it is key that communication between the auditor, TCWG and management is constant and ongoing. Therefore, ESMA is of the view that when grounded signals exist of fraud being committed or suspected fraud, the engagement partner should have reinforced responsibilities to enquire the management and the TCWG to understand if those signals or suspicions materialise. Furthermore, ESMA considers that the engagement partner and/or the auditor should consider involving the relevant authorities (either criminal or regulatory) without undue delay in specific circumstances. To this end, ESMA is of the view that this aspect

should be explicitly referred to in paragraph 58 of the ED-240 by including a cross reference to paragraph 69 (a). Provided that no legislative impediments exist, a prompt communication could enable the relevant authorities (such as securities regulators) to timely act to safeguard the public interest.

4. Jurisdictional and National Auditing Standard Setters

Wirtschaftsprüferkammer

As mentioned above, we basically would like to emphasize the importance of clearly articulating that the audit of the financial statements should not be mistaken for a forensic audit.

Moreover, the extensive requirements in paragraph 55 need not only to be applied to instances of fraud but also to instances of suspected fraud. However, the term “suspected fraud” is not defined in the proposed ED-240. Paragraph 7 merely states that „suspected fraud includes allegations of fraud that come of the auditor’s attention during the course of the audit“. Paragraph 8 adds that „the auditor’s determination of whether a fraud or suspected fraud is material to the financial statements involves the exercise of professional judgment“.

We recommend to give more guidance as to how the auditor shall deal with allegations of fraud and under which conditions such allegations need to be addressed as suspected fraud applying the requirements of paragraph 55. A revision in this respect is encouraged.

With regard to specific proposed provisions we are particularly concerned that the requirements in paragraph 55 need not only to be applied to instances of fraud but also to instances of suspected fraud, especially due to the fact that the term “suspected fraud” is not defined in the proposed ED-240.

Institut der Wirtschaftsprüfer in Deutschland

Neither agree/disagree, but see comments below

With the exception of the matters that we address in our response to this Question, we generally agree with the work effort requirements and application material to address circumstances when instances of fraud or suspected fraud are identified in the audit. In particular, we refer to our response to Question 1 on alleged fraud vs. suspected fraud, where we make the case that alleged fraud and suspected fraud need to be distinguished from one another in the standard and therefore do not agree with the work effort proposed in the draft for alleged fraud due to alleged fraud being conflated with suspected fraud.

For example, paragraph 29(b), presumes that any allegation of fraud is suspected fraud. However, if the auditor is more familiar with the circumstances than the alleging party or the allegations are clearly spurious, in line with our response to Question 1, it does not automatically follow that every alleged fraud is suspected fraud and that therefore, unless alleged frauds are determined to be suspected frauds, would not have an impact on the overall audit strategy and audit plan. Likewise, with the exception of our comments below, all of the requirements in paragraphs 55 and 56 and their corresponding application material appear to be appropriate for suspected fraud, but not necessarily for alleged fraud. For example, unlike suspected fraud, alleged fraud would not lead to the auditor:

determining the effect on the audit, unless the understanding that the auditor obtains of the matter based upon the auditor’s knowledge and inquiries about the matter with a level of management that is at least one level above those that are allegedly involved leads to the auditor concluding that the alleged fraud is suspected fraud (paragraph 55 introductory phrase and (a)) evaluating whether the entity’s process to investigate the matter is appropriate, unless the auditor concludes that the alleged fraud is suspected fraud evaluating remediation measures that the entity has implemented – in fact, the entity would not have any such measures in this case (55(c)) determining whether control deficiencies exist.

Treating alleged fraud the same as suspected fraud may also lead to dysfunctional work effort for auditors when so-called “allegation bombing” occurs – that is, cases in which companies may be inundated with allegations from campaign groups trying to obtain an – objectively unjustified – focus on their concerns. With ever more sophisticated automated tools generated by artificial intelligence, this danger is increasing as can be seen by the prevalence of manipulation of online product and service reviews. The IAASB needs to anticipate such issues, that may be exacerbated by technology, to “future-proof” the standard.

Since in paragraph 55(d) the auditor is only concerned about significant deficiencies in controls relating to the prevention or detection of material misstatements due to fraud, the words “material misstatements due to” should be inserted prior to the word “fraud”.

The wording in paragraph 59 needs to be aligned with that used for scope limitations in the ISAs, which means the wording of the sentence should start as follows: “If the auditor is unable to obtain sufficient appropriate audit evidence to enable the auditor to conclude whether....”.

In relation to paragraph A144, which applies to both identified fraud or suspected fraud, the ending of the sentence only refers to fraud, but not suspected fraud. Consequently, “or suspected fraud” should be added at the end of the sentence. With respect to second bullet point, it is not clear whether the auditor’s or the entity’s external counsel is meant (unlike in paragraph A146, where this is specified). We suggest inserting “the auditor’s” prior to “external”. If the entity’s external counsel is meant, then clarification would need to be given that management of the entity would need to permit its external counsel to consult with the auditor.

In relation to the first sub-bullet of the third bullet of paragraph A146, reference is made to making further inquiries of the entity’s external legal counsel. Clarification should be given that management of the entity would need to permit its external counsel to consult with the auditor.

In relation to paragraph A146, an additional consideration for the auditor when evaluating the appropriateness of the entity’s process is whether the cost of the entity’s process for responding to immaterial fraud and addressing control deficiencies regarding the prevention or detect of fraud, or whether the outcome of the process is likely to prevent the reoccurrence of fraud, is worth the benefits. For example, in some circumstances, immaterial fraud by third parties (e.g., customers) is regarded as a cost of doing business because the costs seeking to prevent or detect the fraud exceed the cost of the fraud. We also note that in the second bullet the reference to “or suspected fraud” should be deleted because the outcome of a process is supposed to prevent fraud, not suspected fraud.

In relation to the first bullet of paragraph A150, we note that the consideration in that bullet point should extend to not only the susceptibility of a loss due to fraud, but also the potential size of the loss due to fraud. The wording should therefore be changed to read: “The susceptibility and potential size of the loss due to fraud...”.

While paragraph A151 addresses indicators of significant deficiencies in internal control, it does not address the countervailing aspect when these indicators may not apply. In particular, the paragraph does not address situations where the costs of controls to prevent or detect non-material fraud considerably exceed the cost of the fraud, in which case these indicators of significant deficiencies would not apply.

Paragraph A153 addresses the fact that sometimes extending an audit reporting deadline may not be possible under applicable law or regulation. We believe that this paragraph confuses the reporting deadlines of the entity with auditor responsibilities. The fact that an entity may have reporting deadlines for issuing audited financial statements set forth in law or regulation (or otherwise set by the entity) does not mean that auditors are required to meet those deadlines if circumstances do not permit the auditor to do so. In particular, auditors cannot issue a modified opinion due to a scope limitation unless the auditor is unable to obtain sufficient

appropriate evidence – regardless of whether the auditor needs more time to determine that the auditor is or is not able to obtain that evidence: there are no “self-imposed” scope limitations for auditors. For these reasons, we believe that this paragraph needs to clearly distinguish between entity deadlines and auditor responsibilities and clarify that there are no auditor-imposed scope limitations in this respect.

5. Accounting Firms

Crowe

Neither agree/disagree, but see comments below

We believe that the revised requirements for when instances of fraud or suspected fraud are identified in the audit will drive more consistent auditor behavior and responses. However, we are concerned about the scope and scalability of the proposal.

The proposal indicates that “For all instances of fraud or suspected fraud identified by the auditor, ED-240 requires the auditor to apply at least some of the fraud or suspected fraud requirements that are applicable in the circumstances to determine the effect on the audit engagement.” Conceptually we agree with this, as it is critical for the auditor to sufficiently understand any fraud or suspected fraud matter to be able to perform a thorough risk assessment, to determine the appropriate audit response. However, we believe that certain of the proposed requirements appear to be overly prescriptive, for example in a case where management identified fraud which was deemed to be clearly not material, yet management communicated the matter to the auditors (e.g., a bank teller misappropriating cash from a teller drawer).

Specifically, ED-240 requires the auditor to perform procedures prescribed in paragraph 55 (a) through (d), and to apply the determinations required in paragraph 56. We understand that based on this process, portions or all of paragraphs 57-58 may not be applicable; this does provide some scalability. However, as noted in our response to Question 1, we believe there could be instances where an auditor is able to quickly determine, based on their professional judgment, that there is not a risk of material misstatement to the financial statements related to a particular fraud or suspected fraud matter. This could be because the fraud or suspected fraud matter was deemed to be clearly inconsequential. In these cases, the performance of all the procedures included in paragraphs 55 through 57 would not appear to be necessary.

Again, as stated in paragraph 6 of ED-240, “the auditor is concerned with a material misstatement of the financial statements due to fraud.” We believe that the requirement in ED-240 paragraph 55(a) for the auditor to make inquiries about the matter with a level of management that is at least one level above those involved and, when appropriate with those charged with governance, is critical to the auditor gaining an understanding of the matter. These inquiries should include how management responded to the matter. Based on the auditor’s understanding, including inquiries made, the auditor should exercise professional judgment to determine if further procedures, including further risk assessment, are needed relative to the identified matter. For a matter that is deemed by the auditor to be clearly inconsequential or to have no possible risk of material misstatement to the financial statements, further procedures should not be required. We propose that the requirements of paragraphs 55 (b) through (d), 56, and 57 should not be explicitly required if the auditor has determined that there is not a reasonable possibility of a related risk of material misstatement.

We also believe that it would be appropriate for the requirements in paragraph 56 to be performed by someone other than the engagement partner, given the engagement partner’s overall responsibility for review and supervision. Therefore, we recommend that paragraph 56 be revised as follows: “Based on the understanding obtained in accordance with paragraph 55, the auditor engagement partner shall:”.

Paragraph 55a in ED-240 requires the auditor to make inquiries about a fraud or suspected fraud “with a level of management that is at least one level above those involved” with the matter. This appears to be too prescriptive as a requirement. We recommend the requirement be revised to require the auditor to make inquiries with an appropriate level of management. We believe it would be appropriate to include application guidance indicating that an effective approach is to make the inquiries about the matter at least one level above those involved.

Baker Tilly International

Neither agree/disagree, but see comments below

The criticism of auditors is that they do not detect enough fraud, not what they do once fraud is suspected or detected.

Crowe Global

ED-240 does establish robust work effort requirements and application material to address circumstances when instances of fraud or suspected fraud are identified in the audit. However, for a matter that is deemed by the auditor to be clearly inconsequential or to have no possible risk of material misstatement to the financial statements, further procedures should not be required.

6. Public Sector Organizations

Government Accountability Office – United States

We believe that the IAASB should consider if the work effort requirements and application material exceed what may be appropriate when instances of fraud or suspected fraud are identified at the auditee during the audit. In ED-240 paragraph 55, the requirements in (a) through (d) for fraud or suspected fraud apply without consideration for materiality. In addition, we believe (a) through (d) in paragraph 55 go beyond “obtain an understanding of” by evaluating and making determinations. We recommend revising the requirements to align the work efforts in paragraph 55(a) through (d) with those appropriate for “obtaining an understanding” and consider whether these procedures are appropriate for every instance of fraud or suspected fraud, even those that are clearly insignificant to the risk of material misstatement of the financial statements. Further, paragraph A10 provides guidance for responding to suspected fraud by an outside party. We suggest the paragraph more clearly refer to third-party fraud or suspected fraud consistent with other sections of ED-240.

Riksrevisionen (Swedish National Audit Office)

Neither agree/disagree, but see comments below

In paragraph 7 the standards state that the auditor shall consider any information received about suspected fraud. The application material (A10) states that the auditor should also consider information received from external sources or whistleblowers. The auditor is guided to perform certain procedures based on the information. These procedures may be overwhelming and specifically performing the procedures in paragraph 55, before even concluding on whether the information is relevant for the audit. Specifically point d) in paragraph 55.

There are numerous false accusations, and specifically it could be so in the public sector. This could lead to a waste of audit resources and auditors focusing on issues not relevant to the audit.

Our suggestion is that the requirement and application material should clarify that the auditor should assess whether the information is relevant to the audit before doing any additional procedures.

can dismiss the information if not relevant to the audit.

Paragraph 55 states:

"If the auditor identifies fraud or suspected fraud, the auditor shall obtain an understanding of the matter in order to determine the effect on the audit engagement. In doing so, the auditor shall:

- a) Make inquiries about the matter with a level of management that is at least one level above those involved and, when appropriate in the circumstances, make inquiries about the matter with those charged with governance;
- b) If the entity has a process to investigate the matter, evaluate whether it is appropriate in the circumstances;
- c) If the entity has implemented remediation measures to respond to the matter, evaluate whether they are appropriate in the circumstances;
- d) Determine whether control deficiencies exist, including significant deficiencies in internal control related to the prevention or detection of fraud, relating to the identified fraud or suspected fraud.

The writing does not contain references to material misstatements of fraud but any "fraud". It is quite extensive efforts that we are expected to carry out before we have even assessed whether the fraud (suspected fraud) is relevant to the audit. This applies above all to d), which means that we must assess whether the internal control is effective.

Our conclusion is that paragraph 55 may mean that we need to do more work than the audit requires. Our suggestion is that it should be sufficient to carry out a–c to assess whether the irregularity is relevant to the audit.

7. Member Bodies and Other Professional Organizations

European Federation of Accountants and Auditors for SMEs

Neither agree/disagree, but see comments below

We note that in paragraphs 55-59 the public interest table (B.19) clarifies that "the "fraud or suspected fraud requirements" applies to all instances of fraud or suspected fraud identified by the auditor, irrespective of materiality, and that the auditor is required to apply some or all of those requirements before determining the implications of the fraud or suspected fraud on the audit, including whether it is inconsequential." We believe the expectations with regard to the level of enquiries and work that needs to be conducted in relation to non-material fraud is unclear.

Center for Audit Quality

Neither agree/disagree, but see comments below

Scalability of the fraud or suspected fraud requirements

We appreciate the IAASB's efforts to keep the fraud or suspected fraud requirements scalable, but we have concerns that the level of scalability needed to make the standard operable in practice will not be achieved through the requirements as currently proposed. As described in the ED, for all instances of fraud or suspected fraud identified by the auditor, ED-240 requires the auditor to apply at least some of the fraud or suspected fraud requirements that are applicable in the circumstances to determine the effect on the audit engagement.

For all instances of fraud or suspected fraud identified, the auditor is required to obtain an understanding of the matter, including performing the specific procedures outlined in ED-240.55. We understand, as explained in the ED, that the IAASB's basis for including this requirement is that obtaining an understanding of the fraud

or suspected fraud in accordance with paragraph 55 is necessary to inform the determinations required in paragraph 56. The ED further explains the IAASB's view that scalability has been introduced into ED-240 because, depending on the nature of the fraud or suspected fraud and the determinations made by the engagement partner in accordance with paragraph 56, some of the fraud or suspected fraud requirements [those in paragraphs 57 through 59] may not be applicable.

We acknowledge that some level of scalability will be achieved as described in the ED, however, we are concerned that the proposed requirements are not sufficiently scalable. The requirement for the auditor to perform the procedures described in ED-240.55 for all instances of fraud or suspected fraud could be read as including matters that are easily identified as clearly inconsequential and unlikely ever to result in a material misstatement of the financial statements, as well as matters that do not relate to fraudulent financial reporting or misappropriation of assets. Further, it is unclear from the Explanatory Memorandum as to the intent of paragraph 55 and whether each element of the requirement needs to be applied for every identified fraud or suspected fraud, including those that are clearly inconsequential.

We acknowledge that, with respect to some instances of fraud or suspected fraud, performing the procedures described in paragraph 55 would be necessary in order for the auditor to obtain an understanding of the matter sufficient to enable the auditor to appropriately evaluate management's conclusions as to whether fraud occurred and, if so, the impact on the financial statements and the audit. However, there may be many instances of fraud or (likely more commonly) suspected fraud for which the auditor will be able to appropriately reach such conclusions without performing all (or potentially any beyond inquiry) of the procedures described in paragraph 55. For example, at many large public companies, whistleblower hotlines may yield lists of hundreds or potentially even thousands of matters per year, many of which may have the potential to relate to fraudulent financial reporting or misappropriation of assets. According to a report from Navex, there were 1.86 million whistleblower reports in 2023 (across 3,784 organizations and 57 million employees). The median overall substantiation rate, meaning allegations that when investigated prove to be correct or partially correct, was 45% (i.e., majority of allegations were unsubstantiated). Additionally, not all of these substantiated allegations would be considered fraud in accordance with ISA 240/ED-240, as not all relate to fraudulent financial reporting or misappropriation of assets.

We believe that, if not clarified, the requirements in ED-240.55 would be overly prescriptive, are not suitable for a principles-based standard, and could result in auditors expending significant amounts of time and effort performing and documenting procedures that are unnecessary to achieve the objective of assessing and responding to risks of material misstatement to the financial statements. In order for the requirements of ED-240 to be appropriately scalable, we believe it is important that the auditor is able to exercise professional judgment in determining which matters they need to understand and what procedures are necessary to perform in order to obtain a sufficient understanding of those matters. Additionally, we believe that an increased emphasis in ED-240 on the relevance of management's processes and conclusions related to instances of fraud or suspected fraud to the auditor's risk assessment and related professional judgments could further contribute to its scalability. Accordingly, we recommend that the Board consider making revisions to paragraph 55 of ED-240 to better reflect the auditor's work effort based on the nature of the fraud. That is, that the auditor may not need to perform all of the procedures in paragraph 55 to obtain an understanding of the identified fraud or suspected fraud, sufficient to conclude on next steps, based upon the significance of the identified fraud or suspected fraud (i.e., scalability based on the nature and significance of the identified fraud or suspected fraud). To further clarify this point and enhance the scalability of the standard, we suggest that the Board include additional language in paragraph 6 of ED-240 regarding the auditor's responsibility related to matters identified that are clearly inconsequential (as reflected in the suggested edits below).

We also have the following additional concerns related to the proposed requirements in paragraph 55:

We believe that the phrase “the auditor identifies fraud or suspected fraud” may be misunderstood by users, irrespective of the key concepts described in paragraph 7. As drafted, the phrase could be interpreted to apply to those fraud matters that have been identified specifically by the auditor and would not include other ways in which the auditor becomes aware of fraud or suspected fraud. Accordingly, we recommend paragraph 55 include “or otherwise become aware of” to clarify and reinforce the scope of the performance requirements in paragraph 55.

We have concerns regarding the requirement to make inquiries of management at least one level above those involved in the matter identified. We believe that in some cases this requirement could, in practice, be difficult to satisfy or demonstrate

based on the entity’s organizational structure and/or the specific facts and circumstances of the matter. We recommend that the requirement in paragraph 55(a) be revised from “with a level of management that is at least one level above those involved” to “with an appropriate level of management.”

Because the auditor may not have enough information to make a determination about whether a control deficiency exists related to the fraud or suspected fraud, we recommend that the requirement in paragraph 55(d) be revised from “determine” to “consider”.

To address the aforementioned concerns, we recommend that the Board consider making the following revisions to paragraphs 6 and 55, which we believe are also better aligned with the IESBA code requirements related to fraud (deletions are struck through, additions are marked as underlined):

6. Although fraud is a broad legal concept, for the purposes of the ISAs, the auditor is concerned with a material misstatement of the financial statements due to fraud. Although the auditor may identify or suspect the occurrence of fraud as defined by this ISA, the auditor does not make legal determinations of whether fraud has actually occurred. Although matters may be identified during an audit that may constitute fraud in a broad legal sense, the auditor is not required to respond to matters that clearly could not result in material misstatement of the financial statements.

55. If the auditor identifies or otherwise becomes aware of fraud or suspected fraud, the auditor shall obtain an understanding of the nature and circumstances of the matter in order to determine the effect on the audit engagement. In doing so, the auditor shall: (Ref: Para. A146–A151)

(a) Make inquiries about the nature and circumstances of the matter and how management has responded to the matter with an appropriate level of management that is at least one level above those involved and, when appropriate in the circumstances, make inquiries about the matter with those charged with governance;

(b) If the results of the procedures in paragraph (a) indicate the matter is other than clearly inconsequential, the auditor shall:

(i) (b) evaluate how management has responded to the matter, including the nature and status of the investigations and remediation measures management has taken or plans to take; and If the entity has a process to investigate the matter, evaluate whether it is appropriate in the circumstances

(c) If the entity has implemented remediation measures to respond to the matter, evaluate whether they are appropriate in the circumstances; and

(ii) (d) consider Determine whether control deficiencies may exist, including significant deficiencies in internal control related to the prevention or detection of fraud, relating to the identified fraud or suspected fraud.

Additionally, we are concerned with the scalability of proposed paragraph 56 of ED-240. ED-240.56(a)(i) and (ii) specifically require the engagement partner “to determine whether to” perform certain risk assessment procedures and design and perform further audit procedures. In some situations, this requirement could pose scalability challenges due to the volume of relevant matters (e.g., in very large audits), and/or language and custom related barriers (e.g., in group audits). While we believe it is appropriate for the engagement partner to take overall responsibility for the audit, including the judgments made and procedures performed by the engagement team in complying with ISA 240, we believe this can be effectively achieved in a more scalable way by requiring the auditor to perform the procedures described in ED-240.56 and adding a broad requirement regarding the engagement partner’s ultimate responsibilities, similar to what is included in ISA 600 (Revised) and ISA 220 (Revised).

Similarly, we are concerned that the requirement in ED-240.56(a)(iii) for the engagement partner to determine whether there are additional responsibilities under, law, regulation, or relevant ethical requirements about the entity’s non-compliance with laws or regulations in accordance with ISA 250 may not be operable in many group audit situations. It is important for the standard to permit the engagement partner to use information and resources from the firm or other members of the engagement team when making such determinations.

To address these concerns, we recommend that the Board consider making the following revisions to paragraph 56 of ED-240 (deletions are struck through, additions are marked as underlined):

56. Based on the understanding obtained in accordance with paragraph 55, the engagement partner auditor shall: (Ref: Para. A152–A153)

Determine whether:

- (i) To perform additional risk assessment procedures to provide an appropriate basis for the identification and assessment of the risks of material misstatement due to fraud in accordance with ISA 315 (Revised 2019);
 - (ii) To design and perform further audit procedures to appropriately respond to the risks of material misstatement due to fraud in accordance with ISA 330; and
 - (iii) There are additional responsibilities under law, regulation or relevant ethical requirements about the entity’s non-compliance with laws or regulations in accordance with ISA 250 (Revised).
- (b) If applicable, consider the impact on other engagements, including audit engagements from prior years.

Additionally, we recommend that the Board consider adding a new paragraph into ED-240 as follows:

X. The engagement partner may obtain information from the firm or other members of the engagement team, but remains ultimately responsible, and therefore accountable, for compliance with the requirements of this ISA.

Institute of Chartered Accountants of Scotland

Neither agree/disagree, but see comments below

We question whether it is practical for the requirements set out in paragraph 55 to apply to all cases of fraud or suspected fraud, given that there will be inconsequential potential frauds. We therefore believe that there is a need for the IAASB to revisit this approach to ensure that this requirement is appropriately targeted.

4 Disagree

4. Jurisdictional and National Auditing Standard Setters

American Institute of Certified Public Accountants

Disagree, with comments below

Fraud or Suspected Fraud

We understand the IAASB's desire to include requirements in ED-240 (paragraphs 55-59 of ED-240) to enhance the auditor's responsibilities when fraud or suspected fraud is identified beyond the requirements that currently exist, given that auditors may look to ISA 250, Consideration of Laws and Regulations in an Audit of Financial Statements, the IESBA Code of Ethics for Professional Accountants, and other regulatory requirements (such as, section 10A of the United States Securities Exchange Act of 1934) for guidance. While we support the intent of these requirements, we are concerned that the requirement in paragraph 55 of ED-240 is not scalable. It is unclear from the explanatory memorandum as to the intent of paragraph 55 and whether each element of the requirement needs to be applied for every identified fraud or suspected fraud, including those that are clearly inconsequential. We believe that paragraph 55 of ED-240 could result in an onerous and unnecessary work effort by the auditor on matters that are clearly inconsequential. Directing resources to areas of remote risk of material misstatement to the financial statement is contrary to the risk-based audit approach that underpins ISA 315 (Revised 2019) and ISA 330, The Auditor's Responses to Assessed Risks. This could negatively affect audit quality by unnecessarily diverting the auditor's attention from higher risk areas. We encourage the IAASB to better clarify the auditor's responsibilities in ED-240 in such circumstances.

We believe that the phrase "the auditor identifies fraud or suspected fraud" may be misunderstood by auditors, irrespective of the key concepts described in paragraph 7. As drafted, the phrase could be interpreted to apply to those fraud matters that have been identified specifically by the auditor and would not include other ways in which the auditor becomes aware of fraud or suspected fraud. Accordingly, we recommend adding to paragraph 55 (and other paragraphs throughout ED-240, as necessary) the phrase "or otherwise become aware of" to clarify and reinforce the scope of the performance requirements in paragraph 55.

We believe that the auditor's work effort should align with the IESBA code requirements as it relates to fraud. Paragraph 14 of ED-240 states that "For the purposes of this and other relevant ISAs, fraud constitutes an instance of non-compliance with laws and regulations." Section R360.7 A2 of the IESBA code states the following:

360.7 A2 A professional accountant who encounters or is made aware of matters that are clearly inconsequential is not required to comply with this section. Whether a matter is clearly inconsequential is to be judged with respect to its nature and its impact, financial or otherwise, on the client, its stakeholders and the general public.

Section R360 of the IESBA code states the following:

R360.10 If a professional accountant engaged to perform an audit of financial statements becomes aware of information concerning non-compliance or suspected non-compliance, the accountant shall obtain an understanding of the matter. This understanding shall include the nature of the non-compliance or suspected non-compliance and the circumstances in which it has occurred or might occur.

Accordingly, we recommend the following changes be made to the requirements in paragraph 55 to better align with the IESBA Code and to better reflect the auditor's work effort based on the nature of the fraud. That is, the auditor may not need to perform all of the procedures in paragraph 55 to obtain an understanding of the identified fraud or suspected fraud, sufficient to conclude on next steps, based upon the significance of the identified fraud or suspected fraud (i.e., scalability based on the nature and significance of the identified fraud or suspected fraud).

We recommend the requirements in paragraph 55(b) and (c) be combined and revised to use plain English to explain what the auditor’s work effort should be because it was unclear what was meant by the entity’s process.

Further we recommend that the requirement in paragraph 55(d) be revised from “determine” to “consider” because the auditor may not have enough information to make a determination about whether a control deficiency exists related to the fraud or suspected fraud.

We have concerns about whether the requirement in paragraph 56(a)(iii) is operable in many group audit situations. Paragraph 56(a)(iii) requires the engagement partner to determine whether there are additional responsibilities under, law, regulation, or relevant ethical requirements about the entity’s non-compliance with laws or regulations in accordance with ISA 250. It is important for the standard to permit the engagement partner to use information and resources from the firm or other members of the engagement team when making such determinations. We ask the IAASB to consider whether clarification is needed in paragraph 56 to clarify the engagement partner’s responsibilities or whether the requirement

should be for the engagement partner to “take responsibility” for this requirement.

Paragraph 55 and Related Application Material

Paragraph 55

55. If the auditor identifies or otherwise becomes aware of fraud or suspected fraud, the auditor shall obtain an understanding of the nature and circumstances of the matter in order to determine the effect on the audit engagement. In doing so, the auditor shall : (Ref: Para. A146–A151)

(a) Make inquiries about the nature and circumstances of the matter and how management has responded to the matter with a level of management that is at least one level above those involved and, when appropriate in the circumstances, make inquiries about the matter with those charged with governance;

(b) If the results of the procedures in paragraph (a) indicate the matter is other than clearly inconsequential, the auditor shall:

(i) (b) evaluate how management has responded to the matter, including the nature and status of the investigations and remediation measures management has taken or plans to take If the entity has a process to investigate the matter, evaluate whether it is appropriate in the circumstances

(c) If the entity has implemented remediation measures to respond to the matter, evaluate whether they are appropriate in the circumstances; and

(ii) (d) Consider Determine whether control deficiencies may exist, including significant deficiencies in internal control related to the prevention or detection of fraud, relating to the identified fraud or suspected fraud

Paragraph A147

We believe it would be helpful if the examples in paragraph A147 provide further insights into how the engagement partner made the determination that a matter did not give rise to the need for additional risk assessment procedures.

Impact on the Overall Audit Strategy

Application Material Related to Paragraph 56

Paragraph A153

As drafted, paragraph A153 implies that the auditor may issue an unmodified opinion if an extension of time to file is not possible under applicable law or regulation. If the auditor is unable to conclude whether the financial statements are materially misstated as a result of the fraud, the auditor may have a limitation on the scope of the audit and should determine the implications for the auditor's opinion. We believe that the discussion in paragraph A153 is one possible situation and others may exist. Therefore, we recommend the following changes be made to refer to AU-C section 705.

A153. Based on the understanding obtained about the fraud or suspected fraud and the impact on the overall audit strategy, the engagement partner may determine that it is necessary to discuss an extension of the audit reporting deadlines with management and those charged with governance, where an extension is possible under applicable law or regulation. If an extension is not possible, ISA 705 (Revised) deals with the implications for the auditor's opinion on the financial statements.

Communications with Management and Those Charged with Governance

Communication with Those Charged with Governance

Application Material Related to Paragraph 68

Paragraph A187

We encourage the IAASB to include a reminder in paragraph A187 for the auditor to discuss with those charged with governance when the entity does not have controls to address risks of material misstatement due to fraud when those matters are considered significant deficiencies.

Other Matters Related to Fraud (Ref: Para. 68)

A187. In accordance with ISA 265, the auditor is required to communicate with those charged with governance significant deficiencies in internal control identified during the audit. This includes the absence of controls to address risks of material misstatement due to fraud when those matters are determined to be significant deficiencies. Other matters related to fraud to be discussed with those charged with governance of the entity may include, for example:

- Concerns about the nature, extent, and frequency of management's assessments of the controls in place to prevent or detect fraud and of the risk that the financial statements may be misstated.
- A failure by management to appropriately address identified significant deficiencies in internal control, or to appropriately respond to an identified fraud.
- The auditor's evaluation of the entity's control environment, including questions regarding the competence and integrity of management.
- Actions by management that may be indicative of fraudulent financial reporting, such as management's selection and application of accounting policies that may be indicative of management's effort to manage earnings in order to deceive financial statement users by influencing their perceptions as to the entity's performance and profitability.
- Concerns about the adequacy and completeness of the authorization of transactions that appear to be outside the normal course of business.

Other Paragraphs

Please see our response to question 10 for comments that are more editorial in nature related to paragraphs A146 (par. 55), 149 (par. 55), A150 (par. 55), A151 (par. 55), and A155 (par. 56)

Scalability of Requirements When Fraud or Suspected Fraud is Identified

We understand the IAASB's desire to include requirements in ED-240 (paragraphs 55-59 of ED-240) to enhance the auditor's responsibilities when fraud or suspected fraud is identified beyond the requirements that currently exist, given that auditors may look to ISA 250, Consideration of Laws and Regulations in an Audit of Financial Statements, the IESBA Code of Ethics for Professional Accountants, and other regulatory requirements (such as, section 10A of the U.S. Securities Exchange Act of 1934) for guidance. While we support the intent of these requirements, we are concerned that the requirement in paragraph 55 of ED-240 is not scalable. It is unclear from the explanatory memorandum as to the intent of paragraph 55 and whether each element of the requirement needs to be applied for every identified fraud or suspected fraud, including those that are clearly inconsequential. We believe that paragraph 55 of ED-240 could result in an onerous and unnecessary work effort by the auditor on matters that are clearly inconsequential. Directing resources to areas of remote risk of material misstatement to the financial statement is contrary to the risk-based audit approach that underpins ISA 315 (Revised 2019) and ISA 330, The Auditor's Responses to Assessed Risks. This could negatively affect audit quality by unnecessarily diverting the auditor's attention from higher risk areas. We encourage the IAASB to better clarify the auditor's responsibilities in ED-240 in such circumstances. See our further response to question 4.

Australian Auditing and Assurance Standards Board

Disagree, with comments below

The AUASB is concerned with the practicality and scalability of the requirements in paragraph 55 applying to all instances of identified fraud or suspected fraud.

The AUASB agrees with the basis of the IAASB's conclusions that an understanding of the fraud or suspected fraud is necessary to inform the engagement partner's determinations as required by paragraph 66; i.e. how do you know the trivial or inconsequential fraud isn't indicative of a wider issue. However, the AUASB considers the absence of materiality reference in paragraph 55, unduly expands the expectations of the auditor and that the requirements described in paragraph 55 are too onerous from both a practical perspective and a documentation perspective.

While supportive of the IAASB's basis for paragraph 55 and in recognising scalability concerns, the AUASB suggests the following:

Splitting paragraph 55 with only 55(a) and 55(b) required for all instances of identified fraud or suspected fraud.

Paragraph 55(c) and 55(d) are not required where instances of fraud or suspected fraud are clearly trivial.

Adding application material supporting paragraph 55 to explain that the tolerance for fraud in the public sector may be such that it would be rare for an instance of fraud or suspected fraud to be considered trivial.

Making the requirement in paragraph 55(a) to inquire about the matter with a level of management that is at least one level above those involved, subject to any legislation that may prevent the auditor from making a direct enquiry to management, such as where the auditor is notified of a fraud or suspected fraud by an anti-corruption regulator. Indirect enquiry may be possible.

The assessment in paragraph 56 should be imposed on the auditor rather than the engagement partner. In practice it may be made by the engagement partner but that may not be practical in some scenarios, such as large groups with component audits.

Paragraph 66 should not require the auditor to communicate frauds or suspected frauds already known to management. This would avoid the possibility of undermining the impact of communicating matters not known to management.

Introducing a stand-back requirement at the conclusion of the audit into ED-240 to further address the possibility of an accumulation of matters that alone might be considered clearly trivial. This would complement the overarching requirement in paragraph 21 of ED-240 for the auditor to remain alert throughout the audit engagement for information that is indicative of fraud or suspected fraud.

5. Accounting Firms

Grand Thornton International

Disagree, with comments below

We have several concerns with how to operationalize the requirements in ED-240, paragraphs 55-56, as noted below. We believe the work effort requirements and application material related to ED-240, paragraphs 57-59 and 66-69 are appropriate.

Concerns related to requirements in ED-240, paragraph 55:

We believe the requirement in the lead-in of ED-240, paragraph 55 will limit scalability of the requirement for group audits and very large audits by not including an element of auditor judgment in determining whether it is necessary to obtain such a thorough understanding of identified or suspected fraud. For example, at these types of entities, if management has robust controls to detect fraud, it is likely that many immaterial instances of fraud or suspected fraud may be identified by management, investigated, and determined to not present a material risk to the overall control environment or financial statements. Such a scenario could include tips to the whistleblower hotline by disgruntled employees, or limited instances of timecard fraud or company credit card fraud. Additionally, in certain industries, such as the retail industry where individually low value sales are conducted in cash, there is a higher risk of low value fraud and in fact management may tolerate a certain level of such fraud. In these cases, using a risk-based framework, the engagement partner may obtain an understanding of the matters in aggregate through inquiries of management and other procedures as necessary, and reasonably conclude the matter does not need to be discussed with those charged with governance and that detailed documentation in the audit file is not necessary. We suggest the IAASB revise the lead-in of ED-240, paragraph 55 to allow the auditor to exercise judgment in determining the nature, timing, and extent of procedures performed.

We believe the requirement in ED-240, paragraph 55(b) is not appropriately scalable to smaller entities, such as owner-managed entities that may not have a formal process to investigate fraud but will still investigate allegations of fraud or suspected fraud via an ad-hoc process. In practice, the auditor would still understand and evaluate management's investigation of the matter. We suggest the IAASB revise the requirement to indicate that the auditor evaluates management's process to investigate the matter and determine whether it is appropriate in the circumstances. We believe the second example in ED-240, paragraph A151 should also be removed or revised as we believe the lack of a formal process to investigate fraud or suspected fraud may not always be an indicator of a significant deficiency (such as in the case of a smaller entity or owner-managed entity).

We suggest the requirement in ED-240, paragraph 55(d) be revised to include consideration of whether internal control deficiencies exist in management's remediation measures.

We suggest removing and/or revising the first example presented in ED-240, paragraph A146 as it implies that management knew of the fraud and did not reveal the matter to the auditor during planning, which would

give rise to other fraud risk indicators and may lead to a different conclusion by the engagement partner than the conclusion presented in the example.

Concerns related to requirements in ED-240, paragraph 56:

We do not believe this requirement for the engagement partner to perform the listed procedures can be appropriately operationalized as written on group audits or very large engagements. As it relates to group audits, we believe there are scenarios where the component engagement partner or component auditor may be better suited to perform these procedures due to language and cultural understanding as well as potential access limitations. As it relates to very large engagements, we believe the requirement as written may have the unintended consequence of the group engagement partner spending a disproportionate amount of time on immaterial fraud or suspected fraud at the expense of time that could be spent on significant transactions and other significant risks. It may be appropriate to delegate the fraud procedures listed in paragraph 56 to other members of the engagement team. We believe this requirement should be written in a manner consistent with ISA 600 (Revised), in which the auditor performs these procedures with the engagement partner taking ultimate responsibility for the direction, supervision, and review of the work.

We believe the requirement in ED-240, paragraph 56(a) has a typo as these procedures are already required under ISA 330. We suggest the IAASB revise to include the word additional: “To design and perform additional further audit procedures...”

We suggest the IAASB revise ED-240, paragraph 56(b) to include consideration of fraud and suspected fraud related to subsequent events.

Forvis Mazars

Disagree, with comments below

We are concerned with the reference in ED240.7 that "suspected fraud includes allegations". These are two very different concepts and, although allegations may lead to suspected fraud, it is not appropriate to treat all allegations as suspected fraud as this could lead to an unnecessary burden in terms of work effort due to the lower bar where auditors need to take action. As written ED240.7 suggests that any allegation should be treated as suspected fraud. We suggest that IAASB may wish to consider a conditional requirement for auditors to assess whether an allegation has merit and is indicative of a fraud and, only where they conclude there is a risk, take further action as appropriate.

We support the creation of a separate section of the standard setting out the requirements when responding to identified fraud or suspected fraud set out in ED240.55-59. These requirements are largely clear and logical in setting out what an auditor would reasonably be expected to do where fraud or suspected fraud is identified. However, we make the following observations:

As noted above, the requirement in ED240.55 to “determine whether control deficiencies exist” may indicate an expectation that the auditor would test the operating effectiveness of controls, which is not the case in every audit. It is not clear if this is the IAASB’s attention. Greater clarity could be provided as to expectations in this area.

Furthermore, as noted above, we are concerned that the requirements in ED240.55 also create an impression that auditors may be more responsible for identifying fraud related control deficiencies than for other deficiencies (e.g. related to error), which we do not believe is appropriate.

The requirement in ED240.55 to make inquiries with “a level of management that is at least one level above those involved” may appear logical in larger, complex entities but the application of this requirement in smaller,

less complex entities (such as owner managed businesses) will be problematic. The IAASB may wish to provide greater clarity over how this requirement can be scaled to different types of entity. Furthermore, there may be circumstances where the auditor may potentially be in a position of ‘tipping off’ management when making fraud-related enquiries which, in some jurisdictions, may be a criminal offence; for example, where the auditor makes a disclosure likely to prejudice a money laundering investigation when discussing an identified or suspected fraud with the potential perpetrators.

We suggest adding a further example to ED240.A29: “A regulatory authority has commenced an investigation at the entity”.

7. Member Bodies and Other Professional Organizations

Fraud Advisory Panel

Disagree, with comments below

ED paragraphs 55 to 59 do not sufficiently provide guidance to auditors in relation to fraud perpetrated by management and those charged with governance. Nor does this section sufficiently highlight the risk of tipping off or committing money laundering offences (in the UK).

Similarly, ED paragraphs 66 to 68 should be expanded to take into account where management or those charged with governance have perpetrated the fraud, and there is no one above these perpetrators to communicate the fraud to.

While we note that ED Paragraph 22, we consider that reference to consulting subject matter (fraud) experts or forensic accountants in the body of the standard (rather than in the application notes) is necessary at ED paragraph 55 to 59 to ensure that those evaluating identified fraud or suspected fraud, and the investigation carried out by the entity have the appropriate skills and expertise to carry out that evaluation.

Pennsylvania Institute of Certified Public Accountants

Disagree, with comments below

The scope of the work outlined in paragraphs 55 through 59 is unclear relative to materiality considerations. Are these procedures required to be performed if the fraud is not material or inconsequential?

Note that 55 (b) and (c) start with “if,” which does not seem to fit based on the construct of the sentence. We request that the wording be adjusted for these two requirements.

The committee noted that the requirement under paragraph 55 (b) refers to an entity’s “process to investigate.” This terminology is somewhat unclear. The requirements for addressing noncompliance with laws and regulations outlined in the IESBA Code of Professional Conduct discuss the communication requirements and evaluation of the appropriateness of the response of management or those charged with governance, but do not refer to a “process.” Is it intended that there are no follow-up requirements if management does not have a “process”? What does this process entail? We request that the phrasing of this requirement be revised to be consistent with the language in the IESBA Code or to clarify what the expectations are and refer more generically to how management will address the potential fraud.

Unmodified opinion in application guidance – We noted that paragraph A153 could be misread to mean that the auditor may issue an unmodified opinion if an extension of time to file is not possible under applicable law or regulation. The committee recommends clarification to note that if the auditor is unable to conclude whether the financial statements are materially misstated as a result of fraud, the auditor may have a limitation on the scope of the audit and should determine the implications for the auditor’s opinion.

CPA Australia

Disagree, with comments below

We do not believe ED-240 clearly delineates the varying work efforts required for fraud, suspected fraud, and allegations of fraud. While the basic procedure for all types of fraud involves gaining an understanding, the approach can vary significantly based on the credibility of the initial information. For example, dealing with baseless allegations from disgruntled employees requires a different work effort to establish that the allegation has foundation.

Given the potential progression from alleged or suspected fraud to identified fraud and the iterative nature of fraud risk assessment, we urge the IAASB to develop a decision tree or flowchart. Similar to the ISA 315 First-time implementation guide, this tool would map out the execution of requirements and their dependencies based on the outcomes of the preceding steps.

Additionally, the examples in paragraph A29, which indicate fraud or suspected fraud, mostly apply to larger entities. We recommend including examples relevant to smaller entities to improve scalability and practical application as noted in our response to Question 2 above.

Institute of Chartered Accountants in England and Wales

Disagree, with comments below

Paragraph 55(a) of ED-240 does not deal with the situation in which there is no 'level of management (...) at least one level above those involved', with whom the auditor could make fraud-related enquiries, especially for smaller and less complex entities. It is important that the revised standard clarifies to whom auditors of such entities address their fraud enquiries.

Most SMPs we consulted had concerns about the requirement of ED-240 Para. 55(a) to make enquiries about identified or suspected fraud with 'a level of management that is at least one level above those involved.' Applying this requirement to smaller, less complex entities with a simplified management structure and no internal audit function or audit committee is problematic.

In many cases of corporate fraud, it is not uncommon for there to be a notable void above the individual(s) involved, of whom to make enquiries. The standard does not make clear what the auditor's response should be in this scenario.

Where an entity has a simplified management structure, particularly where management and TCWG are one and the same, the standard does not alert the auditor to potential 'tipping off' concerns when making fraud-related enquiries. In the UK and other jurisdictions a criminal offence is committed by making a disclosure likely to prejudice a money laundering investigation. This could include discussing an identified or suspected fraud with the potential perpetrators. In the UK, this can lead to potential penalties of an unlimited fine and up to five years' imprisonment.

In addition, ED-240 Para. 7 makes it clear that suspected fraud 'includes allegations of fraud that come to the auditor's attention during the course of the audit', underscored by Para. A10. Neither the requirement nor the application material address clearly trivial allegations. At present ED-240 implies that any allegation must be classed as suspected fraud without exception for vexatious allegations.

We acknowledge the challenge of articulating the judgement needed to determine whether an alleged fraud is vexatious, but ED-240 could at least refer to the distinction. A good first step for any auditor in this area that should be highlighted in the revised standard, is to make enquiries with the person at the audited entity responsible for any whistleblowing function, and to inspect whistleblower files.

We agree that it makes sense to highlight the importance of considering the potential for internal control deficiencies when obtaining an understanding of identified or suspected fraud, as made clear in ED-240 Para. 55. However, the requirement for the auditor to 'determine whether control deficiencies exist' must not lead to any expectation that the auditor will test the operating effectiveness of controls where they otherwise would not have been tested, as in many smaller audits. The revised standard should clarify that this is not the requirement's intent.

Scalability

ICAEW is not persuaded that ED-240 is sufficiently scalable.

South African Institute of Chartered Accountants

Disagree, with comments below

While we appreciate the new procedures that were included in the ED-240 by the IAASB, SAICA is of the view that the procedures are very broad. Suspected fraud can have a more pervasive effect on the audit compared to known fraud. There is a need for clarity on how the auditor's required response differs in this instance, for example: how does the auditor obtain further information about the matter when they don't know if management or those charged with governance (TCWG) are involved? It is our view that responding to suspected fraud is more complex than responding to known fraud.

Consider including procedures part of Par 55 (a) to be performed by the auditor where TCWG are also involved in perpetrating fraud. The requirement and application material don't provide any guiding principles on how auditors must approach instances of fraud or suspected fraud committed by TCWG or instances where management does not respond to identified fraud.

Par 69. ED-240 deals with reporting to an appropriate authority outside the entity. Consider moving the requirements in Par. 69 to Par. 55 (a) to address instances where TCWG are involved in fraud or management does not respond to fraud or suspected fraud.

The application material indicates the possibility of those charged with governance being involved in perpetrating fraud, but does not elaborate on the possible procedures or actions to be taken by the auditor: Para. A7–A10, A29 and A144–A145)

There is a risk that the standard may create the perception that the guiding principles reflected in par 55 of the standard and application material are written with the view that those charged with governance will never be in a position to perpetrate fraud which will negatively impact on the ability of the auditor to exercise professional skepticism.

Par. 55 (b) If the entity has a process to investigate the matter, evaluate whether it is appropriate in the circumstances.

This paragraph seems to indicate that management has an option not to have a process in place to investigate fraud by using the word "IF". This contradicts with the responsibility of management to identify and prevent fraud as the first line of defence.

The standard does not include guidance on what the auditor should do in instances where management or TCWG does not understand their roles and responsibilities in relation to fraud in the audit of financial statements, which indirectly affects the audit report and the need to report a KAM.

The difference between procedures required to be performed in responding to significant fraud risks versus confirmed fraud versus suspected fraud is unclear. Applying the requirements in paragraphs 43 – 54 may not

result in sufficient audit evidence to respond to a significant fraud risk that has not yet been linked to fraud or suspected fraud.

There is also a concern that this could result in more work for the auditor which is investigative in nature rather than providing reasonable assurance that the financial statements are free from material misstatements.

The IAASB should also consider including a procedure that relates to international and local laws and regulations as part of understanding the fraud. For example in South Africa, as part of understanding local laws and regulations, the auditor must consider the reporting of Reportable irregularities (RIs) to the local regulator. Par. 56 a(iii) may be added to the procedures of understanding fraud or suspected fraud in Par. 55 (a) in order to enhance ED-240 in this regard.

ED-240 needs to make provision for jurisdictional adaptations to the proposed KAM requirements, where law or regulation requires external reporting or may prohibit public reporting of a fraud-related matter. For example, in South Africa, section 45 of the APA requires a registered auditor to report a reportable irregularity without delay, if the registered auditor is satisfied or has reason to believe that a reportable irregularity has taken place or is taking place.

Par 57 (b): This paragraph is silent on the extent and value of the fraud; the significance of the fraud will depend on the level at which it is committed.

Par. A146 and A148 do not provide guidance on what to do if the entity denies the allegations or has done no further work or investigation into the matter. Is it then responsibility of the auditor to obtain an understanding of the matter via extended audit procedures to determine how; who perpetrated the fraud; and the extent of the fraud? We note that the standard is written for the auditor. Therefore, it is essential to provide guidance when management is not taking responsibility. Guidance should be included on what the auditor's response would be in such an instance where there is no management process.

Par. A148: Relates to scenarios of instances where management has a process in place and has acted on the identified or suspected fraud, consider including examples of instances where there is no process, or where no action has been taken by management or TCWG as part of Par. Consider including the details in A 150 and A151 in Par. 55 (d) of the standard to provide clarity.

We recommend the following to enhance the standard further:

The standard is unclear on what is required of the auditor when those charged with governance (TCWG) are involved in fraud or suspected fraud. Consider including application guidance or procedures to assist the auditor in such instances.

The examples provided in the ED-240 are financial statements driven, while auditors in public sector operate in environments where more than just the information in the annual financial statements are audited. Consider adding additional examples that focus on areas other than financial statements for public sector audits.

Consider including examples in the application material of how instances of fraud can come to the attention of the auditor, at acceptance and continuance stage of the audit by involving a fraud specialist , media reports and investigations reports.

If suspected fraud can be concluded to be immaterial without further investigation? What further steps are required to be taken by the auditor post concluding that fraud is immaterial. There is a specific concern about the potential implication of accumulation of non-material fraud on the group financial statements and consequently the responsibilities of the group auditor. This will promote consistent behaviour.

Institute of Chartered Accountants of Sri Lanka

Disagree, with comments below

Jurisdictions with developing markets will have difficulties in obtaining and retaining specialized resources, including forensic experts. Therefore, scalability in relation to application of these requirements needs to be reinforced, giving less complex jurisdictions the ability to scale down.

Further, more examples on reporting, especially explaining clearly how to deal with environments with pervasive control deficiencies, and hence fully substantive audit approaches are generally followed, will be helpful.

California Society of Certified Public Accountants

Disagree, with comments below

There is concern with the scalability of this standard as it relates to inconsequential / immaterial fraud or suspected fraud (i.e. information received through a whistle-blower program)

5 No response

1. Monitoring Group

International Forum of Independent Audit Regulators

9. Individuals and Others

Dr. Rasha Kassem

No response