

Meeting: IAASB Consultative Advisory Group (CAG)

Meeting Location: Virtual Zoom Meeting

Meeting Date: March 8–9, 2022

Agenda Item H

Fraud in an Audit of Financial Statements – Cover and Report Back

Objectives of Agenda Item

1. The objectives of this Agenda Item are to:
 - (a) Obtain the IAASB CAG Representatives' views on selected topics on fraud in an audit of financial statements.
 - (b) Report back on the November 2021 IAASB CAG meeting.

Update on Activities Since the November 2021 IAASB CAG Meeting

2. At its December 2021 meeting, the IAASB discussed and approved the project proposal for the revision of ISA 240¹ and the conforming and consequential amendments to other relevant ISAs. In the project proposal, the IAASB recognized the importance of the role of its standards in the financial reporting ecosystem. Therefore, the project will be focused on specific standard-setting actions aimed at enabling consistent and improved auditor behavior.
3. Since November 2021 IAASB CAG meeting, the Fraud Task Force (the Task Force) discussed the following topics:
 - Identifying and assessing the risks of material misstatement due to fraud;
 - Communication with those charged with governance (TCWG);
 - Transparency in reporting on fraud; and
 - Developing non-authoritative guidance illustrating the relationship between and linkage of ISA 240 and other ISAs.

Way Forward

4. Following the March 2022 IAASB meeting, the Task Force will continue to discuss the topics included in the issues paper for the March 2022 IAASB meeting (**Agenda Item H.2**). In doing so, the Task Force will consider the IAASB CAG's and the IAASB's feedback. In addition, the Task Force will develop its thinking on the introduction section, the definitions, the requirements related to journal entries, specialized skills and the presumption of fraud risk in revenue recognition, and the related application and other explanatory material.

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

5. In June 2022, the Task Force will bring the topics highlighted in paragraphs 3 and 4 above to the IAASB for discussion, including drafting for certain of these topics.
6. The Task Force will liaise with other IAASB task forces, working groups and consultation groups as needed. The Task Force will also liaise with the International Ethics Standards Board for Accountants to identify any ethics considerations or matters of relevance in terms of fraud.
7. To promote the IAASB's ongoing focus on fraud and continue to remind stakeholders in the financial reporting ecosystem of the importance of this topic, Staff supporting the Task Force, and the International Federation of Accountants' Communications department are developing a communications plan for fraud. Planned activities include, among other matters, the release of certain non-authoritative guidance, a Question & Answer article, and LinkedIn live sessions.
8. The **Appendix** to this paper provides a history of previous discussions with the IAASB CAG and the IAASB on this topic, including links to the relevant IAASB CAG documentation.

Outreach with Users of the Financial Statements

9. In September 2020 the Fraud and Going Concern Working Groups published a Discussion Paper, [*Fraud and Going Concern in an Audit of Financial Statements*](#). The Discussion Paper included a question on whether more transparency is needed about the auditor's work in relation to fraud in an audit of financial statements (Question 2(d)).
10. Given the mixed views by respondents to the Discussion Paper and the IAASB on transparency in reporting on fraud, the Task Force is moving to find an appropriate way forward that balances the different views, recognizing that there will always be robust discussions on this topic reflecting differing perspectives. Therefore, the Task Force intends to undertake targeted outreach to users of general-purpose financial reports to obtain their views on the specific alternatives as set out in **Section IV of Agenda Item H.2**. This targeted outreach will help inform the IAASB about what additional information they are looking for from the auditor to provide greater transparency about the audit that was performed with regard to fraud, thereby informing changes to meet their needs.
11. The Task Force will present the results of the targeted outreach to the IAASB in June 2022.

IAASB CAG Discussion in March 2022

12. For purposes of the IAASB CAG discussion, the Task Force prepared a presentation (**Agenda Item H.1**) highlighting its discussions and decisions related to the following topics:
 - Identifying and assessing the risks of material misstatement due to fraud;
 - Communication with TCWG;
 - Transparency in reporting on fraud; and
 - Developing non-authoritative guidance illustrating the relationship between and linkage of ISA 240 and other ISAs.
13. In addition to covering the topics noted in paragraph 12 more broadly, the Task Force Chair intends to further discuss the topic of transparency in reporting on fraud. Representatives will have the opportunity to comment on other areas as well.

In preparation for the IAASB CAG Discussion on Fraud, Representatives are encouraged to read **Section IV of Agenda Item H.2**.

Matters for IAASB CAG Consideration

1. Representatives are asked for their views on:
 - (a) Whether alternatives 1-3 presented in **Section IV of Agenda Item H.2** (and slide 5 of **Agenda Item H.1**) are the appropriate alternatives to discuss with users of the financial statements. Representatives are also asked for any ideas on alternative 4 (“other mechanisms”)
 - (b) Any other matters raised in **Agenda Item H.1**

Feedback

14. Extracts from the draft November 2021 IAASB CAG meeting minutes, as well as an indication of how the Task Force or the IAASB has responded to the Representatives’ comments, are included below:

Representatives’ Comments	Task Force / IAASB Response
EMPHASIS ON THE AUDITOR’S ROLE AND RESPONSIBILITIES (INCLUDING THE RESPONSIBILITIES OF OTHERS IN THE FINANCIAL REPORTING ECOSYSTEM)	
Messrs. Ishiwata, Hansen, Thompson and Ms. Landell-Mills pointed out that ISA 240 gives undue emphasis as it relates to the inherent limitations of an audit but not enough emphasis on the auditor’s responsibilities regarding fraud. They were of the view that focusing on and clarifying the auditor’s responsibilities about what the auditor will do rather than what they will not do may help narrow the expectation gap (performance/delivery gap).	<p>Point noted.</p> <p>Mrs. Provost expressed appreciation for the support for proposals to emphasize the auditor’s role and responsibilities regarding fraud and acknowledged the importance of how the auditor’s role and responsibilities are described.</p> <p>The Task Force will discuss with users of the financial statements whether there is anything can be done to clarify the Auditor’s Responsibilities for the Audit of Financial Statements section in the auditor’s report (see paragraph 5 above).</p>
Ms. Blomme highlighted the importance of the role that others (e.g., management, TCWG, regulators, etc.) play in the financial reporting ecosystem in addressing fraud. She encouraged the IAASB to think about how it could use its global voice to encourage others to play their part in addressing the issues regarding fraud. Mr. Hansen noted that the IAASB, the International Federation of Accountants (IFAC) or other stakeholders may	<p>Point noted.</p> <p>Mrs. Provost reiterated that all parts of the financial reporting ecosystem are essential to help effectively narrow the expectation gap. While the IAASB could not on its own ‘close’ the expectation gap, she explained that strengthening ISA 240 will help narrow it (which is predicated on the revised standard being appropriately applied). She explained that the proposed actions include</p>

Representatives' Comments	Task Force / IAASB Response
consider actions such as encouraging the sharing of information about fraud through mechanisms such as a fraud center (e.g., recent trends in cyber fraud) that may enable fraud to be more proactively addressed.	initiatives of an educational nature or other outreach that are within the remit of the IAASB. She further explained that the proposed actions also include continued dialogue and engagement with others (e.g., IFAC's International Panel on Accountancy Education) on issues that relate to actions that are not solely within the IAASB's remit and require efforts from others in the financial reporting ecosystem.
SPECIALIZED SKILLS	
Messrs. Hansen and Kabwe expressed support for proposals addressing specialized skills. In circumstances that need the use of forensic skills (or specialists), Mr. Hansen noted it would be important to clarify whether such circumstances would still form part of the audit engagement or be considered a separate other assurance engagement (or a non-attest service). Mr. Kabwe noted that having a robust set of criteria is critical in identifying circumstances when it is appropriate for the auditor to consider the need for specialized skills, including the use of forensic specialists.	Point noted. Mrs. Provost highlighted that the possible actions relating to "forensic specialists" have been expanded to address "specialized skills" (including forensic skills) more broadly, recognizing the need for skills other than forensic skills in addressing fraud.
RESPONSES TO THE ASSESSED RISKS OF MATERIAL MISSTATEMENT	
Mmes. Wolf and Landell-Mills highlighted the fraud risk from management bias in developing accounting estimates (e.g., estimates relating to insurance reserves) and noted that this matter needs to be addressed in the project proposal. Mr. Dalkin noted the importance for the auditor to consider conflicting external information when considering the risk of fraud.	Point noted. Mrs. Provost noted that the proposed actions in the draft project proposal includes focusing on an emphasis on management bias as an indicator of fraud when considering the appropriateness of accounting estimates, and strengthening the link to the procedures required in ISA 540 (Revised). ² She further noted that the proposals include considering a stand-back requirement in ISA 240 to evaluate all relevant audit evidence obtained, whether corroborative or contradictory.
WRITTEN REPRESENTATIONS FROM MANAGEMENT	

² ISA 540 (Revised), *Auditing Accounting Estimates and Related Disclosures*

Representatives' Comments	Task Force / IAASB Response
In extending the existing written representations on fraud in ISA 240, Mr. Ishiwata noted it is important for auditors to communicate the required written representations from management at an early stage in the audit so that management has ample time to respond and take appropriate action.	Point noted. Mrs. Provost acknowledged it is helpful to communicate the required written representations early in the process, which may also form part of the proposals.
TECHNOLOGY CONSIDERATIONS IN THE CURRENT ENVIRONMENT	
Mr. Sobel highlighted two aspects of technology in the current environment— the use of technology that enables fraud, as well as the auditor's ability to use technology in detecting indicators of fraud. He also encouraged the IAASB to consider the upcoming key updates to the Fraud Risk Management Guide of the Committee of Sponsoring Organizations of the Treadway Commission, emphasizing the impact of technology on fraud (anticipated in quarter 2 of 2022).	Point noted. Mrs. Provost noted that the project proposal intends to address both aspects of technology (i.e., fraud risks presented by the use of technology, as well as the auditor's use of technology to perform fraud-related procedures). She also explained that ongoing activities in the project will include staying closely connected with all stakeholder groups as the project advances to consider developments in different jurisdictions that may be relevant to the revision of ISA 240.
PROCEDURES WHEN FRAUD IS IDENTIFIED OR SUSPECTED, INCLUDING THE RELATIONSHIP BETWEEN ISA 240 AND ISA 250 (REVISED) ³	
Depending on the applicable law, regulation or relevant ethical requirements, Mr. Pavas noted other jurisdictions may have more stringent requirements addressing fraud than those in ISA 240. In such instances, he noted that it may be useful to provide guidance in navigating the required actions to be taken when responding to identified fraud or suspected fraud.	Point noted. Mrs. Provost noted the proposed actions include designating a separate section in ISA 240 for required audit procedures when fraud is identified or suspected, with guidance to navigate the required actions to be taken when responding to identified or suspected fraud under ISA 240, non-compliance under ISA 250 (Revised), and non-compliance with laws and regulations under the IESBA Code. ⁴
PROFESSIONAL SKEPTICISM	
Mmes. Blomme, Meng and Landell-Mills	Support noted.

³ ISA 250 (Revised), *Consideration of Laws and Regulations in an Audit of Financial Statements*

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

Representatives' Comments	Task Force / IAASB Response
expressed support for the proposals addressing enhancing the auditor's exercise of professional skepticism throughout the audit. Mmes. Blomme and Landell-Mills encouraged clarity around the auditor's considerations in maintaining professional skepticism throughout the audit. Ms. Meng noted that the findings from the additional root cause analysis of fraud cases reinforces the proposed actions addressing professional skepticism.	Mrs. Provost thanked Representatives of their support for proposals to reinforce the exercise of professional skepticism throughout the audit (and the standard).
TRANSPARENCY WITH TCWG AND IN THE AUDITOR'S REPORT ON FRAUD-RELATED RESPONSIBILITIES AND PROCEDURES	
Mmes. Blomme and Meng expressed support for the proposals addressing transparency. Ms. Blomme noted it would be useful to provide guidance through a "decision tree" when determining the auditor's actions when addressing transparency (i.e., whether with TCWG, in the auditor's report or both). Ms. Meng noted that the findings from the additional root cause analysis of fraud cases reinforces the proposed actions addressing transparency.	Point noted. Mrs. Provost acknowledged the support for transparency but at the same time recognized the challenges ahead in determining a balanced approach in addressing this matter, given the mixed views expressed by stakeholders on this matter. She noted that the comment about having steps in process ("decision tree") when addressing transparency is a good thought to take forward.
SCALABILITY	
Messrs. Ishiwata and Thompson recognized the importance of considering scalability in revising ISA 240 and noted that the proposed actions addressing risk identification and assessment include illustrating the scalability of the requirements by providing examples that are more relevant to less complex entities (LCEs). Given the proposed separate standard for audits of LCEs, Mr. Ishiwata suggested to refrain from using the term LCE when revising ISA 240 to avoid confusion. In addition, Mr. Thompson queried whether the separate standard for audits of LCEs would be expected to incorporate the changes being	Point noted. Mrs. Provost explained that scalability is one of the qualitative characteristics set out in the Public Interest Framework ⁵ that will be considered in revising ISA 240 (e.g., identifying circumstances when it may be appropriate to use specialized skills, including forensic skills). She further explained that the project will also consider the conforming and consequential amendments arising from this project in the separate standard for audits of LCEs (if any). Mrs. Provost also noted that changes to ISA 240 would be considered in future conforming amendments to the proposed

⁵ Public Interest Framework published by the Monitoring Group in July 2020 (as part of their report "[Strengthening the International Audit and Ethics Standard-Setting System](#)")

Representatives' Comments	Task Force / IAASB Response
proposed to revise ISA 240.	separate standard for audits of LCEs, similar to any other revisions that may result from updates to existing or new ISAs.
OTHER COMMENTS	
Mr. Ishiwata noted that while there are many key issues identified that will be addressed by a project on fraud, “balance” needs to be kept in mind in revising ISA 240 to refrain from changes that are onerous, overburden the auditor or that may inadvertently result in unintended challenges when maintaining professional skepticism.	Point noted. The project proposal sets out the intended actions which are aimed at developing principles-based requirements and application material to address the public interest issues that have been identified. The Task Force, when developing the revisions to ISA 240, will also take into account the drafting principles and guidelines set out in the IAASB's Complexity, Understandability, Scalability and Proportionality Drafting Principles.
Mr. Ishiwata suggested that the proposed actions include addressing circumstances especially when there is an auditor change and how that impacts the audit when performing fraud procedures (for the successor auditor).	Point noted. As part of the project proposal, the requirements will be enhanced to highlight the importance of information obtained from acceptance and continuance procedures and the impact of that information when the auditor is considering possible misstatements that arise due to fraud.
Mr. Dalkin suggested the IAASB to consider the effectiveness of the existing requirements in ISA 240 when revising the standard.	Point noted. In developing the project proposal, the IAASB considered the effectiveness of the requirements in extant ISA 240.

Material Presented – IAASB CAG Papers

Agenda Item H.1 Presentation

Material Presented – IAASB CAG Reference Papers

Agenda Item H.2 IAASB Issues Paper March 2022

Appendix

Project Details and History

Project: Fraud

Link to IAASB Project Page: [Fraud Project Page](#)

Task Force Members

- Lyn Provost, IAASB Member and Task Force Chair
- Julie Corden, IAASB Member
- Josephine Jackson, IAASB Member
- Len Jui, IAASB Deputy Chair
- Diane Larsen, IAASB Member

Summary

	IAASB CAG Meeting	IAASB Meeting
Information Gathering	September 2020 March 2021 September 2021	August 2020 December 2020 April 2021 June 2021 July 2021
Project Proposal	November 2021	December 2021
Development of Exposure Draft	March 2022	March 2022

IAASB CAG Discussions: Detailed References

Information gathering	<p><u>September 2020</u></p> <p>See IAASB CAG meeting material and IAASB CAG meeting minutes (Agenda Item F).</p> <p>https://www.iaasb.org/cag/meetings/iaasb-cag-meeting-september-8-9-2020-virtual</p> <p><u>March 2021</u></p> <p>See IAASB CAG meeting material and CAG meeting minutes (Agenda Item C).</p> <p>https://www.iaasb.org/cag/meetings/iaasb-cag-meeting-march-8-9-2021-virtual</p>
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	<p><u>September 2021</u></p> <p>See IAASB CAG meeting material and IAASB CAG meeting minutes (Agenda Item I).</p> <p>https://www.iaasb.org/cag/meetings/iaasb-cag-meeting-september-8-9-2021-virtual</p>
Project Proposal	<p><u>November 2021</u></p> <p>See IAASB CAG meeting material and IAASB CAG meeting minutes (Agenda Item A).</p> <p>https://www.iaasb.org/cag/meetings/iaasb-cag-meeting-november-30-2021-virtual</p>
Development of Exposure Draft	<p><u>March 2022</u></p> <p>See IAASB CAG meeting material and IAASB CAG meeting minutes (Agenda Item H).</p> <p>https://www.iaasb.org/cag/meetings/iaasb-cag-meeting-march-8-9-2022</p>