

Transparency in Reporting on Fraud

The IAASB is exploring enhancing transparency in the auditor's report about the auditor's approach to fraud risks and related actions in an audit of financial statements and is interested in your views on whether one or more of the proposed options set out in this paper will provide users of the financial statements with insightful information that will impact their decision-making related to the entity.

Background

Corporate failures and scandals across the globe in recent years have brought the topic of fraud to the forefront and led the IAASB's stakeholders to question the role and responsibilities of the auditor for fraud in an audit of financial statements. As described in the IAASB's [Strategy for 2020-2023](#), the IAASB is focused on prioritizing emerging public interest issues and, as such, commenced information-gathering activities on fraud in an audit of financial statements in early 2020.

The objective of the information gathering and research activities on fraud was to further consider the issues and challenges in applying the international standard on auditing related to fraud (ISA 240)¹ in light of the evolving environment, jurisdictional developments and changing public expectations. Among other activities, the IAASB held roundtables and developed a [Discussion Paper](#), *Fraud and Going Concern in an Audit of Financial Statements: Exploring the Differences Between Public Perceptions About the Role of the Auditor and the Auditor's Responsibilities in a Financial Statement Audit*, which was published in September 2020 for consultation.

Leveraging the feedback obtained as a result of the information gathering and research activities, including targeted outreach, the IAASB developed and approved a [project proposal](#) to revise ISA 240 in December 2021. The project proposal sets out the IAASB's proposed actions to address the identified public interest issues. One of the actions proposes that the IAASB explore the need for more transparency in the auditor's report describing fraud-related matters, and if needed, how this may be done.

Based on the work performed to date, the IAASB notes that transparency in the auditor's report about fraud is a theme that has persisted since the IAASB's project on auditor reporting which commenced in 2010. Despite previous consultations and enhancements to the auditor's report, this matter continues to be the subject of interest and there remains ongoing and consistent feedback from certain stakeholder groups that more should be done in this area.

The IAASB also recognizes that several jurisdictions have recently enhanced their local auditing standards in relation to describing fraud related matters in the auditor's report (reporting on fraud), for example, the European Union, the United Kingdom, and the Netherlands.



Given the mixed views on this topic by respondents to the Discussion Paper and by members of the IAASB, the IAASB is looking for an appropriate way forward that balances the different views and is therefore interested in your perspectives on enhancing transparency in reporting on fraud in the auditor's report. These perspectives will be analyzed and assessed in combination with views from other stakeholders to determine the appropriate way forward.

¹ International Standard on Auditing (ISA) 240, *The Auditor's Responsibilities Relating to Fraud in an Audit of Financial Statements*
Prepared by: Sally Ann Bailey, Jasper van den Hout and Hanken Jane Talatala (August 2022)

Possible Options to Enhance the Transparency in Reporting on Fraud

To date the IAASB discussed five options on how the auditor’s report can be enhanced in relation to reporting on fraud, being:

- *Option 1:* Describing the auditor’s approach to fraud risks.
- *Option 2:* Describing the identified and assessed fraud risks, and the auditor’s response to the assessed fraud risks.
- *Option 3:* Describing the identified and assessed fraud risks, the auditor’s response to the assessed fraud risks, and the auditor’s findings/ observations when responding to the assessed fraud risks.
- *Option 4:* Emphasizing the use of the existing requirements for the communication of Key Audit Matters (KAMs) for listed entities when there is a fraud risk.
- *Option 5:* Reporting identified significant deficiencies² in internal control that are relevant to the prevention and detection of fraud.

The options set out above are not mutually exclusive. For example, option 5 could be combined with option 1, 2 or 3 and option 1 could be combined with option 4. An overview of the options discussed is presented in the table below. To help visualize each of the options, illustrative examples are included in the **Appendix**.

	Separate section specific to fraud in the auditor’s report	Description in the auditor’s report about the auditor’s approach to fraud risks	Description in the auditor’s report of the identified and assessed fraud risks	Description in the auditor’s report of the auditor’s response to the assessed fraud risks	Description in the auditor’s report of the auditor’s findings / observations when responding to the assessed fraud risks	Description in the auditor’s report of identified significant deficiencies in internal control related to fraud
Option 1	<input checked="" type="checkbox"/>	<input checked="" type="checkbox"/>				
Option 2	<input checked="" type="checkbox"/>	<input checked="" type="checkbox"/>	<input checked="" type="checkbox"/>	<input checked="" type="checkbox"/>		
Option 3	<input checked="" type="checkbox"/>	<input checked="" type="checkbox"/>	<input checked="" type="checkbox"/>	<input checked="" type="checkbox"/>	<input checked="" type="checkbox"/>	
Option 4			<input checked="" type="checkbox"/>	<input checked="" type="checkbox"/>		
Option 5						<input checked="" type="checkbox"/>

² A significant deficiency is a deficiency or combination of deficiencies in internal control that, in the auditor’s professional judgment, is of sufficient importance to merit the attention of those charged with governance.

Questions

The IAASB is interested in your views on the following:

1. Which of the options, if any, do you prefer to be included in the auditor's report? Please explain why, or why not, and how you would use such information.
2. Do you have any other recommendations for improving transparency about fraud in the auditor's report?



Appendix

Examples of Transparency in the Auditor's Report

This appendix provides examples of transparency in the auditor's report. The examples related to options 1, 2, 3 and 4 are based on extracts from issued auditor's reports. The example related to option 5 was developed by staff of the IAASB.

Example of Option 1

Audit Approach to Fraud Risks

We identified and assessed the risks of material misstatements of the financial statements due to fraud. During our audit we obtained an understanding of the company and its environment and the components of the system of internal control. This includes the risk assessment process and management's process for responding to the risks of fraud and monitoring the system of internal control and how those charged with governance exercise oversight, as well as the outcomes.

We evaluated the design and relevant aspects of the system of internal control and in particular management's fraud risk assessment, as well as among others the code of conduct, whistle blower procedures and incident registration. We discussed the fraud risk assessment with the Company's risk management and compliance officer. We evaluated the design and the implementation and, where considered appropriate, tested the operating effectiveness, of internal controls designed to mitigate fraud risks.

We considered available information and made enquiries of relevant executives, directors (including internal audit, legal, compliance, human resources and regional directors) and those charged with governance.

We incorporated elements of unpredictability in our audit. We also considered the outcome of our other audit procedures and evaluated whether any findings were indicative of fraud or noncompliance.

Example of Option 2

The **bold** text in the example below, is in addition to the text set out in option 1.

Audit Approach to Fraud Risks

We identified and assessed the risks of material misstatements of the financial statements due to fraud. During our audit we obtained an understanding of the company and its environment and the components of the system of internal control. This includes the risk assessment process and management's process for responding to the risks of fraud and monitoring the system of internal control and how those charged with governance exercise oversight, as well as the outcomes.

We evaluated the design and relevant aspects of the system of internal control and in particular management's fraud risk assessment, as well as among others the code of conduct, whistle blower procedures and incident registration. We discussed the fraud risk assessment with the Company's risk management and compliance officer. We evaluated the design and the implementation and, where considered appropriate, tested the operating effectiveness, of internal controls designed to mitigate fraud risks.

We considered available information and made enquiries of relevant executives, directors (including internal audit, legal, compliance, human resources and regional directors) and those charged with governance.

We incorporated elements of unpredictability in our audit. We also considered the outcome of our other audit procedures and evaluated whether any findings were indicative of fraud or noncompliance.

Identified Fraud Risks and the Auditor’s Response

We identified the following fraud risk factors:

- **The Company enters into revenue contracts that are considered complex from a revenue recognition perspective. The nature of those contracts requires management to estimate the costs to completion. Estimates are inherently uncertain and might be subject to management bias; and**
- **Management’s incentive to meet incentive plan targets could lead to management override of controls.**

Identified fraud risks	Our Response
<i>Risk of Fraud in Revenue Recognition</i>	
<p>As part of our risk assessment and based on a presumption that there are risks of fraud in revenue recognition, we evaluated which types of revenue transactions and assertions give rise to the risk of fraud in revenue recognition.</p> <p>The Company enters into contracts that are considered complex from a revenue recognition perspective. We focused on those contracts which include a fixed price element. The nature of those contracts require management to estimate the cost to complete, that impacts the revenue recognized.</p> <p>Estimates are inherently uncertain and might be subject to management bias. There might be incentives for management to use estimates in order to satisfy stakeholders, reach KPIs outlined in compensation plans and/or to meet debt covenants.</p>	<p>Where relevant to our audit, we assessed the design of the internal control measures related to revenue recognition and in the processes for generating and processing journal entries related to the revenue.</p> <p>We used a primarily substantive testing-based approach with respect to the cost to complete. The audit procedures included obtaining evidence to support applied hourly rates, challenging the number of expected hours to complete the project and reconciling changes in budgets to supporting evidence such as contract modifications. We also discussed the progress of the projects with the respective project managers and management of the operating companies. When performing these audit procedures, we remained alert to the inherent risk of management bias.</p>
<i>Risk of Management Override of Controls</i>	
<p>Management is in a unique position to perpetrate fraud because of management’s ability to manipulate accounting records and prepare fraudulent financial statements by</p>	<p>We evaluated the design of the internal control environment that reduces the risk of a breach of internal controls. Also, we paid specific attention to user access management in the IT system and</p>

<p>overriding controls that otherwise appear to be operating effectively.</p> <p>We paid attention to the risk of management override of controls, including risks of potential misstatements due to fraud based on an analysis of potential interests of management including the incentive to meet certain targets. Considering this analysis, we paid specific attention to the estimate of the cost to complete on revenue contracts.</p>	<p>performed compensating procedures when necessary.</p> <p>We selected journal entries based on risk criteria and performed audit procedures to validate these entries.</p> <p>We also performed specific audit procedures regarding important estimates made by management, including the cost to complete revenue contracts for clients. In our assessment of estimates, we remained alert to the inherent risk of bias from management with regards to estimates.</p>
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Example of Option 3

The **bold** text in the example below, is in addition to the text set out in option 2.

Audit Approach to Fraud Risks

We identified and assessed the risks of material misstatements of the financial statements due to fraud. During our audit we obtained an understanding of the company and its environment and the components of the system of internal control. This includes the risk assessment process and management's process for responding to the risks of fraud and monitoring the system of internal control and how those charged with governance exercise oversight, as well as the outcomes.

We evaluated the design and relevant aspects of the system of internal control and in particular management's fraud risk assessment, as well as among others the code of conduct, whistle blower procedures and incident registration. We discussed the fraud risk assessment with the Company's risk management and compliance officer. We evaluated the design and the implementation and, where considered appropriate, tested the operating effectiveness, of internal controls designed to mitigate fraud risks.

We considered available information and made enquiries of relevant executives, directors (including internal audit, legal, compliance, human resources and regional directors) and those charged with governance.

We incorporated elements of unpredictability in our audit. We also considered the outcome of our other audit procedures and evaluated whether any findings were indicative of fraud or noncompliance.

*Identified Fraud Risks, the Auditor's Response **and Observations***

We identified the following fraud risk factors:

- The Company enters into revenue contracts that are considered complex from a revenue recognition perspective. The nature of those contracts requires management to estimate the costs to completion. Estimates are inherently uncertain and might be subject to management bias; and
- Management's incentive to meet incentive plan targets could lead to management override of controls.

Identified fraud risks	Our response and observations
<i>Risk of Fraud in Revenue Recognition</i>	
<p>As part of our risk assessment and based on a presumption that there are risks of fraud in revenue recognition, we evaluated which types of revenue transactions and assertions give rise to the risk of fraud in revenue recognition.</p> <p>The Company enters into contracts that are considered complex from a revenue recognition perspective. We focused on those contracts which include a fixed price element. The nature of those contracts require management to estimate the cost to complete, that impacts the revenue recognized.</p> <p>Estimates are inherently uncertain and might be subject to management bias. There might be incentives for management to use estimates in order to satisfy stakeholders, reach KPIs outlined in compensation plans and-/or to meet debt covenants.</p>	<p>Where relevant to our audit, we assessed the design of the internal control measures related to revenue recognition and in the processes for generating and processing journal entries related to the revenue.</p> <p>We used a primarily substantive testing-based approach with respect to the cost to complete. The audit procedures included obtaining evidence to support applied hourly rates, challenging the number of expected hours to complete the project and reconciling changes in budgets to supporting evidence such as contract modifications. We also discussed the progress of the projects with the respective project managers and management of the operating companies. When performing these audit procedures, we remained alert to the inherent risk of management bias.</p> <p>Our audit procedures did not identify instances of fraud and did not identify any specific indications of fraud or suspicions of fraud with respect revenue recognition.</p>
<i>Risk of Management Override of Controls</i>	
<p>Management is in a unique position to perpetrate fraud because of management's ability to manipulate accounting records and prepare fraudulent financial statements by overriding controls that otherwise appear to be operating effectively.</p> <p>We paid attention to the risk of management override of controls, including risks of potential misstatements due to fraud based on an analysis of potential interests of management including the incentive to meet certain targets. Considering this analysis, we paid specific attention to the estimate of the cost to complete on revenue contracts.</p>	<p>We evaluated the design of the internal control environment that reduces the risk of a breach of internal controls. Also, we paid specific attention to user access management in the IT system and performed compensating procedures when necessary.</p> <p>We selected journal entries based on risk criteria and performed audit procedures to validate these entries.</p> <p>We also performed specific audit procedures regarding important estimates made by management, including the cost to complete revenue contracts for clients. In our assessment of estimates, we remained alert to the inherent risk of bias from management with regards to estimates.</p> <p>Our audit procedures did not identify instances of fraud and did not identify any specific</p>

	indications of fraud or suspicions of fraud with respect management override of controls.
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Example of Option 4

The example below would be included in the KAM section of the auditor’s report (for listed entities only)

Key Audit Matters

Key audit matters are those matters that, in our professional judgment, were of most significance in our audit of the financial statements of the current period. This matter was addressed in the context of our audit of the financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on this matter.

Project Revenue Recognition and Valuation of Contract Assets

Refer to notes 7, 21, and 22 of the financial statements.

We consider this a key audit matter since project revenue recognition and the valuation of contract assets are significant to the financial statements based on materiality and because of the degree of management judgement involved.

Management applies judgement to determine the cost to complete for contracts, which is the basis for revenue recognition and contract asset valuation, as well as for assessing provisions for onerous contracts.

In addition, the valuation of contract assets requires significant management judgement in determining recoverability, especially in the Middle East region, considering the above average ageing and the magnitude of the contract assets.

We evaluated which types of revenue transactions or assertions give rise to the risk of fraud in revenue recognition. As the Company enters into contracts that are considered complex from a revenue recognition perspective. We focused on those contracts which include a fixed price element. The nature of those contracts require management to estimate the cost to complete, that impacts the revenue recognized.

Estimates are inherently uncertain and might be subject to management bias. There might be incentives for management to use estimates in order to satisfy stakeholders, reach KPIs outlined in compensation plans and/or to meet debt covenants.

We assessed the nature of the Company’s revenue contracts. Where relevant to our audit, we evaluated the effectiveness of the design of the internal control measures and determined whether the controls have been implemented related to revenue recognition and in the processes for generating and processing journal entries related to the revenue. We also performed substantive audit procedures on individually significant projects as well as high-risk projects. In addition, we took a sample over the remaining population to ensure sufficient coverage over all projects.

These substantive procedures focused on the key assumptions applied by the Company to determine the cost to complete. The audit procedures included obtaining evidence to support applied hourly rates, challenging the number of expected hours to complete the project and reconciling changes in budgets to supporting evidence such as contract modifications. We also discussed the progress of the projects with the respective project managers and management of the operating companies. When performing these audit procedures, we remained alert to the inherent risk of management bias.

With regards to the above average ageing, magnitude of the contract assets in the Middle East region, and the announced decision to reduce the Company's footprint in the Middle East region, specific attention has been given to the collection of trade receivables and valuation of several contracts with significant contract assets. We have discussed management's position papers for these projects with the responsible project managers, the contract solutions team and the regional CFO and CEO. We have obtained supporting documentation, which included support for contract modifications, correspondence with the client and minutes confirming the status of negotiations with the client.

We assessed the adequacy of the disclosures relating to revenue recognition, in accordance with the requirements of IFRS 15.

Examples of Option 5

Two examples of option 5 are presented. In both examples the auditor does not have a responsibility to express an opinion on the effectiveness of internal control in conjunction with the audit of the financial statements and the auditor has identified significant deficiencies in internal control that are relevant to the prevention and detection of fraud.

In example A, the financial statements provide adequate disclosures on the matter while in example B, the financial statements do not provide adequate disclosures on the matter.

Example A: Significant Deficiency in Internal Control Relevant to the Prevention and Detection of Fraud

We have identified a significant deficiency in internal control relevant to the prevention and detection of fraud based on our understanding of the Company's system of internal control. We have communicated the significant deficiency in internal control to those charged with governance. The matter has been described in a note [x] to the financial statements, including management's plans to remediate the significant deficiency.

Example B: Significant Deficiency in Internal Control Relevant to the Prevention and Detection of Fraud

We have identified a significant deficiency in internal control relevant to the prevention and detection of fraud based on our understanding of the Company's system of internal control. We have communicated the significant deficiency in internal control to those charged with governance. The communication noted that the controls to address the risk of material misstatement due to fraud in revenue recognition specific to the XYZ revenue stream that commenced in December 20x0, have not been appropriately designed to support the operation of other controls as intended.