



# Fraud

*Agenda Item 3-B*

*IAASB April 2021 Meeting*  
*Lyn Provost, Fraud Working Group Chair*




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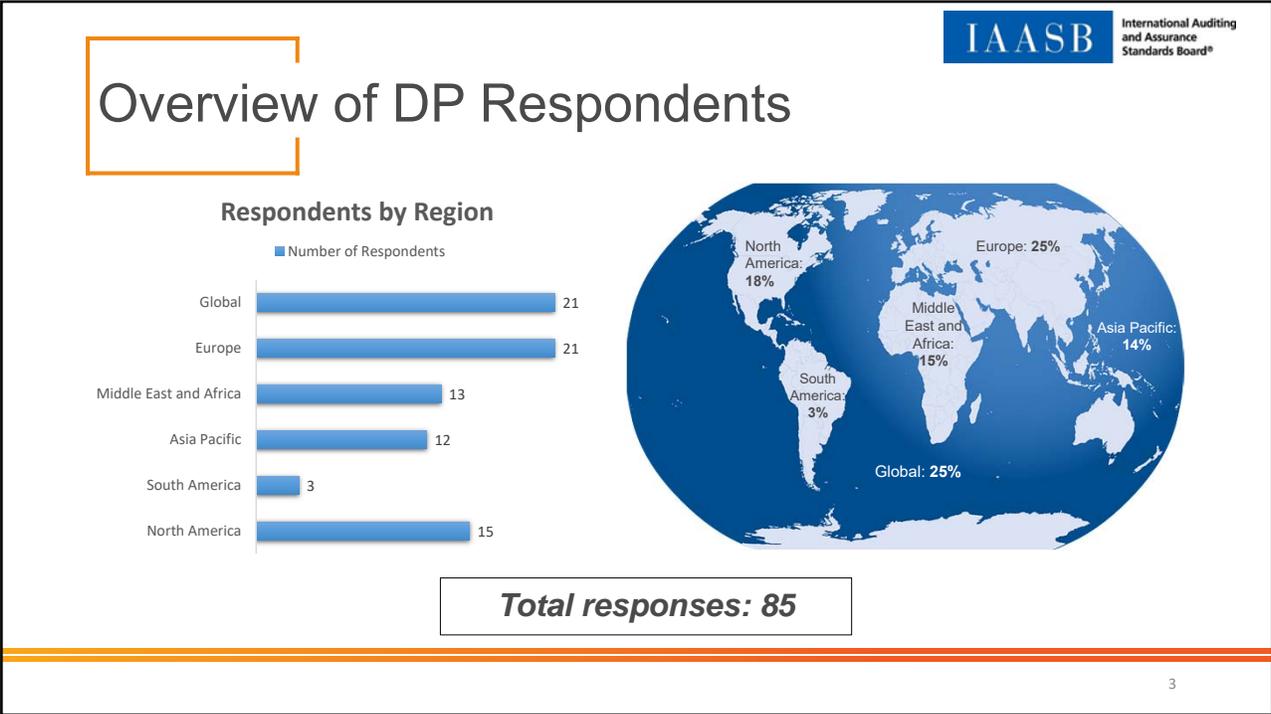
# Objectives

- a) Provide an overview of feedback received related to fraud from the DP
- b) Obtain Board views on the proposed possible way forward on the matters relating to fraud that have been identified

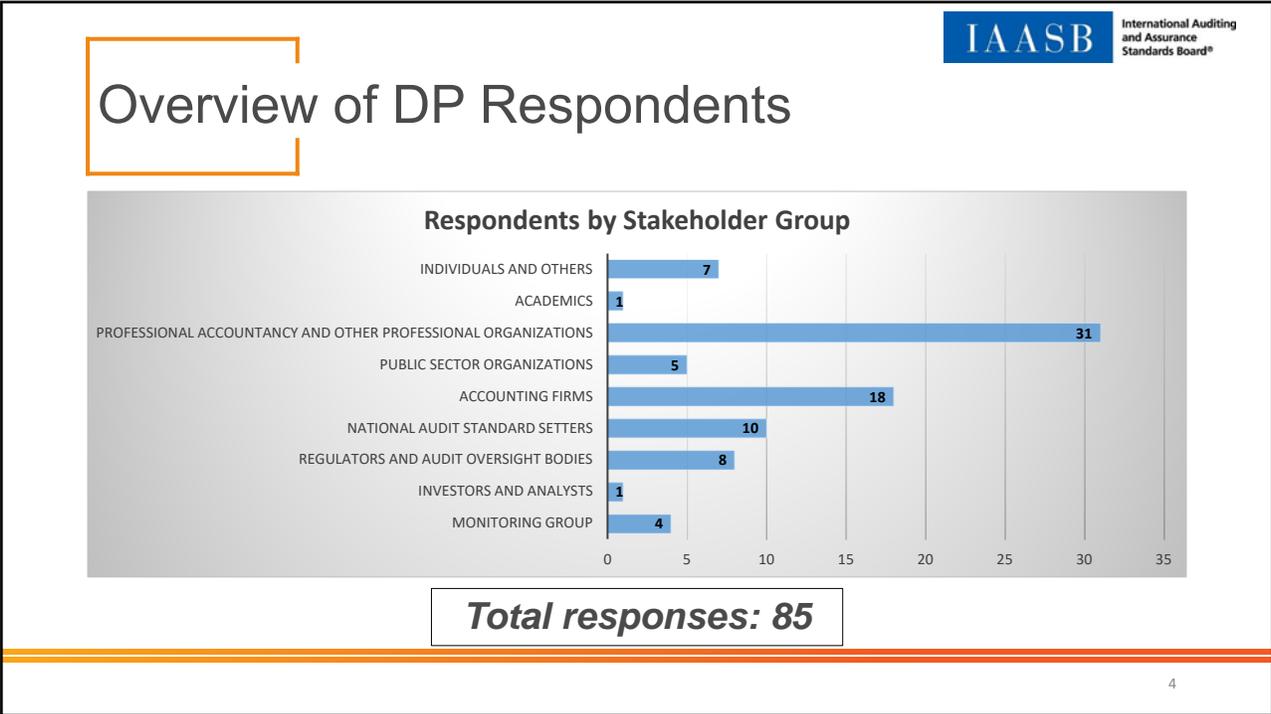
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## Matters for IAASB Consideration

1. Board members are asked, for each of the themes set out below in this Agenda Item, whether they agree with the proposed possible actions, and if not, why not.
2. Board members are asked whether there is anything further that the WG should consider as it develops the project proposal.

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# Standard Setting

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## Stronger Linkages to ISA 315 (Revised 2019)

- Enhanced requirements and linkage related to elements of risk assessment process, including:
  - Obtaining an understanding of the entity and its environment, applicable financial reporting framework and the entity’s system of internal control
  - Identifying and assessing risks of material misstatement due to fraud
  - Understanding the control environment, including corporate culture

**Possible Action #1 - Strengthen the auditor’s consideration of fraud when identifying and assessing risks of material misstatement**

- Standard-setting in ISA 240 to enhance the requirements and application material, as necessary.

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## Enhanced Transparency with TCWG, and Closer or Enhanced Linkage to ISA 550, *Related Parties*

- Enhanced Transparency with TCWG: More robust 2-way communication throughout the audit strengthen link to ISA 260 (Revised)
- Enhanced Linkage to ISA 550: Emphasize consideration of related parties by strengthening link between ISA 240 and ISA 550

**Possible Action #2 – Enhancing the Auditor’s Communications with TCWG**

- Standard-setting in ISA 240 and ISA 260 (Revised) to enhance the requirements and application material, as necessary.

**Possible Action #3 – Enhancing ISA 240 to Make the Link to Related Parties Stronger**

- Standard-setting in ISA 240 to enhance the requirements
- Exploring possible issuance of non-authoritative guidance

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## Matters for IAASB Consideration

1. Board members are asked whether they agree with the proposed possible actions, and if not, why not, for each of the following themes:
  - a. Stronger Linkages to ISA 315 (Revised 2019)
  - b. Enhanced Transparency with TCWG
  - c. Closer or Enhanced Linkage to ISA 550, *Related Parties*
2. Board members are asked whether there is anything further that the WG should consider as it develops the project proposal.

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## Suspicious Mindset and Professional Skepticism

- Not a lot of support for starting from “Suspicious mindset” in all audits, but rather support for enhancing existing concept of professional skepticism

**Possible Action #4 – Enhancements for Professional Skepticism, including Views about Suspicious Mindset**

- Not to pursue concept of “suspicious mindset” more broadly in the ISAs
- Further explore elements of the audit that may benefit from a suspicious mindset (for discussion at future Board meeting)
- Standard-setting to consider changes made in ISA 315 (Revised 2019) and ISA 540 (Revised) for professional skepticism and enhance linkage to ‘stand back’ requirements in other ISAs
- Non-authoritative guidance on application of professional skepticism

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## Journal Entry Testing and Technology

- Journal Entry Testing: Clarify how risk assessment drives nature, timing and extent of journal entry procedures and consider if requirements remain fit for purpose
- Technology: Modernize ISA 240 for advancements in technology

**Possible Action #5 – Making the Journal Entry Testing Requirements More Robust**

- Standard-setting in ISA 240 to enhance the requirements and application material, as necessary.
- Consideration of non-authoritative guidance

**Possible Action #6 – Enhancing ISA 240 for Advancements in Technology**

- Standard-setting in ISA 240 to modernize and enhance application material
- Work collaboratively with Technology Working Group

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## Matters for IAASB Consideration

1. Board members are asked whether they agree with the proposed possible actions, and if not, why not, for each of the following themes:
  - a. Suspicious Mindset and Professional Skepticism
  - b. Journal Entry Testing
  - c. Technology
2. Board members are asked whether there is anything further that the WG should consider as it develops the project proposal.

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## Non-Material Fraud and Unpredictability Procedures

- Non-Material Fraud:
  - Did not support expanding role of auditor to detect all non-material fraud
  - Suggested enhanced linkage to ISA 320, *Materiality in Planning and Performing an Audit*
- Unpredictability:
  - Clarity around the types of unpredictability procedures that can be performed

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## Non-Material Fraud and Unpredictability Procedures

**Possible Action #7 – Considering whether Further Action is Needed for Non-Material Fraud**

- Does not recommend expanding the scope of the auditor to detect all non-material fraud
- Standard-setting in ISA 240 to enhance the requirements and application material, as necessary.
- Consideration of non-authoritative guidance

**Possible Action #8 – Enhancing the Auditor’s Consideration of Unpredictability Procedures in an Audit**

- Standard-setting in ISA 240 enhance application material
- Consideration of non-authoritative guidance

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## Audit Documentation

- Enhancements to specific documentation requirements in ISA 240

**Possible Action #9 – Enhancing and Clarifying the Documentation Requirements in ISA 240**

- Consider if specific documentation requirements needed in ISA 240
- Monitor CUSP project and consider if non-authoritative guidance needed

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## Analytical Procedures, and Enhanced Linkage to Other ISAs

- Analytical Procedures: More robust requirements for planning and completion analytics
- Enhanced Linkage to Other ISAs: Strengthen links between ISA 240 and other ISAs (described in Agenda Item 3)

**Possible Action #10 – Making Analytical Procedures at the Planning and Closing Stages of the Audit More Robust**

- Standard setting to enhance requirements or application material
- Non-authoritative guidance

**Possible Action #11 – Linkage to Other ISAs**

- Standard-setting in ISA 240 enhance requirements or application material
- Consideration of appendix or non-authoritative guidance to show interconnectivity between ISA 240 and other ISAs

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## Matters for IAASB Consideration

1. Board members are asked whether they agree with the proposed possible actions, and if not, why not, for each of the following themes:
  - a. Non-Material Fraud
  - b. Unpredictability Procedures
  - c. Audit Documentation
  - d. Analytical Procedures
  - e. Enhanced Linkage to Other ISAs
2. Board members are asked whether there is anything further that the WG should consider as it develops the project proposal.

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## Areas Where Further Work Group and Board Discussion Needed

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# Forensic Specialists




**Supporting views:**

- Not in all audits, but when fraud is identified or suspected or in high-risk entities
- Use in risk assessment/engagement team discussion or to conduct further investigation when fraud identified or suspected

**Opposing views:**

- Extant standard allows flexibility for practitioner to decide
- Forensic audits differ in nature to financial statement audits
- Scalability and proportionality
- May widen expectation gap

**Possible Action #12 - Determining Whether, and How, Forensic Type Procedures May be Appropriate in an Audit**

- Further analysis and discussion with WG and Board at future meeting

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# Definition of Fraud



- Term “fraud” is used in many contexts, which is sometimes not the same as the way fraud is ‘defined’ in ISA 240
- Consider including other concepts (e.g., bribery and corruption)

**Possible Action #13 - Further Consideration About Whether a Change to the Definition of Fraud is Needed**

- Further analysis and discussion with WG and Board at future meeting

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## Matters for IAASB Consideration

1. Board members are asked whether they agree with the proposed possible actions, and if not, why not, for each of the following themes:
  - a. Forensic Specialists
  - b. Definition of Fraud
2. Board members are asked whether there is anything further that the WG should consider as it develops the project proposal.

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## Transparency: Auditor’s Report

<p><b>Supporting views:</b></p> <ul style="list-style-type: none"> <li>• Increased transparency about auditor’s responsibilities, procedures and conclusions related to fraud</li> <li>• Non-boilerplate, bespoke information</li> </ul>	<p><b>Opposing views:</b></p> <ul style="list-style-type: none"> <li>• Increased length and complexity</li> <li>• May become perfunctory and boilerplate over time</li> <li>• May not effectively address knowledge gap</li> </ul>
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**Possible Action #14 - Exploring Whether to Consider Requiring More Transparency in the Auditor’s Report about Fraud**

- Further analysis and discussion with WG and Board at future meeting
- Coordination with Auditor Reporting Post Implementation Review Working Group

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## Revisit Introductory Language in ISA 240 About Inherent Limitations of an Audit

- Respondents notes the language in the introductory material of ISA 240 around inherent limitations may diminish or add confusion around the auditor’s responsibilities

**Possible Action #15 - Exploring Whether Changes are Needed to the Introductory Paragraphs of ISA 240 About Inherent Limitations of an Audit**

- Further analysis and discussion with WG and Board at future meeting

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## Making the Fraud Brainstorming (Engagement Team Discussion) More Robust

- Enhance rigor of discussion and consider requiring specialists to attend
- Consider requiring more than one engagement team discussion during the audit

**Possible Action #16 - Making the Engagement Team Discussion More Robust for the Auditor’s Considerations Around Fraud**

- Standard setting in ISA 240 to enhance requirements and application material, as necessary
- Further analysis and discussion with WG and Board at future meeting about a requirement to hold more than one engagement team discussion during the audit

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## Clarifying the Relationship Between ISA 240 and ISA 250 (Revised)

- Support for enhancements to clarify the relationship between responding to non-compliance with laws and regulations and responding to instances of fraud

**Possible Action #17—Clarifying the Relationship between ISA 240 and ISA 250 (Revised)**

- Further analysis and discussion with WG and Board at future meeting

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## Matters for IAASB Consideration

1. Board members are asked whether they agree with the proposed possible actions, and if not, why not, for each of the following themes:
  - a. Transparency in the Auditor's Report
  - b. Revisit Introductory Language in ISA 240 About Inherent Limitations of an Audit
  - c. Making the Fraud Brainstorming (Engagement Team Discussion) More Robust
  - d. Clarifying the Relationship Between ISA 240 and ISA 250 (Revised)
2. Board members are asked whether there is anything further that the WG should consider as it develops the project proposal.

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## Rebuttable Presumption

- Inconsistent application of when it is appropriate to rebut
- Questioned if there are other areas beyond revenue that should be emphasized in fraud standard (e.g. inventory, property valuation)

**Possible Action #18—Further Considering the Presumed Risk of Fraud in Revenue Recognition and What Changes Are Needed**

- Further analysis and discussion with WG and Board at future meeting

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## Requirements When Fraud is Detected, and External Confirmations

- Requirements when Fraud is Detected:
  - Clarification and enhancements around the requirements when fraud is suspected or identified
- External Confirmations:
  - How to assess reliability of external confirmations with regard to possibility of fraud
  - How to respond when there is no reply to confirmation request
  - Stronger expectations for obtaining external confirmations
  - Professional skepticism when evaluating external confirmations

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## Requirements When Fraud is Detected, and External Confirmations (cont.)

**Possible Action #19 – Further Considering What Changes are Needed Related to Procedures when Fraud is Detected or Identified**

- Further analysis and discussion with WG and Board at future meeting

**Possible Action #20—Strengthening Requirements About the Auditor’s Considerations for External Confirmations**

- Further analysis and discussion with WG and Board at future meeting

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## Matters for IAASB Consideration

1. Board members are asked whether they agree with the proposed possible actions, and if not, why not, for each of the following themes:
  - a. Rebuttable Presumption
  - b. Requirements When Fraud is Detected
  - c. External Confirmations
2. Board members are asked whether there is anything further that the WG should consider as it develops the project proposal.

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# Non-Authoritative Guidance

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## Third-Party Fraud



- Clarification of auditor’s responsibilities on third-party fraud

**Possible Actions #22—Addressing Auditor’s Considerations Relating to Third-Party Fraud**

- Does not recommend expanding the role of the auditor to detect third-party fraud that is not directly related to a material misstatement in the financial statements
- Consider issuing non-authoritative guidance

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## Development of Non-Authoritative Materials

- Respondents provided suggestion of areas where non-authoritative materials may be helpful.

**Possible Actions #21—Development of Non-Authoritative Materials**

- Further WG analysis of areas where non-authoritative guidance is needed
- Discussion with Board at future meeting

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## Matters for IAASB Consideration

1. Board members are asked whether they agree with the proposed possible actions, and if not, why not, for each of the following themes:
  - a. Third-party fraud
  - b. Development of Non-Authoritative Materials
2. Board members are asked whether there is anything further that the WG should consider as it develops the project proposal.

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# No Further Action Recommended

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## Engagement Quality Reviews (EQR)



- EQRs when auditor has determined a suspicion or heightened risk of material misstatement due to fraud exists
- ISQM standards fit for purpose

**Possible Action #23—Enhancing Requirements for Engagement Quality Reviews**

- No further action recommended as ISQM standards are sufficiently robust

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## Expectation Gap

- Respondents thought the DP’s explanation of the expectation gap was helpful (ACCA 3-component definition), though some suggested alternative frameworks or terminology
- Responses related to primary cause of expectation gap did not necessarily correlate to solutions proposed

**Possible Action #24—Expectation Gap**

- No further action recommended to refine description of expectation gap

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## Matters for IAASB Consideration

1. Board members are asked whether they agree with the proposed possible actions, and if not, why not, for each of the following themes:
  - a. Engagement Quality Reviews
  - b. Expectation gap
2. Board members are asked whether there is anything further that the WG should consider as it develops the project proposal.

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# Other General Recommendations

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## Root Cause Analysis



- Respondents called for root cause analysis to understand the roles of all parties and the underlying reasons for corporate failures
- Changes to audit standards should not be made without evidence that proposed changes will address the underlying issues.

**Possible Action #25—Root Cause Analysis**

- Further outreach with regulators, forensic investigation specialists and crime commission representatives as well as accounting firms

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## Work of Others, Continued Outreach, and Coordination with IESBA and Other Projects

- Respondents encouraged:
  - Monitoring work being done in other jurisdictions or organizations related to fraud
  - Continued outreach with stakeholders
  - Coordination with IESBA
  - Coordination with other IAASB projects

**Possible Action #26—Ongoing Activities**

- The WG will continue the above-noted activities over the course of the project.

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## Education

- Respondents commented about the need for education and/or training on fraud

**Possible Action #27—Education Activities**

- Consider how the IAASB can best encourage others to consider the matters raised
- Consider further action for areas within the IAASB's remit

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## Importance of the Role of Others

- Respondents suggested actions for other stakeholders in the financial reporting ecosystem
- Emphasized importance of multi-stakeholder approach

**Possible Action #28—Encouraging Others in the Financial Reporting Ecosystem to Take Action**

- Issue communication from the IAASB Chair.
- Continued participation in the global discussion on this topic through outreach with others.
- Further consideration of how the IAASB can encourage others in the financial reporting ecosystem to act.

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## Other Matters

- Respondents commented on the following other matters:
  - Emphasized importance of developing principles-based standards
  - Separate assurance engagements over internal controls
  - Application material specific to public sector

**Possible Actions #29—Other Actions**

- Continue to develop standards and guidance that are scalable, proportionate, and principles based.
- Monitor developments on internal controls engagements and requirements globally.
- Enhance application material or issue guidance to provide public sector context as needed.

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## Matters for IAASB Consideration

1. Board members are asked whether they agree with the proposed possible actions, and if not, why not, for each of the following themes:
  - a. Root Cause Analysis
  - b. Work of Others, Continued Outreach, and Coordination with IESBA and Other Projects
  - c. Education
  - d. Importance of the Role of Others
  - e. Other Matters
2. Board members are asked whether there is anything further that the WG should consider as it develops the project proposal.

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