

RESPONSE TEMPLATE FOR THE EXPOSURE DRAFT OF PROPOSED ISA 240 (REVISED)

Guide for Respondents

Comments are requested by **June 5, 2024**.

This template is for providing comments on the Exposure Draft (ED) of *Proposed International Standard on Auditing 240 (Revised), The Auditor's Responsibilities Relating to Fraud in an Audit of Financial Statements and Proposed Conforming and Consequential Amendments to Other ISAs (ED-240)*, in response to the questions set out in the Explanatory Memorandum (EM) to the ED. It also allows for respondent details, demographics and other comments to be provided. Use of the template will facilitate the IAASB's automated collation of the responses.

You may respond to all questions or only selected questions.

To assist our consideration of your comments, please:

- For each question, start by indicating your overall response using the drop-down menu under each question. Then below that include any detailed comments, as indicated.
- When providing comments:
 - Respond directly to the questions.
 - Provide the rationale for your answers. If you disagree with the proposals in the ED, please provide specific reasons for your disagreement and specific suggestions for changes that may be needed to the requirements, application material or appendices. If you agree with the proposals, it will be helpful for the IAASB to be made aware of this view.
 - Identify the specific aspects of the ED that your response relates to, for example, by reference to sections, headings or specific paragraphs in the ED.
 - Avoid inserting tables or text boxes in the template when providing your responses to the questions because this will complicate the automated collation of the responses.
- Submit your comments, using the response template only, without a covering letter or any summary of your key issues, instead identify any key issues, as far as possible, in your responses to the questions.

The response template provides the opportunity to provide details about your organization and, should you choose to do so, any other matters not raised in specific questions that you wish to place on the public record. All responses will be considered a matter of public record and will ultimately be posted on the IAASB website.

Use the "**Submit Comment**" button on the ED [web page](#) to upload the completed template.

PART A: Respondent Details and Demographic information

Your organization's name (or your name if you are making a submission in your personal capacity)	AUASB
Name(s) of person(s) responsible for this submission (or leave blank if the same as above)	Doug Niven – AUASB Chair
Name(s) of contact(s) for this submission (or leave blank if the same as above)	Rene Herman
E-mail address(es) of contact(s)	rherman@auasb.gov.au
Geographical profile that best represents your situation (i.e., from which geographical perspective are you providing feedback on the ED). Select the most appropriate option.	Asia Pacific
	If "Other," please clarify.
The stakeholder group to which you belong (i.e., from which perspective are you providing feedback on the ED). Select the most appropriate option.	Jurisdictional/ National standard setter
	If "Other," please specify.
Should you choose to do so, you may include information about your organization (or yourself, as applicable).	

Should you choose to do so, you may provide overall views or additional background to your submission. **Please note that this is optional.** The IAASB's preference is that you incorporate all your views in your comments to the questions (also, question no. 10 in Part B allows for raising any other matters in relation to the ED).

Information, if any, not already included in responding to the questions in Part B:

This submission clearly identifies where the views are those of the AUASB, which may be informed by feedback from Australia practitioners. This submission also outlines feedback from Australia practitioners that is not necessarily the view of the AUASB.

PART B: Responses to Questions for Respondents in the EM for the ED

For each question, please start with your overall response by selecting one of the items in the drop-down list under the question. Provide your detailed comments, if any, below as indicated.

Responsibilities of the Auditor

1. Does ED-240 clearly set out the auditor's responsibilities relating to fraud in an audit of financial statements, including those relating to non-material fraud and third-party fraud?

(See EM, Section 1-C, paragraphs 13–18 and Section 1-J, paragraphs 91–92)

(See ED, paragraphs 1–11 and 14)

Overall response: [Agree, with comments below](#)

Detailed comments (if any):

The AUASB is supportive of the auditor's responsibilities relating to fraud as set out in ED-240. The auditor has the primary responsibility for audit quality. While fraud can be more difficult to detect, overall ED-240 appropriately outlines the auditor's responsibilities in obtaining reasonable assurance that the financial report is not materially misstated, whether due to error or fraud.

We also agree that the primary responsibility for the prevention and detection of fraud rests with management and those charged with governance (TCWG). Australian practitioners have highlighted continuing concerns with expectation gaps and that some users of financial reports and others may have a perception that the auditor has sole or primary responsibility for preventing and detecting material fraud.

While recognising the challenges in addressing expectation gaps, there should be appropriate communication and education in national jurisdictions on the responsibilities of management and TCWG. Greater transparency by the auditor should be complemented in due course by jurisdictional requirements for statements by TCWG as to how the risks of material fraud have been identified and addressed.

We also note that securities and audit regulators in Australia and elsewhere have worked to educate and remind management and TCWG on their roles and responsibilities in relation to financial reporting quality, as well as how they can support audit quality. Guidance issued by IOSCO for audit committees and others includes [IOSCO Report on Good Practices for Audit Committees in Supporting Audit Quality](#) (January 2019) and [IOSCO Consultation on Goodwill \(June 2023\)](#).

Other matters raised by Australian practitioners in connection with expectation gaps included:

- ED-240 does not adequately convey in all instances that auditors are only responsible for financial statement fraud that could result in a material misstatement. For example, paragraph 2 on the auditor's responsibilities refers to the risk of material misstatement, whereas subparagraph 2(b) on reporting does not refer to the risk of material misstatement.
- Paragraph A21 should state the auditor is not responsible for conducting an in-depth assessment of third-party fraud risk and that a more specific targeted engagement would be required to address those risks. Practitioners noted that the example of a cybersecurity breach in paragraph A16 may be contradictory to the intent of IAASB not to expand the auditor's role.

- The use of the word ‘possibility’ through ED-240, for example in paragraphs 12 and 19, could be interpreted as potentially broadening the auditor’s role and responsibilities. Paragraph 19 should be more closely aligned with ISA 200, which states, “The auditor shall plan and perform an audit with professional skepticism recognizing that circumstances may exist that cause the financial statements to be materially misstated.”
- Reversing the order of the introductory paragraphs on the auditor’s responsibilities and management’s responsibilities.
- Paragraph A12 on the factors that may make it more difficult to detect fraud compared to error (e.g. collusion) should be reinstated into the introductory paragraphs.

Professional Skepticism

2. Does ED-240 reinforce the exercise of professional skepticism about matters relating to fraud in an audit of financial statements?

(See EM, Section 1-D, paragraphs 19–28)

(See ED, paragraphs 12–13 and 19–21)

Overall response: [Agree, with comments below](#)

Detailed comments (if any):

The AUASB considers ED-240 appropriately reinforces the exercise of professional scepticism about matters relating to fraud in an audit of financial statements. However, the IAASB should consider:

- Adding application material to enhance the requirement in paragraph 21 of ED-240 for the auditor to ‘remain alert’ to information throughout the audit that may indicate a risk of fraud. The auditor should be more proactive and challenging but there should not be a requirement to consider fraud in relation to all information as this would create an unduly burdensome documentation requirement.
- Reinstating the text from extant ISA 240 paragraph 13 “notwithstanding the auditor’s past experience of the honesty and integrity of the entity’s management and those charged with governance” to remind the auditor to set aside any potential biases and encourage the exercise of professional scepticism.
- Limiting ED-240 paragraph 21 to events or conditions that indicate an incentive or pressure to commit fraud or provide an opportunity to commit fraud so that it is clear that the auditor is not required to always undertake extensive fraud related procedures throughout the audit.

The second sentence in paragraph 14 of extant ISA 240 on authenticity of documents remains in paragraph 20 of ED-240 - ‘If conditions identified during the audit cause the auditor to believe that a document may not be authentic or that terms in a document have been modified but not disclosed to the auditor, the auditor shall investigate further.’ The AUASB is supportive of the removal of the first sentence in paragraph 14 of the extant ISA 240 and in ISA 200 - ‘Unless the auditor has reason to believe the contrary, the auditor may accept records as genuine’.

Risk Identification and Assessment

3. Does ED-240 appropriately build on the foundational requirements in ISA 315 (Revised 2019)¹ and other ISAs to support a more robust risk identification and assessment as it relates to fraud in an audit of financial statements?

(See EM, Section 1-F, paragraphs 36–46)

(See ED, paragraphs 26–42)

Overall response: [Agree, with comments below](#)

Detailed comments (if any):

The AUASB is strongly supportive of the strengthening of requirements and application material as it relates to risk assessment procedures and related activities. The AUASB is particularly supportive of the following new/enhanced requirements:

- Paragraph 33 of ED-240 focusing on aspects of the auditor’s understanding of the entity and its environment.
- Paragraphs 34-38 of ED-240 focusing on aspects of the auditors understanding of the components of the entity’s system of internal control.
- Paragraph 39 of ED-240 for the auditor to determine whether there are deficiencies in internal control identified relevant to the prevention or detection of fraud.
- Paragraph 16 of ED-240 making the engagement team discussions more robust.

The AUASB makes the following recommendations for the IAASB:

- The rebuttal of the presumption of the significant risk of fraud in revenue recognition should be at the assertion level rather than the account level. The associated inherent risk assessment is performed at the assertion level.
- Further consideration should be given to whether the pressures or incentives for management to commit fraudulent financial reporting and to manipulate the revenue growth or profit, may be less significant for smaller unlisted entities, where owners are also managers. The risks may lie more in the presentation of liabilities, affecting banking facilities and covenants.
- Consider including examples specific to public sector entities. For example:
 - The presumed fraud risk for revenue may be more easily rebutted for appropriation funding; and
 - Highlighting the possible greater risk in the public sector procurement / contract management concerning undisclosed conflicts of interest.
- Clarity and consistency across ED-240 paragraphs 42 and 48. ED-240 paragraph 42 requires that management override is always treated as a significant risk, while paragraph 48 seems to indicate that this is not always the case ‘irrespective of the auditor’s assessment of the risks of management override...’.

¹ ISA 315 (Revised 2019), *Identifying and Assessing the Risks of Material Misstatement*

Fraud or Suspected Fraud

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?

(See EM, Section 1-G, paragraphs 47–57 and Section 1-E, paragraph 35)

(See ED, paragraphs 55–59 and 66–69)

Overall response: [Disagree, with comments below](#)

Detailed comments (if any):

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:

1. Splitting paragraph 55 with only 55(a) and 55(b) required for all instances of identified fraud or suspected fraud.
2. Paragraph 55(c) and 55(d) are not required where instances of fraud or suspected fraud are clearly trivial.
3. 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.
4. 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.
5. 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.
6. 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.
7. 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.

Transparency on Fraud-Related Responsibilities and Procedures in the Auditor's Report

5. Does ED-240 appropriately enhance transparency about matters related to fraud in the auditor's report?

(See EM, Section 1-H, paragraphs 58–78)

(See ED, paragraphs 61–64)

Overall response: [Disagree, with comments below](#)

Detailed comments (if any):

On balance, in the public interest and to satisfy the needs expressed by users of financial statements for more transparency about matters related to fraud in the auditor's report, the AUASB supports enhanced transparency through key audit matter (KAM) style reporting in the auditor's report for listed entities about matters related to fraud. However, the AUASB believes that the IAASB should not proceed with the proposed requirements without addressing the following:

- Replacing the heading 'Key Audit Matters Including Matters Related to Fraud' in the audit report with 'Key Audit Matters (Including Matters Related to Fraud and Error)' for consistency with the text that appears immediately after the heading. This will avoid over-emphasising the importance of fraud risk compared to risk of error.
- Including appropriate examples in the application material demonstrating that fraud related KAMs are often interlinked with KAMs related to error (e.g. a KAM related to an estimate). Otherwise, KAM related fraud risks may always be treated as stand-alone KAMs, which may drive boilerplate statements.
- Where there are no KAMs related to fraud, highlighting in the auditor's report that the auditor's objective is to obtain reasonable assurance that the financial report as a whole is free of material misstatement, whether due to fraud or error.

In due course, national jurisdictions should consider complementing greater transparency by the auditor with more transparency from directors around the responsibilities of management and TCWG in relation to the prevention and detection of fraud, including how the risks of material fraud have been identified and addressed.

Australian practitioners expressed concern that increased transparency in relation to fraud in the auditor's report places undue focus on fraud and may increase the expectation gap. Some practitioners were concerned with possible litigation where a material fraud is later discovered but there was no KAM in the auditor's report. Additionally, a fraud matter may still be under investigation at the time of the audit report and communicating the matter in a KAM could create legal risk for both the company and the auditor.

Australian practitioners expressed concern that some auditors could include boilerplate fraud related KAMs (e.g. on management override of controls) to avoid stating that there are no KAMs related to fraud to communicate.

6. In your view, should transparency in the auditor's report about matters related to fraud introduced in ED-240 be applicable to audits of financial statements of entities other than listed entities, such as PIEs?

(See EM, Section 1-H, paragraphs 76–77)

(See ED, paragraphs 61–64)

Overall response: [Disagree, with comments below](#)

Detailed comments (if any):

The AUASB's response to the IAASB's PIE Track 2 ED was not supportive of extending the extant differential requirements for communicating KAM to apply to PIEs rather than listed entities only.

In December 2022, the AUASB conducted an Auditor Reporting Post Implementation Review (PIR) and feedback from Australian stakeholders included:

- KAMs should not be expanded to unlisted PIEs in the absence of clear evidence that there would be benefits for users. Stakeholders acknowledged that it is difficult to gather this evidence.
- ISA 701 currently permits auditors of non-listed entities to voluntarily report KAMs, but this is done infrequently because KAMs are not considered valuable for such entities.
- Whilst KAMs are not mandatory in the public sector, a number of public sector audit offices in Australia have adopted the reporting of KAMs for certain entities that they audit, noting they are an effective tool for increasing the transparency of auditors in the conduct of their work.

Considering a Separate Stand-back Requirement in ED-240

7. Do you agree with the IAASB's decision not to include a separate stand-back requirement in ED-240 (i.e., to evaluate all relevant audit evidence obtained, whether corroborative or contradictory, and whether sufficient appropriate audit evidence has been obtained in responding to the assessed risks of material misstatement due to fraud)?

(See EM, Section 1-J, paragraphs 107–109)

Overall response: [Disagree, with comments below](#)

Detailed comments (if any):

A stand back provision would be an important part of our suggestion in response to Question 4 to introduce a clearly trivial exclusion from applying all parts of paragraph 55. See our response to Question 4 for more information.

Scalability

8. Do you believe that the IAASB has appropriately integrated scalability considerations in ED-240 (i.e., scalable to entities of different sizes and complexities, given that matters related to fraud in an audit of financial statements are relevant to audits of all entities, regardless of size or complexity)?

(See EM, Section 1-J, paragraph 113)

Overall response: [Disagree, with comments below](#)

Detailed comments (if any):

See Response to Question 4.

ED-240 paragraph A88 states that “When there are no formalized processes or documented policies or procedures, the auditor is still required to obtain an understanding of how management, or where appropriate, those charged with governance identify fraud risks related to the misappropriation of assets and fraudulent financial reporting and assesses the significance of the identified fraud risks.” Additional guidance on what constitutes appropriate and sufficient audit evidence that is required to conclude on the entity’s control environment for smaller entities should be considered.

The examples in ED-240 paragraph A29 may apply mainly to larger, more complex entities (such as references to audit committee, internal audit function and whistleblower program). We recommend including examples relevant to smaller entities to better address scalability.

Linkages to Other ISAs

9. Does ED-240 have appropriate linkages to other ISAs (e.g., ISA 200,² ISA 220 (Revised),³ ISA 315 (Revised 2019), ISA 330,⁴ ISA 500,⁵ ISA 520,⁶ ISA 540 (Revised)⁷ and ISA 701⁸) to promote the application of the ISAs in an integrated manner?

(See EM, Section 1-J, paragraphs 81–84)

Overall response: [Agree \(with no further comments\)](#)

Detailed comments (if any):

² ISA 200, *Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with International Standards on Auditing*

³ ISA 220 (Revised), *Quality Management for an Audit of Financial Statements*

⁴ ISA 330, *The Auditor’s Responses to Assessed Risks*

⁵ ISA 500, *Audit Evidence*

⁶ ISA 520, *Analytical Procedures*

⁷ ISA 540 (Revised), *Auditing Accounting Estimates and Related Disclosures*

⁸ ISA 701, *Communicating Key Audit Matters in the Independent Auditor’s Report*

Other Matters

10. Are there any other matters you would like to raise in relation to ED-240? If so, please clearly indicate the requirement(s) or application material, or the theme or topic, to which your comment(s) relate.

Overall response: [Yes, with comments below](#)

Detailed comments (if any):*Documentation*

Paragraph 70 of the ISA-240 ED contains detailed documentation requirements but these requirements are not complete. For example, paragraph 70(c) does not require documentation on the responses to identified and assessed risks. While it may be arguable that the principles in ASA 230 *Documentation* are sufficient, the IAASB should consider whether including many detailed documentation requirements but excluding some others might imply to some practitioners that the excluded requirements do not apply in the case of fraud.

The IAASB should also consider the following matters in connection with *communications with those charged with governance (TCWG)*:

- Paragraph 67 requires an auditor to communicate to TCWG identified fraud or suspected fraud involving management, employees who have significant roles in internal control or others where the fraud results in a material misstatement in the financial statements. Paragraph 67 should cover all identified fraud or suspected fraud, for example, including third party fraud matters. The only exclusion should be where the auditor has clear direct evidence that TCWG are already aware of a fraud, its nature and extent (e.g. through Board minutes, investigation reports commissioned by the Board, public announcements by the company, or communications by TCWG to the auditor).
- Requiring the auditor to sense check why there is no KAM for a risk or matter communicated to TCWG.

The IAASB could consider providing additional application guidance in the following areas:

- The content of paragraph 55 of the Explanatory Memorandum could be included in paragraphs A7-A9 to make it clear that the phrase “fraud or suspected fraud identified by the auditor” covers both fraud and suspected fraud (including allegations of fraud) and fraud identified directly or indirectly.
- Paragraph A31 could include remote working by members of the engagement team as another example of a circumstance that may impede the exercise of professional skepticism.
- Application guidance could be provided to paragraph 56(b) about the impact of identified or suspected fraud on other engagements including engagements from prior years. Where the fraud impacts on prior periods, it may be useful to cover:
 - the extent of audit procedures for the prior period(s); and
 - whether the auditor should only go back as far as the current period opening balance.
- A decision tree or flowchart could be provided showing the potential progression from alleged or suspected fraud to identified fraud and the iterative nature of fraud risk assessment.
- The example in paragraph A166 could refer to management overlays for ECLs to cover data, assumption and model limitations. Such overlays may also be subject to management bias.

Other matters that should be considered by the IAASB are:

- *Analytical procedures:* paragraph A114 of ISA-240 ED should specifically refer to ‘substantive analytical procedures’ rather than ‘analytical procedures’.
- *Fraud risk factors:* The first sentence of paragraph A22 refers to consideration of fraud risk factors as inherent risk factors. The third sentence of paragraph A22 says that fraud risk factors may also relate to events or conditions that exist in the entity’s system of internal controls. There should be clarity that fraud risk factors are inherent risks that may not be adequately addressed by the system of internal controls. If the IAASB is of the view that the system of internal controls could be the source of a fraud risk in itself in the absence of an inherent risk, it would be useful to provide further explanation or examples.

Translations

11. Recognizing that many respondents may intend to translate the final ISA for adoption in their own environments, the IAASB welcomes comment on potential translation issues respondents note in reviewing the ED-240.

Overall response: No response

Detailed comments (if any):

Effective Date

12. Given the need for national due process and translation, as applicable, and the need to coordinate effective dates with the Going Concern project and the Listed Entity and PIE – Track 2 project, the IAASB believes that an appropriate effective date for the standard would be for financial reporting periods beginning approximately 18 months after approval of the final standard. Earlier application would be permitted and encouraged. Would this provide a sufficient period to support effective implementation of the ISA?

(See EM, Section 1-J, paragraphs 115–116)

(See ED, paragraph 16)

Overall response: No response

Detailed comments (if any):