

## 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)	Independent Regulatory Board for Auditors (IRBA)
Name(s) of person(s) responsible for this submission (or leave blank if the same as above)	Imran Vanker Liesel du Preez
Name(s) of contact(s) for this submission (or leave blank if the same as above)	
E-mail address(es) of contact(s)	<a href="mailto:ivanker@irba.co.za">ivanker@irba.co.za</a> <a href="mailto:ldupreez@irba.co.za">ldupreez@irba.co.za</a>
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.	<a href="#">Africa and Middle East</a>
	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.	<a href="#">Jurisdictional/ National standard setter</a>
	If “Other,” please specify.
Should you choose to do so, you may include information about your organization (or yourself, as applicable).	The IRBA is both the audit regulator and national audit and ethics standard setter in South Africa. Its statutory objectives include the protection of the public by regulating audits performed by registered auditors, and the promotion of investment and employment in the Republic. The statutory Committee for Auditing Standards (CFAS) is responsible for assisting the IRBA to adopt, develop, maintain, issue, and prescribe auditing pronouncements.

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:**

1. We appreciate this opportunity to comment on ED-240.

2. From a public interest perspective, we support the IAASB's objectives to:
  - Clarify the role and responsibilities of the auditor for fraud in an audit of financial statements.
  - Promote consistent behaviour and facilitate effective responses to identified risks of material misstatement due to fraud.
  - Enhance transparency on fraud-related procedures where appropriate.
3. In our responses to the specific questions, we propose further enhancements related to these objectives, specifically:
  - Enhancements to the introduction section of ED-240 to achieve a synonymous understanding of the auditor's responsibilities related to fraud, including the meaning of fraud to promote consistent behaviour in responding to fraud and to enhance auditor accountability.
  - Encouraging the IAASB to select a uniform approach to building on the foundational requirements from other standards, and balancing incorporating the principles from other ISAs and tailoring those principles to be relevant to the auditor's responsibilities related to fraud in order to promote understandability.
  - Differentiation between the applicability of requirements to different fraud or suspected fraud scenarios.
  - Encouraging the IAASB to reflect on whether the practical challenges surrounding the communication of fraud-related KAMs can be overcome to enable enhanced transparency.
  - Encouraging the IAASB to consider proposed enhancements to the director's responsibilities paragraph in the auditor's report (ISA 700 (Revised)) to further support transparency of fraud-related responsibilities in the public interest.
4. We trust that these recommendations will be useful to the IAASB in finalising ED-240.
5. The IRBA Task Group that drafted this comment letter on behalf of the IRBA represents members from the audit profession, including auditors that practice within the private and the public sector (representatives from the Auditor-General of South Africa), forensic experts, academics, audit standard-setters and regulatory bodies.

## 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):**

1. We support the following steps taken by the IAASB to address the key issues identified in the project proposal related to the roles and responsibilities of the auditor:
  - 1.1. Decoupling the auditor's responsibilities from the inherent limitations<sup>1</sup>
  - 1.2. Not expanding the role and responsibilities of the auditor<sup>2</sup>
2. However, we are concerned that the IAASB has not done enough to achieve its objectives of clarifying the auditor's (general) responsibilities relating to fraud in an audit of financial statements, and specifically non-material and third-party fraud. Our rationale for proposing further enhancements is that clarity about the auditor's responsibilities related to fraud, including the meaning of fraud, will contribute to the public interest objective of promoting consistent behaviour and facilitating effective responses to identified risks of material misstatement due to fraud in an audit of financial statements. We therefore propose:

### **Enhancements to the introduction section of ED-240, including:**

#### **Explaining the interrelated roles and responsibilities of management, those charged with governance and auditors related to fraud.**

- 2.1. The separation of the responsibilities of the *auditor* and *management and those charged with governance* in ED-240, creates the perception that these responsibilities are mutually exclusive and independent of each other. This is contrary to the position that the effectiveness of fraud prevention and detection is contingent upon the synergistic efforts of both *management and those charged with governance*, and the auditor.

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<sup>1</sup> Explanatory Memorandum paragraph 15

<sup>2</sup> Explanatory Memorandum paragraph 17

- 2.2. The [IAASB's Discussion Paper on Fraud and Going Concern in an Audit of the Financial Statements](#) emphasised that auditors have a key dependency on others in the financial reporting ecosystem. For example, *management*, for the prevention and detection of fraud, and *those charged with governance* to work with management, to oversee the establishment of appropriate anti-fraud controls and take the necessary steps when fraud is detected.<sup>3</sup>
- 2.3. The *Responsibilities of the Auditor, Management and Those Charged with Governance* section of the introduction to ED-240 could acknowledge that there is a financial reporting ecosystem and could emphasise the synergy of these parties' responsibilities through explaining their interrelated roles and responsibilities.

### **Elevating the engagement partner's leadership responsibilities related to fraud.**

- 2.4. ISA 220 (Revised), *Quality Management for an Audit of Financial Statements*, deals with the specific responsibilities of the auditor regarding quality management at the engagement level for an audit of financial statements, and the related responsibilities of the engagement partner.<sup>4</sup> Paragraphs 13 - 15 of this ISA elaborates on the engagement partner's responsibility to create an environment for the audit engagement that emphasizes the firm's culture and expected behaviour of engagement team members, including emphasising:
- (a) That all engagement team members are responsible for contributing to the management and achievement of quality at the engagement level;
  - (b) The importance of professional ethics, values, and attitudes to the members of the engagement team;
  - (c) The importance of open and robust communication within the engagement team, and supporting the ability of engagement team members to raise concerns without fear of reprisal; and
  - (d) The importance of each engagement team member exercising professional scepticism throughout the audit engagement.<sup>5</sup>
- 2.5. The introduction section to ED-240 could benefit from emphasising, not only professional scepticism and professional judgement as it currently does in paragraphs 12 and 13, but the broader leadership responsibility of the engagement partner that encompasses creating an audit environment that is conducive to fraud risk identification<sup>6</sup> to enforce accountability.
- 2.6. We therefore propose expanding on this current link from ISA 220 and incorporating this broader leadership responsibility into the *Responsibilities of the Auditor*,

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<sup>3</sup> [IAASB's Discussion Paper on Fraud and Going Concern in an Audit of the Financial Statements](#) page 14

<sup>4</sup> ISA 220 paragraph 1

<sup>5</sup> ISA 220 paragraph 14

<sup>6</sup> [IRBA Fraud Staff Audit Practice Alert](#)

*Management and Those Charged with Governance* section of the introduction to ED-240.

### Explaining the manner in which information that is indicative of fraud or suspected fraud comes to the auditor's attention throughout the audit<sup>7</sup>

- 2.7. Paragraph A29 in ED-240 explains that there are various ways in which information that is indicative of fraud or suspected fraud can come to the auditor's attention for example, through management, employees, or internal auditors. Incorporating this into the introduction section of ED-240 has the following potential benefits:
- a. It emphasises that the auditor is not solely responsible for the identification of fraud.
  - b. It enhances the understanding of the meaning of fraud in the context of a financial statement audit.
  - c. It sets the scene for a response section that is tailored to the specific circumstances of the fraud or suspected fraud. Refer to our response to Question 4.
- 2.8. We propose introducing a new subheading under the Key Concepts in this ISA section of the introduction to ED-240, namely *Understanding fraud and how it can come to the auditor's attention* and incorporating paragraph A29 under this heading.

### Enhancements to the inherent limitations paragraph

- 2.9. We support the inclusion of the statement in ED-240 paragraph 9 that the inherent limitations do not diminish the auditor's responsibilities relating to fraud.
- 2.10. Additionally, we propose incorporating the fact that the auditor does not make legal determinations of whether fraud has actually occurred into the *inherent limitations*' subsection because it does influence the auditor's ability to assess the impact on the financial statements and take further steps in accordance with ED-240 in the midst of an open investigation. It also better aligns with ISA 200.A52.
- 2.11. Overall, we reflected on the length and complexity of the *Inherent Limitations* section and question whether:
- a. the inherent limitations are understandable (the repeated use of "not"), and
  - b. balanced in comparison with how the introduction addresses the auditor's responsibilities related to fraud.
- 2.12. We propose that it may benefit from redrafting for clarity and conciseness.

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<sup>7</sup> ED-240 paragraph A29

## Non-material fraud

3. We agree conceptually that:
  - 3.1. fraud can be non-material i.e., based on the quantitative assessment it can be immaterial to the financial statements.
  - 3.2. the auditor's judgement about materiality must involve both quantitative and qualitative considerations.
4. However, ED-240 doesn't go far enough in defining non-material fraud and the auditor's responsibilities related to responding to non-material fraud. Therefore, we encourage the IAASB to do more to achieve its objective of promoting consistent behaviour and effective response in this regard. For example:
  - Given that suspected fraud is not always quantifiable, how do you determine if it is non-material suspected fraud?
  - What is the difference between non-material suspected fraud and suspected fraud that cannot (perhaps yet) be directly linked to the financial statements for example third-party fraud and fraudulent acts extending from suspicions of corruption, bribery or money laundering?
  - Can fraud perpetrated by management be non-material to the financial statements? We acknowledge the application material in A11 indicates that if fraud is perpetrated by management, a quantitatively immaterial fraud *may* be qualitatively material. Is the intention then to suggest that it can also still be non-material?
  - Considering fraud is by nature *intentional*, what is a reasonable explanation for *why* the fraud was perpetrated? What reason will lead the auditor to conclude that a quantitatively immaterial fraud is also qualitatively non-material? The example in paragraph A11(b) is unclear because it involves management which would support that the fraud is material regardless of the *why*.
  - Paragraph 8 is not explicit about fraud that is quantitatively material i.e. it doesn't specify that fraud that is quantitatively material to the financial statements is always material. Does the IAASB envision a scenario where a quantitatively material fraud could be concluded to be non-material for qualitative reasons, for example if the nature of the misstatement due to fraud is misclassification or disclosure related only; or if the fraud was committed by a lower-level employee?
  - What is the auditor's responsibility in responding to non-material fraud for example, do the requirements in ED-240 only apply to material fraud or suspected fraud? Or what further steps, if any, is the auditor required to take in responding to non-material fraud post concluding that it is non-material.
  - There is a need to clarify the potential implication of the accumulation of non-material misstatements of the financial statements due to fraud. An accumulation of non-material frauds could be indicative of a more pervasive risk of material misstatement



due to fraud, for example, entity-level control deficiencies. This is because there is no explicit linkage between ED-240 and ISA 450, *Evaluation of Misstatements Identified During the Audit*.

5. Based on the above, we propose that more guidance is needed to enable a better understanding of the concept of a non-material fraud. It would also be helpful to understand whether the auditor's evaluation of misstatements due to fraud is intended to be applied in the same way that it is applied in ISA 450.

### Third-party fraud

6. We support the IAASB's objective not to expand the auditor's role and responsibilities related to third-party fraud that is not directly related to a risk of material misstatement due to fraud in the financial statements.<sup>8</sup>
7. However, we are uncertain about what the auditor's responsibilities are related to third-party fraud.
8. We observed that the definition of non-compliance with laws and regulations (NOCLAR) in the Code<sup>9</sup> is confined to acts perpetrated by *a client, those charged with governance of a client, management of a client, or other individuals working for or under the direction of a client*. Similarly, from a local legislative perspective, we observed that reportable irregularities<sup>10</sup>, which per definition includes unlawful acts or omissions that are fraudulent, are also confined to those matters committed by any person responsible for the management of the entity. The definition of fraud, including third-party fraud as detailed in paragraph A21 of ED-240, is therefore much broader.
9. We propose to incorporate into the definition of fraud, the link to the *risk of material misstatements of the financial statements*, to help clarify the parameters of the auditor's responsibilities related to fraud, including third party fraud. Specifically, we propose:
  - Adapting the definition of fraud in ED-240 paragraph 18(a) to read, "*An intentional act by one or more individuals among management, those charged with governance, employees, or third parties, involving the use of deception to obtain an unjust or illegal advantage through misstatement of the financial statements.*"
  - Adapting paragraph A21 to read, "*Fraud as defined in paragraph 18(a) can include an intentional act by a third party. Fraud or suspected fraud committed against the entity by customers, suppliers, service providers, or other external parties which may cause the financial statements to be misstated is generally described as third-party fraud.*"

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<sup>8</sup> Explanatory Memorandum paragraph 92

<sup>9</sup> In South Africa the Code is the [IRBA Code of Professional Conduct for Registered Auditors](#)

<sup>10</sup> [Auditing Profession Act \[ No. 26 of 2005\] \(www.gov.za\)](#)

10. Additionally, we encourage the IAASB to provide guidance related to practical impediments to the auditor's ability to fulfil its responsibilities related to third-party fraud, including for example:
- The premise in ISA 500, *Audit Evidence*, that the reliability of audit evidence is increased when it is obtained from independent sources outside the entity. Therefore, the auditor won't necessarily have a reason to doubt or question the information provided to the entity by a third-party.
  - Constraints, such as limited access to third parties, which can impede the auditor's ability to investigate suspicions of fraud thoroughly, including instances of potentially falsified documents.

*Professional Scepticism*

2. Does ED-240 reinforce the exercise of professional scepticism 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 \(with no further comments\)](#)

**Detailed comments (if any):**

1. On balance ED-240 adequately addresses the exercise of professional scepticism in relation to fraud in an audit of financial statements.
2. Our view is based on the fact that the auditor's responsibility to exercise professional scepticism is clearly explained in paragraph 15 and A20-A24 of the overarching standard, ISA 200, *Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with International Standards on Auditing*, which is referenced in paragraph 8 of ED-240.

*Risk Identification and Assessment*

3. Does ED-240 appropriately build on the foundational requirements in ISA 315 (Revised 2019)<sup>11</sup> 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](#)

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<sup>11</sup> ISA 315 (Revised 2019), *Identifying and Assessing the Risks of Material Misstatement*

**Detailed comments (if any):**

1. We agree that the risk identification and assessment procedures in ED-240, when compared to extant ISA 240 has been significantly enhanced to align with the ISA 315 (Revised 2019) and therefore that it is more robust. However, we are concerned that:

**Striking the right balance between incorporating principles from ISA 315 (Revised 2019) and other ISAs and tailoring those principles to be relevant to the auditor's responsibilities related to fraud in order to promote understandability remains a challenge.**

2. Examples of paragraphs that may not be sufficiently tailored include:
  - Paragraphs 28 and A47 do not explain how the auditor, through performing the retrospective review would distinguish between intentional versus unintentional bias (to distinguish between fraud versus error).
  - Paragraph 30 doesn't explain why or if inconsistent information is always indicative of fraud.
  - Paragraphs 37 and A95 – A97 do not link this risk assessment procedure with the auditor's ability to identify and assess the presumed risk of management override of controls.
  - Paragraphs 33(b) and A67 do not explain how the auditor would distinguish between deliberate versus erroneous misapplication of accounting policies.
3. As the intention is to build on the foundational elements of ISA 315 (Revised 2019) to enhance fraud risk identification, we propose that the IAASB incorporate into ED-240 considerations relevant to fraud to explain how the foundational risk assessment requirements of ISA 315 (Revised 2019) are to be applied in the context of fraud.

**The current approach to building on the foundational requirements from other standards appears to be inconsistent and could benefit from applying uniform approach.**

4. We have observed inconsistencies in the approach to incorporating principles from other ISAs and tailoring those principles to be relevant to the auditor's responsibilities related to fraud. The consequence is requirements that are be scattered across various ISAs, raising doubts about completeness of the principal requirements, and a disconnect between principles addressed in the different phases of the audit i.e., risk identification and assessment versus response. For example:
  - ED-240 does not sufficiently emphasise the importance of understanding the business model for the purpose of determining susceptibility of the financial statements to material misstatement due to fraud. ISA 315 (Revised 2019) paragraph A61 explains why the auditor obtains an understanding of the entity's business model. In the context of fraud risk identification, understanding the business at a strategic level, including the business risks it faces is important because it provides the auditor with insight into management's

intentions, i.e. the motivation behind their business decisions. Given *intention* is the key differentiator between material misstatement due to *fraud* versus error, this is considered a key omission in ED-240, needing to be addressed.

- ED-240 emphasises responding to management override of controls without elaborating on the risk assessment and related activities that inform this response. The detailed guidance related to understanding and articulating the risk of material misstatement due to management override of controls resides in ISA 315 (Revised 2019) (for example paragraph A195). Thus, when reading ED-240, there is a disconnect between the auditor's fraud risk assessment and response.
- ED-240 omits the requirements with respect to understanding accounting estimates, including the controls around estimates as it relates to risk of material misstatement of estimates due to fraud. We noted the requirements to perform a retrospective review of the outcome of previous accounting estimates in ED-240 paragraph 28, and the evaluation of management's judgments and decisions in making the accounting estimates included in the financial statements in ED-240 paragraph 51 and 52. We however observe the absence of requirements with respect to *understanding* the estimates, including the *controls* around estimates as it relates to risk of material misstatement of estimates due to fraud. i.e., the link between ISA 315 (Revised 2019) and ISA 540 (Revised) and *the context that explains the purpose of the assessment* is included in these ISAs.
- ED-240 emphasises risk assessment and related procedures for the audit of estimates but does not follow a similar approach for related parties. Specifically, although Appendix 5 references the paragraphs in ISA 550 with specific requirements that refer to fraud or suspected fraud, the risk identification and assessment principles in ISA 550 have not been incorporated into ED-240, unlike the principles from ISA 540 (Revised).

**Other comments related to building on the foundational requirements in ISA 315 (Revised 2019) for the IAASB's consideration include:**

5. A proposal to enhance paragraph 29 of ED-240 to require a discussion about the presumed risks of fraud in revenue recognition and management override of controls. This can be achieved through adding a new paragraph 29(c).
6. Clarification of the requirement related to *other sources*. ED-240 paragraph 27 will be easier to understand and apply with a fraud lens if the *other sources* is identified (or less laborious), so it eliminates the need to go into ISA 315 (Revised 2019) to understand the intention of ED-240 paragraph 27. We propose adapting the application material for this purpose, for example:

*"Information obtained from other sources in accordance with paragraphs 15–16 of ISA 315 (Revised 2019), may include information from the auditor's procedures regarding acceptance or continuance, other engagements performed for the entity by the engagement*

*partner or from previous audits and may be relevant to the identification of fraud risk factors by providing information and insights about...”*

7. Clarifying the IAASB’s intentions related to the auditor’s responsibilities to perform a retrospective review for “significant accounting estimates” versus “accounting estimates”. ISA 540 (Revised), paragraph A57, states that a retrospective review of management judgments and assumptions related to “significant accounting estimates” is required by ISA 240. Paragraph 33 of the extant ISA 240 requires retrospective reviews to be performed for “significant accounting estimates”. The term “significant” has been removed in ED-240, paragraphs 28, A47, and A136 and ISA 540 (Revised), paragraph A57. By removing the word “significant” from ED-240 and ISA 540 (Revised), auditors would now be required to consider all estimates regardless of their nature, size, or inherent risk. Accordingly, we recommend that the IAASB reconsider this matter.

*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:** [Agree, with comments below](#)

**Detailed comments (if any):**

1. We agree that ED-240 sets robust work effort requirements, but we have concerns about the applicability of the requirements to different fraud or suspected fraud scenarios.
2. Our response to question one, specifically the comment made in 2.7, highlights that there are various ways in which information that is indicative of fraud or suspected fraud can come to the auditor’s attention. As it relates to the requirements to respond to Fraud or Suspected Fraud, ED-240 does not:

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

3. We acknowledge the explanations about the *Scalability of the Fraud or Suspected Fraud Requirements*<sup>12</sup>. However, ED-240 can benefit from further enhancements related to the applicability of the required procedures in different circumstances. For example:

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<sup>12</sup> Explanatory Memorandum paragraphs 54 – 57

**For confirmed fraud:**

- May auditors rely on internal investigation reports, or is an independent investigation by the auditor necessary?
- How does the auditor evaluate whether the remedial actions are appropriate?

**For suspected fraud:**

- What should auditors do if inquiries do not yield further information and management takes no action?
- Is there a requirement for auditors to engage an investigator or expert to assess the need for an investigation?

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

4. An ongoing investigation can significantly delay the finalisation of an audit and therefore the issue of the financial statements due to uncertainties related to suspected fraud. This delay may not be in the public interest. For ongoing investigations, we question:
  - a. Whether the auditor can conclude the audit (assuming this is also allowed legally)?
  - b. What intermediate actions the auditor must take in the public interest to be able to finalise the audit and allow for the issue of the financial statements?
  - c. How the auditor would bring to the attention of the users of the financial statements the fact that a suspected fraud investigation is ongoing if the audit is finalised, and the financial statements are issued before the finalisation of the fraud investigation.

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

5. Assuming the auditor is unable to obtain further information, and therefore unable to perform the procedures in paragraphs 56 – 59, we question:
  - a. Is it sufficient for auditors to seek legal advice and consider withdrawal, or are there minimum procedures to follow / complete first?
  - b. How does the auditor comply with the requirements in ED-240 paragraph 60, such as the requirement to identify a misstatement and communicate with the appropriate level of management and those charged with governance about the auditor's withdrawal from the engagement and the reasons for the withdrawal?

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

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

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

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

*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:** [Neither agree/disagree, but see comments below](#)

**Detailed comments (if any):**

8. We agree with the need for enhanced transparency about the auditor's responsibilities related to fraud, because of the public interest and user demand.
9. Despite this, we have reservations about whether leveraging the ISA 701 KAM requirements for listed entities will achieve the desired transparency.
10. There are multiple practical challenges in determining the Fraud-related KAM population and applying the filtering mechanism like the one used to communicate KAMs in ISA 701. Additionally, the challenges that prevented auditors from reporting Fraud-related KAMs under ISA 701 may still remain. Therefore, there is a risk, if these issues remain unresolved, that the new fraud-related KAM requirements may still result in no or limited KAMs being reported by the auditor which still won't fully achieve the public interest objective. We look forward to how the IAASB would resolve these issues.

11. We commend the IAASB for the extensive exploration, outreach, and consideration of multiple solutions to aim to improve transparency.<sup>13</sup> Because of the importance of transparency, we would support the IAASB's reconsideration of previously proposed options<sup>14</sup> that may be easier to implement and therefore more likely to enhance transparency in the auditor's report.
12. Additionally, we propose that transparency of fraud-related responsibilities in the public interest may be further supported through enhancements to the director's responsibilities paragraph in the auditor's report.
13. Our comments below elaborate on these points.

### Challenges with determining the population for fraud-related KAMs.

13.1. ED-240 paragraph 61 identifies the starting point for the determination of KAMs as "matters related to fraud communicated with those charged with governance", however this may unintentionally exclude:

- a. Matters communicated by / from management or those charged with governance. We propose enhancing this requirement, in line with the IAASB's objective to enhance communication requirements with management and those charged with governance<sup>15</sup>, to emphasise the two-way exchange of fraud-related information between the auditor and those charged with governance by using a phrase like "matters related to fraud communicated between those charged with governance and the auditor" instead. This will enable inclusion of all fraud-related matters communicated between these parties into the KAM population as a starting point. This enhancement does not necessarily change the work effort, but what it does achieve is ensure that the population of matters communicated by management or those charged with governance to the auditors is not excluded from potential KAMs.
- b. Matters that have not been communicated with those charged with governance because the auditor suspects that management or those charged with governance are involved in the suspected fraud. Therefore, consideration should be given as to how matters that may be significant but have not been explicitly communicated could be included in the fraud-related KAM population.

13.2. Acknowledging the challenge identified by the IAASB in helping the auditor to identify when and what to report<sup>16</sup>, how would the auditor determine what level of suspicion will be reasonable for a suspected fraud to be included in the KAM population?

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<sup>13</sup> Explanatory Memorandum paragraphs 61 - 65

<sup>14</sup> [20220912-IAASB-Agenda Item 6-A-Document Used for Outreach.pdf](#)

<sup>15</sup> Explanatory Memorandum paragraph 30.

<sup>16</sup> Explanatory Memorandum paragraph 64.



- a. Potentially reporting unsubstantiated claims to the public may have other unintended consequences, such as creating public doubt about management or those charged with governance's integrity prematurely.
- b. Enforcing this may be equally as challenging because in the absence of the legal determination of fraud. How can this evaluation be performed and reperformed consistently?

### **Challenges with identifying fraud-related matters that required significant auditor attention.**

- 13.3. It is possible that the unintended consequence of the enhancement to ISA 701 paragraph A21 may cause the presumed risk of fraud in revenue recognition to become a "standard KAM" going forward. This is because auditing revenue always requires significant auditor attention. Therefore, it is recommended that the IAASB consider providing application material that helps the auditor to distinguish between "normal" significant auditor attention and potential *additional* significant auditor attention because of the associated fraud risk that will require a fraud-related KAM to be reported by the auditor.
- 13.4. It is unlikely that identification and communication of a significant deficiency in the system of internal controls related to fraud prevention and detection will meet the "significant auditor attention" threshold because the effectiveness of the controls are not necessarily tested as part of the audit if a fully substantive audit approach is followed. The unintended consequence is that significant deficiencies in internal controls will not be publicly disclosed.
- 13.5. Given that management and those charged with governance are responsible for the prevention and detection of fraud, wouldn't it be important to also consider if the matter required significant attention by management or those charged with governance (as opposed to just significant audit effort), as the auditor is unlikely to drive the investigation and mitigation of fraud or suspected fraud? Could this not also be a consideration for the selection of fraud related KAMs?

### **Proposed enhancements to the director's responsibilities paragraph in the auditor's report (ISA 700 (Revised)) to further support transparency of fraud-related responsibilities in the public interest**

- 13.6. We acknowledge the IAASB's identification of the value that users place on insights about an entity's internal control environment.<sup>17</sup>
- 13.7. We observed that:
  - a. ISA 700 (Revised) paragraph 34(a) requires the auditor's responsibilities paragraph to describe management's responsibility for:

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<sup>17</sup> Explanatory Memorandum paragraph 65.

- (a) Preparing the financial statements in accordance with the applicable financial reporting framework, and for such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error;
  - b. ISA 700 (Revised) paragraph A45 acknowledges there may be circumstances when it is appropriate for the auditor to add to the descriptions of the responsibilities of management and those charged with governance in paragraphs 34–35 to reflect additional responsibilities that are relevant to the preparation of the financial statements in the context of the particular jurisdiction or the nature of the entity.
  - c. The *Illustrations of Independent Auditor's Reports on Financial Statements* in ISA 700 (Revised) includes the standard director's responsibilities paragraph but does not explicitly acknowledge this allowance in ISA 700 paragraph A45.
- 13.8. In the interest of enhanced transparency on jurisdictional requirements about fraud-related responsibilities in the preparation of the financial statements, we propose that paragraph A45 be elevated to a requirement in ISA 700 (Revised) paragraph 34 and explicitly acknowledged in the *Illustrations*. In addition, it can also benefit from being enhanced to include consideration of both required and voluntary adopted recognised governance frameworks in local jurisdictions. In South Africa such provisions may include the [Johannesburg Stock Exchange \(JSE\) Listing Requirements](#) and the [King IV Code on Corporate Governance](#).
- 13.9. Because IFRS does not require directors to report on fraud-related matters in the financial statements, this requirement to add to the descriptions of the responsibilities of management and those charged with governance where appropriate based on jurisdictional requirements, may encourage transparency and have the added benefit of driving jurisdictional changes to laws and regulations to support enhanced corporate governance requirements and practices.

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

**Detailed comments (if any):**

*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:** [Agree, with comments below](#)

**Detailed comments (if any):**

1. Supporters in our Task Group of the proposal to include a stand-back requirement in ED-240 argued that such a provision is essential for ensuring auditors take a comprehensive and critical look at all the audit evidence related to fraud. They say that a deliberate stand-back prompts auditors to holistically assess the evidence, both corroborative and contradictory, to determine if sufficient and appropriate audit evidence has been obtained related to fraud. This stand-back “moment” is seen as a crucial checkpoint to guard against overlooking signs of fraud that might have been obscured during the detailed phases of the audit.
2. Others in our Task Group held the opposite view, that a separate stand-back requirement is not needed. They contend that ED-240 already requires auditors to be vigilant for indicators of fraud throughout the audit. They maintain that the suite of ISAs, when properly applied together, inherently encompasses the considerations that a stand-back procedure aims to address. From this perspective, introducing a distinct stand-back requirement could be seen as redundant or potentially misleading, suggesting that fraud considerations are only relevant at a specific point in the audit rather than being pervasive to the audit.
3. In conclusion, incorporating considerations specific to fraud into the existing stand-back provisions in other standards and providing more guidance on how auditors should perform the stand-back requirements could be a middle-ground solution that satisfies the need for a critical look at the audit evidence related to fraud without introducing a new, stand-alone requirement into ED-240.

*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:** [Agree, with comments below](#)

**Detailed comments (if any):**

1. The opinions of our Task Group varied on whether the fraud requirements should be reduced/simplified for smaller audits or entities. Some argued that fraud's significance is independent of entity size, rendering scalability moot.

2. Others pointed out a lack of guidance in the standard for conducting risk assessments for companies without a formal control framework, a notable concern for smaller entities where management override risks are higher due to less segregation of duties.
3. Additionally, we observed that the transparency requirements for smaller audits are not apparent.
4. In conclusion, we recommend that although the essence of fraud and the auditor's reaction cannot be diminished, the standard should offer more detailed guidance on tailoring fraud risk assessment and responses to entities of varying sizes.

*Linkages to Other ISAs*

9. Does ED-240 have appropriate linkages to other ISAs (e.g., ISA 200,<sup>18</sup> ISA 220 (Revised),<sup>19</sup> ISA 315 (Revised 2019), ISA 330,<sup>20</sup> ISA 500,<sup>21</sup> ISA 520,<sup>22</sup> ISA 540 (Revised)<sup>23</sup> and ISA 701<sup>24</sup>) to promote the application of the ISAs in an integrated manner?

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

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

**Detailed comments (if any):**

**Our responses to earlier questions in our comment letter refer to linkages with other ISAs and include proposals related to where these linkages can be improved.**

1. In relation to the auditor's responsibilities, we motivate that the introduction section to ED-240 could benefit from elaborating on the requirements in ISA 220 (Revised), emphasising the engagement partner's broader leadership responsibilities which encompasses creating an audit environment that is conducive to fraud risk identification.
2. In relation to non-material fraud, we propose a clearer link between ED-240 and ISA 450, *Evaluation of Misstatements Identified During the Audit* as it relates to the determination of material versus non-material fraud.
3. In relation to third-party fraud, we identify that the premise in ISA 500, *Audit Evidence*, that the reliability of audit evidence is increased when it is obtained from independent sources

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<sup>18</sup> ISA 200, *Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with International Standards on Auditing*

<sup>19</sup> ISA 220 (Revised), *Quality Management for an Audit of Financial Statements*

<sup>20</sup> ISA 330, *The Auditor's Responses to Assessed Risks*

<sup>21</sup> ISA 500, *Audit Evidence*

<sup>22</sup> ISA 520, *Analytical Procedures*

<sup>23</sup> ISA 540 (Revised), *Auditing Accounting Estimates and Related Disclosures*

<sup>24</sup> ISA 701, *Communicating Key Audit Matters in the Independent Auditor's Report*

outside the entity may be a limitation to the auditor's ability to fulfil its responsibilities related to third-party information.

4. As it relates to risk identification and assessment, we propose:
  - a. Striking the right balance between incorporating principles from ISA 315 (Revised 2019) and other ISAs and tailoring those principles to be relevant to the auditor's responsibilities related to fraud in order to promote understandability.
  - b. That the current approach to building on the foundational requirements from other ISAs appears inconsistent and could benefit from a uniform approach to prevent requirements that are scattered across the ISAs and a disconnect between principles addressed in the different phases of the audit i.e., risk identification and assessment versus response.
5. Regarding enhanced transparency, we encourage the IAASB to consider proposed enhancements to the director's responsibilities paragraph in the auditor's report (ISA 700 (Revised) paragraph 34) to further support transparency of fraud-related responsibilities in the public interest.
6. Lastly, in considering all the enhancements made in ED-240, we were concerned that the auditor's responsibilities related to fraud in the context of a group audit and the potential complexities that may exist in a group audit scenario may have not been appropriately addressed i.e. as it relates to the linkage with ISA 600 (Revised). We propose that the IAASB consider explicit acknowledgement of the communication requirements in a group audit in ED-240.

*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):**

**Enhancements related to communication requirements.**

1. We propose that the IAASB consider elevating application paragraph A39 of ED-240 which emphasises that the communication requirements incorporate robust two-way communication.
2. Additionally, we propose adapting the language from communication with management and those charged with governance to communication between management and those charged with governance to clearly indicate two-way communication.

## Enhancements with respect to engagement resources, and specifically the use of forensic skills in the audit

3. We want to encourage the IAASB to elevate the consideration for the involvement of someone with forensic skills on the audit in ED-240
4. We are supportive of the application material in ED-240 paragraphs A33 – A36 but are of the view that the link to ISA 220 (Revised) in the requirements section in ED-240 paragraph 22 is redundant.
5. We recognize that ED-240 cannot prescribe that the auditor must involve someone with forensic skills. We are also not advocating for this, because we know it may not be feasible to involve someone with forensic skills for every audit due to cost and skills shortages.
6. Instead, we propose a requirement for the explicit consideration by the auditor to involve someone with forensic skills as part of the auditor's responsibilities related to fraud, based on the nature and circumstances of the audit engagement. The application material could be used to highlight the nature and circumstances that may indicate a need for the involvement of someone with forensic skills on the audit, For example:
  - If information obtained at acceptance and continuance phase already identifies fraud or suspected fraud.
  - If risk assessment and related activities indicate anomalies in accounting estimates or analytical procedures performed by the auditor that are unexplained.
  - Multiple significant transactions outside the normal course of business that don't have a clear business purpose.
  - Management provides inconsistent responses, or their actions lead the auditor to doubt their integrity.
  - If significant deficiencies in the company's system of internal controls indicate pervasive susceptibility of the financial statements to material misstatement due to fraud.
7. Additionally, we encourage the IAASB to consider incorporating in the application material a paragraph that explains the interaction between the auditor's professional scepticism and engagement resources, specifically explaining that having the forensic skills on the engagement can enhance the auditor's ability to exercise professional scepticism related to fraud in the audit. For example, challenging the auditor's thinking on fraud-related matters and influencing their response in ways that they might not have considered, due to the auditor not possessing forensic skills.

## Use of Technology

8. We recognise the enhancements that the IAASB has made to ED-240 related to how technology may be used by the company to perpetrate fraud or by auditors to perform fraud-related audit procedures.<sup>25</sup>
9. We welcome these enhancements, but question their sufficiency, given the sophisticated nature of fraud and the vulnerability of companies to fraud because of the impact that advanced technologies, such as Artificial Intelligence and Robotic Processing Automation, have on their internal controls.<sup>26</sup> This is not explicitly acknowledged and catered for in ED-240.
10. We propose that the IAASB enhance the prominence of the impact of rapid-changing technologies on the perpetration of fraud and how this may impact the auditor's responsibilities related to fraud. Specifically:
  - a. Explicit reference to these complexities in the introduction to the standard, relating to *Understanding fraud and how it can come to the auditor's attention* (refer to par 3.4.2).
  - b. Similarly, explicit reference to how this may contribute to the inherent limitations of the auditor to identify risks of material misstatement due to fraud.
  - c. A requirement for a determined effort by the auditor to understand what the company's vulnerabilities are in this respect as part of the risk assessment procedures and related activities (acknowledging that the impact and consequently the audit effort may differ substantially depending on the nature and circumstances of the company).
  - d. A requirement for the auditor to understand and evaluate management or those charged with governance risk management plans or procedures in response to these vulnerabilities as part of the auditor's evaluation of the components of the company's system of internal control.
11. The auditor must be required to consider how changes in technology impact the business and specifically the financial reporting process, whether the company is actively managing these vulnerabilities as part of their understanding of the components of the entity's system of internal controls and consequently the impact on the risk identification and assessment of risks of material misstatement due to fraud.

## Clarifying terminology in ED-240 to support the understanding of the auditor's responsibilities related to fraud

12. We observed frequent use of the phrase "*if the auditor identifies fraud...*" throughout ED-240, possibly contributing to the public misconception that the auditor is solely responsible for identifying all fraud.

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<sup>25</sup> Explanatory memorandum paragraphs 85 - 88.

<sup>26</sup> [IAASB-Fraud-Going-Concern-Roundtables-Takeaways.pdf \(ifac.org\)](#)

13. We propose that using more specific terminology, for example “if fraud or suspected fraud comes to the auditor’s attention...”, may contribute to alleviating this misconception.

*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):**