



Response to the FRC's Consultation Paper
Proposing Revisions to ISA (UK) 240
The Auditor's responsibilities Relating to Fraud
in an Audit of Financial Statements

29 January 2021

INTRODUCTION

ICAS welcomes the opportunity to comment on the FRC's proposed revised ISA (UK) 240 'The Auditor's responsibilities Relating to Fraud in an Audit of Financial Statements'.

Our CA qualification is internationally recognised and respected. We are a professional body of over 22,000 members who work in the UK and in more than 100 countries around the world. Our members represent different sizes of accountancy practice, financial services, industry, the investment community and the public sector. Almost two thirds of our working membership work in business, many leading some of the UK's and the world's great companies.

Our Charter requires its committees to act primarily in the public interest, and our responses to consultations are therefore intended to place the public interest first. Our Charter also requires us to represent our members' views and to protect their interests, but in the rare cases where these are at odds with the public interest, it is the public interest which must be paramount.

Any enquiries should be addressed to James E Barbour, Director, Policy Leadership.

General comments

We are supportive of the approach proposed in the November 2020 exposure draft of ISA (UK) 240 (Revised). We welcome that the FRC's approach recognises that it will require to wait to see the outcome from the forthcoming BEIS audit reform consultation before it can determine whether further changes are required to this standard. As recognised in the Brydon review, a holistic approach to tackling fraud will be required.

Responses to Specific Questions

Question 1

Has ISA (UK) 240 been appropriately revised to give increased clarity as to the auditor's obligations relating to fraud in the audit of financial statements. If you do not consider this to be the case, please set out why and how you believe those obligations should be clarified.

Response 1

We believe that ISA (UK) 240 has been appropriately revised to give increased clarity as to the auditor's obligations relating to fraud in the audit of financial statements.

Question 2

Have appropriate enhancements been made to the requirements for the identification and assessment of risk of material misstatement due to fraud, and the procedures to respond to those risks, to promote a more consistent and robust approach to the auditor's responsibilities in relation to fraud? If you do not consider this to be the case, please set out why and how you believe the requirements should be enhanced.

Response 2

We believe that appropriate enhancements have been made to the requirements for the identification and assessment of material misstatement due to fraud, and the procedures to respond to those risks, to promote a consistent and robust approach to the auditor's responsibilities in relation to fraud.

We would, however, query the wording of the proposed revision to paragraph 3 that states:

"For example, a fraud or suspected fraud by a key member of management may be considered qualitatively material, even if the potential misstatement is less than materiality determined in quantitative terms."

We are supportive of the concept that the auditor when assessing identified intentional misstatements, would consider both the qualitative and quantitative impact of such misstatements, including whether such an occurrence calls into question the integrity of key management. Additionally, when performing a risk assessment, we agree that it is important for the auditor to also consider the risk of qualitatively material misstatements. However, our concern is whether this proposed revision is intended to suggest that any fraud committed by key members of management should always be considered material? If that is the case, this will obviously have implications in that all audits will need to be planned so as to detect all fraud by key management, regardless of their value. We would welcome some clarification as to whether this is what is intended.

Question 3

Have appropriate enhancements been made to the application material? If you do not consider this to be the case, please set out why and how you believe the application material should be enhanced.

Response 3

We believe that appropriate enhancements have been made to the application material.

Question 4

Do the proposals sufficiently support the appropriate exercise of professional scepticism throughout the risk assessment procedures, the procedures to respond to those risks and the evaluation of audit evidence obtained? If you do not consider this to be the case, please give reasons and describe how you consider the exercise of professional scepticism could be better supported.

Response 4

We do believe that the proposals sufficiently support the appropriate exercise of professional scepticism throughout the risk assessment procedures, the procedures to respond to those risks and the evaluation of audit evidence obtained.

Question 5

ISA (UK) 240 establishes a rebuttable presumption that there are risks of fraud in revenue recognition (paragraph 26). Are there other account balances, transactions or disclosures for which such a rebuttable presumption should be established? If you consider there are, please identify them and set out why.

Response 5

We believe that such matters should be left to the professional judgement of the auditor and therefore would not support widening the scope of the extant rebuttable presumption. Currently, in the midst of this Covid-19 pandemic, many businesses and individuals are under extreme financial pressure. Therefore, in the current environment it would appear a reasonable assumption that the financial statements of some businesses may be more susceptible to material irregularities in a range of areas as a consequence of error and/or fraud. It will therefore be key for audit teams to look at a broad range of risks relevant to the entity being audited.

Question 6

ISA (UK) 240 specifies particular audit procedures responsive to risks related to management override of controls (paragraphs 31 – 33). Are there other audit procedures responsive to those risks, or any other risks of material misstatement due to fraud, that you believe should be required for all audits? If you consider there are, please describe them and set out why.

Response 6

We do not believe that at this time there are necessarily other audit procedures responsive to those risks, or any other risks of material misstatement due to fraud, that should be required for all audits. However, given its very nature, collusion is difficult to detect when only using information from the entity being audited. Therefore, consideration might be given by the auditor to accessing information from outside the entity to get better insights into the performance of the audited entity. Such additional audit procedures might include performing key ratio analysis comparisons with competitors which may help to identify any areas where the entity may appear to be an outlier.

Question 7

In complying with the requirements of ISA (UK) 240 (Revised), the auditor may also need to consider whether there has been non-compliance with laws and regulations, and therefore that requirements in ISA (UK) 250 Sections A and B (Revised November 2019) also apply. Is it sufficiently clear in these ISAs (UK) of the interaction between them?

Response 7

We believe that this is sufficiently clear. However, a further enhancement to include a direct reference in the requirements section of the standard could be considered.

Question 8

Are the requirements and application material sufficiently scalable, including the ability to apply ISA (UK) 240 (Revised) to the audits of entities with a wide range of sizes, complexities and circumstances? If you do not consider this to be the case, please set out why and how you believe that could be addressed.

Response 8

We believe that the requirements and application material are sufficiently scalable.

Question 9

References to 'computer assisted audit techniques' have been updated to 'automated tools and techniques' and we have identified that these may enable more extensive testing and assist in identifying unusual transactions or relationships (paragraphs A44, A48 and A50). Is there other guidance in relation to the use of automated tools and techniques that you believe could assist auditors in relation to their obligations with regard to fraud? If you consider there is, please give an explanation of it.

Response 9

We are supportive of the proposed updating of 'computer assisted techniques' to 'automated tools and techniques'. We are not aware of other guidance that should be referred to.

Question 10

Do you agree with the proposed effective date of audits of financial statements for periods beginning on or after 15 December 2021, with early adoption permitted, which is aligned with the effective date of ISA (UK) 315 (Revised July 2020)? If not, please give reasons and indicate the effective date that you would consider appropriate.

Response 10

We are supportive of the proposed effective date of audits of financial statements for periods beginning on or after 15 December 2021, with early adoption permitted.

Question 11

Should an additional requirement be placed on auditors to have a specific discussion with those charged with governance on the risks of material fraud in the business, including those which are business sector specific, in order to further the risk assessment process in respect of the risk of material error in the financial statements relating to fraud?

Response 11

We are supportive of the proposed inclusion of a requirement for the auditor to have a specific discussion with those charged with governance on the risks of material fraud in the audited entity, including those with business sector specific relevance in order to enhance risk assessment procedures related to material misstatement of the financial statements due to fraud.