Guide to: ISA 240 (Revised)
The Auditor's Responsibilities Relating to Fraud in an Audit of Financial Statements

A summary of the major changes of the impacts for audits of financial statements for periods starting on or after 15 December 2021.

Background

In May 2021, the Financial Reporting Council (FRC) published revisions to the International Standard on Auditing (ISA) (UK) 240: The Auditor's Responsibilities Relating to Fraud in an Audit of Financial Statements.

The revisions are effective for audits for periods beginning on or after 15 December 2021. They were made to address concerns about audit quality and the effectiveness of audit, and to clarify auditors' responsibilities in respect of the risk of fraud in the financial reporting process.

Changes for auditors

The revisions include:

- Clarification that the objective of auditors with respect to fraud is to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement due to fraud.
- Enhancements to the requirements for the identification and assessment of risk of material misstatement due to fraud and the procedures to respond to those risks.
- A requirement to ensure that audit procedures are not biased towards obtaining corroborative evidence at the expense of excluding evidence that is contradictory.
- A greater focus on the need for professional scepticism. For example, a reminder that auditors should 'remain alert for conditions that indicate a record or document may not be authentic' and a requirement to investigate where management's responses to an auditor's enquiries appear implausible.
- The standard is now explicitly referenced to ISA 550: Related Parties to reflect the risk that the nature of related party relationships and transactions may, in some circumstances, give rise to higher risks of material misstatement.
- A new requirement to make inquiries about allegations of fraud raised within an entity, eg to management or those responsible for whistleblowing procedures.
- A new requirement to consider whether the audit engagement team requires specialised skills during the planning or performance of an audit to assist with the audit of complex issues and matters within an audit engagement.

Changes to the annual audit

While the changes in some cases represent the codification of current best practice, audit teams will need to ensure that the new objectives are met and fully documented in line with the revised requirements. The requirements to review the design of audit tests and sufficiency of the evidence required is likely to change procedures performed in prior years and additional work may be required to obtain sufficient corroborative and contradictory evidence.

The link to ISA 550 on related party transactions and balances will serve as a reminder to ensure that the auditor's knowledge of related party relationships and transactions is up to date and sufficient.

For those audits where fraud has occurred or is suspected, or the complexities of circumstances make fraud risk greater, there is likely to be a greater impact, for example through the use of specialists.

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Conclusions

In their impact statement, the FRC acknowledged that concerns persisted about the ability of audit to detect fraud following high profile corporate failures that had involved undetected fraud.

The changes clarify the auditor's responsibilities in relation to fraud and promote a more consistent and robust approach to those responsibilities. However, while not as significant as the revisions to ISA (UK) 315, the revisions to the standard will have a cost impact on audits. As acknowledged by the FRC, time will be incurred by audit firms meeting the new requirements on each audit while firms will need to provide additional staff training and familiarise themselves with the new requirements.

To meet the increased requirements of the new regulations in an efficient and timely manner, that minimises as much as possible the additional time and cost expected, auditors should liaise with management and finance teams early in the audit planning process to set out the impact of the new requirements on the audit plan, make the necessary new enquiries, and obtain the necessary deliverables from management.

At haysmacintyre our investment in new audit software and other investments in technology, such as data analytics and file sharing software, help us to maintain an efficient audit process and we hope to minimise the time cost increases due to ISA (UK) 240. However, the new requirements will require additional information and evidence gathering and changes or additions to our procedures performed in prior years. Consequently, increases to audit fees are expected. As above, we plan to work closely with our clients to minimise, as much as possible, increases in audit time costs and fees.