

Irish Auditing and Accounting Supervisory Authority
E-mail: submissions@iaasa.ie

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To whom it may concern,

Consultation: Proposal to revise ISA (Ireland) 240 The Auditor’s Responsibilities Relating to Fraud in an Audit of Financial Statements

Chartered Accountants Ireland is pleased to have the opportunity to comment on the proposed changes to ISA (Ireland) 240. We are welcoming of changes and enhancements to auditor’s responsibilities relating to fraud.

We have commented on the individual questions posed in the attached appendix.

Please do not hesitate to contact me at mark.donnelly@charteredaccountants.ie to discuss any of the issues raised in our response.

Yours sincerely

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Appendix

General comments

The comments included in this section relate to points made by Chartered Accountants Ireland on the Financial Reporting Council's (FRC) consultation on ISA (UK) 240, that have not been reflected in IAASA's exposure draft for ISA (Ireland) 240 which we believe require further consideration.

Auditor's obligations relating to fraud in the audit of financial statements

Paragraph 14 has been revised to require the auditor to investigate responses to enquires which appear implausible. The term "appear implausible" is highly subjective. As such, we believe to achieve consistent application of this requirement, a framework of factors or indicators needs to be provided to allow auditors to assess inquiry responses against, to identify those that appear implausible.

Paragraph 14-1 has been added, this paragraph states that the auditor must also comply with ISA (Ireland) 550. The auditor is already required to comply with this standard and as such, it is not clear what this paragraph achieves. We believe the intent of this paragraph should be clarified.

An addition has been made to paragraph 15 which we believe should be revised to read "(including the individual primary statements and the disclosures)".

The final sentence added to paragraph 16 refers to the susceptibility of assertions to material misstatement due to fraud. We believe this should be clarified to state "the susceptibility at the assertion level of classes of transactions, account balances and disclosures to material misstatement due to fraud."

Paragraph 24-1 has been added to the standard which requires the auditor to determine whether the engagement team requires specialised skills or knowledge to perform risk assessment procedures. Factors the auditor may consider in making this determination are set out in paragraph A27-1, however, these factors are very subjective. We believe in order to achieve consistent application of this requirement additional application guidance is required to provide a framework of objective factors which can be assessed in making this determination.

We do not believe the intent of the addition at paragraph 32-1 is clear. If this addition is simply to highlight the requirements of ISA (Ireland) 540 we feel that should be stated.

We believe in order for there to be meaningful auditor reporting in the area of auditor reporting on fraud, there first needs to be a statement by the directors in the directors' report or financial statements in relation to the actions they have taken to prevent fraud against which the auditor can then report in a meaningful way. Indeed this was one of the core recommendations of the Brydon review.

We believe the addition of the words "hard to reach" in paragraph A23 is inappropriate. Businesses have a legitimate basis to set targets which are hard to reach, and shareholders and other stakeholder expect bonus-based compensation to be granted based on strong performance.

Application material

Generally, while we believe that enhancements made to the application material support the objective of clarifying the auditor's responsibilities, we do have some concerns as noted below. Further clarity on these matters would be welcomed.

- Paragraph A9-1 includes a list of conditions which may indicate that a document is not authentic, one of which states "Information that appears implausible...". As explained under question 1, the term appears implausible is highly subjective and consistent application of this requirement may not be possible.
- Under the extant standard, paragraph A11 included the paragraph starting with "An exchange of ideas among engagement team members about how and where they believe..." – this paragraph has been removed from the proposed new standard. This paragraph originates from the IAASB's standard and we believe it to have continuing relevance, it is not clear to us why it has been removed. We believe this should be retained.
- Paragraph A25 states that "Fraud risk factors may relate to incentives, pressures or opportunities that arise from conditions that create susceptibility to misstatement, before consideration of controls."

It would appear that the intention was to make fraud risk factors comparable to inherent risk factors as used in ISA (Ireland) 315 (Revised July 2020), however, operationally, when determining whether a fraud risk factor is present you would have to consider whether controls are in place as the lack of controls is often that which causes the opportunity for fraud risk factors to be present.

This is further referred to later in the paragraph where it says "Fraud risk factors may also relate to conditions within the entity's system of internal control that provide opportunity to commit fraud..." as well as in paragraph A26 where it lists a number of controls generally implemented in order to deter fraud. For example: effective oversight by those charged with governance; appropriate segregation of responsibilities to reduce the opportunities for a person to both perpetrate and conceal fraud; and effective IT processes that manage access to the IT environment, manage program changes or changes to the IT environment and manage IT operations (for example, to ensure that access and changes to the data is by persons with appropriate authority).

- Paragraph A25 further states "Fraud risk factors, which include intentional management bias, are, insofar as they affect inherent risk, inherent risk factors." It is not clear why only those that include intentional management bias are deemed to be inherent risk factors. Was the intent here to rather say "inherent fraud risk factors"?
- Paragraph A32 replaced the words "In doing so" with "In identifying the controls that address the risks of material misstatement due to fraud" and "obtaining this understanding" with "identifying these controls and evaluating their design and determining whether they have been implemented". In doing so, certain elements of the requirements from the IAASB's standard has been removed/altered and we are concerned that the intention of the IAASB paragraph is lost.

For example, the requirement under the extant standard was for the auditor to "obtain an understanding of the controls that management has designed, implemented and maintained". By using

the words “in identifying”, it assumes that there are controls in place which might not always be the case. Furthermore, the extant standard requires the auditor to obtain an understanding of how the controls were maintained. This does not appear to be considered under the proposed revised wording as it only considers the identification, design and implementation.

- Paragraph A43, the third bullet proposes to replace the words “steps and procedures” with “controls” and to remove “procedures and” from the sentence. We believe this change is unnecessary, as it is not only controls that are relevant given the matter being described is “The entity’s financial reporting process and the nature of evidence that can be obtained”.
- Paragraph A50 included two additional items when describing unusual relationships involving year-end revenue and income, one of which says, “uncharacteristically high levels of refunds or credit notes.” We believe this should include the words “in the subsequent period”.

Professional scepticism throughout the risk assessment procedures

We do not believe that the proposals sufficiently support the exercise of professional scepticism throughout the audit. Whilst effort has been made to increase the extent of risk assessment procedures to be performed, we do not believe that they necessarily explain HOW professional scepticism should be applied during the audit and, in certain instances, may also lead to inconsistent application.

For example, the term “appear implausible” is likely to have been included in the standard to strengthen the application of the auditors’ professional scepticism, however as described above, consistent application of this requirement may not be possible.

In general, our concerns stem from the overall complexity around articulating exactly what the exercise of professional scepticism is. We believe that this is more akin to having a questioning mind set rather than applying some form of check box risk assessment and response exercise that is performed during the audit. We do acknowledge that there may be a wider uncertainty around the concept of exercising professional scepticism throughout the ISA’s and, other than the point referred to above, we are not proposing any amendments to the standard on this matter.

Link between ISA (Ireland) 240 and ISA (Ireland) 250 Sections A and B

Reference to ISA (Ireland) 250 Section A has been included in paragraph A5a-2. ISA (Ireland) 250 Section B has not been specifically referenced in ISA (Ireland) 240 (Revised). Paragraph 8a of the revised standard indicates that in complying with any additional responsibilities under other ISAs (Ireland), in this case, ISA (Ireland) 250, these may provide further information that would be relevant to the auditors work on fraud. However, the application material appears to only state the objectives of the auditor under ISA (Ireland) 250 Section A. It is not clear from this additional paragraph (A5a-2) what the interaction between ISA (Ireland) 240 (Revised) and ISA (Ireland) 250 Sections A and B is or how the auditor should interpret this linkage in a way that is relevant to the auditor’s responsibility with respect to fraud.

Use of automated tools and techniques

The supplementation to the application material only indicates where the use of automated tools and techniques “may” assist the auditor, yet it does not explicitly outline “how” this can be achieved. Technology is a hot topic specifically in relation to how it is used to perpetrate fraud, and how an auditor can use technology to identify, assess and respond to risks of material misstatement due to fraud.

Practical guidance on how the use of technology can help in certain areas would be very helpful for audit practitioners. The standard historically and still does take a very in-depth focus on journals, yet not all fraud scandals are perpetrated through journals fraud. There are other areas where fraud could potentially occur and where technology could be leveraged. In terms of useful sources of information to develop such practical guidance for auditors, this may include analysing recent fraud scandals and how technology could have helped the auditor.

Effective use of technology by the auditor also comes with its own challenges. It is very dependent on the acquisition of complete and accurate data and is also dependent on the adequacy of the systems the company itself has in place. In addition, where an analytics tool may be used on a large data population, dealing with outliers and exceptions in the results can be challenging. Practical guidance on how to deal with such challenges would be beneficial.

Responses to questions

- 1. In the context of IAASA’s policy to make minimal amendments to the UK standards, are there any amendments proposed to ISA (Ireland) 240 that, in your opinion conflict with Irish or EU law?**

Please see general comments above.

- 2. In the context of IAASA’s policy to make minimal amendments to the UK standards, are there any areas not identified in this consultation paper where there are distinct differences between the Irish and UK markets which, in your opinion, would impact on the applicability of the proposed amendments to the standard in Ireland?**

We note that the FRC are bringing in changes to ISAs (UK) which are being made in contemplation of other changes which will be made to the requirements on directors via Law, corporate governance and reporting standards. However, in Ireland we are getting just the changes being made to ISAs (UK) and will end up with asymmetrical requirements in our corporate governance, reporting and audit standard which will further exacerbate the expectations gap and in the long term will be detrimental to audit quality. IAASA should consider this in the context of bringing in changes to ISAs (Ireland) which simply mirror changes to ISAs (UK) going forward.

- 3. Is the proposed effective date, i.e. for financial periods beginning on or after 15 December 2021, appropriate? If not, please give reasons and indicate the effective date that you would consider appropriate.**

We think the proposed effective date is appropriate.