

## 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)	CFA Institute
Name(s) of person(s) responsible for this submission (or leave blank if the same as above)	Matthew P. Winters, CPA, CFA Sandra J. Peters, CPA, CFA
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:Matt.winters@cfainstitute.org">Matt.winters@cfainstitute.org</a> <a href="mailto:Sandra.peters@cfainstitute.org">Sandra.peters@cfainstitute.org</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="#">Global</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="#">Investors and Analysts (Preparer or users of financial information)</a> Respectfully, responses from "preparers of financial information" should not be aggregated with responses from users of financial information, such as investors and analysts. They are different stakeholder groups with distinct perspectives.
Should you choose to do so, you may include information about your organization (or yourself, as applicable).	With offices in Charlottesville, VA; New York; Washington, DC; Brussels; Hong Kong SAR; Mumbai; Beijing; Shanghai; Abu Dhabi; and London, CFA Institute is a global, not-for-profit professional association of more than 190,000 members, as well as 160 member societies around the world. Members include investment analysts, advisers, portfolio managers, and other investment professionals. CFA Institute administers the Chartered Financial Analyst® (CFA®) Program.  CFA Institute has a long history of promoting fair and transparent global capital markets and advocating for strong investor protections. An integral part of our efforts toward meeting those goals is ensuring that corporate reporting and disclosures and the related assurance provided to investors and other end users are of high

	quality. Our advocacy position is informed by our global membership who invest both locally and globally.
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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:

#### OVERALL VIEWS

We thank the IAASB for its proposal to strengthen its auditing standard on fraud in response to recent high-profile frauds (e.g., Autonomy<sup>1</sup>, Toshiba<sup>2</sup>, Steinhoff<sup>3</sup>, Carillion<sup>4</sup>, Luckin Coffee<sup>5</sup>, NMC Health<sup>6</sup>, Wirecard<sup>7</sup>) that resulted in significant investor losses and have shaken the public's trust in the auditing profession and capital markets generally.

We have **six overall views** to our submission:

**1. *Increasing the Transparency of the Auditor's Report About Matters Related to is Necessary, but Commingling with Key Audit Matters May Reduce Emphasis***

The auditor's report is the only part of the audit observable by investors, who are the end customer/consumer of the auditor/audit opinion and the ones at risk of losses from misstatements of the financial statements.

We believe the "expectations gap" between what investors think auditors do and what auditors do is largely the result of a lack of transparency in the auditor's report: auditors do not tell investors what they do and have resisted attempts at improving transparency. We addressed that expectations gap and the topic of fraud in our [2019 Comment Letter to the UK Government on Independent Review into the Quality and Effectiveness of Audit Call for Views \(Brydon Review\)](#).

We see **four benefits to enhancing the transparency of the auditor's report** about matters related to fraud:

- a. ***Auditors Efforts Enhanced*** – Improved transparency may increase auditors' effort in detecting fraud.
- b. ***Enhanced Auditors Efforts May Have Effect of Increase Management and TCWG Efforts*** – An increase in auditors' effort at detecting frauds, from the increased transparency, may in turn increase effort by those charged with governance and management in preventing and detecting fraud, for example through investment in internal audit and internal control processes.
- c. ***Better Investor Evaluation of the Audit Committee and Auditor*** – More informative audit reports may enable better evaluation of audit committees and auditors by shareholders as

<sup>1</sup> [Deloitte faces record £15m fine for 'serious' failures in Autonomy audits](#)

<sup>2</sup> [Toshiba Accounting Scandal Draws Record Fine From Regulators](#)

<sup>3</sup> [Steinhoff shareholders sue Deloitte for damages](#)

<sup>4</sup> [KPMG faces £14.4mn fine for misleading UK regulators over Carillion audit](#)

<sup>5</sup> [Luckin Coffee to pay \\$180m in accounting fraud settlement](#)

<sup>6</sup> [EY accused of basic failings in \\$2.7bn claim over NMC collapse](#)

<sup>7</sup> [EY's Wirecard audits marred by 'repeated grave' violations of duties, says watchdog](#)

they oversee and elect the chair of the audit committee and its members, ratify the audit committee's selection of the auditor, and their remuneration (a voluntary, non-binding vote in some jurisdictions but a mandatory vote in others such as Germany).

- d. **Possible Increase in Trust** – More informative audit reports may increase investors' trust in the financial statements and, more broadly, in capital markets.

The IAASB's reforms to the auditor's report with key audit matters (KAMs) have been successful in many cases, particularly in the UK, at improving transparency with engagement-specific information (unlike critical audit matters requirements in the US which have been a struggle<sup>8</sup>). We are strong supporters of strengthening KAMs requirements over time to continue improving transparency, but **we believe matters relating to fraud should be in its own section under its own heading in the auditor's report, not commingled with other KAMs, with distinct requirements for the auditor to discuss:**

- Fraud risks identified in risk assessment;
- The auditor's response to the identified fraud risks; and
- The auditor's findings and conclusions.

**Fraud is behind the most catastrophic losses, as material frauds have resulted in total losses for investors in some cases. As such, in the eyes of investors, auditors' responsibilities related to fraud are amongst their most important responsibilities and therefore most deserving of discussion in the auditor's report.**<sup>9</sup> Commingling KAMs and matters relating to fraud poses the following risks:

- Reduces the emphasis of fraud by presenting it with other KAMs that may be less significant to investors.
- May reduce the number of non-fraud KAMs discussed in the auditor's report, as the fraud KAM counts towards an arbitrary target number that the practitioner is seeking to meet.
- By increasing the length of a single section of the auditor's report and aggregating disparate topics, the contents within the section are more likely to be obscured.

## **2. We are Unsure About Other Proposed Changes: Do They Address Problems Revealed by Recent Frauds or Not?**

We expected the Exposure Draft to include analyses of investigations, court cases, discussions with audit regulators from recent frauds (high profile and otherwise) and the [Association of Certified Fraud Examiners' biennial report](#) which found that auditors uncover but a fraction of frauds compared to those found through whistleblower programs. Then, based on the analyses, we expected the Board to identify specific areas of ISA-240 to be strengthened that would prevent incidents similar to the recent frauds from reoccurring. Essentially, we expected the Board to take an approach like the aviation industry and its regulators do after accidents and near misses.<sup>10</sup>

**Unfortunately, we are not able to tell from the Exposure Draft how the IAASB incorporated lessons learned from recent frauds and inspection findings from regulators.** Instead, the Exposure Draft mentions how the proposed changes are responsive to concerns raised by respondents to the [Discussion](#)

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<sup>8</sup> [Briefing to the PCAOB – Critical Audit Matters](#). Subcommittee on Standards, PCAOB Investor Advisory Group Meeting. June 7, 2023

<sup>9</sup> It's our view that errors in the financial statements do not typically result in *material* losses for investors, though they may point to weaknesses in internal controls and management competence that can be costly to restore to an acceptable level.

<sup>10</sup> See generally Recommendation 1 in [U.S. Department of the Treasury, Final Report of the Advisory Committee on the Auditing Profession to the U.S. Department of the Treasury](#) (October 6, 2008) at VII:1.

[Paper](#) (of which the vast majority of comment letter respondents were audit practitioners) and, in more abstract terms, the public interest. Without a better understanding of the problems that must be solved, we're unable to evaluate whether the Exposure Draft improves investor protections.

**At a basic level, investors do not know if external auditors are failing to uncover frauds because they are doing everything they are supposed to do (i.e., conducting audits in accordance with IAASB standards) but are thwarted by management or other forces, which would point to the need for better auditing standards, or if external auditors are in fact not conducting audits in accordance with IAASB standards, which suggests that the solution lies in better inspections and enforcement of auditing standards.**

### ***3. Auditor's Responsibilities Relating to Fraud: We Recommend Going a Step Further and Removing Mention of Management's "Primary" Responsibility Entirely.***

While extant ISA-240 and ED-240 state that "the primary responsibility for the prevention and detection of fraud rests with both management and those charged with governance of the entity," **we observe that management is often directly involved in most if not all high-profile frauds.**

Management has a responsibility to not commit fraud and to prevent and detect fraud committed by those they oversee. **For frauds involving management, the responsibility rests with those charged with governance of the entity (particularly independent audit committee members) and external auditors. Investors cannot rely on management to police themselves.** Independent board members and external auditors are investors' checks on management and act as important gatekeepers in the financial reporting ecosystem.<sup>11</sup>

We commend the IAASB for placing less emphasis on the responsibilities of management in ED-240 vs. extant ISA-240. We recommend the Board finishes the job and delete paragraph 3 of ED-240 entirely.

**It's not necessary to describe the responsibilities of management and those charged with governance in an auditing standard.** The responsibilities of management and those charged with governance are well established elsewhere in statutes, court cases, and corporate governance codes. We don't expect management teams and boards to consult auditing standards to understand their responsibilities. **Describing those responsibilities here at worst dilutes auditors' responsibilities and, at best, is stating the obvious.**

### ***4. Some Public Interest Issues Including Those Discussed by PIOB Appear Unaddressed.***

Over the life of the Board's project on fraud, [the Public Interest Oversight Board \(PIOB\) has emphasized several areas of ISA-240](#) that should be strengthened to better meet the public's expectations, including:

- "...to explore how the auditor should consider aspects such as external sources of information, culture, tone at the top, the role of the group auditor in respect of the risk of material misstatement at a component level, and the use of IT tools, and consider how these could impact the detection of fraud."
- Transparency requirements and impact of fraud on auditor's report; and
- Auditor's role with respect to authenticity of documentation.

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<sup>11</sup> See generally [The Council of Institutional Investors policy on Financial Gatekeepers](#).

The Board's [public interest mapping document](#) does not align with issues discussed by the PIOB, but it's our understanding based on our read of ED-240 that several of these issues, other than the transparency requirements addressed above, have not been addressed. For example:

- **Use of technology to improve fraud detection or reduce inherent limitations of the audit.**  
As of 2024, a significant portion of entities' transactions with customers, employees, suppliers, and providers of finance are digital. It's also our impression that it is easier to audit a greater number of digital transactions at lower cost than it was to audit paper records, which were the norm when the first auditing standards were created that prominently featured the language regarding the "inherent limitations" of an audit.

We recommend the Board adds a paragraph to ED-240 like the following:

*"Technological developments including the digitalization of books and records and automated tools that can analyze large quantities of data reduce the inherent limitations of an audit and, in general, increase users' expectations of assurance."*

- **The Importance of External Sources of Information and Whistleblower Programs.**  
Paragraphs A65 and A66 state that the auditor "may consider" listening to the entity's earnings calls, reading analysts' research reports, management's compensation packages, short-selling reports, negative media attention, or negative analyst reports.

Similarly, paragraph A70 states that the auditor "may consider" obtaining an understanding of, inspecting, and following up on matters related to an entity's whistleblower program.

Given that whistleblower programs may be more effective than auditors at detecting fraud and that some high-profile frauds seem to have been detected by short sellers and financial journalists before auditors, **we urge the Board to elevate these requirements from "may consider" to "must consider."**<sup>12</sup>

- **The Presumption of Document Authenticity has Been Deleted from ED-240 But, Confusingly, Retained in ISA 200.** We're not sure how to interpret this decision and urge the Board to delete this presumption from ISA 200 to avoid conflicts between the two standards.

##### **5. There are Changes the Board Should Make to its Communication Approach to Increase Investor and User Engagement.**

The ED-240 consultation should be presented in a manner which better enables conversation and engagement with investors and enables them to respond effectively. We believe the IAASB needs to develop outreach materials and more concise summaries of its exposure drafts that focus more on what is changing for investors and what problems it is intending to solve.

One example from ED-240 is the discussion of changes to the auditor's report regarding matters related to fraud – the example of what the proposed KAMs section may look like is buried at the end of the consultation, on page 147 of 162 in the discussion of conforming amendments to ISA 700/701. **Investors do not know what ISA 700/701 are, nor do they know to look at that section for what is the only change from ED-240 that will be observable to them.**

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<sup>12</sup> See the comment letter by [Members of the Investor Advisory Group to the PCAOB regarding the proposed standard on Noncompliance with Laws and Regulations](#), page 27.

To connect and engage with investors and other users of financial statements, the IAASB needs to write documents and outreach materials that start with what change investors/users will see in what they can observe. Only then can the IAASB deepen its engagement with investors regarding the changes in processes and procedures that they cannot observe. More concise summary documents in language which is not audit standard setting heavy which highlight the issues seeking to be resolved by the proposed standard and how the changes address such investor/user concerns would also facilitate broader engagement with investors and other users.

It would also be helpful if ED-240 included a redline version that tracked the changes from extant ISA-240.

***6. We Urge the Board to Work Globally with Other Standard Setters to Achieve Convergence***

Our views with respect to high-quality audits, generally, and audit procedures related to fraud, more specifically, are jurisdictionally agnostic. Our aforementioned comment letter in response to the UK Brydon Review highlights this. We note that the US Public Company Accounting Oversight Board (PCAOB) is currently working on a project related to fraud and [had a meeting discussing the topic with the Standards and Emerging Issues Advisory Group in May 2024](#) where fraud was the primary topic.

Investors invest globally. It is crucial for audit standard setters, particularly the IAASB and PCAOB given their “tentpole” status as the primary audit standard setters globally, to work toward a high quality, investor focused, converged, global baseline for auditors’ responsibilities related to fraud.

## 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:** Neither agree/disagree, but see comments below

#### **Detailed comments (if any):**

See our overall comments in Part A regarding the deletion of paragraph 3 of ED-240 that discusses management's responsibilities.

We agree with the application material that describes how quantitatively immaterial fraud can be "qualitatively material" if it is perpetrated by senior management. Any fraud or suspected fraud involving senior management is material.

### **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 no further comments)

#### **Detailed comments (if any):**



**Risk Identification and Assessment**

3. Does ED-240 appropriately build on the foundational requirements in ISA 315 (Revised 2019)<sup>13</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](#)

**Detailed comments (if any):**

Risk identification and assessment are at the heart of auditor’s responsibilities with respect to fraud in a financial statement audit. **Investors conduct many of the same risk assessment procedures (albeit with less privileged information) described in ED-240, which are used to develop forecasts, credit ratings, and equity risk premia that inform investment decisions.** CFA Institute’s curriculum for its CFA® Program highlights many of the same “warning signs” or “red flags” identified in Appendix 1.<sup>14</sup>

Investors take a risk-based approach to prioritize their resources, as fraud risk is only one consideration in an investment decision and different entities can present significantly different levels of risk. For example, investors would spend significant time assessing fraud risk factors when analyzing securities issued by small company with significant insider ownership and related party transactions based in a jurisdiction with weak laws and regulations, and far less vs. a large company with significant internal controls and a strong track record of transparency. **Investors expect auditors to do the same.**

We recommend the following to augment Appendix 1:

- **Order Risk Factors** – Order the risk factors from greatest to least concern, consider a requirement that auditors *must* assess the presence of the risk factors of greatest concern.
  - We suggest, for example, that “known history of violations of securities laws or other laws and regulations, or claims against the entity, its senior management, or those charged with governance alleging fraud or violations of laws and regulations, including those dealing with corruption, bribery, and money laundering,” past restatements, turnover in the CFO and senior finance ranks, and significant related party transactions would be risk factors of greatest concern.
  - Pressure to meet expectations or key performance indicators in general strikes us as a lower concern because it is present in virtually every entity; we’re not aware of any entity in which management feels no pressure to meet expectations. Of course, that pressure can become excessive, thus elevating the risk factor.
- **Add Risk Factors** – Add the following risk factors:
  - Complexity of business and transactions (“black box” risk).
  - Significant short interest and published short sellers’ reports.
  - Small size and/or newly established entity.

<sup>13</sup> ISA 315 (Revised 2019), *Identifying and Assessing the Risks of Material Misstatement*

<sup>14</sup> See LI *Financial Reporting Quality* and LII *Evaluating Quality of Financial Reports* readings.

- Significant adjustments to reported IFRS or GAAP figures.
- Domicile or incorporation in jurisdiction with weak laws and regulations, protection of property rights.
- Mergers and acquisitions.

We would also note that [at the recent PCAOB SEIAG meeting on fraud highlighted above](#) one panelist – a lawyer bringing cases against auditors – noted that risk identification is not the most challenging procedure for auditors, it is planning and executing procedures to address those risks where the audit falls short. We are not sure this is evident in the drafting of the proposal.

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

**Detailed comments (if any):**

See our overall comments in Part A regarding our uncertainty in evaluating whether the proposed changes in ED-240 address shortcomings in existing practice as revealed by recent frauds.

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

**Detailed comments (if any):**

See our overall comments in Part A regarding the proposed changes to enhance the transparency of the auditor's report about matters related to fraud.

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

**Detailed comments (if any):**

We agree with Board Member Kienhuis's dissent and recommend the IAASB include a separate stand-back requirement in 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: No response

Detailed comments (if any):

**Linkages to Other ISAs**

9. Does ED-240 have appropriate linkages to other ISAs (e.g., ISA 200,<sup>15</sup> ISA 220 (Revised),<sup>16</sup> ISA 315 (Revised 2019), ISA 330,<sup>17</sup> ISA 500,<sup>18</sup> ISA 520,<sup>19</sup> ISA 540 (Revised)<sup>20</sup> and ISA 701<sup>21</sup>) to promote the application of the ISAs in an integrated manner?

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

Overall response: No response

Detailed comments (if any):

**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: No response

Detailed comments (if any):

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<sup>15</sup> ISA 200, *Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with International Standards on Auditing*

<sup>16</sup> ISA 220 (Revised), *Quality Management for an Audit of Financial Statements*

<sup>17</sup> ISA 330, *The Auditor's Responses to Assessed Risks*

<sup>18</sup> ISA 500, *Audit Evidence*

<sup>19</sup> ISA 520, *Analytical Procedures*

<sup>20</sup> ISA 540 (Revised), *Auditing Accounting Estimates and Related Disclosures*

<sup>21</sup> ISA 701, *Communicating Key Audit Matters in the Independent Auditor's Report*

**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:** [See comments on effective date below](#)

**Detailed comments (if any):**

We always support the earliest possible adoption of new standards so that investors can benefit from new protections as soon as possible. Fraud is of paramount concern for investors; we do not support delaying the effective date of ED-240 for other projects.