

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)	Hong Kong Institute of Certified Public Accountants
Name(s) of person(s) responsible for this submission (or leave blank if the same as above)	Selene Ho
Name(s) of contact(s) for this submission (or leave blank if the same as above)	
E-mail address(es) of contact(s)	selene@hkipa.org.hk
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.	Asia Pacific
	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.	Jurisdictional/ National standard setter
	If "Other," please specify.
Should you choose to do so, you may include information about your organization (or yourself, as applicable).	

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:

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: [Disagree, with comments below](#)

Detailed comments (if any):

Given that the primary responsibility for the prevention and detection of fraud rests with both management and those charged with governance ("TCWG") of the entity, the order of the paragraphs describing the responsibilities of management and TCWG (ED-240.3) should be before the auditor's responsibilities (ED-240.2), which reflects the usual flow of the fraud process and follows a more logical sequence. This is also consistent with the order of presentation of the information in the auditor's report according to ISA 700, *Forming an Opinion and Reporting on Financial Statements*.

Paragraph 3 of the extant ISA 240 states that the auditor may identify the occurrence of fraud in rare cases while ED-240.6 mentions that the auditor may identify or suspect fraud, without highlighting that such circumstances are only identified in rare cases. The explanatory memorandum ("EM") for ED-240 did not provide the background information for including the reference to "rare cases" in the extant ISA 240 nor explain the omission of the reference to circumstances of "rare cases" when elevating the guidance from extant ISA to ED-240. We believe that the inclusion of reference to "rare cases" serves to manage the expectation gap between the financial statements users and auditors regarding the auditor's responsibilities relating to fraud in an audit and so we suggest that it should be retained in ED-240.6.

Besides, we also note that the whole paragraph 6 of the extant ISA 240 which describes the inherent limitations is elevated into ED-240.A12 except for the sentence "While the auditor may be able to identify potential opportunities for fraud to be perpetrated, it is difficult for the auditor to determine whether misstatements in judgment areas such as accounting estimates are caused by fraud or error." No explanation for the omitted sentence is included in the EM. We are of the view that the omitted sentence should be reinstated to help provide the context under which the auditor is responsible for fraud when performing an audit of financial statements. If the sentence is excluded in the final ISA 240, we suggest that the IAASB provide an explanation in the Basis for Conclusion.

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 comments below](#)

Detailed comments (if any):

The IAASB reinforces the exercise of professional skepticism in ED-240 by retaining in ED-240.19 the requirement stated in paragraph 13 of the extant ISA 240 emphasizing the importance of auditors maintaining professional skepticism throughout the audit and removing the reference to the auditor's preconceptions based on past experience about the honesty and integrity of management and TCWG, as it may serve to undermine the exercise of professional skepticism (ref: paragraph 23 of the EM). Our stakeholders believed that the auditor's past experience about the honesty and integrity of management and TCWG is one of the factors that could provide insights into the possibility of fraudulent transactions of the audit client and hence it should be retained in ED-240 by aligning the requirement in ED-240.19 with paragraph 13 of the extant ISA 240.

In addition, according to paragraph 25 of the EM, the IAASB suggested removing "Unless the auditor has reason to believe the contrary" from paragraph 14 of the extant ISA 240 as the same sentence is included in paragraph A24 of ISA 200, *Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with International Standards on Auditing* - "The auditor may accept records and documents as genuine unless the auditor has reason to believe the contrary" and it is unwarranted to repeat the same sentence in ED-240.20. Given that ISA 200 and ED-240 are two separate pronouncements with different objectives, we consider it is necessary to retain the sentence "Unless the auditor has reason to believe the contrary" in ED-240.20 to ensure consistency in the application of the ISAs.

Furthermore, ED-240.28 requires the auditor to perform a retrospective review of management judgments and assumptions related to the outcome of previous accounting estimates. Similar requirement in paragraph 33(b)(ii) of the extant ISA 240 highlights that the auditor shall perform a retrospective review of management judgments and assumptions related to "significant" accounting estimates reflected in the financial statements of the prior year. The exclusion of "significant" in ED-240.28 may imply that all accounting estimates, regardless of their nature and inherent risks, must be reviewed by the auditors. Therefore, it is suggested that the IAASB clarify its intention regarding the scope of the retrospective review necessary to fulfil the requirement as proposed in ED-240.28 (i.e. whether it is intentionally extended to all accounting estimates), and highlight in the Basis for Conclusion the rationale for the difference in the scope of the retrospective review as required by the extant ISA 240 and ED-240.

Risk Identification and Assessment

3. Does ED-240 appropriately build on the foundational requirements in ISA 315 (Revised 2019)¹ 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):

Our stakeholders suggested the IAASB to consider using "may" instead of "ordinarily" in ED-240.A110 when highlighting the appropriateness of rebutting the presumption of risks of material misstatement due to fraud in revenue recognition based on the auditor's professional judgment on the significance of the fraud risk factors. The use of "ordinarily" in the given context introduces challenges when applying professional judgment as it implies that in most cases or under normal circumstances, the presence of fraud risk factors related to revenue recognition would indicate a risk of material misstatement due to fraud, regardless of the significance of fraud risk factors as stated in ED-240.A110 and hence, the presumption should not be

¹ ISA 315 (Revised 2019), *Identifying and Assessing the Risks of Material Misstatement*

rebutted. By using “may” in ED240.A110, it allows the auditor to evaluate the significance of the fraud risk factors to determine if the presumption can be rebutted.

In addition, ED-240.41 requires the auditor, taking into account related fraud risk factors, to determine which types of revenue, revenue transactions or relevant assertions give rise to the risks of material misstatements due to fraud. We are not aware of guidance or linkage provided in ED-240 on how the fraud risk factors are being evaluated to reach the conclusion that they are not significant and hence the presumption of fraud risk may be appropriate to be rebutted. We would recommend that the IAASB develop implementation guidance such as non-authoritative material in respect of ED-240.41 to ensure consistent application of the requirements.

We also note that ED-240 provides more examples in ED-240.A111 compared to the extant ISA 240. While the examples aim to be broadly relevant, practitioners have conveyed that they are relatively straightforward, implying that the presumption could be easily rebuttable and they may not fully reflect certain practical situations encountered in audits. Practitioners have requested further illustrative examples reflecting the circumstances of entities with revenue, such as from telecommunication subscriptions, gambling machines that heavily rely on highly automated systems to process large volumes of data and low-value transactions, with sophisticated controls effectively operated, thereby minimizing opportunities for intervention. Appropriately reflecting such circumstances would enhance the practicality and relevance of the standard’s application.

Besides, we note that ED-240.29 focuses on discussion of material misstatements of the financial statements due to fraud, while the subparagraph (b) requires the engagement team to discuss consideration of any fraud or suspected fraud which seems to extend to all types of fraud and not just those might lead to material misstatements. Therefore, we would recommend that the IAASB remove “any” from the subparagraph (b) of ED-240.29 to achieve consistency in ED-240.29 and to limit the extent to only material misstatements of the financial statements due to fraud.

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):

ED-240.55 requires that the auditor shall obtain an understanding of the matter in relation to the identified fraud or suspected fraud in order to determine the effect on the audit engagement. In doing so, the auditor shall perform ED-240.55(a) to (d). Apart from ED-240.55(a) which requires the auditor to make inquiries about the matter, the requirements set out in ED-240.55(b) to (d) go beyond simply to “obtain an understanding of the matter” as stated in ED-240.55. ED-240.55(b) to (d) require the auditor to determine whether control deficiencies exist, and evaluate whether the entity’s process to investigate the matter and whether the remediation measures are appropriate if the entity has such process and remediation measures are in place. Therefore, we recommend that the IAASB clarify the requirements in ED-240.55 and the circumstances under which ED-240.55(b) to (d) would be carried out.

In addition, additional guidance on the implementation of the procedure outlined in ED-240.56(b), which states “If applicable, consider the impact on other engagements, including audit engagements from prior

years.” would be helpful, such as clarification on the nature of considerations and the timeframe (i.e. number of years) to be taken into account. Notably, for new audit clients, there is no similar requirement set out in ISA 510, *Initial Audit Engagements —Opening Balances*. We would suggest that the IAASB provide guidance in ED-240.56(b) or application material on its expected implementation of the required procedure.

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: [Disagree, with comments below](#)

Detailed comments (if any):

Under the proposed ED-240 conforming amendments, the IAASB suggests including additional statements in the auditor’s report:

- Informing that the auditor has communicated with TCWG regarding identified or suspected fraud, as well as other fraud-related matters, if any, deemed relevant by the auditor (i.e. pages 147 and 148 of the Conforming and Consequential Amendments arising from Proposed ISA 240 (Revised)).
- Stating that there are no key audit matters related to fraud to communicate if the auditor determines that, depending on the facts and circumstances of the entity and the audit, there are no key audit matters related to fraud to communicate. (i.e. ED-240.64)

However, by merely reading the new additional statements without explaining the context of those statements in the auditor’s report, our stakeholders raised concerns that the expectation gap between the financial statements users and auditors might be widened as financial statements users may wrongly assume that auditors are solely responsible for detecting fraud in the course of the audit or they might have higher expectations regarding the auditor’s role in detecting fraud, which could lead to misinterpretation of the auditor’s role and the scope of the auditor’s work. This misinterpretation could result in unintended consequences, for example, negatively impacting the auditor’s reputation and imposing undue burden if fraud incidents are subsequently reported on the entity, despite the auditor’s compliance with ED-240 when conducting the audit. To avoid this misinterpretation, our stakeholders recommended not to include the additional statements in the auditor’s report as currently drafted. Alternatively, the IAASB may consider:

- Including a statement in the auditor’s responsibilities section of the auditor’s report that acknowledges the inherent limitations of an audit in respect of identifying fraud or suspected fraud. This would inform users that, despite proper planning and performance of the audit in accordance with the ISAs, there is a risk that some material misstatements may not be detected (as described in ED-240.9).
- Stating in the directors’ and TCWG’s responsibilities section of the auditor’s report that the primary responsibility for the prevention and detection of fraud lies with both management and TCWG of the entity (as outlined in paragraph 16 of the EM).

In this regard, it is also recommended that the IAASB work with local professional accountancy bodies and standard setters to educate the general public through discussion forums or publications. A full understanding of the work performed by auditors and its limitations and the responsibility of management and TCWG related to fraud would be helpful to narrow the expectation gap. The HKICPA is willing to work with the IAASB to organize discussion forums or develop publications.

Furthermore, in order to enhance comprehension and consistent application of the application material in ED-240, we recommend that the IAASB provide examples to illustrate the circumstances referred to in (a) ED-240.A168 and the proposed conforming amendments in ISA 701.A21 regarding “certain risks of material misstatement due to fraud not requiring significant auditor attention” and (b) ED-240.A176 which pertains to a listed entity where “in certain limited situations, the auditor may determine that there are no matters related to fraud that are key audit matters”.

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: [Disagree, with comments below](#)

Detailed comments (if any):

See comments in Q5, but should the IAASB decide to finalize the proposed requirement to enhance transparency in the auditor’s report, it should only be extended to PIEs, but not to other entities that are not PIEs. The IAASB could consider adding in application material similar to paragraph A41 of ISA 700 (Revised) where the auditor may decide to communicate matters related to fraud in the auditor’s report for other entities.

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 share the same view of the IAASB regarding the crucial role of the stand-back requirement in the overall evaluation process. We believe that the significance of the stand-back requirement in the fraud risks assessment should be emphasized by including it in the requirement section of ED-240 rather than implying the principle in ED-240.21 as currently drafted. ED-240.21 requires the auditor to remain alert throughout the audit and ED-240.19 requires the auditor to maintain professional skepticism throughout the audit. We consider that requiring the auditor to “maintain professional skepticism” and “remain alert” without specifying corresponding actions may create ambiguity regarding the specific procedures the auditor should undertake to fulfill the requirements, as well as creating inconsistent application of the relevant requirements in practice. Therefore, we recommend that the IAASB, aligning the approach of ISA 315 (Revised 2019) and ISA 540 (Revised), include an explicit stand-back requirement in ED-240 that requires the auditor to perform the overall evaluation by taking into account all audit evidence obtained from the procedures performed, whether corroborative or contradictory.

Besides, we find that the application materials in ED-240.A29 to A32 do not provide guidance on how to demonstrate the auditor's thought process in reaching the conclusion in the audit documentation. We recommend that the application material be expanded to address the nature and extent of documentation required in relation to the "maintaining professional skepticism" and "remain alert" requirements, or develop non-authoritative materials such as case studies to highlight how the auditor maintained professional skepticism and remained alert as required 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: Agree (with no further comments)

Detailed comments (if any):

Linkages to Other ISAs

9. Does ED-240 have appropriate linkages to other ISAs (e.g., ISA 200,² ISA 220 (Revised),³ ISA 315 (Revised 2019), ISA 330,⁴ ISA 500,⁵ ISA 520,⁶ ISA 540 (Revised)⁷ and ISA 701⁸) to promote the application of the ISAs in an integrated manner?

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

Overall response: Agree (with no further comments)

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: Yes, with comments below

² ISA 200, *Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with International Standards on Auditing*

³ ISA 220 (Revised), *Quality Management for an Audit of Financial Statements*

⁴ ISA 330, *The Auditor's Responses to Assessed Risks*

⁵ ISA 500, *Audit Evidence*

⁶ ISA 520, *Analytical Procedures*

⁷ ISA 540 (Revised), *Auditing Accounting Estimates and Related Disclosures*

⁸ ISA 701, *Communicating Key Audit Matters in the Independent Auditor's Report*

Detailed comments (if any):

In general, our stakeholders provided positive feedback that the appendices 1-5 give a comprehensive list of factors or considerations with regard to the concerned areas which help facilitate an auditor's better understanding of the requirements. In addition to these appendices, our stakeholders suggested that the IAASB offer implementation guidance to assist them in transitioning smoothly from the current ISA 240 to ED-240 once the final standard is released.

In addition, ED-240.48 requires the auditor to determine whether other audit procedures are needed in addition to those in paragraphs ED-240.49-53 to respond to the identified risks of management override of controls. Procedures in paragraphs ED-240.49-53 include inquiries of management, journal entries testing, evaluation of accounting estimates as well as evaluation of unusual transactions. We recommend the IAASB to provide practical examples or case studies to demonstrate the auditor's thought process involved in the determination and what appropriate "other audit procedures" as referred to in ED-240.48 would enable the auditors to effectively respond to the identified risks related to management override of controls.

Besides, we would suggest that the IAASB consider rephrasing ED-240.A11(a) as the current drafting of ED-240.A11(a) implies fraud involving staff or management other than senior management is considered not significant or not qualitatively material. We do not believe that fraud involving lower grade staff is insignificant. In addition, we are of the view that the requirement set out in ED-240.A11(b) is not practical as in reality, auditors might not know the reasons why a fraud was perpetrated and might involve undue resources to investigate the reasons. Therefore, we seek clarification by the IAASB on its expectation on the extent of work in this area.

Moreover, we also recommend the IAASB together with professional accountancy bodies to continuously educate stakeholders that not all misstatements in the financial statements, including those related to fraud, will be detected, even though the audit is properly planned and performed in accordance with ISAs. Given that good corporate culture and integrity of the management team lay the foundations of corporate governance and internal controls system of the entity which are essential in detecting and preventing fraudulent activities in an entity, the importance of setting the "tone at the top" by senior management should be periodically re-iterated.

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):