

ASA 240
(October 2009)

Explanatory Statement

ASA 240 The Auditor's Responsibilities Relating to Fraud in an Audit of a Financial Report

Issued by the **Auditing and Assurance Standards Board**



Australian Government

Auditing and Assurance Standards Board

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Explanatory Statement ASA 240 *The Auditor's Responsibilities Relating to Fraud in an Audit of a Financial Report*

**Reasons for Issuing Auditing Standard ASA 240
*The Auditor's Responsibilities Relating to Fraud in
an Audit of a Financial Report***

The Auditing and Assurance Standards Board (AUASB) issues Auditing Standard ASA 240 *The Auditor's Responsibilities Relating to Fraud in an Audit of a Financial Report* pursuant to the requirements of the legislative provisions and the Strategic Direction explained below.

The AUASB is an independent statutory board of the Australian Government established under section 227A of the *Australian Securities and Investments Commission Act 2001*, as amended (ASIC Act). Under section 336 of the *Corporations Act 2001* (the Act), the AUASB may make Auditing Standards for the purposes of the corporations legislation. These Auditing Standards are legislative instruments under the *Legislative Instruments Act 2003*.

Under the Strategic Direction given to the AUASB by the Financial Reporting Council (FRC), the AUASB is required to have regard to any programme initiated by the International Auditing and Assurance Standards Board (IAASB) for the revision and enhancement of the International Standards on Auditing (ISAs) and to make appropriate consequential amendments to the Australian Auditing Standards. The IAASB has undertaken a programme to redraft, and in some cases, revise, in "clarity" format, the entire suite of ISAs. Accordingly, the AUASB has decided to revise and redraft the Australian Auditing Standards using the equivalent redrafted ISAs.

The Auditing Standard conforms with ISA 240 *The Auditor's Responsibilities Relating to Fraud in an Audit of Financial Statements*.

Operative Date

ASA 240 *The Auditor's Responsibilities Relating to Fraud in an Audit of a Financial Report* is operative for financial reporting periods commencing on or after 1 January 2010.

Purpose of Auditing Standard ASA 240 *The Auditor's Responsibilities Relating to Fraud in an Audit of a Financial Report*

The purpose of the Auditing Standard is to establish requirements and to provide application and other explanatory material to auditors regarding their responsibilities relating to fraud in an audit of a financial report.

Main Features

This Auditing Standard:

- (a) distinguishes fraud from error and describes the types of fraud relevant to the auditor, that is, misstatements resulting from misappropriation of assets and misstatements resulting from fraudulent financial reporting;
- (b) describes the responsibility for the prevention and detection of fraud;
- (c) describes the auditor's responsibility for maintaining an attitude of professional scepticism throughout the audit, considering the potential for management override of controls and recognising the fact that audit procedures that are effective for detecting error may not be effective in detecting fraud;
- (d) requires the auditor to:
 - (i) discuss among the engagement team members how and where the entity's financial report may be susceptible to material misstatement due to fraud, including how fraud might occur;
 - (ii) obtain an understanding of the entity and its environment, including the entity's internal control and obtain information for use in identifying the risks of material misstatement due to fraud at the financial report level and at the assertion level; and
 - (iii) determine responses to address the assessed risks of material misstatement due to fraud;
- (e) requires written representations from management relating to fraud;

Explanatory Statement ASA 240 *The Auditor's Responsibilities Relating to Fraud in an Audit of a Financial Report*

- (f) requires communications to management and with those charged with governance on matters related to fraud; and
- (g) establishes documentation requirements.

Preamble and Overall Objectives

ASA 240 is to be read in conjunction with ASA 101 *Preamble to Australian Auditing Standards*, which sets out the intentions of the AUASB on how the Australian Auditing Standards, operative for financial reporting periods commencing on or after 1 January 2010, are to be understood, interpreted and applied. ASA 240 is to be read also in conjunction with ASA 200 *Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with Australian Auditing Standards*.

Process of making Australian Auditing Standards

The AUASB's Strategic Direction, *inter alia*, provides that the AUASB develop Australian Auditing Standards that:

- have a clear public interest focus and are of the highest quality;
- use the International Standards on Auditing (ISAs) of the International Auditing and Assurance Standards Board (IAASB) as the underlying standards;
- conform with the Australian regulatory environment; and
- are capable of enforcement.

In implementing the FRC's Strategic Direction, the AUASB has undertaken a process of revising and redrafting the Australian Auditing Standards that has:

- updated the form, layout and content of the Australian Auditing Standards;
- addressed the legal enforceability of mandatory obligations;
- maintained clarity of the auditor's obligations;
- incorporated appropriate references to Australian laws and regulations;

Explanatory Statement ASA 240 *The Auditor's Responsibilities Relating to Fraud in an Audit of a Financial Report*

- clearly identified, by use of the prefix “Aus”, AUASB additions to paragraphs in the requirements or the application and other explanatory material; and
- included other amendments as necessary.

Consultation Process prior to issuing the Auditing Standard

The AUASB has consulted publicly as part of its due process in developing the Auditing Standard. Exposure Draft ED 5/08 *Proposed Auditing Standard: The Auditor's Responsibilities Relating to Fraud in an Audit of a Financial Report* (Re-issuance of ASA 240), was issued on 31 July 2008 with a 30 day comment period.

As an integral part of its consultation with the public, the AUASB sought comments on specific questions including:

- the completeness and accuracy of references in the Auditing Standard to relevant laws and regulations;
- the significant costs, if any, and benefits, of compliance with any additional requirements under the Auditing Standard; and
- whether or not there exist any matters of public interest affecting the issuance of the Auditing Standard.

Submissions were received by the AUASB and these were considered as part of the development and finalisation of the Auditing Standard.

Regulation Impact Statement

A *Regulation Impact Statement* (RIS) has been prepared in connection with the redrafting of Australian Auditing Standards in “clarity” format, including ASA 240 *The Auditor's Responsibilities Relating to Fraud in an Audit of a Financial Report*.

The RIS has considered both the expected benefits and expected costs of the introduction of clarified auditing standards, including comments provided by stakeholders during the redrafting process. It concluded that expected benefits to users of audit services, users of audit reports, auditors and the Australian economy in general are, on balance, likely to outweigh expected costs.

Main Differences from ASA 240 *The Auditor's Responsibility to Consider Fraud in an Audit of a Financial Report* (April 2006)

The main differences between the Auditing Standard and the Auditing Standard that it supersedes, ASA 240 *The Auditor's Responsibility to Consider Fraud in an Audit of a Financial Report* (April 2006), are:

1. Auditing Standard ASA 240 is written in the “clarity” format using the equivalent International Standard on Auditing (ISA 240 *The Auditor's Responsibilities Relating to Fraud in an Audit of Financial Statements*) as the underlying Auditing Standard. Consequently, the format, layout, and paragraph numbering styles are different from the extant Auditing Standard.
2. To improve clarity, certain requirements and guidance in the extant Auditing Standard have been re-written, however, the equivalent meaning has been retained.
3. Certain guidance material in the extant Auditing Standard has been elevated to requirements.
4. The following mandatory obligations in the extant Auditing Standard are (now) included, in part or full, in other Auditing Standards:
 - (a) In planning and performing the audit to reduce audit risk to an acceptably low level, the auditor shall consider the risks of material misstatements in the financial report due to fraud. (Ref: Extant ASA 240, paragraph 6). This requirement is now covered in ASA 200 *Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with Australian Auditing Standards*.
 - (b) When identifying and assessing the risks of material misstatement at the financial report level, and at the assertion level for classes of transactions, account balances and disclosures, the auditor shall identify and assess the risks of material misstatement due to fraud. Those assessed risks that could result in a material misstatement due to fraud are significant risks and accordingly, to the extent not already done so, the auditor shall evaluate the design of the entity's related controls, including relevant control activities, and determine whether they have been

Explanatory Statement ASA 240 *The Auditor's Responsibilities Relating to Fraud in an Audit of a Financial Report*

implemented. (Ref: Extant ASA 240, paragraph 61). This requirement is now covered in ASA 315 *Identifying and Assessing the Risks of Material Misstatement through Understanding the Entity and Its Environment*; and ASA 330 *The Auditor's Responses to Assessed Risks*.

- (c) The auditor shall make those charged with governance and management aware, as soon as practicable, and at the appropriate level of responsibility, of material weaknesses in the design or implementation of internal control to prevent and detect fraud which may have come to the auditor's attention. (Ref: Extant ASA 240, paragraph 106). This requirement is now covered in ASA 260 *Communication with Those Charged with Governance*.