

THE FRAUD LENS – INTERACTIONS BETWEEN SLAuS 240 AND OTHER SLAuSs

This publication about the fraud lens¹ to explain the relationship between, and linkage of, Sri Lanka Auditing Standard (SLAuS) 240, The Auditor’s Responsibilities Relating to Fraud in an Audit of Financial Statements, and other SLAuSs when conducting an audit.

This publication does not amend or override the SLAuSs, the texts of which alone are authoritative. The non-authoritative guidance is not meant to be exhaustive² and reading this publication is not a substitute for reading the SLAuSs.

Sri Lanka Auditing Standard (SLAuS) 200³ is the foundational standard that sets out the independent auditor’s overall objectives when conducting an audit of financial statements in accordance with the SLAuSs and establishes the obligation of the auditor to comply with all the SLAuSs. The objectives in SLAuS 200 reflect (in part) that the auditor addresses material misstatement whether due to **fraud or error** when conducting an audit to form and express an opinion, and report, on the financial statements.

SLAuS 240 Is Read in Conjunction with SLAuS 200



SLAuS 240 deals with the auditor’s responsibilities for fraud in an audit of financial statements and in doing so reinforces the continued use of the **fraud lens** throughout the audit engagement. SLAuS 240 also clarifies that the distinction between fraud and error is based on intent.⁴ There is an additional emphasis on the importance of maintaining an attitude of professional skepticism which is especially relevant when identifying and assessing risks of material misstatement due to fraud and responding appropriately to the assessed risks due to fraud. These assessed fraud risks relate to those intentional misstatements that could arise either from fraudulent financial reporting, or the misappropriation of assets.

SLAuS 240 paragraph 11: The objectives of the auditor are:

- a) To **identify and assess the risks of material misstatement** of the financial statements due to fraud;
- b) To obtain **sufficient appropriate audit evidence** regarding the assessed risks of material misstatement due to fraud, through **designing and implementing appropriate responses**; and
- c) To **respond appropriately** to fraud or suspected fraud identified during the audit.

Relationship Between SLAuS 240 and Other SLAuSs

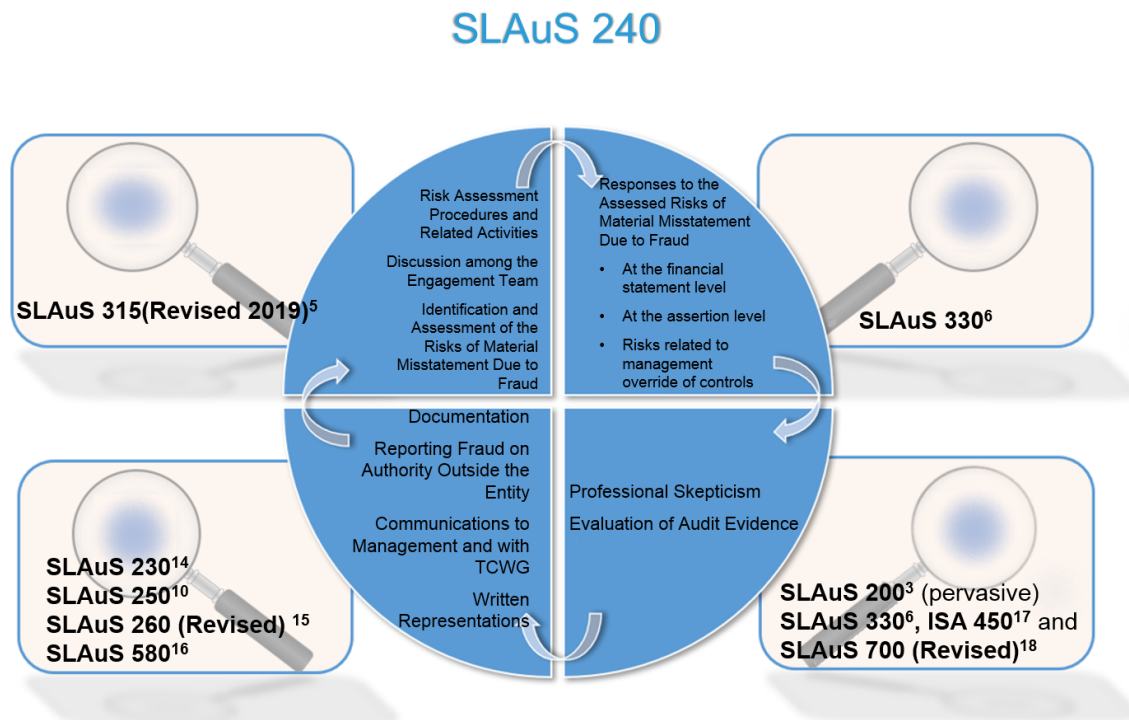
SLAuS 240 both expands on certain SLAuSs as well as provides fraud-specific audit procedures that complement the other SLAuSs. In doing so, SLAuS 240 broadly focuses on the auditor’s **fraud lens** when planning and performing an audit of financial statements, and reporting on the financial statements.



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The diagram depicts the key areas that SLAuS 240 addresses and highlights the explicit references from SLAuS 240 to other SLAuSs that further strengthen the interrelationships between the auditing standards.



SLAuS 240 expands on SLAuS 315 (Revised 2019)⁵ and SLAuS 330⁶

While other key standards address the core requirements for identifying and assessing the risks of material misstatement (SLAuS 315 (Revised 2019)) and responding to those risks of material misstatement (SLAuS 330), SLAuS 240⁷ expands on how these standards are applied with a **fraud lens**.⁸ In particular, in identifying and assessing the risks of material misstatement due to both fraud and error under SLAuS 315 (Revised 2019), the auditor takes into account the inherent risk factors, which include the susceptibility to misstatement due to management bias or other fraud risk factors.⁹

The emphasis in SLAuS 240 on risk identification and assessment and responding to those risks of material misstatement through modifying the nature, timing and extent of the work effort when there is a risk of material misstatement due to fraud, highlights the importance of obtaining an understanding of the entity and its environment, the applicable financial reporting framework, and the entity's system of internal control with a **fraud lens**. Key aspects that underpin the auditor's consideration of the potential risks of material misstatement due to fraud include the entity's culture (including tone at the top), as well as the environment in which the entity operates. Purposeful engagement team discussions on these key aspects, as well as other matters or areas that have been identified as being susceptible to possible misstatement due to fraud, will help all engagement team members apply the **fraud lens** in undertaking their work.

SLAuS 240 paragraph 28: Assessed risks of material misstatement due to fraud are treated as **significant risks**

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In addition to designing and implementing overall responses to address the assessed risks of material misstatement due to fraud at the financial statement level, the auditor is also required to design and perform further audit procedures that are responsive to the assessed risks of material misstatement due to fraud at the assertion level. In doing so, the auditor may, when applying the *fraud lens*, modify the nature, timing and extent of the further audit procedures in order to be responsive to the assessed fraud risks. For example, the auditor may amend the timing of the further audit procedures performed to incorporate additional elements of unpredictability, or assign engagement team members who have more experience or have the necessary specialized skills or knowledge to address changes to the nature of the further audit procedures performed.

SLAuS 240 includes fraud-specific audit procedures

SLAuS 240 includes certain requirements that provide the auditor with the necessary *fraud lens* when designing and performing audit procedures that are responsive to risks related to management override of controls and to address specific aspects of other SLAuSs, such as when reporting fraud to an appropriate authority outside the entity in accordance with SLAuS 250¹⁰. These fraud-related audit procedures are intended to be embedded throughout the audit process. The requirement in SLAuS 240¹¹ to review accounting estimates for biases and evaluate whether the circumstances producing the bias, if any, represent a risk of material misstatement due to fraud, is an example of a fraud-related procedure that is to be performed in conjunction with addressing the requirements in SLAuS 540 (Revised)¹². Other audit procedures in SLAuS 240 that are designed and performed irrespective of the auditor's assessment of the risks of management override of controls include those that address journal entries and significant transactions that are outside the normal course of business for the entity, or that otherwise appear to be unusual (including related party relationships and transactions).



Linkage of Other SLAuSs to SLAuS 240

Other relevant topic or subject-matter specific SLAuSs have explicit references to SLAuS 240. The fraud-specific requirements in other SLAuSs serve to focus the auditor's work effort on the identification and assessment of the risks of material misstatement due to fraud and the responses to address the assessed fraud risks. For example, SLAuS 550¹³ includes requirements to meet the following stated objective, "to obtain an understanding of

related party relationships and transactions sufficient to be able to recognize fraud risk factors, if any, arising from related party relationships and transactions that are relevant to the identification and assessment of the risks of material misstatement due to fraud." In this instance SLAuS 550 expands upon how SLAuS 240, SLAuS 315 (Revised 2019) and SLAuS 330 are to be applied in relation to risks of material misstatement associated with related party relationships and transactions.

Understand the Interdependencies

A clear understanding of the relationship between, and linkage of, SLAuS 240 and the other SLAuSs will assist the auditor to enhance audit execution when applying a *fraud lens*. This will in turn fulfil the auditor's responsibilities under SLAuS 240 and other SLAuSs that contain the broader requirements for an audit.



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Endnote

- ¹ The phrase *fraud lens* should be read in context. The lens is intended to “magnify” and provide a clear “focus” or “spotlight” on the topic of fraud.
- ² While certain SLAuS requirements and application and other explanatory material are highlighted, this non-authoritative guidance does not cover all of the SLAuS provisions that are relevant to the auditor’s responsibilities relating to fraud in an audit of financial statements that are effective as of June 2022.
- ³ SLAuS 200, *Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with Sri Lanka Auditing Standards*
- ⁴ SLAuS 240, paragraphs 2, 3 and 12(a)
- ⁵ SLAuS 315 (Revised 2019), *Identifying and Assessing the Risks of Material Misstatement*
- ⁶ SLAuS 330, *The Auditor’s Responses to Assessed Risks*
- ⁷ SLAuS 240 as amended for the conforming and consequential amendments resulting from the approval of SLAuS 315 (Revised 2019).
- ⁸ SLAuS 240, paragraph 1
- ⁹ SLAuS 315 (Revised 2019), paragraphs 19(c) and 31(a)
- ¹⁰ SLAuS 250, *Consideration of Laws and Regulations in an Audit of Financial Statements*
- ¹¹ SLAuS 240, paragraph 33(b)
- ¹² SLAuS 540 (Revised), *Auditing Accounting Estimates and Related Disclosures*
- ¹³ SLAuS 550, *Related Parties*
- ¹⁴ SLAuS 230, *Audit Documentation*
- ¹⁵ SLAuS 260 (Revised), *Communication with Those Charged With Governance*
- ¹⁶ SLAuS 580, *Written Representations*
- ¹⁷ SLAuS 450, *Evaluation of Misstatements Identified During the Audit*
- ¹⁸ SLAuS 700 (Revised), *Forming an Opinion and Reporting on Financial Statements*