Advanced Auditing - Week 3

Michael Kiersten

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1. Public expectations of fraud are particularly high. The public expect auditors to detect and deter all frauds. Their job is seen as someone who is capable of eradicating fraud within business's. Auditor's are responsible for the detection of material misstatement that may mean the financial statements do not present a true and fair view, and not to detect fraud, but to conduct audit tests in such a way to limit the possibility that material fraud goes undetected. This rhetoric goes against what has been set down in ISA240, it also has a slight lack of scepticism on the part of the public that an auditor may be someone who can help assure the safety of a business and its financial statements, but not have them be fool-proof. It would be best if the public realised that an auditor signing-off on the business gave it credibility.

2. The auditor may have the ability to conduct a forensic audit but as forensic audit is something that is seen as routine, the expansion of responsibility of detecting fraud may not be appropriate as the reactive side of the detection is missing and auditors are confined to sampling a business and ensuring that all is well. The auditor is a patrol man who in his duties must be able to be reasonably sure that no fraud has occurred. He is not someone who through a forensic audit, say as a patrol man would check the door handles of garages he patrols, would be expected to be in all places at once and catch all fraud, or all car thefts. He is constrained by sampling, or choosing when he drives past the garages. He also would use forensic audit as part of his routine duties and this does not lend itself to finding as a patrol man the lights being off and him knowing there is car theft going on inside when all looks well. Forensic audit requires a different type of wherewithal of the person conducting it to be counted upon.

3. 'Auditors must be sensitive to fraud risk, assessing it to be higher when a fraud exists than when it does not.'. If a company is suspected/under fraud investigation, there should be a higher fraud risk than if there is no mention of fraud. If the managers are under suspicion of earnings management, the auditors must include this in their discussions and planning for fraud risk.

'Next, auditors must budget and plan effective fraud-detection procedures that are linked to the fraud risk.'. If there was an earnings management possibility the auditors would need to conduct fraud-detection procedures that focused on and highlighted the area of earnings management. This mean more in depth tests and a longer testing of the appropriate area.

'Third, they must effectively collect and interpret the evidence from the procedures.'. They must, say in the case of earnings management run procedures to test, maybe the expenses to ensure that what is reported gives a true and fair view of the company and is ethical and does not break the law. This might mean checking the estimates given by the company for depreciation.

'Last, auditors must appropriately respond to their audit finding.'. Once the the evidence has been found, if the expenses were too low, there must be corrective action taken. This may involve consulting with management to see if they will change their figures, and possibly modifying the audit opinion, dropping the client, or calling in the audit committee.

4. Auditors should update their procedures in response to the fraud risk assessment. The paper highlights that auditors may struggle to update their audit procedures in response to any fraud risk that has been highlighted. This limits the audit as the procedures carried out are not sensitive to the fraud risk that has been found. So the procedures remain similar if there is a high fraud risk found or a low fraud risk found. This may mean that management can hide fraud from the auditors during to their not being scrupulous enough by missing changing their procedures. The hiding will happen as the management can know what top suspect given standard audit procedures.

5. Higher-order strategic reasoning involves taking into account the fact that the auditee may be aware of the audit procedures and try to conceal any fraud they have committed. This means that the auditor in a state of planning is beginning to scope in on more possibilities that may occur, given an educated and devious fraudster. This planning would lead to more frauds possibly being caught as manoeuvres used to conceal fraud could be uncovered. The fact that this type of thinking can be quite difficult is a negative. There are many dimensions that must be taken into account in order to effectively conduct higher-order strategic reasoning and the difficulty for a single auditor to do this is what means the technique has some downsides. When thinking of the possible concealments of a perpetrator while designing audit procedures, there my be some difficulty in tying the plan together so that the moves against the auditor fit within their expanded tests. The auditors can fight this expansion difficulty by breaking down the higher-order strategic reasoning so it is easier to manage.

Brainstorming involves bringing auditors together in order to design audit procedures in response to fraud risk. This is helpful in that it reduces the difficulty of coming up with the ideas alone and can mean more and more creative tactics can be used in the audit procedures. It does however come with problems of inhibition, either through waiting or fear. This may make any brainstorming done not as effective as it could have been.

6. Standard audit plans force rigidity in action. There may be less careful planning done and a tendency to jump into conducting the audit procedure without prior thought. This is as they are standard procedures that may be relied upon. The reliance may breed a lack of carefulness. They may also not be helpful in having an auditor think properly about other parts of the audit or having an ability to reason as to what is their next best move to do. The following of a standard checklist seems to block the required higher mental functions of the auditors. This may happen as following a given list does not tend to have an auditor come away from thinking on the list.

7. Brydon mentions that ISA240 goes some way to lowering the expectations of an auditor in relation to fraud. He says that in doing this the position that was left was not one that was clear as to what the duties of an auditor were. With less clarity on the role of an auditor it may be that the public are less clear on what an auditor does. It also leads to the issue of the auditor presenting an opinion of having assurance the finical statements provided a true and fair view although there may have been a material fraud they have failed to detect.He says it is too much to expect the users to be aware that the auditor had done enough work to reach a reasonable expectation of the financial statements being free of material misstatements as a default.

8. 14.1.5 It is an obligation of an auditor to endeavour to detect material fraud in all reasonable ways. The practicalities of this recommendation may miss the constraints that auditors come under given their profession. It's expectation is that auditors are to strive to find all material frauds that are committed, but given the position of audit, and the nature of their work as someone who is sampling transactions this may leave them with more to do than they are able to. The impact of this may be furthering worsening of the opinion of audit and less trust from users, leading to weaker business prospects. This all should be handled very carefully, as with some tweaks and done correctly a stronger audit would surely be a good thing.

14.2.2 Directors should report on the actions they have taken to fulfil their obligations to prevent and detect material fraud against the background of their fraud risk assessment. This idea would mean that directors are to note all of the actions they take to detect fraud given what they have found in their risk assessment. This is a duty that a director can be reasonably be considered to carry out with full cooperation of the business and it's managers. This may not always be the case and these reports may leave director's with more work to do than they can feasibly garner. It is important that directors are aware of fraud and do take steps to lower it along with documented action plans, but it is difficult to measure if they would be in a position to have a cohesive report made. The groundwork for this though could be placed and the recommendation would add tremendously to stopping fraud.

14.3.3 Training in both forensic accounting and fraud awareness are to be parts of the formal qualification and continuous learning process to practice as a financial statement auditor. This is something that would help an auditor to be better at fraud detection, though cannot be expected to help with them in detecting all fraud. The nature of an auditors job is not to be a forensic accountant and the extra work although necessary does not extend the auditors position to be one that covers all fraud detection.

14.3.5. Auditor's report state explicitly the work performed to conclude whether the director's statement regarding the actions they have taken to prevent and detect material fraud is appropriate. Furthermore the auditors should state what steps they have taken to assess the effectiveness of the relevant controls and to detect any such fraud. This, if the directors report was properly implemented would seem to be a natural follow on and once again something that could be built into the audit and put to work. It would position audit closer to a fundamental opinion on the business, and possibly extend into a governance monitoring role.

14.4.3 ARGA maintains an open access case study register detailing corporate frauds that have occurred in order that auditors can learn in real time from these frauds. This would be a great asset to anti-fraud campaigns as it would provide details of how frauds previous had occurred. These materials would shape the view auditors had of fraud and better enable them to be aware in their anti-fraud education.

14.5.4 ARGA establish an independent Auditor Fraud Panel to which it would refer the resulted of investigations into auditor failure to detect material frauds. This panel may be slightly remiss in being set up as it does not concentrate on the most important things that are currently expected from auditors. It would place more pressure on auditors in fraud detection and this is something that may not be helpful in conducting a good audit.

9. These recommendations would create more resources for auditors to use to support them in their job. It is a well thought out action course that has been deliberated by many important thinkers in the field. The possibility of more fraud being detected is a central theme here but it is not put as a deliberate aim of the action steps. The paper seems to better align with auditors current responsibilities. The detection of fraud may well be improved though by the paper, as the help for auditors in their role will clarify their direction during the audit work.

10. Both papers agree that there would be better served audit if there was a fraud database of some kind available, to view previous fraud cases. The ACCA paper recommends a more conservative, or status quo approach to its action steps. These can possibly be thought as more achievable. They are in support of ISA 240 and see it needing enhanced definitions, whereas Brydon does not think it has done enough and calls for auditors to endeavour to detect fraud in all material ways, probably. The suspicious mindset mentioned in the ACCA paper could be thought to be referencing some practices such as higher-order strategic reasoning, though this is not said definitely. The ACCA paper seems to be stronger aim at moving forward than Brydon. It is aligned with ISA240 and is pushing deliberately for more resources for auditors rather than asking more of them explicitly.