

# Africa FY16 >> Audit Quality Update

**Fraud:  
Case, cause & our response**



A high-angle photograph of a golf green. Two golfers are visible from the waist down, standing on the left side of the frame. They are wearing light-colored trousers and golf shoes. Long, dark shadows of the golfers and their clubs stretch across the green towards the right. A large, dark shadow of a person, possibly the photographer, is cast across the lower half of the green. A yellow rectangular frame with a black border is overlaid on the right side of the image, containing the text.

**Is thinking about fraud really  
that important?**

# 2014 Global Fraud Survey Results

**33%** would offer more flexible product return policies

**39%** believe bribery and corruption is common

**14%** would change valuations/reserves assumptions

**11%** of CEOs are willing to misstate financial performance

**11%** would extend reporting periods

**21%** have been asked to pay a bribe

**8%** would backdate contracts



# The Worlds Biggest Accounting Scandals



# Toshiba \$1.2bn accounting scandal claims first scalps



**Revenue  
Recognition!**

Profits ramped up over a  
period of 6 years

Overstated profits by  
Yen 151.8bn (\$1.2bn)

Pressure to meet  
performance targets

# Olympus scorched



**Profit  
smoothing!**

Buried losses for over  
20 years

Irregular payments for  
acquisitions (\$687 in  
advisory fees)

Pressure to cover  
massive impairment  
losses

# Fraud causes collapse of 12th largest privately held U.S. Company - SemGroup




**Fraudulent  
trade deals!**

Unauthorised energy  
trading caused \$3.2bn  
loss

Complex derivatives  
trading strategy with no  
oversight

Pressure to continue  
rapid growth despite  
lack of controls

A low-angle, upward-looking photograph of a tall, modern building at night. The building's facade is illuminated from within, showing many lit windows and balconies. The sky is dark with some light clouds. A bright yellow rectangular frame is superimposed on the image, containing the text. The frame has a thick yellow border and a semi-transparent yellow fill.

**What is the most common  
area where fraud occurs?**



# Revenue Recognition


**Percentage Completion calculation, particularly in construction contracts**

**Claims on contracts, particularly in construction contracts**

**Provisions**

**Cut off**

**Selling without title passing**

A close-up photograph of a stack of books with various colored spines (green, yellow, blue, red, teal). A yellow trapezoidal frame is superimposed on the image, containing the text. The frame has a thick yellow border and a black interior. The text is white and centered within the black area. The bottom-left corner of the frame features a small graphic of three yellow squares and a grey rectangle.

**How can the auditor ever know  
when fraud is happening?**



Responsibility for preventing and detecting fraud lies with management (ISA 240)

Typical components of a fraud management programme are:

**Code of ethics**

**Anti-fraud programme & policies**

**Fraud risk assessment and response plan**

**Fraud controls monitoring**

**Communications and training**

**WHISTLEBLOWING**



Obtain **reasonable assurance** that the financial statements are free from material misstatement

- ▶ Misstatements can arise from fraud or error
  - ▶ Distinction is whether the underlying action is intentional or unintentional
  - ▶ Unavoidable risk that some material misstatements may not be detected
  - ▶ Risk of not detecting a material misstatement resulting from fraud is higher than that from error, as fraud is concealed

Professional Scepticism



# Fraud Risk Discussions



## WHAT

Client discussions	Internal discussions
<ul style="list-style-type: none"><li>▶ Assessment of risk of material misstatements due to fraud</li><li>▶ Management's process to mitigate risks</li><li>▶ Knowledge of actual and suspected frauds</li><li>▶ Management's communication protocols</li></ul>	<ul style="list-style-type: none"><li>▶ Fraud risk factors</li><li>▶ Risks of material misstatement</li><li>▶ Results of client discussions</li><li>▶ Understanding of client's fraud management programs</li><li>▶ Prior year ELC testing</li><li>▶ Planned audit approach to address the risks identified</li></ul>

# Fraud Risk Discussions



## WHO

Client discussions	Internal discussions
Management from a variety of functions - not just finance - as well as internal audit	The entire team, led by the engagement partner

# Evaluation of the entity's controls in respect of fraud risks

What evidence do you have on file that the design and implementation of controls in respect of fraud risks have been evaluated?

- ▶ **Example: Whistleblowing – what are our audit procedures?**
  - ▶ Review the policy
  - ▶ Test the reporting lines
  - ▶ Assess the process for investigating whistleblowing reports
  - ▶ Review the log of reports and investigation outcomes
  - ▶ Review the information provided to the audit committee
  - ▶ Conclude on design and implementation of whistleblowing as an internal control



ISA 240 requires that journal entry testing is performed to respond to the risk of management override

- ▶ External regulatory reviews identified:
  - ▶ Journal entry testing was not always performed in response to fraud risks identified
  - ▶ Rationale for sample sizes was not always clear
  - ▶ Journals discussed with management without corroboration
- ▶ Data Analytics:
  - ▶ Use of automated tools to test journal entries was limited
  - ▶ Where automated tools identified large numbers of journals with the set risk criteria, the rationale for only testing a sample of these was not well documented





Questions?