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Introduction

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Definition – What is Fraud?

“An intentional act by one or more individuals among management, those charged with governance, employees or third parties, involving the use of deception to obtain an unjust or illegal advantage”

Fraud can be segregated into two segments.

a) Fraudulent Financial Reporting

[illegible]

b) Misappropriation of Assets



Important

Although fraud is a broad concept, for the purpose of audit, the auditor is concerned about frauds that cause material misstatements in the financial statements.

Responsibility for the Prevention and Detection of Fraud

a) Responsibility of the Management

CV Learning

b) Responsibility of the Auditor

Auditor who conducts in accordance with S.L.Au.S is responsible for obtaining a reasonable assurance that the Financial Statements are taken as a whole are free from material misstatements, whether due to Fraud or Error.

Due to the inherent limitations of an audit, there is an unavoidable risk that some material misstatements due to fraud, may not be detected and the potential effects are significantly high.

This is because a fraud may involve sophisticated and carefully organized scheme designed to conceal it. Further, the fraud may be perpetrated by individuals by collusions. Frauds committed by the management are harder to detect because management is in a position to manipulate accounting records or override controls. Therefore, the Auditor should perform following audit procedures to reduce the risk.

Therefore, the auditor should perform following procedures when conducting the audits to reduce the risk.

What are Fraud Risk Factors?

Conditions or events which increase the Risk of Fraud and Errors are referred as Fraud Risk Factors.

Fraud Risk Factor	Fraudulent Financial Reporting	Misappropriation of Assets
Opportunities	Weaknesses in the internal control systems	Weaknesses in the internal control systems
	High complex transactions	Large amount of cash on hand or processed daily
Employee Attitudes	Integrity of Management/Board of Directors	Integrity of Management/Board of Directors
Incentives and Pressures	Higher level of competition accompanied by declining margins	Personal financial obligations
	Increase in operating losses, which creates a threat of Bankruptcy.	Recent changes of employee benefits plans
	Negative cashflows	

