

OBJECTIVE: To “brainstorm” among team members as to how and where a material misstatement of the financial statements, resulting from fraudulent financial reporting or misappropriation of assets, might be committed and concealed. The results of this session are used in the consideration of audit risk at the overall financial statement level and the account balance, transaction class, or disclosure level.

CONSIDERATIONS: At various stages throughout the audit, including the planning phase, the overall review phase and any other time deemed necessary, a meeting of the audit team will be convened to discuss the possibility of material misstatement due to fraud and errors, with an emphasis on fraud.

Brainstorm the following:

- Specific ways in which the entity’s financial statements might be susceptible to material misstatement due to *fraudulent financial reporting*, including how it could happen and how it could be concealed.
- Specific ways in which the entity’s financial statements might be susceptible to material misstatement due to *misappropriation of assets*, including how it could happen and how it could be concealed.

For each fraud scheme, discuss:

- Likely perpetrators
- The likely perpetrators’ possible motives or pressures that might induce them to commit fraud
- The opportunities that might exist to enable the scheme to occur
- The likely perpetrators’ possible rationalizations

Helpful information to consider in the brainstorming session:

- Previous knowledge of the entity and its management
- Prior year financial statements, adjustments and working papers
- Prior year auditor reports and management letter
- Interim financial statements
- Preliminary analytical review results
- Press releases or media coverage
- Client acceptance or continuation information

At the conclusion of the brainstorming session, the team will recap the fraud schemes deemed possible and formulate conclusions regarding the schemes that might be occurring. For each viable scheme, document the risk identified and how that the audit team will respond to that risk in the audit documentation including (a) the Consideration of Audit Risk at the Overall Financial Statement Level and (b) the Consideration of Audit Risk at the Account Balance, Transaction Class Level.

This session requires **creative thinking** and an emphasis on **professional skepticism**. *Professional skepticism is an attitude that includes a questioning mind and a critical assessment of audit evidence. Each auditor should conduct the engagement with a questioning mind that recognizes the possibility that a material misstatement due to fraud could be present, regardless of any past experience with the entity and regardless of the auditor's belief about management's honesty and integrity. The need to maintain this questioning-mind attitude throughout the engagement should lead audit team members continually to be alert for information or other conditions that indicate that a material misstatement due to fraud may have occurred. Emphasize that in exercising professional skepticism in gathering and evaluating evidence, audit team members should not be satisfied with less than persuasive evidence because of a belief that management is honest.*

BRAINSTORMING SESSION:

Date of the Brainstorming Session	
Phase of the Audit Engagement	
Participating Audit Team Members	
Potential Material Fraud Schemes	General Audit Response to Potential Scheme