

AGENDA ITEM 14-C (UPDATED)¹
INTERNATIONAL STANDARD ON AUDITING 705
(REVISED AND REDRAFTED)
MODIFICATIONS TO THE OPINION IN THE
INDEPENDENT AUDITOR’S REPORT

(Effective for audits of financial statements for periods beginning on or after December 15, 2009)

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¹ [Agenda Item 14-C was updated during the June 16-20, 2008 IAASB meeting to reflect in marked text changes based on decisions taken at the meeting. The updated agenda item is included here for information purposes only and is not the final pronouncement. Interested parties are discouraged from distributing, translating or using the updated agenda item for any purpose. They should await the release of the final pronouncement, which may contain minor modifications when compared to the updated agenda item. The final pronouncement is that approved by the IAASB and published by IFAC after the Public Interest Oversight Board (PIOB) has confirmed that due process was followed in its development. It will be available at <http://www.ifac.org/IAASB/Resources.php>.

References in this ISA to other ISAs that have not yet been finalized reflect the working titles of those ISAs. The references are indicated in brackets and will be updated when those ISAs are finalized.]

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Appendix: Illustrations of Auditors’ Reports with Modifications to the Opinion

International Standard on Auditing (ISA) 705 (Revised and Redrafted), “Modifications to the Opinion in the Independent Auditor’s Report,” should be read in conjunction with ISA 200 (Revised and Redrafted), “Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with International Standards on Auditing.”

Introduction

Scope of this ISA

1. This International Standard on Auditing (ISA) deals with the auditor's responsibility ~~of the auditor~~ to issue an appropriate report in circumstances when, in forming an opinion in accordance with ISA 700 (Redrafted),¹ the auditor concludes that a modification to the auditor's opinion on the financial statements is necessary.
2. ~~Although directed towards modifications to an auditor's opinion on a complete set of general purpose financial statements this ISA, adapted as necessary in the circumstances, also applies to modifications to the auditor's opinion on a single financial statement, an element of a financial statement or special purpose financial statements.~~
3. ~~This ISA does not apply to engagements covered by ISA 810 (Revised and Redrafted),² which deals with circumstances when the auditor modifies the opinion on summary financial statements derived from financial statements audited by the same auditor.~~

Types of Modified Opinions

24. This ISA establishes three types of modified opinions, namely, a qualified opinion, an adverse opinion, and a disclaimer of opinion. The decision regarding which type of modified opinion is appropriate depends upon: (Ref: Para. A1)
 - (a) The nature of the matter giving rise to the modification, that is, whether the financial statements are materially misstated or, in the case of an inability to obtain sufficient appropriate audit evidence, may be materially misstated; and
 - (b) The auditor's judgment about the pervasiveness of the effects or possible effects of the matter on the financial statements. (~~Ref: Para. A1~~)

Effective Date

35. This ISA is effective for audits of financial statements for periods beginning on or after December 15, 2009.

Objective

46. The objective of the auditor is to express clearly an appropriately modified opinion on the financial statements that is necessary when:
 - (a) The auditor concludes, based on the audit evidence obtained, that the financial statements as a whole are not free from material misstatement; or
 - (b) The auditor is unable to obtain sufficient appropriate audit evidence to conclude that the financial statements as a whole are free from material misstatement.

Definitions

57. For purposes of the ISAs, the following terms have the meanings attributed below:

¹ [ISA 700 (Redrafted), "Forming an Opinion and Reporting on Financial Statements."]

² ~~ISA 810 (Revised and Redrafted), "Engagements to Report on Summary Financial Statements."~~

- (a) Pervasive – ~~A~~ term used, in the context of misstatements, to describe the effects on the financial statements of ~~detected~~ misstatements or the possible effects on the financial statements of undetected misstatements, if any, that are undetected due to an inability to obtain sufficient appropriate audit evidence. Pervasive effects ~~or possible effects~~ on the financial statements are those that, in the auditor’s judgment:
- (i) ~~are~~ Are not confined to specific elements, accounts or items of the financial statements; ~~or;~~
 - (ii) ~~if~~ If so confined, represent or could represent a substantial proportion of the financial statements; or
 - ~~(ii)~~(iii) In relation to disclosures, are fundamental to users’ understanding of the financial statements.
- (b) Modified opinion – A qualified opinion, an adverse opinion or a disclaimer of opinion.

Requirements

Circumstances ~~w~~When a Modification to the Auditor’s Opinion Is Required

- ~~68~~ 78. The auditor shall modify the opinion in the auditor’s report when:
- (a) The auditor concludes that, based on the audit evidence obtained, the financial statements as a whole are not free from material misstatement; or (Ref: Para. A2-A7)
 - (b) The auditor is unable to obtain sufficient appropriate audit evidence to conclude that the financial statements as a whole are free from material misstatement. (Ref: Para. A8-A12)

Determining the Type of Modification to the Auditor’s Opinion

Qualified Opinion

- ~~79~~ 79. The auditor shall express a qualified opinion when:
- (a) The auditor, having obtained sufficient appropriate audit evidence, concludes that misstatements, individually or in the aggregate, are material, but not pervasive, to the financial statements; or
 - (b) ~~When~~ ~~the~~ The auditor is unable to obtain sufficient appropriate audit evidence on which to base the opinion, but the auditor concludes that the possible effects on the financial statements of undetected misstatements, if any, are could be material but not pervasive.

Adverse Opinion

- ~~84~~ 84. The auditor shall express an adverse opinion when the auditor, having obtained sufficient appropriate audit evidence, concludes that misstatements, individually or in the aggregate, are both material and pervasive to the financial statements.

Disclaimer of Opinion

~~9~~11. The auditor shall disclaim an opinion ~~on the financial statements as a whole~~ when the auditor is unable to obtain sufficient appropriate audit evidence on which to base the opinion, and the auditor concludes that the possible effects on the financial statements of undetected misstatements, if any, are could be both material and pervasive.

~~10~~12. The auditor shall disclaim an opinion ~~on the financial statements as a whole~~ when, in extremely rare circumstances involving multiple uncertainties, the auditor concludes that, notwithstanding having obtained sufficient appropriate audit evidence regarding each of the individual uncertainties, it is not possible to form an opinion on the financial statements ~~as a whole~~ due to the potential interaction of the uncertainties and their possible cumulative effect on the financial statements.

Consequence of an Inability to Obtain Sufficient Appropriate Audit Evidence ~~Due to a Management-Imposed Limitation after the Auditor Has Accepted the Engagement~~

~~11~~13. If, after accepting the engagement, the auditor becomes aware that management has imposed a limitation on the scope of the audit that the auditor considers likely to result in the need to express a qualified opinion or to disclaim an opinion on the financial statements, the auditor shall request that management remove the limitation.

~~12~~14. If management refuses ~~the auditor's request to remove~~ thea limitation referred to in paragraph 11 ~~that management has imposed on the scope of the audit,~~ the auditor shall communicate the matter to those charged with governance and determine whether it is possible to perform alternative procedures to obtain sufficient appropriate audit evidence ~~on which to base an unmodified opinion.~~

~~13~~15. If the auditor is unable to obtain sufficient appropriate audit evidence ~~on which to base the opinion,~~ the auditor shall determine the implications as follows:

- (a) If the auditor concludes that the possible effects on the financial statements of undetected misstatements, if any, could beare material but not pervasive, the auditor shall qualify the opinion; or
- (b) If the auditor concludes that the possible effects on the financial statements of undetected misstatements, if any, could beare both material and pervasive so that a qualification of the opinion would be inadequate to communicate the gravity of the situation, the auditor shall either: (Ref: Para. A13-A14)
 - (i) ~~The auditor shall r~~Resign from the audit, where practicable and not prohibited by law or regulation; or (Ref: Para. A13)
 - (ii) If resignation from the audit before issuing the auditor's report is not practicable or possible, ~~the auditor shall disclaim an opinion on the financial statements as a whole.~~ (Ref: Para. A14)

~~14~~16. If the auditor ~~resigns~~concludes ~~that resignation from the audit is necessary because of a limitation on the scope of the audit imposed by management,~~ as contemplated by paragraph ~~13~~15(b)(i), before resigning, the auditor shall communicate to those charged

with governance any matters regarding misstatements identified during the audit of which the auditor has become aware that would have given rise to a modification of the opinion regarding misstatements identified during the audit. (Ref: Para. A15)

Other Considerations ~~R~~elating to an Adverse Opinion or Disclaimer of Opinion

~~15~~17. When the auditor considers it necessary to express an adverse opinion or disclaim an opinion on the financial statements as a whole, the auditor's report shall not also include an unmodified opinion with respect to the same financial reporting framework on a single financial statement or one or more specific elements, accounts or items of a the financial statements. To include such an unmodified opinion in the same report³ in these circumstances would contradict the auditor's adverse opinion or disclaimer of opinion on the financial statements as a whole. (Ref: Para. A16-A17)

Form and Content of the Auditor's Report ~~w~~hen the Opinion Is Modified

Basis for Modification Paragraph

~~16~~18. When the auditor modifies the opinion on the financial statements, the auditor shall, in addition to the specific elements required by ISA 700 (Redrafted), include a paragraph in the auditor's report that provides a description of the matter giving rise to the modification. The auditor shall place this paragraph immediately before the opinion paragraph in the auditor's report and use the heading "Basis for Qualified Opinion," "Basis for Adverse Opinion," or "Basis for Disclaimer of Opinion," as appropriate. (Ref: Para. A17~~+~~8)

~~17~~19. If there is a material misstatement of the financial statements that relates to specific amounts in the financial statements (including quantitative disclosures), the auditor shall include in the basis for modification paragraph a description and quantification of the financial effects of the misstatement, unless impracticable. If it is not practicable to quantify the financial effects, the auditor shall so state in the basis for modification paragraph. (Ref: Para. A18~~+~~9)

~~18~~20. If there is a material misstatement of the financial statements that relates to narrative disclosures, the auditor shall include in the basis for modification paragraph an explanation of how the disclosures are misstated.

~~19~~21. If there is a material misstatement of the financial statements that relates to the non-disclosure of information required to be disclosed, the auditor shall:

- (a) Discuss the non-disclosure with those charged with governance;
- (b) Describe in the basis for modification paragraph the nature of the omitted information; and,

³ [Proposed] ISA 805 (Revised and Redrafted), "Special Considerations—Audits of Single Financial Statements and Specific Elements, Accounts or Items of a Financial Statement" deals with circumstances where the auditor is engaged to express a separate opinion on one or more specific elements, accounts or items of a financial statement.

- (c) Unless prohibited by law or regulation, include the omitted disclosures, provided it is practicable to do so and the auditor has obtained sufficient appropriate audit evidence about the omitted information. (Ref: Para. A1920)

~~20~~22. If the modification results from an inability to obtain sufficient appropriate audit evidence, the auditor shall include in the basis for modification paragraph the reasons for that inability.

~~21~~23. Even if the auditor has expressed an adverse opinion or disclaimed an opinion on the financial statements ~~as a whole~~, the auditor shall describe in the basis for modification paragraph the reasons for any other matters of which the auditor is aware that would have required a modification to the opinion, and the effects thereof. (Ref: Para. A2024)

Opinion Paragraph

~~22~~24. When the auditor modifies the audit opinion, the auditor shall use the heading “Qualified Opinion,” “Adverse Opinion,” or “Disclaimer of Opinion,” as appropriate, for the opinion paragraph. (Ref: Para. A2122, A23-A24-A25)

~~23~~25. When the auditor expresses a qualified opinion due to a material misstatement in the financial statements, the auditor shall state in the opinion paragraph that, in the auditor’s opinion, except for the effects of the matter(s) described in the Basis for Qualified Opinion paragraph:

- (a) ~~;~~ The financial statements present fairly, in all material respects (or “give a true and fair view”) in accordance with the applicable financial reporting framework when reporting in accordance with a fair presentation framework; or
- (b) The financial statements have been prepared, in all material respects, in accordance with the applicable financial framework when reporting in accordance with a compliance framework.

When the modification arises from an inability to obtain sufficient appropriate audit evidence, the auditor shall use the corresponding phrase “except for the possible effects of the matter(s) ...” for the modified opinion. (Ref: Para. A2223)

~~24~~26. When the auditor expresses an adverse opinion, the auditor shall state in the opinion paragraph that, in the auditor’s opinion, because of the significance of the matter(s) described in the Basis for Adverse Opinion paragraph:

- (a) ~~;~~ The financial statements do not present fairly (or “give a true and fair view”) in accordance with the applicable financial reporting framework when reporting in accordance with a fair presentation framework; or
- (b) The financial statements have not been prepared, in all material respects, in accordance with the applicable financial reporting framework when reporting in accordance with a compliance framework.

~~25~~27. When the auditor disclaims an opinion due to an inability to obtain sufficient appropriate audit evidence, the auditor shall state in the opinion paragraph that:

- (a) because of the significance of the matter(s) described in the Basis for Disclaimer of Opinion paragraph, the auditor has not been able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion; and, accordingly,
- (b) the auditor does not express an opinion on the financial statements.

Description of Auditor's Responsibility ~~¶~~When the Auditor Expresses a Qualified or Adverse Opinion

~~26~~28. When the auditor expresses a qualified or adverse opinion, the auditor shall amend the description of the auditor's responsibility to state that the auditor believes that the audit evidence the auditor has obtained is sufficient and appropriate to provide a basis for the auditor's modified audit opinion.

Description of Auditor's Responsibility ~~¶~~When the Auditor Disclaims an Opinion

~~27~~29. When the auditor disclaims an opinion due to an inability to obtain sufficient appropriate audit evidence, the auditor shall amend the introductory paragraph of the auditor's report to state that the auditor was engaged to audit the financial statements. The auditor shall also amend the description of the auditor's responsibility and the description of the scope of the audit to state only the following: "Our responsibility is to express an opinion on the financial statements based on conducting the audit in accordance with International Standards on Auditing. Because of the matter(s) described in the Basis for Disclaimer of Opinion paragraph, however, we were not able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion."

Communication with Those Charged with Governance

~~28~~30. When the auditor expects to modify the opinion in the auditor's report, the auditor shall communicate with those charged with governance the circumstances that led to the expected modification and the proposed wording of the modification. (Ref: Para. ~~A25~~26)

Application and Other Explanatory Material

Scope of this ISA

Types of Modified Opinions (Ref: Para. 24)

- A1. The table below illustrates how the auditor's judgment about the nature of the matter giving rise to the modification, and the pervasiveness of its effects or possible effects on the financial statements, affects the type of opinion to be expressed.

<i>Nature of Matter Giving Rise to the Modification</i>	<i>Auditor's Judgment about the Pervasiveness of the Effects or Possible Effects on the Financial Statements</i>	
	<i>Material but nNot Pervasive</i>	<i>Material and Pervasive</i>
Financial statements are materially misstated	Qualified opinion	Adverse opinion
Inability to obtain sufficient appropriate audit evidence	Qualified opinion	Disclaimer of opinion

Nature of Material Misstatements (Ref: Para. 68(a))

- A2. ISA 700 (Redrafted) ~~requires the auditor~~ ~~deals with the auditor's responsibility~~, in order to forming an opinion on the financial statements, to conclude as to whether reasonable assurance has been obtained about whether the financial statements as a whole are free from material misstatement.⁴ This conclusion takes into account the auditor's evaluation of uncorrected misstatements, if any, on the financial statements in accordance with ISA 450 (Revised and Redrafted).⁵
- A3. ISA 450 (Revised and Redrafted) defines a misstatement as a difference between the amount, classification, presentation, or disclosure of a reported financial statement item and the amount, classification, presentation, or disclosure that is required for the item to be in accordance with the applicable financial reporting framework. Accordingly, a material misstatement of the financial statements may arise in relation to:
- The appropriateness of the selected accounting policies;
 - The application of the selected accounting policies; or
 - The appropriateness or adequacy of disclosures in the financial statements.

Appropriateness of the Selected Accounting Policies

- A4. In relation to the appropriateness of the accounting policies management has selected, material misstatements of the financial statements may arise when:
- The selected accounting policies are not consistent with the applicable financial reporting framework; or
 - ~~¶~~The financial statements, including the related ~~explanatory~~ notes, do not ~~faithfully~~ represent the underlying transactions and events in a manner that achieves fair presentation.

⁴ [ISA 700 (Redrafted), paragraph [to be inserted].]

⁵ ISA 450 (Revised and Redrafted), "Evaluation of Misstatements Identified during the Audit," paragraph 4(a).

- A5. Financial reporting frameworks often contain requirements for the accounting for, and disclosure of, changes in accounting policies. Where the entity has changed its selection of significant accounting policies, a material misstatement of the financial statements may arise when the entity has not complied with these requirements.

Application of the Selected Accounting Policies

- A6. In relation to the application of the selected accounting policies, material misstatements of the financial statements may arise:
- (a) When management has not applied the selected accounting policies consistently with the financial reporting framework, including when management has not applied the selected accounting policies consistently between periods or to similar transactions and events (consistency in application); or
 - (b) Due to the method of application of the selected accounting policies (such as an unintentional error in application).

Appropriateness or Adequacy of Disclosures in the Financial Statements

- A7. In relation to the appropriateness or adequacy of disclosures in the financial statements, material misstatements of the financial statements may arise when:
- (a) The financial statements do not include all of the disclosures required by the applicable financial reporting framework;
 - (b) The disclosures in the financial statements are not presented in accordance with the applicable financial reporting framework; or
 - (c) The financial statements do not provide the disclosures necessary to achieve fair presentation.

Nature of an Inability to Obtain Sufficient Appropriate Audit Evidence (Ref: Para. ~~68~~(b))

- A8. The auditor's inability to obtain sufficient appropriate audit evidence (also referred to as a limitation on the scope of the audit) may arise from:
- (a) Circumstances beyond the control of the entity;
 - (b) Circumstances relating to the nature or timing of the auditor's work; or
 - (c) Limitations imposed by management.
- A9. An inability to perform a specific procedure does not constitute a limitation on the scope of the audit if the auditor is able to obtain sufficient appropriate audit evidence by performing alternative procedures. If this is not possible, the requirements of paragraphs ~~79~~(b) and ~~104~~ apply as appropriate. Limitations imposed by management may have other implications for the audit, such as for the auditor's assessment of fraud risks and consideration of engagement continuance.
- A10. Examples of circumstances beyond the control of the entity include when:
- The entity's accounting records have been destroyed.

- The accounting records of a significant component have been seized indefinitely by governmental authorities.

A11. Examples of circumstances relating to the nature or timing of the auditor's work include when:

- The entity is required to use the equity method of accounting for an associated entity, and the auditor is unable to obtain sufficient appropriate audit evidence about the latter's financial information to evaluate whether the equity method has been appropriately applied.
- The timing of the auditor's appointment is such that the auditor is unable to observe the counting of the physical inventories.
- The auditor determines that performing substantive procedures alone is not sufficient, but the entity's controls are not effective.

A12. Examples of an inability to obtain sufficient appropriate audit evidence arising from a limitation on the scope of the audit imposed by management include when:

- Management prevents the auditor from observing the counting of the physical inventory.
- Management prevents the auditor from requesting external confirmation of specific account balances.

Consequence of an Inability to Obtain Sufficient Appropriate Audit Evidence ~~due~~ Due to a Management-imposed Limitation after the Auditor Has Accepted the Engagement (Ref. Para. ~~13(b)-14+5-16~~)

A13. ~~The practicality of resigning from the audit~~~~timing of the auditor's resignation~~ may depend on the stage of completion of the engagement at the time that management imposes the scope limitation. If the auditor has substantially completed the audit, the auditor may decide to complete the audit to the extent possible, disclaim an opinion and explain the scope limitation in the Basis for Disclaimer of Opinion paragraph prior to resigning.

A14. In certain circumstances, resignation from the audit may not be possible if the auditor is required by law or regulation to continue the audit engagement. This may be the case for an auditor that is appointed to audit the financial statements of public sector entities. It may also be the case in jurisdictions where the auditor is appointed to audit the financial statements covering a specific period, or appointed for a specific period and is prohibited from resigning before the completion of the audit of those financial statements or before the end of that period, respectively. The auditor may also consider it necessary to include an Other Matter paragraph in the auditor's report.⁶

A15. When the auditor concludes that resignation from the audit is necessary because of a scope limitation, there may be a professional, regulatory or legal requirement for the

⁶ ISA 706 (Revised and Redrafted), paragraph A5.

auditor to communicate matters relating to the resignation from the engagement to regulators or the entity's owners.

Other Considerations relating to an Adverse Opinion or Disclaimer of Opinion (Ref: Para. 15+7)

~~A16. Inclusion of an unmodified opinion on a single financial statement or one or more specific elements and an adverse opinion or a disclaimer of opinion on the financial statements as a whole, in the same report and with respect to the same financial reporting framework, is contradictory. It is accordingly not permitted.~~

A167. The following are examples of reporting circumstances that would not contradict the auditor's adverse opinion or disclaimer of opinion~~This does not include, for example:~~

- ~~The expression of an unmodified opinion on financial statements prepared under a given financial reporting framework and, within the same report, the expression of an adverse opinion or the issue of a disclaimer of opinion on the same financial statements under a different financial reporting framework.⁷ For example, the auditor may express an adverse opinion on financial statements prepared in accordance with a financial reporting framework designed to achieve fair presentation, and within the same report, express an unmodified opinion with respect to the proper preparation of the financial statements in accordance with specific legal requirements not designed to achieve fair presentation.~~
- ~~Unless prohibited by law or regulation, t~~The expression of an disclaimer of opinion which is qualified or disclaimed, as appropriate, regarding the results of operations, and cash flows, where relevant, and an unmodified opinion regarding the financial position (see ISA 510 (Redrafted).⁸). In this case, the auditor has not expressed a disclaimer of opinion on the financial statements as a whole.

~~The expression of an unmodified opinion on specific elements, accounts or items of the financial statements in a separate report as described in ISA 800 (Revised and Redrafted).⁹~~

Form and Content of the Auditor's Report when the Opinion Is Modified

Basis for Modification Paragraph (Ref: Para. 16-17, 19(b), 21+8-23)

~~A178.~~Consistency in the auditor's report helps to promote the users' understanding and to identify unusual circumstances when they occur. Accordingly, although uniformity in the wording of a modified opinion and in the description of the basis for the modification may not be possible, consistency in both the form and content of the auditor's report is desirable.

⁷ [See paragraph [to be inserted] of ISA 700 (Redrafted) for a description of this circumstance.]

⁸ ISA 510 (Redrafted), "Initial Audit Engagements—Opening Balances," paragraph 10.

⁹ ~~ISA 800 (Revised and Redrafted), "Special Considerations—Audits of Single Financial Statements and Specific Elements, Accounts or Items of a Financial Statement."~~

~~A189.~~ An example of the ~~quantification~~ of the financial effects of material misstatements that the auditor may ~~describe~~~~include~~ in the basis for modification paragraph in the auditor's report is the quantification of the effects on income tax, income before taxes, net income and equity if inventory is overstated.

~~A1920.~~ Disclosing the omitted information in the basis for modification paragraph would not be practicable if:

- (a) The disclosures have not been prepared by management ~~and~~~~or~~ the disclosures are otherwise not readily available to the auditor; or
- (b) In the auditor's judgment, the disclosures would be unduly voluminous in relation to the auditor's report.

~~A2024.~~ An adverse opinion or a disclaimer of opinion ~~to address the effects of a misstatement or possible effects of an undetected misstatement~~ relating to a specific matter ~~to be~~ described in the basis for qualification paragraph does not justify the omission of a description of other identified matters that would have otherwise required ~~warrant~~ a modification of the auditor's opinion. In such cases, the disclosure of such other matters of which the auditor is aware may be relevant to users of the financial statements, for example misstatements regarding the recognition, measurement or disclosure of certain assets and liabilities (for example, the existence of inventory).

Opinion Paragraph (Ref: Para. ~~22-2324-25~~)

~~A2122.~~ Inclusion of this paragraph heading makes it clear to the user that the auditor's opinion is modified and indicates the type of modification.

~~A2223.~~ When the auditor expresses a qualified opinion, it would not be appropriate to use phrases such as "with the foregoing explanation" or "subject to" in the opinion paragraph as these are not sufficiently clear or forceful.

Illustrative Auditors' Reports

~~A2324.~~ Illustrations 1 and 2 in the Appendix contain auditors' reports with qualified and adverse opinions, respectively, as the financial statements are materially misstated.

~~A2425.~~ Illustration 3 in the Appendix contains an auditor's report with a qualified opinion as the auditor is unable to obtain sufficient appropriate audit evidence. Illustration 4 contains a disclaimer of opinion due to an inability to obtain sufficient appropriate audit evidence about a single element of the financial statements. Illustration 5 contains a disclaimer of opinion due to an inability to obtain sufficient appropriate audit evidence about multiple elements of the financial statements. In each of the latter two cases, the possible effects on the financial statements of the inability are both material and pervasive.

Communication with Those Charged with Governance (Ref: Para. ~~2830~~)

~~A2526.~~ Communicating with those charged with governance the circumstances that lead to an expected modification to the auditor's opinion and the proposed wording of the modification enables:

- (a) The auditor to give notice to those charged with governance of the intended modification(s) and the reasons (or circumstances) for the modification(s);
- (b) The auditor to seek the concurrence of those charged with governance regarding the facts of the matter(s) giving rise to the expected modification(s), or to confirm matters of disagreement with management as such; and
- (c) Those charged with governance to have an opportunity, where appropriate, to provide the auditor with further information and explanations in respect of the matter(s) giving rise to the expected modification(s).

Appendix

(Ref: Para. A23-24-25)

Illustrations of Auditors' Reports with Modifications to the Opinion

- Illustration 1: An auditor's report containing a qualified opinion due to a material misstatement of the financial statements.
- Illustration 2: An auditor's report containing an adverse opinion due to a material misstatement of the financial statements.
- Illustration 3: An auditor's report containing a qualified opinion due to the auditor's inability to obtain sufficient appropriate audit evidence.
- Illustration 4: An auditor's report containing a disclaimer of opinion due to the auditor's inability to obtain sufficient appropriate audit evidence about a single element of the financial statements.
- Illustration 5: An auditor's report containing a disclaimer of opinion due to the auditor's inability to obtain sufficient appropriate audit evidence about multiple elements of the financial statements.

Illustration 1:

Circumstances include the following:

- **Audit of a complete set of general purpose financial statements prepared by management of the entity in accordance with International Financial Reporting Standards is the applicable financial reporting framework.**
- **The terms of the audit engagement reflect the description of management’s responsibility for the financial statements in [proposed] ISA 210 (Redrafted).¹⁰**
- **Inventories are misstated. The misstatement is deemed to be material but not pervasive to the financial statements.**
- **In addition to the audit of the financial statements, the auditor has other reporting responsibilities required under local law.**

INDEPENDENT AUDITOR’S REPORT

[Appropriate Addressee]

Report on the Financial Statements¹¹

We have audited the accompanying financial statements of ABC Company, which comprise the balance sheet as at December 31, 20X1, and the income statement, statement of changes in equity and cash flow statement for the year then ended, and a summary of significant accounting policies and other explanatory information.

Management’s¹² Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation¹³ of these financial statements in accordance with International Financial Reporting Standards; this includes the design, implementation and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor’s Responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with International Standards on Auditing. Those standards

¹⁰ [Proposed] ISA 210, “Agreeing the Terms of Audit Engagements.”

¹¹ The sub-title “Report on the Financial Statements” is unnecessary in circumstances when the second sub-title “Report on Other Legal and Regulatory Requirements” is not applicable.

¹² Or other term that is appropriate in the context of the legal framework in the particular jurisdiction.

¹³ Depending on the circumstances, this sentence may read: “Management is responsible for the preparation and presentation of financial statements that give a true and fair view in accordance with International Financial Reporting Standards.”

require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation¹⁴ of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control.¹⁵ An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our qualified audit opinion.

Basis for Qualified Opinion

The company's inventories are carried in the balance sheet at xxx. Management has not stated the inventories at the lower of cost and net realizable value but has stated them solely at cost, which constitutes a departure from International Financial Reporting Standards. The company's records indicate that had management stated the inventories at the lower of cost and net realizable value, an amount of xxx would have been required to write the inventories down to their net realizable value. Accordingly, cost of sales would have been increased by xxx, and income tax, net income and shareholders' equity would have been reduced by xxx, xxx and xxx, respectively.

Qualified Opinion

In our opinion, except for the effects of the matter described in the Basis for Qualified Opinion paragraph, the financial statements present fairly, in all material respects, (or "give a true and fair view of") the financial position of ABC Company as at December 31, 20X1, and of its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards.

¹⁴ Depending on the circumstances, this sentence may read: "In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and presentation of financial statements that give a true and fair view in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control."

¹⁵ In circumstances when the auditor also has responsibility to express an opinion on the effectiveness of internal control in conjunction with the audit of the financial statements, this sentence would be worded as follows: "In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances." In the case of footnote 13, this sentence may read: "In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and presentation of financial statements that give a true and fair view in order to design audit procedures that are appropriate in the circumstances."

Report on Other Legal and Regulatory Requirements

[Form and content of this section of the auditor's report will vary depending on the nature of the auditor's other reporting responsibilities.]

[Auditor's signature]

[Date of the auditor's report]

[Auditor's address]

Illustration 2:

Circumstances include the following:

- **Audit of consolidated general purpose financial statements prepared by management of the parent in accordance with International Financial Reporting Standards is the applicable financial reporting framework.**
- **The terms of the audit engagement reflect the description of management’s responsibility for the financial statements in [proposed] ISA 210 (Redrafted).**
- **The financial statements are materially misstated due to the non-consolidation of a subsidiary. The material misstatement is deemed to be pervasive to the financial statements. The effects of the misstatement on the financial statements have not been determined because it was not practicable to do so.**
- **In addition to the audit of the consolidatedthe financial statements, the auditor has other reporting responsibilities required under local law.**

INDEPENDENT AUDITOR’S REPORT

[Appropriate Addressee]

Report on the Consolidated Financial Statements¹⁶

We have audited the accompanying consolidated financial statements of ABC Company and its subsidiaries, which comprise the consolidated balance sheet as at December 31, 20X1, and the consolidated income statement, statement of changes in equity and cash flow statement for the year then ended, and a summary of significant accounting policies and other explanatory information.

Management’s¹⁷ Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation¹⁸ of these consolidated financial statements in accordance with International Financial Reporting Standards; this includes the design, implementation and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

¹⁶ The sub-title “Report on the Consolidated Financial Statements” is unnecessary in circumstances when the second sub-title “Report on Other Legal and Regulatory Requirements” is not applicable.

¹⁷ Or other term that is appropriate in the context of the legal framework in the particular jurisdiction.

¹⁸ Depending on the circumstances, this sentence may read: “Management is responsible for the preparation and presentation of consolidated financial statements that give a true and fair view in accordance with International Financial Reporting Standards.”

Auditor's Responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audit. We conducted our audit in accordance with International Standards on Auditing. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation¹⁹ of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control.²⁰ An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our adverse audit opinion.

Basis for Adverse Opinion

As explained in Note X, the company has not consolidated the financial statements of subsidiary XYZ Company it acquired during 20X1 because it has not yet been able to ascertain the fair values of certain of the subsidiary's material assets and liabilities at the acquisition date. This investment is therefore accounted for on a cost basis. Under International Financial Reporting Standards, the subsidiary should have been consolidated because it is controlled by the company. Had XYZ been consolidated, many elements in the accompanying financial statements would have been materially affected. ~~In the absence of further information about the accounting for the acquisition, however, it is not possible to quantify those effects.~~ The effects on the financial statements of the failure to consolidate have not been determined.

¹⁹ Depending on the circumstances, this sentence may read: "In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and presentation of consolidated financial statements that give a true and fair view in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control."

²⁰ In circumstances when the auditor also has responsibility to express an opinion on the effectiveness of internal control in conjunction with the audit of the consolidated financial statements, this sentence would be worded as follows: "In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances." In the case of footnote 18, this sentence may read: "In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and presentation of financial statements that give a true and fair view in order to design audit procedures that are appropriate in the circumstances."

Adverse Opinion

In our opinion, because of the significance of the matter discussed in the Basis for Adverse Opinion paragraph, the consolidated financial statements do not present fairly (or “do not give a true and fair view of”) the financial position of ABC Company and its subsidiaries as at December 31, 20X1, and of ~~its~~their financial performance and ~~its~~ cash flows for the year then ended in accordance with International Financial Reporting Standards.

Report on Other Legal and Regulatory Requirements

[Form and content of this section of the auditor’s report will vary depending on the nature of the auditor’s other reporting responsibilities.]

[Auditor’s signature]

[Date of the auditor’s report]

[Auditor’s address]

Illustration 3:

Circumstances include the following:

- **Audit of a complete set of general purpose financial statements prepared by management of the entity in accordance with International Financial Reporting Standards is the applicable financial reporting framework.**
- **The terms of the audit engagement reflect the description of management’s responsibility for the financial statements in [proposed] ISA 210 (Redrafted).**
- **The auditor was unable to obtain sufficient appropriate audit evidence regarding an investment in a foreign affiliate. The possible effects of the inability to obtain sufficient appropriate audit evidence are deemed to be material but not pervasive to the financial statements.**
- **In addition to the audit of the financial statements, the auditor has other reporting responsibilities required under local law.**

INDEPENDENT AUDITOR’S REPORT

[Appropriate Addressee]

Report on the Financial Statements²¹

We have audited the accompanying financial statements of ABC Company, which comprise the balance sheet as at December 31, 20X1, and the income statement, statement of changes in equity and cash flow statement for the year then ended, and a summary of significant accounting policies and other explanatory notes.

Management’s²² Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation²³ of these financial statements in accordance with International Financial Reporting Standards; this includes the design, implementation and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

²¹ The sub-title “Report on the Financial Statements” is unnecessary in circumstances when the second sub-title “Report on Other Legal and Regulatory Requirements” is not applicable.

²² Or other term that is appropriate in the context of the legal framework in the particular jurisdiction.

²³ Depending on the circumstances, this sentence may read: “Management is responsible for the preparation and presentation of financial statements that give a true and fair view in accordance with International Financial Reporting Standards.”

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with International Standards on Auditing. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation²⁴ of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control.²⁵ An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our qualified audit opinion.

Basis for Qualified Opinion

ABC Company's investment in XYZ Company, a foreign associate acquired during the year and accounted for by the equity method, is carried at xxx on the balance sheet as at December 31, 20X1, and ABC's share of XYZ's net income of xxx is included in ABC's income for the year then ended. We were unable to obtain sufficient appropriate audit evidence about the carrying amount of ABC's investment in XYZ as at December 31, 20X1 and ABC's share of XYZ's net income for the year because we were denied access to the financial information, management, and the auditors of XYZ. Consequently, we were unable to determine whether any adjustments to these amounts were necessary.

Qualified Opinion

In our opinion, except for the possible effects of the matter described in the Basis for Qualified Opinion paragraph, the financial statements present fairly, in all material respects, (or "give a

²⁴ Depending on the circumstances, this sentence may read: "In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and presentation of financial statements that give a true and fair view in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control."

²⁵ In circumstances when the auditor also has responsibility to express an opinion on the effectiveness of internal control in conjunction with the audit of the financial statements, this sentence would be worded as follows: "In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances." In the case of footnote 23, this sentence may read: "In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and presentation of financial statements that give a true and fair view in order to design audit procedures that are appropriate in the circumstances."

true and fair view of”) the financial position of ABC Company as at December 31, 20X1, and of its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards.

Report on Other Legal and Regulatory Requirements

[Form and content of this section of the auditor’s report will vary depending on the nature of the auditor’s other reporting responsibilities.]

[Auditor’s signature]

[Date of the auditor’s report]

[Auditor’s address]

Illustration 4:

Circumstances include the following:

- **Audit of a complete set of general purpose financial statements prepared by management of the entity in accordance with International Financial Reporting Standards is the applicable financial reporting framework.**
- **The terms of the audit engagement reflect the description of management’s responsibility for the financial statements in [proposed] ISA 210 (Redrafted).**
- **The auditor was unable to obtain sufficient appropriate audit evidence about a single element of the financial statements. That is, the auditor was also unable to obtain audit evidence about the financial information of a joint venture investment that represents over 90% of the company’s net assets. The possible effects of this inability to obtain sufficient appropriate audit evidence are deemed to be both material and pervasive to the financial statements.**
- **In addition to the audit of the financial statements, the auditor has other reporting responsibilities required under local law.**

INDEPENDENT AUDITOR’S REPORT

[Appropriate Addressee]

Report on the Financial Statements²⁶

We were engaged to audit the accompanying financial statements of ABC Company, which comprise the balance sheet as at December 31, 20X1, and the income statement, statement of changes in equity and cash flow statement for the year then ended, and a summary of significant accounting policies and other explanatory notes.

Management’s²⁷ Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation²⁸ of these financial statements in accordance with International Financial Reporting Standards; this includes the design, implementation and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

²⁶ The sub-title “Report on the Financial Statements” is unnecessary in circumstances when the second sub-title “Report on Other Legal and Regulatory Requirements” is not applicable.

²⁷ Or other term that is appropriate in the context of the legal framework in the particular jurisdiction.

²⁸ Depending on the circumstances, this sentence may read: “Management is responsible for the preparation and presentation of financial statements that give a true and fair view in accordance with International Financial Reporting Standards.”

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on conducting the audit in accordance with International Standards on Auditing. Because of the matter described in the Basis for Disclaimer of Opinion paragraph, however, we were not able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion.

Basis for Disclaimer of Opinion

The company's investment in its joint venture XYZ (Country X) Company is carried at xxx on the company's balance sheet, which represents over 90% of the company's net assets as at December 31, 20X1. We were not allowed access to the management and the auditors of XYZ, including XYZ's auditors' audit documentation. As a result, we were unable to determine whether any adjustments were necessary in respect of the company's proportional share of XYZ's assets that it controls jointly, its proportional share of XYZ's liabilities for which it is jointly responsible, its proportional share of XYZ's income and expenses for the year, and the elements making up the statement of changes in equity and cash flow statement.

Disclaimer of Opinion

Because of the significance of the matter described in the Basis for Disclaimer of Opinion paragraph, we have not been able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion. Accordingly, we do not express an opinion on the financial statements.

Report on Other Legal and Regulatory Requirements

[Form and content of this section of the auditor's report will vary depending on the nature of the auditor's other reporting responsibilities.]

[Auditor's signature]

[Date of the auditor's report]

[Auditor's address]

Illustration 5:

Circumstances include the following:

- **Audit of a complete set of general purpose financial statements prepared by management of the entity in accordance with International Financial Reporting Standards is the applicable financial reporting framework.**
- **The terms of the audit engagement reflect the description of management’s responsibility for the financial statements in [proposed] ISA 210 (Redrafted).**
- **The auditor was unable to obtain sufficient appropriate audit evidence about multiple elements of the financial statements. That is, the auditor was unable to obtain audit evidence about the entity’s inventories and accounts receivable. The possible effects of this inability to obtain sufficient appropriate audit evidence are deemed to be both material and pervasive to the financial statements.**
- **In addition to the audit of the financial statements, the auditor has other reporting responsibilities required under local law.**

INDEPENDENT AUDITOR’S REPORT

[Appropriate Addressee]

Report on the Financial Statements²⁹

We were engaged to audit the accompanying financial statements of ABC Company, which comprise the balance sheet as at December 31, 20X1, and the income statement, statement of changes in equity and cash flow statement for the year then ended, and a summary of significant accounting policies and other explanatory notes.

Management’s³⁰ Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation³¹ of these financial statements in accordance with International Financial Reporting Standards; this includes the design, implementation and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

²⁹ The sub-title “Report on the Financial Statements” is unnecessary in circumstances when the second sub-title “Report on Other Legal and Regulatory Requirements” is not applicable.

³⁰ Or other term that is appropriate in the context of the legal framework in the particular jurisdiction.

³¹ Depending on the circumstances, this sentence may read: “Management is responsible for the preparation and presentation of financial statements that give a true and fair view in accordance with International Financial Reporting Standards.”

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on conducting the audit in accordance with International Standards on Auditing. Because of the matters described in the Basis for Disclaimer of Opinion paragraph, however, we were not able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion.

Basis for Disclaimer of Opinion

We were not appointed as auditors of the company until after December 31, 20X1 and thus did not observe the counting of physical inventories at the beginning and end of the year. We were unable to satisfy ourselves by alternative means concerning the inventory quantities held at December 31, 20X0 and 20X1 which are stated in the balance sheet at xxx and xxx, respectively. In addition, the introduction of a new computerized accounts receivable system in September 20X1 resulted in numerous errors in accounts receivable. As of the date of our audit report, management was still in the process of rectifying the system deficiencies and correcting the errors. We were unable to confirm or verify by alternative means accounts receivable included in the balance sheet at a total amount of xxx as at December 31, 20X1. As a result of these matters, we were unable to determine whether any adjustments might have been found necessary in respect of recorded or unrecorded inventories and accounts receivable, and the elements making up the income statement, statement of changes in equity and cash flow statement.

Disclaimer of Opinion

Because of the significance of the matters described in the Basis for Disclaimer of Opinion paragraph, we have not been able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion. Accordingly, we do not express an opinion on the financial statements.

Report on Other Legal and Regulatory Requirements

[Form and content of this section of the auditor's report will vary depending on the nature of the auditor's other reporting responsibilities.]

[Auditor's signature]

[Date of the auditor's report]

[Auditor's address]