

# Chapter - 11 " Audit Reports "

(Lecture No. 2)

- Topics Covered:
- (1) Basics of Audit Report
  - (2) Types of Audit Reports
  - (3) Forming an opinion on f.s.
  - (4) Audit Reports -
    - (i) Audit conducted in accordance with SA
    - (ii) Auditor's Report prescribed by law and Reg.
    - (iii) Audit conducted in accordance with SA and ISA.
  - (5) Supplementary info. presented with the audited f.s. (SA-700)

## (6) Modifications to the Opinion in the Independent Auditor's Report: (SA-705)

### (i) Circumstances when a modification in auditor's report is required:

- (a) Auditor concludes that based on audit evidences obtained, f.s. as a whole are not free from material misstatements; Or.
- (b) Auditor is unable to obtain SAAE to conclude that f.s. as a whole are free from material misstatements.

### (ii) Objectives of auditor as per SA 705:

To Express clearly an appropriately modified opinion on the f.s. that is necessary when:

- (a) Auditor concludes that based on audit evidences obtained, f.s. as a whole are not free from material misstatements; Or
- (b) auditor is unable to obtain SAAE to conclude that f.s. as a whole are free from material misstatements.

- ### (iii) Types of modified opinion: 3 types —
- (a) Qualified opinion
  - (b) Adverse opinion
  - (c) Disclaimer of opinion

(a) Qualified opinion: It is expressed when:

(A) Auditor having obtained SAAE concludes that financial statements are misstated and misstatements are material, but <sup>not</sup> do have pervasive effect.  
Or

(B) Auditor is not been able to collect SAAE for transactions/matters that are material, but do not have pervasive effect.

(b) Adverse opinion: Adverse opinion is expressed when auditor having obtained SAAE, concludes that F.S. are materially misstated and such misstatements are having pervasive effect.

(c) Disclaimer of opinion: Auditor expresses disclaimer of opinion when he is not able to collect SAAE for transactions/matters that are material as well as having pervasive effect.

Note: Decision regarding which type of modified opinion is appropriate, depends upon:

(a) Nature of the matter giving rise to modification (i.e. whether the F.S. are materially misstated or auditor not able to collect SAAE).

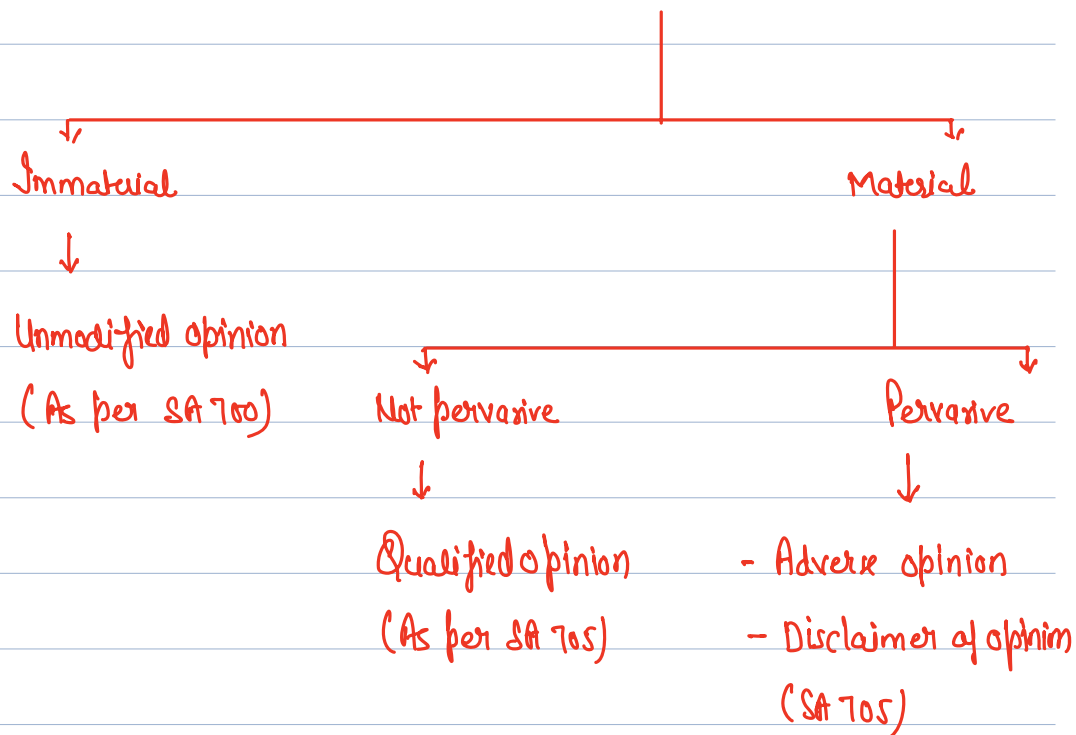
(b) Auditor's judgement about the pervasiveness of the effects.

Nature of Matter giving rise to modification ↓	Auditor's judgement - <u>Not Pervasive</u> -	Material as well as <u>Pervasive</u>
(a) F.S. are materially Misstated	Qualified	Adverse
(b) SAAE not obtained	Qualified	Disclaimer of opinion

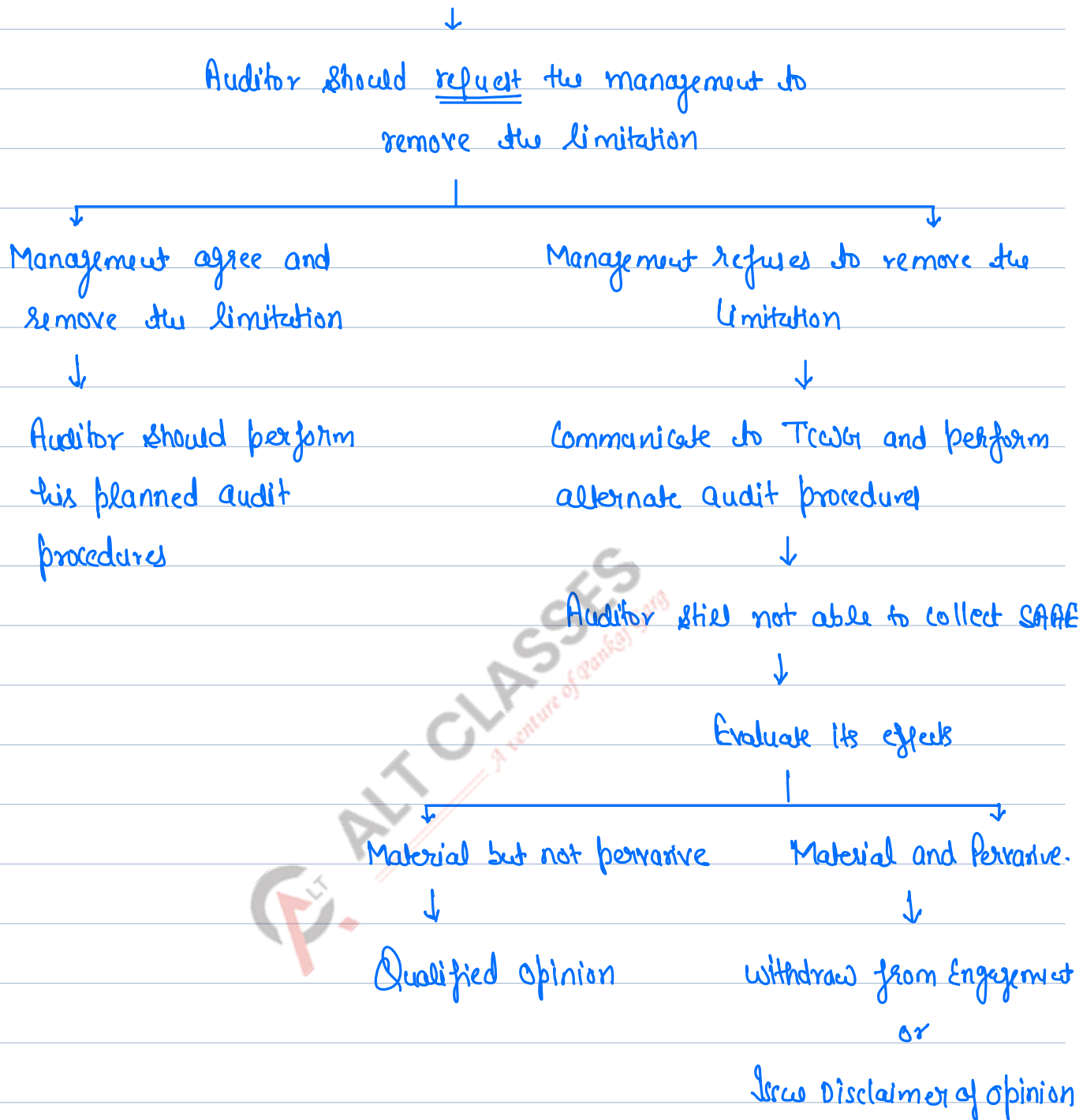
Note: Pervasive Effects: Pervasive effects on the F.S. are those that in the auditor's judgement:

- (a) are not confined to specific element, account or item of the F.S.
- (b) if so confined, represent a substantial proportion of the financial statements; or
- (c) in relation to disclosures, are fundamental to user's understanding of the F.S.

Summary: Auditor → Identify Misstatement | Not able to collect Evidence.



(iv) Auditor unable to collect SAAE due to limitations imposed by Mngt:



(v) Form and Content of Auditor's report when opinion is modified:

(I) Opinion Section: Use the heading - Qualified opinion  
- Adverse opinion  
- Disclaimer of opinion  
as appropriate.

## Wordings of Opinion:

### Qualified Opinion:

In our opinion, except for the effects of matters described in "Basis for Qualified Opinion Section", the financial statements present fairly, in all material respects, in accordance with (applicable FRF)

### Adverse Opinion:

In our opinion, to the best of our information and explanation provided to us, because of the significance of matters described in "Basis for Adverse Opinion Section", the financial statements do not reflect true and fair view of (state of affairs, - - - - -) in accordance with the (applicable FRF).

Imp:

### Disclaimer of Opinion:

When the auditor disclaims an opinion, he shall:

- ✓ (a) State that the auditor does not express an opinion on the F.S.
- ✓ (b) State that because of the significance of the matters described in Basis for disclaimer of Opinion Section, the auditor has not been able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion on the F.S.; and
- ✓ (c) Amend the statement required by SA 700, which indicates that the F.S. has been audited, to state that auditor was engaged to audit the F.S.

## II. Basis for opinion section:

- Amend the heading → Basis for Qualified opinion  
→ " " Adverse "  
→ " " Disclaimer of " | as appropriate.
- Auditor shall include a detailed description of matters due to which opinion is modified.

- If opinion is modified due to material misstatements; audit report shall include:
  - (a) Description of misstatement;
  - (b) Quantification of financial effect,
  - (c) If financial effect is not quantifiable, state the fact.

Ex: If provision is not appropriately accounted for, Basis for Qualified opinion section shall provide:

- (a) Reasons for not making provision
- (b) Amount required to be recorded.

- If opinion is modified due to non availability of information, audit shall state the reasons for inability to obtain SAAE.

For Ex: Records not available due to

- (a) Limitations imposed by management;
- (b) Limitations " " Circumstances (like records destroyed by fire; records seized by tax authorities)

- ✓ If opinion is modified due to non disclosure of information required to be disclosed, auditor shall:

✓ Discuss the non-disclosure with TCG;

✓ Describe the nature of omitted disclosure;

(c) Unless prohibited by law and regulation, include the omitted disclosure, if it is practicable to do so, and auditor has obtained SAAE about the omitted information.

### Impc III. Auditor Responsibility Section in case of disclaimer of opinion:

When auditor disclaims the opinion, the auditor shall amend the description of auditor's responsibilities so as to include the following:

- Statement that auditor's responsibility is to conduct an audit of F.S. in accordance with SAs and to issue auditor's report.
- Statement that because of significance of matter described in "Basis for Disclaimer of Opinion Section", auditor was not able to collect SAAE so as to provide a basis for an audit opinion.
- Statement about auditor's independence and other ethical requirements.

### Notes:

(1) When auditor disclaims an opinion on the F.S., auditor report shall not include "KAM Section" as per SA 701.

(2) When auditor expects to modify the opinion, he shall communicate with TCWG, the circumstances that led to expected modification and wordings of the modification.

(7) EOM Paragraph and OM Paragraph in the Independent Auditor's Report:

(SA 706):

(i) Auditor's Objective as per SA 706: To draw user's attention, by way of clear additional communication in auditor's report w.r.t.

(EOM)

(a) a matter that is appropriately presented or disclosed in the F.S., which is of such importance that it is fundamental to user's understanding of F.S.; or

(OM)

(b) a matter that is relevant to user's understanding of audit, auditor's responsibilities or the Auditor's report.

(ii) Meaning of EOM and OM Paragraph:

(A) EOM: A Paragraph included in auditor's report that refers to a matter appropriately presented or disclosed in the F.S.

↓

that in the auditor's judgement is of such importance that it is fundamental to user's understanding of the F.S.

(B) OM: A Paragraph included in the Auditor's report that refers to a matter other than those presented or disclosed in the F.S.

↓

that in the auditor's judgement is relevant to user's understanding of audit;

Auditor's responsibilities; or

Auditor's report.



### (iii) Requirements w.r.t. EOM Para:

#### Imp: (A) Circumstances in which EOM may be included:

- (1) Uncertainty as to future outcome of exceptional litigation or regulatory action.
- (2) Significant subsequent events occur after the date of f.s., but before the date of audit report.
- (3) Early application of a new AS that has a material effect on f.s. (if permitted).
- (4) Occurrence of a major catastrophe that may have a significant effect on entity financial position.

#### (B) Manner of Inclusion in auditor's report:

- EOM Para should be included in the auditor's report in a separate section titled as "Emphasis of Matter".
- Include in the para a clear reference to the matter being emphasized and to where relevant disclosure that fully describe the matter can be found in the f.s.
- EOM Para refer only to information which is appropriately disclosed in the financial statements.
- It must be indicated that auditor's opinion is not modified in respect of this matter.
- EOM para may be located in audit report immediately following the "Basis for opinion section".

Note: EOM Para is not a substitute for

- (a) Modified opinion when required by circumstances. (SA 705)
- (b) Disclosure in the financial statements.
- (c) reporting in accordance with SA 570 w.r.t. MURG.

(iv) Requirements w.r.t. OM Para:

- (1) OM Para should be included in the audit report in a separate section titled as "Other Matters".
- (2) OM Para may be located in the auditor's report immediately after "Key Audit Matters".
- (3) OM Para should be included in audit report when not prohibited by law or regulation.
- (4) OM Para is not a substitute for KAM.

Note: If auditor expects to include an EOM or OM para in the auditor's report, he shall communicate with TCGI regarding this expectation and the wordings of these paragraphs.