

Chapter 33

SA-700(R)

SA-700 (R) -Forming An Opinion & Reporting On The Financial Statements - [Effective Date 01.04.2018]

Q.1. Why this SA?

This Standard on Auditing (SA) deals with

- the auditor's responsibilities to form an opinion on the financial statements and
- Describes the form and content of the auditor's report issued as a result of an audit of financial statements.

Q.2. What is Objective if auditor under this SA?

The objectives of the auditor are:

- To form an opinion on the financial statements based on an evaluation of the conclusions drawn from the audit evidence obtained; and
- To express clearly that opinion through a written report.

Q.3. What considerations are required for an auditor to form an opinion?

According to this SA the auditor shall form an opinion on whether the financial statements are prepared, in all material respects, in accordance with the applicable financial reporting framework. In order to form such an opinion, the auditor shall conclude as to whether the auditor has obtained reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error. Before drawing such conclusion the auditor shall consider the following

- whether sufficient appropriate audit evidence has been obtained to reduce the audit risk to an acceptable low level as per SA 330
- Whether auditor has reason to conclude in accordance with SA 450, whether uncorrected misstatements are material, individually or in aggregate; and
- The auditor shall evaluate whether the financial statements are prepared, in all material respects, in accordance with the requirements of the applicable financial reporting framework. In particular, the auditor shall evaluate whether, in view of the requirements of the applicable financial reporting framework:

- The financial statements adequately disclose the significant accounting policies selected and applied;
- The accounting policies selected and applied are consistent with the applicable financial reporting framework and are appropriate;
- The accounting estimates made by management are reasonable;
- The information presented in the financial statements is relevant, reliable, comparable, and understandable;
- The financial statements provide adequate disclosures to enable the intended users to understand the effect of material transactions and events on the information conveyed in the financial statements; and
- The terminology used in the financial statements, including the title of each financial statement, is appropriate.

Q.4. When an auditor should express an unmodified opinion?

Unmodified opinion refers to an opinion expressed by the auditor when the auditor concludes that the financial statements are prepared, in all material respects, in accordance with the applicable financial reporting framework.

Q.5. When Auditor shall express a modified opinion?

If the auditor:

- concludes that, based on the audit evidence obtained, the financial statements as a whole are not free from material misstatement; or
- is unable to obtain sufficient appropriate audit evidence to conclude that the financial statements as a whole are free from material misstatement,
- the auditor shall modify the opinion in the auditor's report in accordance with SA 705(Revised).

We all know that usually financial statements are prepared in accordance with fair presentation framework (for example with AS or Ind AS) and if so and fair presentation framework do not achieve fair presentation, the auditor shall discuss the matter with management and, depending on the requirements of the applicable financial reporting framework and how the matter is resolved, shall determine whether it is necessary to modify the opinion in the auditor's report in accordance with SA 705 (Revised).

In other cases when the financial statements are prepared in accordance with a compliance framework (may not be in accordance with AS or Ind AS some other framework used) , the auditor is not required to evaluate whether the financial statements achieve fair presentation. However, if in extremely rare circumstances the auditor concludes that such financial statements are misleading, the auditor shall discuss the matter with management and, depending on how it is resolved, shall determine whether, and how, to communicate it in the auditor's report.

Q.6. What are the basic elements of Auditor's Report?

Followings are the elements of audit report:-

- Title
- Addressee
- Auditors opinion
- Basis of Opinion
- Going Concern
- Key Audit Matters
- Managements responsibility for financial statements
- Auditors responsibility for Financial Statements
- *Other Reporting Responsibilities*
- Signature
- Date
- Place

According to SA 700 the auditor's report shall be in writing and following are the contents of such report:-

Title

The auditor's report shall have a title that clearly indicates that it is the report of an independent auditor.

Addressee

The auditor's report shall be addressed, as appropriate, based on the circumstances of the engagement. Law, regulation or the terms of the engagement may specify to whom the auditor's report is to be addressed in that particular jurisdiction. The auditor's report is normally addressed to those for whom the report is prepared, often either to the shareholders or to those charged with governance of the entity whose financial statements are being audited.

Auditor's Opinion

The first section of the auditor's report shall include the auditor's opinion, and shall have the heading "Opinion." The Opinion section of the auditor's report shall also:

- Identify the entity whose financial statements have been audited;
- State that the financial statements have been audited;
- Identify the title of each statement comprising the financial statements;
- Refer to the notes, including the summary of significant accounting policies; and
- Specify the date of, or period covered by, each financial statement comprising the financial statements.

- When expressing an unmodified opinion on financial statements prepared in accordance with a fair presentation framework, the auditor's opinion shall, unless otherwise required by law or regulation, use one of the following phrases, which are regarded as being equivalent:
- In our opinion, the accompanying financial statements present fairly, in all material respects,
- [...] in accordance with [the applicable financial reporting framework]; or
- In our opinion, the accompanying financial statements give a true and fair view of [...] in accordance with [the applicable financial reporting framework].
- When expressing an unmodified opinion on financial statements prepared in accordance with a compliance framework, the auditor's opinion shall be that the accompanying financial statements are prepared, in all material respects, in accordance with [the applicable financial reporting framework].
- If the reference to the applicable financial reporting framework in the auditor's opinion is not to Accounting Standards, the auditor's opinion shall identify the origin of such other framework.

Basis for Opinion

The auditor's report shall include a section, directly following the Opinion section, with the heading "Basis for Opinion", that:

- States that the audit was conducted in accordance with Standards on Auditing;
- Refers to the section of the auditor's report that describes the auditor's responsibilities under the SAs;
- Includes a statement that the auditor is independent of the entity in accordance with the relevant ethical requirements relating to the audit, and has fulfilled the auditor's other ethical responsibilities in accordance with these requirements. The statement shall refer to the *Code of Ethics issued by ICAI*
- States whether the auditor believes that the audit evidence the auditor has obtained is
- sufficient and appropriate to provide a basis for the auditor's opinion.

Going Concern

Where applicable, the auditor shall report in accordance with SA 570 (Revised).¹³

Key Audit Matters

For audits of complete sets of general purpose financial statements of listed entities, the auditor shall communicate key audit matters in the auditor's report in accordance with SA 701.

When the auditor is otherwise required by law or regulation or decides to communicate key audit matters in the auditor's report, the auditor shall do so in accordance with SA 701.

Responsibilities for the Financial Statements

This section of the auditor's report shall describe management's responsibility for:

- Preparing the financial statements in accordance with the applicable financial reporting framework, and for such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error; and

- Assessing the entity’s ability to continue as a going concern and whether the use of the going concern basis of accounting is appropriate as well as disclosing, if applicable, matters relating to going concern. The explanation of management’s responsibility for this assessment shall include a description of when the use of the going concern basis of accounting is appropriate.
- When the financial statements are prepared in accordance with a fair presentation framework, the description of responsibilities for the financial statements in the auditor’s report shall refer to “the preparation and fair presentation of these financial statements” or “the preparation of financial statements that give a true and fair view,” as appropriate in the circumstances.

Auditor’s Responsibilities for the Audit of the Financial Statements

This section of the auditor’s report shall:

State that the objectives of the auditor are to:

- Obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error; and
- Issue an auditor’s report that includes the auditor’s opinion.
- State that reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with SAs will always detect a material misstatement when it exists; and
- State that misstatements can arise from fraud or error, and either:
 - Describe that they are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements; or
 - Provide a definition or description of materiality in accordance with the applicable financial reporting framework.
- The Auditor’s Responsibilities for the Audit of the Financial Statements section of the auditor’s report shall further:
 - State that, as part of an audit in accordance with SAs, the auditor exercises professional judgment and maintains professional skepticism throughout the audit; and

Describe an audit by stating that the auditor’s responsibilities are:

- To identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error; to design and perform audit procedures responsive to those risks; and to obtain audit evidence that is sufficient and appropriate to provide a basis for the auditor’s opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- To obtain an understanding of internal control relevant to the audit 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. In circumstances when the auditor also has a responsibility to express an opinion on the effectiveness of internal control in conjunction with the audit of the financial statements, the auditor shall omit the phrase that

the auditor's consideration of internal control is not for the purpose of expressing an opinion on the effectiveness of the entity's internal control.

- To evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
- To conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the entity's ability to continue as a going concern. If the auditor concludes that a material uncertainty exists, the auditor is required to draw attention in the auditor's report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify the opinion. The auditor's conclusions are based on the audit evidence obtained up to the date of the auditor's report. However, future events or conditions may cause an entity to cease to continue as a going concern.
- When the financial statements are prepared in accordance with a fair presentation framework, to evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.
- When SA 600 applies, further describe the auditor's responsibilities in a group audit engagement by stating:
- The division of responsibility for the financial information of the entity by indicating the extent to which the financial information of components is audited by the other auditors have been included in the financial information of the entity, e.g., the number of divisions/branches/subsidiaries or other components audited by other auditors

The Auditor's Responsibilities for the Audit of the Financial Statements section of the Auditor's Report also shall:

- State that the auditor communicates with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that the auditor identifies during the audit;
- State that the auditor provides those charged with governance with a statement that the auditor has complied with relevant ethical requirements regarding independence and communicate with them all relationships and other matters that may reasonably be thought to bear on the auditor's independence, and where applicable, related safeguards; and
- For audits of financial statements of all such entities for which key audit matters are communicated in accordance with SA 701, state that, from the matters communicated with those charged with governance, the auditor determines those matters that were of most significance in the audit of the financial statements of the current period and are therefore the key audit matters. In accordance with the requirements of SA 701, the auditor describes these matters in the auditor's report unless law or regulation precludes public disclosure about the matter or when, in extremely rare circumstances, the auditor determines that a matter should not be communicated in the auditor's report because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication.

Other Reporting Responsibilities

If the auditor addresses other reporting responsibilities in the auditor's report on the financial statements that are in addition to the auditor's responsibilities under the SAs, these other reporting responsibilities shall be addressed in a separate section in the auditor's report with a heading titled "Report on Other Legal and Regulatory Requirements" or otherwise as appropriate to the content of the section, unless these other reporting responsibilities address the same topics as those presented under the reporting responsibilities required by the SAs in which case the other reporting responsibilities may be presented in the same section as the related report elements required by the SAs.

Signature of the Auditor

The auditor's report shall be signed. The report is signed by the auditor (i.e. the engagement partner) in his personal name. Where the firm is appointed as the auditor, the report is signed in the personal name of the auditor and in the name of the audit firm. The partner/proprietor signing the audit report also needs to mention the membership number assigned by the Institute of Chartered Accountants of India. They also include the registration number of the firm, wherever applicable, as allotted by ICAI, in the audit reports signed by them.

Place of Signature

The auditor's report shall name specific location, which is ordinarily the city where the audit report is signed.

Date of the Auditor's Report

The auditor's report shall be dated no earlier than the date on which the auditor has obtained sufficient appropriate audit evidence on which to base the auditor's opinion on the financial statements, including evidence that: (Ref: Para. A58–A61)

- All the statements that comprise the financial statements, including the related notes, have been prepared; and
- Those with the recognized authority have asserted that they have taken responsibility for those financial statements.

Q.7. What shall be form and content of the auditor's report if auditor's report is prescribed by laws and regulations?

If the auditor is required by law or regulation applicable to the entity to use a specific layout, or wording of the auditor's report, the auditor's report shall refer to Standards on Auditing only if the auditor's report includes, at a minimum, each of the following elements: (Ref: Para. A62– A63)

- A title.
- An addressee, as required by the circumstances of the engagement.
- An Opinion section containing an expression of opinion on the financial statements and a reference to the applicable financial reporting framework used to prepare the financial statements
- An identification of the entity's financial statements that have been audited.
- A statement that the auditor is independent of the entity in accordance with the relevant ethical requirements relating to the audit, and has fulfilled the auditor's other ethical

responsibilities in accordance with these requirements. The statement shall refer to the Code of Ethics issued by ICAI.

- Where applicable, a section that addresses, and is not inconsistent with, the reporting requirements in paragraph 22 of SA 570 (Revised).
- Where applicable, a Basis for Qualified (or Adverse) Opinion section that addresses, and is not inconsistent with, the reporting requirements in paragraph 23 of SA 570 (Revised).
- Where applicable, a section that includes the information required by SA 701, or additional information about the audit that is prescribed by law or regulation and that addresses, and is not inconsistent with, the reporting requirements in that SA.
- A description of management's responsibilities for the preparation of the financial statements and an identification of those responsible for the oversight of the financial reporting process that addresses, and is not inconsistent with, the requirements in paragraphs 32–35.
- A reference to Standards on Auditing and the law or regulation, and a description of the auditor's responsibilities for an audit of the financial statements that addresses, and is not inconsistent with, the requirements in paragraphs 36–39.
- The auditor's signature.
- The Place of signature
- The date of the auditor's report.

ILLUSTRATIONS OF INDEPENDENT AUDITOR'S REPORTS ON FINANCIAL STATEMENTS

Illustration 1 – Auditor's Report on Financial Statements of a Listed Entity

Prepared in Accordance with a Fair Presentation Framework

For purposes of this illustrative auditor's report, the following circumstances are assumed:

1. Audit of a complete set of financial statements of a listed company (registered under the Companies Act, 2013) using a fair presentation framework. The audit is not a group audit (i.e., SA 600 does not apply).
2. The financial statements are prepared by management of the entity in accordance with the accounting Standards prescribed under section 133 of the Companies Act, 2013.
3. The terms of the audit engagement reflect the description of management's responsibility for
4. the financial statements in SA 210.
5. The auditor has concluded an unmodified (i.e., "clean") opinion is appropriate based on the
6. Audit Evidence obtained.
7. The relevant ethical requirements that apply to the audit comprise the Code of Ethics issued by ICAI together with the other relevant ethical requirements relating to the audit and the auditor refers to both.
8. Based on the audit evidence obtained, the auditor has concluded that a material uncertainty does not exist related to events or conditions that may cast significant doubt on the entity's ability to continue as a going concern in accordance with SA 570 (Revised).
9. Key audit matters have been communicated in accordance with SA 701.
10. Those responsible for oversight of the financial statements differ from those responsible for the preparation of the financial statements.
11. In addition to the audit of the financial statements, the auditor has other reporting responsibilities required under the Companies Act, 2013.

INDEPENDENT AUDITOR'S REPORT

To the Members of ABC Company Limited

Report on the Audit of the Standalone Financial Statements¹ Opinion

We have audited the standalone financial statements of ABC Company Limited (“the Company”), which comprise the balance sheet as at 31st March 20XX, and the statement of Profit and Loss, (*statement of changes in equity*)² and statement of cash flows for the year then ended, and notes to the financial statements, including a summary of significant accounting policies and other explanatory information [in which are included the Returns for the year ended on that date audited by the branch auditors of the Company’s branches located at (location of branches)].

In our opinion and to the best of our information and according to the explanations given to us, the aforesaid standalone financial statements give the information required by the Act in the manner so required and give a true and fair view in conformity with the accounting principles generally accepted in India, of the state of affairs of the Company as at March 31, 20XX, and profit/loss, (*changes in equity*)⁴ and its cash flows for the year ended on that date.

Basis for Opinion

We conducted our audit in accordance with the Standards on Auditing (SAs) specified under section 143(10) of the Companies Act, 2013. Our responsibilities under those Standards are further described in the *Auditor’s Responsibilities for the Audit of the Financial Statements* section of our report. We are independent of the Company in accordance with the *Code of Ethics* issued by the Institute of Chartered Accountants of India together with the ethical requirements that are relevant to our audit of the financial statements under the provisions of the Companies Act, 2013 and the Rules thereunder, and we have fulfilled our other ethical responsibilities in accordance with these requirements and the Code of Ethics. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Key Audit Matters

Key audit matters are those matters that, in our professional judgment, were of most significance in our audit of the financial statements of the current period. These matters were addressed in the context of our audit of the financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters.

[*Description of each key audit matter in accordance with SA 701.*]

Management’s Responsibility for the Standalone Financial Statements

The Company’s Board of Directors is responsible for the matters stated in section 134(5) of the Companies Act, 2013 (“the Act”) with respect to the preparation of these standalone financial statements that give a true and fair view of the financial position, financial performance, (*changes in equity*)⁵ and cash flows of the Company in accordance with⁶ the accounting principles generally accepted in India, including the accounting Standards specified under section 133 of the Act. This responsibility also includes maintenance of adequate accounting records in accordance with the provisions of the Act for safeguarding of the assets of the Company and for preventing and detecting frauds and other irregularities; selection and application of appropriate implementation and

maintenance of accounting policies; making judgments and estimates that are reasonable and prudent; and design, implementation and maintenance of adequate internal financial controls, that were operating effectively for ensuring the accuracy and completeness of the accounting records, relevant to the preparation and presentation of the financial statement that give a true and fair view and are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, management is responsible for assessing the Company's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless management either intends to liquidate the Company or to cease operations, or has no realistic alternative but to do so.

Those Board of Directors are also responsible for overseeing the Company's financial reporting process.

Auditor's Responsibilities for the Audit of the Financial Statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with SAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

Paragraph 40(b) of this SA explains that the shaded material below can be located in an Appendix to the auditor's report. Paragraph 40(c) explains that when law, regulation or applicable auditing standards expressly permit, reference can be made to a website of an appropriate authority that contains the description of the auditor's responsibilities, rather than including this material in the auditor's report, provided that the description on the website addresses, and is not inconsistent with, the description of the auditor's responsibilities below.

As part of an audit in accordance with SAs, we exercise professional judgment and maintain professional skepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances. Under section 143(3)(i) of the Companies Act, 2013, we are also responsible for expressing our opinion on whether the company has adequate internal financial controls system in place and the operating effectiveness of such controls.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.

- Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Company's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Company to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

We communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

We also provide those charged with governance with a statement that we have complied with relevant ethical requirements regarding independence, and to communicate with them all relationships and

Other Matter

We did not audit the financial statements/ information of (number) branches included in the stand alone financial statements of the Company whose financial statements/financial information reflect total assets of Rs. as at 31st March 20XX and the total revenue of Rs.

..... for the year ended on that date, as considered in the standalone financial statements/information of these branches have been audited by the branch auditors whose reports have been furnished to us, and our opinion in so far as it relates to the amounts and disclosures included in respect of branches, is based solely on the report of such branch auditors.

Our opinion is not modified in respect of these matters.

Report on Other Legal and Regulatory Requirements

As required by the Companies (Auditor's Report) Order, 2016 ("the Order"), issued by the Central Government of India in terms of sub-section (11) of section 143 of the Companies Act, 2013, we give in the Annexure a statement on the matters specified in paragraphs 3 and 4 of the Order, to the extent applicable.

As required by Section 143(3) of the Act, we report that:

We have sought and obtained all the information and explanations which to the best of our knowledge and belief were necessary for the purposes of our audit.

In our opinion, proper books of account as required by law have been kept by the Company so far as it appears from our examination of those books [*and proper returns adequate for the purposes of our audit have been received from the branches not visited by us.*^{7]}

[The reports on the accounts of the branch offices of the Company audited under Section 143(8) of the Act by branch auditors have been sent to us and have been properly dealt with by us in preparing this report]

The Balance Sheet, the Statement of Profit and Loss, and the Cash Flow Statement dealt with by this Report are in agreement with the books of account [*and with the returns received from the branches not visited by us*].

In our opinion, the aforesaid standalone financial statements comply with the Accounting Standards specified under Section 133 of the Act, read with Rule 7 of the Companies (Accounts) Rules, 2014.

1. On the basis of the written representations received from the directors as on 31st March, 20XX taken on record by the Board of Directors, none of the directors is disqualified as on 31st March, 20XX from being appointed as a director in terms of Section 164 (2) of the Act.
2. With respect to the adequacy of the internal financial controls over financial reporting of the Company and the operating effectiveness of such controls, refer to our separate Report in “Annexure A”.
3. With respect to the other matters to be included in the Auditor’s Report in accordance with Rule 11 of the Companies (Audit and Auditors) Rules, 2014, in our opinion and to the best of our information and according to the explanations given to us:
4. The Company has disclosed the impact of pending litigations on its financial position in its financial statements – Refer Note XX to the financial statements; [*or the Company does not have any pending litigations which would impact its financial position¹⁰*]
5. The Company has made provision, as required under the applicable law or accounting standards, for material foreseeable losses, if any, on long-term contracts including derivative contracts – Refer Note XX to the financial statements; [*or the Company did not have any long-term contracts including derivative contracts for which there were any material foreseeable losses.*]
6. There has been no delay in transferring amounts, required to be transferred, to the Investor Education and Protection Fund by the Company {*or, following are the instances of delay in transferring amounts, required to be transferred, to the Investor Education and Protection Fund by the Company or there were no amounts which were required to be transferred to the Investor Education and Protection Fund by the Company*}.

For XYZ & Co
Chartered Accountants
(Firm’s Registration No.)

Place of Signature:
Date:

Signature (Name of the Member Signing the Audit Report)
(Designation) (Membership No. XXXXX)

ILLUSTRATION 2 – AUDITOR’S REPORT ON FINANCIAL STATEMENTS OF AN UNLISTED COMPANY PREPARED IN ACCORDANCE WITH A FAIR PRESENTATION FRAMEWORK

For purposes of this illustrative auditor’s report, the following circumstances are assumed:

- Audit of a complete set of financial statements of an unlisted company (registered under the Companies Act, 2013) using a fair presentation framework. The audit is not a group audit (i.e., SA 600 does not apply).
- The financial statements are prepared by management of the entity in accordance with the accounting Standards prescribed under section 133 of the Companies Act, 2013.
- The terms of the audit engagement reflect the description of management’s responsibility for the financial statements in SA 210.
- The auditor has concluded an unmodified (i.e., “clean”) opinion is appropriate based on the audit evidence obtained.
- The relevant ethical requirements that apply to the audit comprise the Code of Ethics issued by ICAI together with the other relevant ethical requirements relating to the audit and the auditor refers to both.
- Based on the audit evidence obtained, the auditor has concluded that a material uncertainty does not exist related to events or conditions that may cast significant doubt on the entity’s ability to continue as a going concern in accordance with SA 570 (Revised).
- The auditor is not required, and has otherwise not decided, to communicate key audit matters in accordance with SA 701.
- Those responsible for oversight of the financial statements differ from those responsible for the preparation of the financial statements.
- In addition to the audit of the financial statements, the auditor has other reporting responsibilities required under the Companies Act, 2013.

INDEPENDENT AUDITOR’S REPORT

To the Members of ABC Company Limited

Report on the Audit of the Standalone Financial Statements²² Opinion

We have audited the standalone financial statements of ABC Company Limited (“the Company”), which comprise the balance sheet as at 31st March 20XX, and the statement of Profit and Loss, (*statement of changes in equity*)²³ and statement of cash flows for the year then ended, and notes to the financial statements, including a summary of significant accounting policies and other explanatory information [in which are included the Returns for the year ended on that date audited by the branch auditors of the Company’s branches located at (location of branches)]²⁴.

In our opinion and to the best of our information and according to the explanations given to us, the aforesaid standalone financial statements give the information required by the Act in the manner so

required and give a true and fair view in conformity with the accounting principles generally accepted in India, of the state of affairs of the Company as at March 31, 20XX, and profit/loss, (*changes in equity*)²⁵ and its cash flows for the year ended on that date.

Basis for Opinion

We conducted our audit in accordance with the Standards on Auditing (SAs) specified under section 143(10) of the Companies Act, 2013. Our responsibilities under those Standards are further described in the *Auditor's Responsibilities for the Audit of the Financial Statements* section of our report. We are independent of the Company in accordance with the *Code of Ethics* issued by the Institute of Chartered Accountants of India together with the ethical requirements that are relevant to our audit of the financial statements under the provisions of the Companies Act, 2013 and the Rules thereunder, and we have fulfilled our other ethical responsibilities in accordance with these requirements and the Code of Ethics. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Responsibility of Management for Standalone Financial Statements

The Company's Board of Directors is responsible for the matters stated in section 134(5) of the Companies Act, 2013 ("the Act") with respect to the preparation of these standalone financial statements that give a true and fair view of the financial position, financial performance, (*changes in equity*)²⁶ and cash flows of the Company in accordance with the accounting principles generally accepted in India, including the accounting Standards specified under section 133 of the Act. This responsibility also includes maintenance of adequate accounting records in accordance with the provisions of the Act for safeguarding of the assets of the Company and for preventing and detecting frauds and other irregularities; selection and application of appropriate implementation and maintenance of accounting policies; making judgments and estimates that are reasonable and prudent; and design, implementation and maintenance of adequate internal financial controls, that were operating effectively for ensuring the accuracy and completeness of the accounting records, relevant to the preparation and presentation of the financial statement that give a true and fair view and are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, management is responsible for assessing the Company's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless management either intends to liquidate the Company or to cease operations, or has no realistic alternative but to do so.

Those Board of Directors are also responsible for overseeing the company's financial reporting process.

Auditor's Responsibilities for the Audit of the Financial Statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with SAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the

aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

Paragraph 40(b) of this SA explains that the shaded material below can be located in an Appendix to the auditor's report. Paragraph 40(c) explains that when law, regulation or the applicable auditing standards expressly permit, reference can be made to a website of an appropriate authority that contains the description of the auditor's responsibilities, rather than including this material in the auditor's report, provided that the description on the website addresses, and is not inconsistent with, the description of the auditor's responsibilities below.

As part of an audit in accordance with SAs, we exercise professional judgment and maintain professional skepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances. Under section 143(3)(i) of the Companies Act, 2013, we are also responsible for expressing our opinion on whether the company has adequate internal financial controls system in place and the operating effectiveness of such controls.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
- Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Company's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Company to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.
- We communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.
- We also provide those charged with governance with a statement that we have complied with relevant ethical requirements regarding independence, and to communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, related safeguards.

Other Matter

We did not audit the financial statements/ information of (number) branches included in the standalone financial statements of the company whose financial statements/financial information reflect total assets of Rs.as at 31st March 20XX and the total revenue of Rs.for the year ended on that date, as considered in the standalone financial statements/information of these branches have been audited by the branch auditors whose reports have been furnished to us, and our opinion in so far as it relates to the amounts and disclosures included in respect of branches, is based solely on the report of such branch auditors.

Our opinion is not modified in respect of these matters.

Report on Other Legal and Regulatory Requirements

As required by the Companies (Auditor’s Report) Order, 2016 (“the Order”), issued by the Central Government of India in terms of sub-section (11) of section 143 of the Companies Act, 2013, we give in the Annexure a statement on the matters specified in paragraphs 3 and 4 of the Order, to the extent applicable.

As required by Section 143(3) of the Act, we report that:

- We have sought and obtained all the information and explanations which to the best of our knowledge and belief were necessary for the purposes of our audit.
- In our opinion, proper books of account as required by law have been kept by the Company so far as it appears from our examination of those books [*and proper returns adequate for the purposes of our audit have been received from the branches not visited by us.*²⁷]
- [*The reports on the accounts of the branch offices of the Company audited under Section 143(8) of the Act by branch auditors have been sent to us and have been properly dealt with by us in preparing this report.*]
- The Balance Sheet, the Statement of Profit and Loss, and the Cash Flow Statement dealt with by this Report are in agreement with the books of account [*and with the returns received from the branches not visited by us.*]
- In our opinion, the aforesaid standalone financial statements comply with the Accounting Standards specified under Section 133 of the Act, read with Rule 7 of the Companies (Accounts) Rules, 2014.
- On the basis of the written representations received from the directors as on 31st March, 20XX taken on record by the Board of Directors, none of the directors is disqualified as on 31st March, 20XX from being appointed as a director in terms of Section 164 (2) of the Act.
- With respect to the adequacy of the internal financial controls over financial reporting of the Company and the operating effectiveness of such controls, refer to our separate Report in “Annexure A”.
- With respect to the other matters to be included in the Auditor’s Report in accordance with Rule 11 of the Companies (Audit and Auditors) Rules, 2014, in our opinion and to the best of our information and according to the explanations given to us:

- The Company has disclosed the impact of pending litigations on its financial position in its financial statements – Refer Note XX to the financial statements; *[or the Company does not have any pending litigations which would impact its financial position]*
- The Company has made provision, as required under the applicable law or accounting standards, for material foreseeable losses, if any, on long-term contracts including derivative contracts – Refer Note XX to the financial statements; *[or the Company did not have any long-term contracts including derivative contracts for which there were any material foreseeable losses.]*
- There has been no delay in transferring amounts, required to be transferred, to the Investor Education and Protection Fund by the Company {*or, following are the instances of delay in transferring amounts, required to be transferred, to the Investor Education and Protection Fund by the Company or there were no amounts which were required to be transferred to the Investor Education and Protection Fund by the Company*}.

For XYZ & Co
Chartered Accountants
(Firm's Registration No.)

Place of Signature: Date:
Signature
(Name of the Member Signing the Audit Report)
(Designation)
(Membership No. XXXXX)

ILLUSTRATION 3 – AUDITOR’S REPORT ON FINANCIAL STATEMENTS OF A NON CORPORATE ENTITY PREPARED IN ACCORDANCE WITH A FAIR PRESENTATION FRAMEWORK

For purposes of this illustrative auditor’s report, the following circumstances are assumed:

- Audit of a complete set of financial statements of a non corporate entity using a fair presentation framework. The audit is not a group audit (i.e., SA 600 does not apply).
- The financial statements are prepared by management of the entity in accordance with the Accounting Standards issued by the Institute of Chartered Accountants of India.
- The terms of the audit engagement reflect the description of management’s responsibility for the financial statements in SA 210.
- The auditor has concluded an unmodified (i.e., “clean”) opinion is appropriate based on the audit evidence obtained.
- The relevant ethical requirements that apply to the audit are the Code of Ethics issued by ICAI.
- Based on the audit evidence obtained, the auditor has concluded that a material uncertainty does not exist related to events or conditions that may cast significant doubt on the entity’s ability to continue as a going concern in accordance with SA 570 (Revised).
- The auditor is not required, and has otherwise not decided, to communicate key audit matters in accordance with SA 701.
- Those responsible for oversight of the financial statements differ from those responsible for the preparation of the financial statements.
- The auditor has no other reporting responsibilities required under local law.
- The auditor elects to refer to the description of the auditor’s responsibility included on a website of an appropriate authority.

INDEPENDENT AUDITOR'S REPORT

To the Partners of ABC & Associates [or Other Appropriate Addressee]

Opinion

We have audited the financial statements of ABC & Associates (the entity), which comprise the balance sheet at March 31st 20XX, and the profit and loss account, *(and statement of cash flows)*³⁵ for the year then ended, and notes to the financial statements, including a summary of significant accounting policies.

In our opinion, the accompanying financial statements give a true and fair view of the financial position of the entity as at March 31, 20XX, and of its financial performance *(and its cash flows)*³⁶ for the year then ended in accordance with the Accounting Standards issued by the Institute of Chartered Accountants of India (ICAI).

Basis for Opinion

We conducted our audit in accordance with the Standards on Auditing (SAs) issued by ICAI. Our responsibilities under those standards are further described in the *Auditor's Responsibilities for the*

Specify any applicable ethical requirements under the relevant laws or regulations applicable to the entity. Where applicable.

Audit of the Financial Statements section of our report. We are independent of the entity in accordance with the ethical requirements that are relevant to our audit of the financial statements in *[jurisdiction]*, and we have fulfilled our other ethical responsibilities in accordance with these requirements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Responsibilities of Management and Those Charged with Governance for the Financial Statements

Management is responsible for the preparation and fair presentation of the financial statements in accordance with the aforesaid Accounting Standards, and for such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, management is responsible for assessing the entity's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless management either intends to liquidate the entity or to cease operations, or has no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the entity's financial reporting process.

Auditor's Responsibilities for the Audit of the Financial Statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with SAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

A further description of the auditor's responsibilities for the audit of the financial statements is located at [*Organization's*] website at: [*website link*]. This description forms part of our auditor's report.

For XYZ & Co
Chartered Accountants
(Firm's Registration No.)

Place of Signature:

Date:

Signature
(Name of the Member Signing the Audit Report)
(Designation)
(Membership No. XXXXX)

Chapter 34

SA-701

SA-701 (Newly)- Communicating Key Audit Matters in the Independent Auditor's Report - [Effective Date 01.04.2018]

Q.1. When this SA is Applicable?

This SA applies to audits of complete sets of general purpose financial statements of listed entities and circumstances when the auditor otherwise decides to communicate key audit matters in the auditor's report. This SA also applies when the auditor is required by law or regulation to communicate key audit matters in the auditor's report

Q.2. What do you mean by Key Audit Matters?

According to this SA the Key Audit Matters are those matters that, in the auditor's professional judgment, were of most significance in the audit of the financial statements of the current period. Key audit matters are selected from matters communicated with those charged with governance (as we learnt communication of matters to those charged with governance in SA 260 and SA 265.

Communicating key audit matters provides additional information to intended users of the financial statements ("intended users") to assist them in understanding those matters that, in the auditor's professional judgment, were of most significance in the audit of the financial statements of the current period. Communicating key audit matters may also assist intended users in understanding the entity and areas of significant management judgment in the audited financial statements.

Q.3. Why This SA?

This SA deals with the auditor's responsibility to communicate key audit matters in the auditor's report. It is intended to address both the auditor's judgment as to what to communicate in the auditor's report and the form and content of such communication.

Q.4. Whether Communication of Key Audit matters relieves management and auditor to some extent to report?

Communicating key audit matters in the auditor's report is in the context of the auditor having formed an opinion on the financial statements as a whole. Communicating key audit matters in the auditor's report :

- Is not a substitute for disclosures in the financial statements that the applicable financial reporting framework requires management to make, or that are otherwise necessary to achieve fair presentation;
- Is not a substitute for the auditor expressing a modified opinion when required by the circumstances of a specific audit engagement in accordance with SA 705 (Revised);¹
- Is not a substitute for reporting in accordance with SA 570 (Revised) when a material uncertainty exists relating to events or conditions that may cast significant doubt on an entity's ability to continue as a going concern; or
- Is not a separate opinion on individual matters.

Q.5. How an auditor shall determine the Key Audit Matters?

The auditor shall determine, from the matters communicated with those charged with governance, those matters that required significant auditor attention in performing the audit. In making this determination, the auditor shall take into account the following:

Areas of higher assessed risk of material misstatement, or significant risks identified in accordance with SA 315.

Significant auditor judgments relating to areas in the financial statements that involved significant management judgment, including accounting estimates that have been identified as having high estimation uncertainty.

The effect on the audit of significant events or transactions that occurred during the period.

Lets have some examples of KAM:-

- Impairment of property, plant and equipment:- with the product industry is dealing is losing its market and there may be chances of impairment of assets, though in this financial year it was not needed to create provision for impairment but in next financial year there may be circumstances for the same.
- Carrying value of intangible assets:- Due to future of the industry predicted worldwide the net cash flow from the intangibles possessed by the entity may not recover the amount over which it is stated in financial statements.
- Valuation of inventory: - As the entity belongs to fashion industry and it has piled up huge inventory of readymade garments and the international online campaign proved failure this year due to which risk of the inventory to realise its cost is uncertain, may be in next financial year there may be substantial loss on this account.
- You may note that the above circumstances are not subject matter of qualification in auditors report as per SA705, nor there is any uncertainty of going concern to be highlighted in the audit report as per SA 700

Q.6. How auditor should communicating Key Audit Matters?

The auditor shall describe each key audit matter, using an appropriate subheading, in a separate section of the auditor's report under the heading "Key Audit Matters," the introductory language in this section of the auditor's report shall state that:

- Key audit matters are those matters that, in the auditor's professional judgment, were of most significance in the audit of the financial statements [of the current period]; and
- These matters were addressed in the context of the audit of the financial statements as a whole, and in forming the auditor's opinion thereon, and the auditor does not provide a separate opinion on these matters.

Q.7. When an Auditor should not communicate significant matters as KAM in a separate section?

The auditor shall not communicate a matter in the Key Audit Matters section of the auditor's report when

- the auditor would be required to modify the opinion in accordance with SA 705 (Revised) as a result of the matter.
- Law or regulation precludes public disclosure about the matter;
- In extremely rare circumstances, the auditor determines that the matter should not be communicated in the auditor's report because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication. This shall not apply if the entity has publicly disclosed information about the matter.
- a material uncertainty related to events or conditions that may cast significant doubt on the entity's ability to continue as a going concern in accordance with SA 570 (Revised)

Q.8. Whether there is any duty to communicate to those charged with governance about key matters?

The auditor shall communicate with those charged with governance:

- Those matters the auditor has determined to be the key audit matters; or
- If applicable, depending on the facts and circumstances of the entity and the audit, the auditor's determination that there are no key audit matters to communicate in the auditor's report.

Q.9. What is requirement of Documentation in this SA?

The auditor shall include in the audit documentation:

- The matters that required significant auditor attention and the rationale for the auditor's determination as to whether or not each of these matters is a key audit matter .
- Where applicable, the rationale for the auditor's determination that there are no key audit matters to communicate in the auditor's report or that the only key audit matters to communicate are those matters addressed by SA 705 or SA 700 (as going concern matter)
- Where applicable, the rationale for the auditor's determination not to communicate in the auditor's report a matter determined to be a key audit matter.

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Chapter 35

SA-705

SA-705 - Modifications To The Opinion In The Independent Auditor's Report - [Effective Date 01.04.2018]

Q.1. What do you mean by Modification to the Opinion?

- ◆ When the Auditor is not giving unmodified opinion it said he is modifying his opinion.
- ◆ According to SA-705(R), Modified opinion refers to a Qualified opinion, an Adverse opinion or a Disclaimer of opinion.

Q.2. When Auditor will decide to modify his Opinion?

According to SA-705(R), The Auditor shall modify the opinion in the Auditor's report when:

- ◆ The **Auditor concludes** that, based on the Audit Evidence obtained, the **Financial Statements as a whole are not free from material Misstatement**; or
- ◆ The Auditor is **unable to obtain Sufficient and Appropriate Audit Evidence** to conclude that the Financial Statements as a whole are free from material Misstatement.

Q.3. What will be the consequence of a Modified Audit report?

This SA 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:

- ◆ 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
- ◆ The Auditor's judgment about the pervasiveness of the effects or possible effects of the matter on the Financial Statements.

Q.4. When an Auditor shall express a qualified Opinion?

The Auditor shall express a qualified Opinion when:

- ◆ The Auditor, having obtained Sufficient and Appropriate Audit Evidence, concludes that Misstatements, individually or in the aggregate, are material, but not pervasive, to the Financial Statements; (Deviation from FRF) or

- ◆ 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, could be material but not pervasive. (Limitation on scope)

✍ For Example Auditor discovers that Company XYZ has not accounted for inventory correctly, has kept incomplete records regarding its cash accounts, and did not provide adequate records for review regarding depreciation. As a result, the Auditor would likely give a qualified opinion for Company XYZ due to both limitation of scope (incomplete records) and deviation from FRF (errors in accounting for inventory).

Q.5. When an Auditor shall express an adverse Opinion?

The Auditor shall express an adverse Opinion when the Auditor, having obtained Sufficient and Appropriate Audit evidence, concludes that misstatements, individually or in the aggregate, are both material and pervasive to the Financial Statements.

Illustration:-

Basis for Adverse Opinion

The Company's financing arrangements expired and the amount outstanding was payable on March 31, 20XX. The Company has been unable to re-negotiate or obtain replacement financing and is considering filing for bankruptcy. These events indicate a material uncertainty that may cast significant doubt on the Company's ability to continue as a going concern and, therefore, it may be unable to realise its assets and discharge its liabilities in the normal course of business. The financial statements (and notes thereto) do not disclose this fact.

Adverse Opinion

In our opinion, because of the omission of the information mentioned in the Basis for Adverse Opinion paragraph, the financial statements do not give the information required by the Companies Act, 2013 in the manner so required and also do not give a true and fair view in conformity with the accounting principles generally accepted in India of the state of affairs of the Company as at 31st March, 20XX, and its profit/loss and its cash flows for the year ended on that date.

Q.6. When an Auditor shall express a disclaimer of Opinion?

The Auditor shall disclaim an opinion 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, could be both material and pervasive.

The Auditor shall disclaim an opinion 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 due to the potential interaction of the uncertainties and their possible cumulative effect on the Financial Statements.

Illustration of Disclaimer of Opinion:-**Basis For disclaimer Opinion**

The company's financing arrangements expired and the amount outstanding was payable on 30 June 20X1. The company has been unable to re-negotiate or obtain replacement financing. The directors have refused to extend their assessment of the company's ability to continue as a going concern beyond 30 September 20X1 given the uncertainty of obtaining suitable replacement financing. We have been unable to obtain alternative evidence which would provide sufficient appropriate Audit evidence as to whether the company may be able to obtain such financing, and hence remove significant doubt of its ability to continue as a going concern within 12 months of the date of this Auditor's report.

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 report.

ILLUSTRATIVE FORMAT OF AUDITORS REPORTS WITH MODIFICATION TO THE OPINION

Case-1 Inventories are misstated. The Misstatement is deemed to be material but not pervasive to the Financial Statements. The Audit opinion is qualified for the Misstatement.

Basis for Qualified Opinion

The Company's inventories are carried in the Balance Sheet at Rs. 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 the Accounting Standards referred to in Section 133 of Companies Act 2013 {Previously subsection (3C) of section 211 of the Companies Act, 1956 ;}. The Company's records indicate that had management stated the inventories at the lower of cost and net realisable value, an amount of Rs. XXX would have been required to write the inventories down to their net realisable value. Accordingly, cost of sales would have been increased by Rs. XXX, and income tax, net profit and shareholders' funds would have been reduced by Rs. XXX, Rs. XXX and Rs. XXX, respectively.

Opinion

In our opinion and to the best of our information and according to the explanations given to us, except for the effects of the matter described in the Basis for Qualified Opinion paragraph, the Financial Statements give the information required by the Act in the manner so required and give a true and fair view in conformity with the accounting principles generally accepted in India:

- (a) In the case of the Balance Sheet, of the state of affairs of the Company as at March 31, 20XX;
- (b) In the case of the Statement of Profit and Loss , of the profit/ loss for the year ended on that date;
and
- (c) In the case of the Cash Flow Statement, of the cash flows for the year ended on that date.

Case-2 the Auditor was unable to obtain sufficient appropriate Audit Evidence regarding existence of investment in a foreign company. The possible effects of the inability to obtain sufficient appropriate Audit Evidence are deemed to be material but not pervasive to the Financial Statement. The Audit opinion is qualified for the Misstatement.

Basis for Qualified Opinion

ABC Company Limited's investment in XYZ Company, a foreign company acquired during the year and accounted as Held to maturity investment in Balance sheet of ABC company' Ltd. We were unable to obtain sufficient appropriate Audit Evidence about the existence of ABC Company Limited's investment in XYZ Company as at March 31, 20XX because we were denied access to the financial information relating to the same, management, consequently, we were unable to determine whether any adjustments to these amounts were necessary.

Qualified Opinion

In our opinion and to the best of our information and according to the explanations given to us, except for the possible effects of the matter described in the Basis for Qualified Opinion paragraph, the Financial Statements give the information required by the Act in the manner so required and give a true and fair view in conformity with the accounting principles generally accepted in India:

- (a) In the case of the Balance Sheet, of the state of affairs of the Company as at March 31, 20XX;
- (b) In the case of the Statement of Profit and Loss , of the profit/ loss for the year ended on that date; and
- (c) In the case of the Cash Flow Statement, of the cash flows fo r the year ended on that date.

Case-3

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. A disclaimer of Audit opinion is given in the circumstances.

Basis for disclaimer of opinion

We were appointed as Auditors of the Company after March 31, 20XX and thus could not observe the counting of physical inventories at the beginning and end of the year. Accordingly, we were unable to satisfy ourselves by alternative means concerning the inventory quantities held at December 31, 20X0 and March 31, 20X1 which are stated in the Balance Sheet at Rs. XXX and Rs. 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 Rs. XXX as at March 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 Statement of Profit and Loss 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.



PRACTICE PROBLEMS

Q.7. The Auditor disagreed with the management with regard to the acceptability of the Accounting policies and the inadequacy of disclosures in the Financial Statements and issued a disclaimer.

False. The Auditor is wrong in issuing a disclaimer. According to SA-705, If the Auditor disagrees with the management in the matters relating to the acceptability of Accounting policies selected and inadequacy of the disclosures in the Financial Statements, he should issue a qualified report or express an adverse opinion.

Q.8. Distinction between Qualified Report and Adverse Report.

A qualified opinion should be expressed when the Auditor concludes that, an unqualified opinion cannot be expressed but that the effect of any disagreement with management is not so material and pervasive as to require an adverse opinion, or limitation on scope is not so material and pervasive as to require a disclaimer of opinion. An adverse opinion should be expressed. In a qualified report, the Auditor's reservation is generally written as "subject to or except for, we report that the Balance sheet shows a true and fair view" Whereas in case of an adverse report, the Auditor states that "the Financial Statements do not present a true and fair view of the state of affairs and working result "

Q.9. State briefly the circumstance when an Auditor issues a disclaimer of opinion.

The Auditor can express a disclaimer of opinion when the possible effect of a limitation on scope of the Auditor's work is so material and pervasive that he has not been able to obtain sufficient and appropriate evidence and is accordingly unable to express an opinion on the Financial Statement. For example, when the Books of Accounts of the Auditee, Company have been seized by Income Tax/Excise authority, the Auditor will be unable to express his opinion on the Financial Statements. A scope of limitation may be imposed by circumstances, For Example, when the timing of the Auditor's appointment is such that he is unable to observe the counting of physical inventories. It may also arise when in the opinion of the Auditor the entity's accounting records are inadequate or when the Auditor is unable to carry out an Audit procedure believed to be desirable. When there is a limitation on the scope of the Auditor's work that requires disclaimer of opinion, the Auditor's report should describe the limitation and indicate the possible adjustment to the Financial Statements that might have been determined to be necessary had the limitation not existed.

THIS SA IN EXAM

Q.10. XYZ Ltd has significant operations in a foreign country. Due to civil and political unrest in that country physical verification of inventory and fixed assets could not be carried out and you are not in a position to obtain Audit Evidence through other Audit procedures also. The value of fixed assets and inventory forms part of 80% of the asset value of the company. As the Auditor of XYZ Ltd what factors do you consider in your reporting responsibility. Also draft a suitable report that will be incorporated in the main Audit report

As per SA-501 “Audit Evidence-Specific Considerations for Selected Items”, if attendance at physical inventory counting is impracticable, the Auditor shall perform alternative Audit procedures to obtain sufficient appropriate Audit Evidence regarding the existence and condition of inventory. If it is not possible to do so, the Auditor shall modify the opinion in the Auditor’s report in accordance with SA 705. In the given case, the Auditor has to modify his report by issuing a **DISCLAIMER** of opinion because Auditor is unable to obtain sufficient and appropriate Audit Evidence that the Financial Statements are free from material Misstatement and the matter is **MATERIAL AND PERVASIVE**. Hence Following factors are to be considered in Auditor’s reporting responsibility:

- ◆ Inventories and the Fixed Assets are material and **PERVASIVE** to the Financial Statements
- ◆ Auditor is unable to attend physical verification of the inventories and fixed assets In other words, physical verification becomes impracticable due to civil and political unrest in the foreign country, where the inventory and fixed assets are located, posing threats to the safety of Auditor.
- ◆ Auditor failed to obtain proper and sufficient Audit Evidence, even by alternative Audit procedures. Draft of the suitable report to be incorporated in the main Audit report:

AUDITORS RESPONSIBILITY PARA

Our responsibility is to express an opinion on these Financial Statements based on our Audit in accordance with the Standards on Auditing issued by the Institute of Chartered Accountants of India. 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 PARA

We were appointed as Auditors of the Company and we report that we could not observe the counting of physical inventories and physical verification of fixed assets due to civil and political unrest in foreign country where the company has significant operation. We were also unable to satisfy ourselves by alternative means concerning the inventory quantities and fixed assets of the company held at March 31st 20XX, which are stated in the Balance Sheet at ` XXX and ` XXX, respectively.

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

As required by section 143 (3) of the Companies Act, 2013, we report that: As described in the Basis for Disclaimer of Opinion paragraph, we were unable to obtain all the information and explanations which to the best of our knowledge and belief were necessary for the purpose of our Audit.

Q.11. Under the applicable Standards on Auditing, in what circumstances does the report of the statutory Auditor require modification? What are the types of modifications possible to the said report? (Nov 12/ 6 Marks)

Hint The Auditor shall modify the opinion in the Auditor's report when:

- ◆ The Auditor concludes that, based on the Audit Evidence obtained, the Financial Statements as a whole are not free from material Misstatement; or
- ◆ The Auditor is unable to obtain sufficient appropriate Audit Evidence to conclude that the Financial Statements as a whole are free from material Misstatement.

According to SA-705, following are the type of Modification to the Auditor's opinion:

- ◆ Qualified Opinion.
- ◆ Disclaimer of Opinion.
- ◆ Adverse Opinion.

Following are the circumstances raise modification in opinion

- ◆ The Auditor shall express a qualified opinion when:
 - 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
 - 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, could be material but not pervasive.
- ◆ 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.
- ◆ The Auditor shall disclaim an opinion 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, could be both material and pervasive.



Chapter 36

SA-706

SA-706-Emphasis of Matter Paragraphs & Other Matter Paragraphs In The Independent Auditor's Report - [Effective Date 01.04.2018]

Q.1. Why This SA ?

This Standard on Auditing (SA) deals with additional communication in the auditor's report when the auditor considers it necessary to:

- Draw users' attention to a matter or matters presented or disclosed in the financial statements that are of such importance that they are fundamental to users' understanding of the financial statements; or
- Draw users' attention to any matter or matters other than those presented or disclosed in the financial statements that are relevant to users' understanding of the audit, the auditor's responsibilities or the auditor's report.

Q.2. What do you mean by Emphasis of the Matter Para? What considerations are required while including such para in the report?

As per this SA – Emphasis of Matter para means - A paragraph included in the auditor's report that refers to a matter appropriately presented or disclosed in the financial statements that, in the auditor's judgment, is of such importance that it is fundamental to users' understanding of the financial statements.

The auditor would not be required to modify the opinion in accordance with SA 705 (Revised)³ as a result of the matter; and

When SA 701 applies, the matter has not been determined to be a key audit matter to be communicated in the auditor's report.

Examples:-

- An uncertainty relating to the future outcome of exceptional litigation or regulatory action.
- A significant subsequent event that occurs between the date of the financial statements and the date of the auditor's report.⁶
- Early application (where permitted) of a new accounting standard that has a material effect on the financial statements.

- A major catastrophe that has had, or continues to have, a significant effect on the entity's financial position.

Considerations:-

When the auditor includes an Emphasis of Matter paragraph in the auditor's report, the auditor shall:

- Include the paragraph within a separate section of the auditor's report with an appropriate heading that includes the term "Emphasis of Matter";
- Include in the paragraph a clear reference to the matter being emphasized and to where relevant disclosures that fully describe the matter can be found in the financial statements. The paragraph shall refer only to information presented or disclosed in the financial statements; and
- Indicate that the auditor's opinion is not modified in respect of the matter emphasized.

Illustration:-

Emphasis of Matter

We draw attention to Note X of the financial statements, which describes the effects of a fire in the Company's production facilities. Our opinion is not modified in respect of this matter.

Q.3. What do you mean by emphasis of other matter para and what considerations are required while including such para in the report?

This SA that Other Matter paragraph – A paragraph included in the auditor's report that refers to a matter other than those presented or disclosed in the financial statements that, in the auditor's judgment, is relevant to users' understanding of the audit, the auditor's responsibilities or the auditor's report. The auditor shall include an Other Matter paragraph in the auditor's report, provided:

This is not prohibited by law or regulation; and

- When SA 701 applies, the matter has not been determined to be a key audit matter to be communicated in the auditor's report.
- When the auditor includes an Other Matter paragraph in the auditor's report, the auditor shall include the paragraph within a separate section with the heading "Other Matter," or other appropriate heading.

Illustration:-

Other Matter

The financial statements of ABC Company for the year ended March 31, 20X0, were audited by another auditor who expressed an unmodified opinion on those statements on March 31, 20X1.

Q.4. Is there any duty to communicate to those charged with governance about such matter?

If the auditor expects to include an Emphasis of Matter or an Other Matter paragraph in the auditor's report, the auditor shall communicate with those charged with governance regarding this expectation and the wording of this paragraph.



THIS SA IN EXAM

Q.5. Beta Limited, is a company registered with SEBI, having five subsidiaries. M/s XYZ, Chartered Accountants, have been appointed as Statutory Auditors for the Audit of the Consolidated Financial Statements for the year ending March 31, 2013. Out of five subsidiaries, the Audit of one subsidiary was conducted by another Auditor, M/s Badnam and Company, Chartered Accountants. The "Opinion" Para of Audit report furnished by M/s XYZ Chartered Accountants is given below: In our opinion and to the best of our information and according to the explanations given to us the consolidated Financial Statements give a true and fair view, except the Financial Statement of one subsidiary whose accounts were Audited by M/s Badnam and Company, Chartered Accountants and about the same we are not in a position to express our opinion as the Audit has not been performed by us:

- (a) In the case of the consolidated Balance Sheet, of the state of affairs of the Company as at March 31, 2013.**
- (b) In the case of the consolidated Statement of Profit and Loss, of the profit/loss for the year ended on that date.**

Do you find any deficiencies in the opinion Para? If yes, you are required to give your suggestions and Redraft the opinion Para.(Nov 13/ 5 Marks)

Yes, the opinion Para contains the following deficiencies.

- ◆ Out of five subsidiaries, the Audit of one subsidiary was conducted by another Auditor, M/s Badnam and Company which would be reported in other matter Para.
- ◆ After point no. (i) in the opinion Para, point no. (i) would appear as under- "in the case of the consolidated Cash Flow Statement, of the cash flows for the year ended on that date."

The redrafted opinion Para and other matter Para are given hereunder as per SA 706 on Emphasis of Matter Paragraphs and Other Matter Paragraphs in the Independent Auditor's Report-

Opinion Para: In our opinion and to the best of our information and according to the explanations given to us and based on the consideration of the reports of the other Auditors on the Financial Statements of the subsidiaries as noted below, the consolidated Financial Statements give a true and fair view in conformity with the accounting principles generally accepted in India:

- (a) In the case of the consolidated balance Sheet, of the state of affairs of the Company as at March 31, 2013;
- (b) In the case of the consolidated Statement of Profit and Loss, of the profit/ loss for the Year ended on that date; and
- (c) In the case of the consolidated Cash Flow Statement, of the cash flows for the year Ended on that date.

Other Matter Para: We did not Audit the Financial Statements of one subsidiary, whose Financial Statements reflect total assets (net) of ` XXXX as at March 31, 2013, total revenues of ` XXXX and net cash outflows amounting to XXXX for the year then ended. These Financial Statements have been Audited by other Auditors M/s Badnam and Company, Chartered Accountants whose reports have been furnished to us by the Management, and our opinion is based solely on the reports of the other Auditors. Our opinion is not qualified in respect of this matter.

Q.6. Give an illustration of an Audit Report containing 'Emphasis of Matter' for a significant uncertainty? (Nov 09/ 8 Marks)

An Illustration of an Audit Report containing emphasis of matter paragraph for a significant uncertainty.

- ◆ An illustration of an emphasis of matter paragraph for a significant uncertainty in an Auditor's report is as follows:

Opinion

In our opinion -

In our opinion and to the best of our information and according to the explanation given to us, the Financial Statements give a true and fair view in conformity with the accounting principles generally accepted in India:

- In the case of the Balance Sheet, of the State of affairs of ----- as on 31 March 2xxxx and
- In the case of the statement of profit and loss, of the profit/loss for the year ended on that date.

"Emphasis of Matter"

"Without qualifying our opinion, we draw attention to Note X of Schedule to the Financial Statements. The entity is the defendant in a lawsuit alleging infringements of certain patent rights and claiming royalties and punitive damages. The entity has filed a counter action, and preliminary hearings and discovery proceedings on both actions are in progress. The ultimate outcome of the matter cannot presently be determined, and no provision for any liability, that may result, has been made in the financial statements.

- The addition of a paragraph, emphasizing a going concern problem or significant uncertainty is ordinarily adequate to meet the Auditor's reporting responsibilities regarding such matters. However, in extreme cases, such as situations involving multiple uncertainties that are significant to the Financial Statements, the Auditor may consider it appropriate to express a disclaimer of opinion instead of adding an emphasis of matter paragraph.

Q.7. Emphasis of matter paragraph in Audit Reports? (MAY, 2008 - 4 Marks)

Hint: Q.2

