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Auditing Standard ASA 510 *Initial Audit Engagements— Opening Balances*

Issued by the **Auditing and Assurance Standards Board**

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Australian Government

Auditing and Assurance Standards Board

Obtaining a Copy of this Auditing Standard

This proposed Auditing Standard is available on the Auditing and Assurance Standards Board (AUASB) website: www.auasb.gov.au.

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PREFACE

Reasons for Issuing Auditing Standard ASA 510 ***Initial Audit Engagements—Opening Balances***

The Auditing and Assurance Standards Board (AUASB) issues Auditing Standard ASA 510 *Initial Audit Engagements—Opening Balances* pursuant to the requirements of the legislative provisions and the Strategic Direction explained below.

The AUASB is an independent statutory board of the Australian Government established under section 227A of the *Australian Securities and Investments Commission Act 2001*, as amended (ASIC Act). Under section 336 of the *Corporations Act 2001*, the AUASB may make Australian Auditing Standards for the purposes of the corporations legislation. These Auditing Standards are legislative instruments under the *Legislative Instruments Act 2003*.

Under the Strategic Direction given to the AUASB by the Financial Reporting Council (FRC), the AUASB is required to have regard to any programme initiated by the International Auditing and Assurance Standards Board (IAASB) for the revision and enhancement of the International Standards on Auditing (ISAs) and to make appropriate consequential amendments to the Australian Auditing Standards. Accordingly, the AUASB has decided to revise and redraft the Australian Auditing Standards using the equivalent redrafted ISAs.

Main Features

This Auditing Standard establishes Requirements and provides Application and Other Explanatory Material regarding the independent auditor's responsibilities relating to opening balances in an initial audit engagement.

This Auditing Standard:

- (a) Establishes Requirements and provides guidance regarding opening balances when the financial report for the prior period was not audited, or the financial report for the prior period was audited by a predecessor auditor;
- (b) Provides audit procedures for the auditor to obtain audit evidence about:
 - whether the opening balances contain misstatements;
 - whether the accounting policies reflected in the opening balances have been consistently applied in the current period's financial report; and
 - whether changes in the accounting policies have been properly accounted for and adequately presented and disclosed; and
- (c) Establishes Requirements and provides guidance on audit conclusions and the auditor's report.

AUTHORITY STATEMENT

The Auditing and Assurance Standards Board (AUASB) makes this Auditing Standard ASA 510 *Initial Audit Engagements—Opening Balances* pursuant to section 227B of the *Australian Securities and Investments Commission Act 2001* and section 336 of the *Corporations Act 2001*.

This Auditing Standard is to be read in conjunction with ASA 101 *Preamble to Australian Auditing Standards*, which sets out the intentions of the AUASB on how the Australian Auditing Standards, operative for financial reporting periods commencing on or after 1 January 2010, are to be understood, interpreted and applied. This Auditing Standard is to be read also in conjunction with ASA 200 *Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with Australian Auditing Standards*.

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Initial Audit Engagements—Opening Balances

Application

- Aus 0.1 This Auditing Standard applies to:
- (a) an audit of a financial report for a financial year, or an audit of a financial report for a half-year, in accordance with the *Corporations Act 2001*; and
 - (b) an audit of a financial report, or a complete set of financial statements, for any other purpose.
- Aus 0.2 This Auditing Standard also applies, as appropriate, to an audit of other historical financial information.

Operative Date

- Aus 0.3 This Auditing Standard is operative for financial reporting periods commencing on or after 1 January 2010.

Introduction

Scope of this Auditing Standard

1. This Auditing Standard deals with the auditor's responsibilities relating to opening balances in an initial audit engagement. In addition to financial statement amounts, opening balances include matters requiring disclosure that existed at the beginning of the period, such as contingencies and commitments. When the financial report includes comparative financial information, the requirements and guidance in ASA 710¹ also apply. ASA 300² includes additional requirements and guidance regarding activities prior to starting an initial audit.

¹ See ASA 710 *Comparative Information—Corresponding Figures and Comparative Financial Reports*.

² See ASA 300 *Planning an Audit of a Financial Report*.

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Effective Date

2. [Deleted by the AUASB. Refer Aus 0.3]

Objective

3. In conducting an initial audit engagement, the objective of the auditor is to obtain sufficient appropriate audit evidence about whether:
- (a) Opening balances contain misstatements that materially affect the current period's financial report; and
 - (b) Appropriate accounting policies reflected in the opening balances have been consistently applied in the current period's financial report, or changes thereto are appropriately accounted for and adequately presented and disclosed in accordance with the applicable financial reporting framework.

Definitions

4. For the purposes of the Australian Auditing Standards, the following terms have the meanings attributed below:
- (a) Initial audit engagement means an engagement in which either:
 - (i) The financial report for the prior period was not audited; or
 - (ii) The financial report for the prior period was audited by a predecessor auditor.
 - (b) Opening balances means those account balances that exist at the beginning of the period. Opening balances are based upon the closing balances of the prior period and reflect the effects of transactions and events of prior periods and accounting policies applied in the prior period. Opening balances also include matters requiring disclosure that existed at the beginning of the period, such as contingencies and commitments.

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- (c) Predecessor auditor means the auditor from a different audit firm, who audited the financial report of an entity in the prior period and who has been replaced by the current auditor.

Requirements

Audit Procedures

Opening Balances

- 5. The auditor shall read the most recent financial report, if any, and the predecessor auditor's report thereon, if any, for information relevant to opening balances, including disclosures.
- 6. The auditor shall obtain sufficient appropriate audit evidence about whether the opening balances contain misstatements that materially affect the current period's financial report by: (Ref: Para. A1–A2)
 - (a) Determining whether the prior period's closing balances have been correctly brought forward to the current period or, when appropriate, have been restated;
 - (b) Determining whether the opening balances reflect the application of appropriate accounting policies; and
 - (c) Performing one or more of the following: (Ref: Para. A3–A7)
 - (i) Where the prior year financial report was audited, reviewing the predecessor auditor's working papers to obtain evidence regarding the opening balances;
 - (ii) Evaluating whether audit procedures performed in the current period provide evidence relevant to the opening balances; or
 - (iii) Performing specific audit procedures to obtain evidence regarding the opening balances.
- 7. If the auditor obtains audit evidence that the opening balances contain misstatements that could materially affect the current period's financial report, the auditor shall perform such additional audit procedures as are appropriate in the circumstances to determine the effect on the current period's financial report. If the

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auditor concludes that such misstatements exist in the current period's financial report, the auditor shall communicate the misstatements with the appropriate level of management and those charged with governance in accordance with ASA 450.³

Consistency of Accounting Policies

8. The auditor shall obtain sufficient appropriate audit evidence about whether the accounting policies reflected in the opening balances have been consistently applied in the current period's financial report, and whether changes in the accounting policies have been appropriately accounted for and adequately presented and disclosed in accordance with the applicable financial reporting framework.

Relevant Information in the Predecessor Auditor's Report

9. If the prior period's financial report was audited by a predecessor auditor and there was a modification to the opinion, the auditor shall evaluate the effect of the matter giving rise to the modification in assessing the risks of material misstatement in the current period's financial report in accordance with ASA 315.⁴

Audit Conclusions and Reporting

Opening Balances

10. If the auditor is unable to obtain sufficient appropriate audit evidence regarding the opening balances, the auditor shall express a qualified opinion or disclaim an opinion on the financial report, as appropriate, in accordance with ASA 705.⁵ (Ref: Para. A8)
11. If the auditor concludes that the opening balances contain a misstatement that materially affects the current period's financial report, and the effect of the misstatement is not appropriately accounted for or not adequately presented or disclosed, the auditor shall express a qualified opinion or an adverse opinion, as appropriate, in accordance with ASA 705.

³ See ASA 450 *Evaluation of Misstatements Identified during the Audit*, paragraphs 8 and 12.

⁴ See ASA 315 *Identifying and Assessing the Risks of Material Misstatement through Understanding the Entity and Its Environment*.

⁵ See ASA 705 *Modifications to the Opinion in the Independent Auditor's Report*.

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Consistency of Accounting Policies

12. If the auditor concludes that:
- (a) the current period's accounting policies are not consistently applied in relation to opening balances in accordance with the applicable financial reporting framework; or
 - (b) a change in accounting policies is not appropriately accounted for or not adequately presented or disclosed in accordance with the applicable financial reporting framework,
- the auditor shall express a qualified opinion or an adverse opinion as appropriate in accordance with ASA 705.

Modification to the Opinion in the Predecessor Auditor's Report

13. If the predecessor auditor's opinion regarding the prior period's financial report included a modification to the auditor's opinion that remains relevant and material to the current period's financial report, the auditor shall modify the auditor's opinion on the current period's financial report in accordance with ASA 705 and ASA 710.
(Ref: Para. A9)

* * *

Application and Other Explanatory Material

Audit Procedures

Considerations Specific to Public Sector Entities (Ref: Para. 6)

- A1. In the public sector, there may be legal or regulatory limitations on the information that the current auditor can obtain from a predecessor auditor. For example, if a public sector entity that has previously been audited by a statutorily appointed auditor (for example, an Auditor General, or other suitably qualified person appointed on behalf of the Auditor General) is privatised, the amount of access to working papers or other information that the statutorily appointed auditor can provide a newly appointed auditor that is in the private sector may be constrained by privacy laws or regulations. In situations where such communications are constrained, audit evidence may need to be obtained through other means and, if sufficient appropriate audit evidence cannot be obtained, consideration given to the effect on the auditor's opinion.
- A2. If the statutorily appointed auditor outsources an audit of a public sector entity to a private sector audit firm, and the statutorily appointed auditor appoints an audit firm other than the firm that audited the financial report of the public sector entity in the prior period, this is not usually regarded as a change in auditors for the statutorily appointed auditor. Depending on the nature of the outsourcing arrangement, however, the audit engagement may be considered an initial audit engagement from the perspective of the private sector auditor in fulfilling their responsibilities, and therefore this Auditing Standard applies.

Opening Balances (Ref: Para. 6(c))

- A3. The nature and extent of audit procedures necessary to obtain sufficient appropriate audit evidence regarding opening balances depend on such matters as:
- The accounting policies followed by the entity.
 - The nature of the account balances, classes of transactions and disclosures and the risks of material misstatement in the current period's financial report.
 - The significance of the opening balances relative to the current period's financial report.

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- Whether the prior period's financial report was audited and, if so, whether the predecessor auditor's opinion was modified.
- A4. If the prior period's financial report was audited by a predecessor auditor, the auditor may be able to obtain sufficient appropriate audit evidence regarding the opening balances by reviewing the predecessor auditor's working papers. Whether such a review provides sufficient appropriate audit evidence is influenced by the professional competence and independence of the predecessor auditor.
- A5. Relevant ethical and professional requirements* guide the current auditor's communications with the predecessor auditor.
- A6. For current assets and liabilities, some audit evidence about opening balances may be obtained as part of the current period's audit procedures. For example, the collection (payment) of opening accounts receivable (accounts payable) during the current period will provide some audit evidence of their existence, rights and obligations, completeness and valuation at the beginning of the period. In the case of inventories, however, the current period's audit procedures on the closing inventory balance provide little audit evidence regarding inventory on hand at the beginning of the period. Therefore, additional audit procedures may be necessary, and one or more of the following may provide sufficient appropriate audit evidence:
- Observing a current physical inventory count and reconciling it to the opening inventory quantities.
 - Performing audit procedures on the valuation of the opening inventory items.
 - Performing audit procedures on gross profit and cut-off.
- A7. For non-current assets and liabilities, such as property plant and equipment, investments and long-term debt, some audit evidence may be obtained by examining the accounting records and other information underlying the opening balances. In certain cases, the auditor may be able to obtain some audit evidence regarding opening balances through confirmation with third parties, for

* See APES 110 *Compiled Code of Ethics for Professional Accountants* issued by the Accounting Professional and Ethical Standards Board. **TO BE RESOLVED**

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example, for long-term debt and investments. In other cases, the auditor may need to carry out additional audit procedures.

Audit Conclusions and Reporting

Opening Balances (Ref: Para. 10)

A8. ASA 705 establishes requirements and provides guidance on circumstances that may result in a modification to the auditor's opinion on the financial report, the type of opinion appropriate in the circumstances, and the content of the auditor's report when the auditor's opinion is modified. The inability of the auditor to obtain sufficient appropriate audit evidence regarding opening balances may result in one of the following modifications to the opinion in the auditor's report:

- (a) A qualified opinion or a disclaimer of opinion, as is appropriate in the circumstances; or
- (b) Unless prohibited by law or regulation, an opinion which is qualified or disclaimed, as appropriate, regarding the results of operations, and cash flows, where relevant, and unmodified regarding financial position.

Appendix 1 includes illustrative auditors' reports.

Modification to the Opinion in the Predecessor Auditor's Report (Ref: Para. 13)

A9. In some situations, a modification to the predecessor auditor's opinion may not be relevant and material to the opinion on the current period's financial report. This may be the case where, for example, there was a scope limitation in the prior period, but the matter giving rise to the scope limitation has been resolved in the current period.

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Conformity with International Standards on Auditing

This Auditing Standard conforms with International Standard on Auditing ISA 510 *Initial Audit Engagements—Opening Balances*, issued by the International Auditing and Assurance Standards Board (IAASB), an independent standard-setting board of the International Federation of Accountants (IFAC).

Paragraphs that have been added to this Auditing Standard (and do not appear in the text of the equivalent ISA) are identified with the prefix “Aus”.

Compliance with this Auditing Standard enables compliance with ISA510.

Draft

Appendix 1

(Ref: Para. A8)

Illustrations of Auditors' Reports with Modified Opinions

Illustration 1:

Circumstances described in paragraph A8(a) include the following:

- **The auditor did not observe the counting of the physical inventory at the beginning of the current period and was unable to obtain sufficient appropriate audit evidence regarding the opening balances of inventory.**
- **The possible effects of the inability to obtain sufficient appropriate audit evidence regarding opening balances of inventory are deemed to be material but not pervasive to the entity's financial performance and cash flows.⁶**
- **The financial position at year end is fairly presented.**
- **In this particular jurisdiction, law and regulation prohibit the auditor from giving an opinion which is qualified regarding the financial performance and cash flows and unmodified regarding financial position.**
- **The financial report is not prepared in accordance with the *Corporations Act 2001*.**

⁶ If the possible effects, in the auditor's judgement, are considered to be material and pervasive to the entity's financial performance and cash flows, the auditor would disclaim an opinion on the financial performance and cash flows.

Example Auditor’s Report
**Qualified Opinion—jurisdiction prohibits a qualified
opinion on performance and cash flows and an unmodified
opinion on financial position**

INDEPENDENT AUDITOR’S REPORT

[Appropriate Addressee]

Report on the Financial Report⁷

We have audited the accompanying financial report of ABC entity, which comprises the statement of financial position as at 30 June 20X1 and the statement of comprehensive income, statement of changes in equity and statement of cash flows for the year then ended, and notes comprising a summary of significant accounting policies and other explanatory information.

*Management’s*⁸ *Responsibility for the Financial Report*

Management is responsible for the preparation and fair presentation⁹ of the financial report in accordance with Australian Accounting Standards, and for such internal control as management determines is necessary to enable the preparation of the financial report that is free from material misstatement, whether due to fraud or error.

Auditor’s Responsibility

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

⁷ The sub-title “Report on the Financial Report” is unnecessary in circumstances when the second sub-title “Report on Other Legal and Regulatory Requirements” is not applicable.

⁸ Or other term that is appropriate in the context of the legal framework in the particular jurisdiction.

⁹ Where management’s responsibility is to prepare a financial report that give a true and fair view, this may read: “Management is responsible for the preparation of the financial report that gives a true and fair view in accordance with Australian Accounting Standards, and for such ...”

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An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial report. The procedures selected depend on the auditor's judgement, including the assessment of the risks of material misstatement of the financial report, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation¹⁰ of the financial report 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.¹¹ An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial report.

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

Basis for Qualified Opinion

We were appointed as auditors of the company on 31 December 20X0 and thus did not observe the counting of the physical inventories at the beginning of the year. We were unable to satisfy ourselves by alternative means concerning inventory quantities held at 30 June 20X0. Since opening inventories enter into the determination of the financial performance and cash flows, we were unable to determine whether adjustments might have been necessary in respect of the income for the year reported in the statement of comprehensive income and the net cash flows from operating activities reported in the statement of cash flows.

Qualified Opinion

In our opinion, except for the possible effects of the matter described in the Basis for Qualified Opinion paragraph, the financial report presents fairly, in all material respects, (or "gives a true and fair view of") the financial position

¹⁰ In the case of footnote 9, this may read: "In making those risk assessments, the auditor considers internal control relevant to the entity's preparation of the financial report that gives a true and fair view in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control."

¹¹ In circumstances when the auditor also has responsibility to express an opinion on the effectiveness of internal control in conjunction with the audit of the financial report, this sentence would be worded as follows: "In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial report in order to design audit procedures that are appropriate in the circumstances." In the case of footnote 9, this may read: "In making those risk assessments, the auditor considers internal control relevant to the entity's preparation of the financial report that gives a true and fair view in order to design audit procedures that are appropriate in the circumstances."

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of ABC entity as at 30 June 20X1 and (of) its financial performance and its cash flows for the year then ended in accordance with Australian Accounting Standards.

Other Matter

The financial report of ABC entity for the year ended 30 June 20X0 was audited by another auditor who expressed an unmodified opinion on the financial report on 30 September 20X0.

Report on Other Legal and Regulatory Requirements

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

[Auditor's signature]

[Date of the auditor's report]

[Auditor's address]

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Illustration 2:

Circumstances described in paragraph A8(b) include the following:

- **The auditor did not observe the counting of the physical inventory at the beginning of the current period and was unable to obtain sufficient appropriate audit evidence regarding the opening balances of inventory.**
- **The possible effects of the inability to obtain sufficient appropriate audit evidence regarding opening balances of inventory are deemed to be material but not pervasive to the entity's financial performance and cash flows.¹²**
- **The financial position at year end is fairly presented.**
- **An opinion that is qualified regarding the financial performance and cash flows and unmodified regarding financial position is considered appropriate in the circumstances.**
- **The financial report is not prepared in accordance with the *Corporations Act 2001*.**

¹² If the possible effects, in the auditor's judgement, are considered to be material and pervasive to the entity's financial performance and cash flows, the auditor would disclaim the opinion on the financial performance and cash flows.

Example Auditor’s Report
Qualified Opinion—jurisdiction permits a qualified opinion
on performance and cash flows and an unmodified opinion
on financial position

INDEPENDENT AUDITOR’S REPORT

[Appropriate Addressee]

Report on the Financial Report¹³

We have audited the accompanying financial report of ABC entity, which comprises the statement of financial position as at 30 June 20X1 and the statement of comprehensive income, statement of changes in equity and statement of cash flows for the year then ended, and notes comprising a summary of significant accounting policies and other explanatory information.

*Management’s*¹⁴ *Responsibility for the Financial Report*

Management is responsible for the preparation and fair presentation¹⁵ of the financial report in accordance with Australian Accounting Standards, and for such internal control as management determines is necessary to enable the preparation of the financial report that is free from material misstatement, whether due to fraud or error.

Auditor’s Responsibility

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

¹³ The sub-title “Report on the Financial Report” is unnecessary in circumstances when the second sub-title “Report on Other Legal and Regulatory Requirements” is not applicable.

¹⁴ Or other term that is appropriate in the context of the legal framework in the particular jurisdiction.

¹⁵ Where management’s responsibility is to prepare a financial report that gives a true and fair view, this may read: “Management is responsible for the preparation of the financial report that gives a true and fair view in accordance with Australian Accounting Standards, and for such ...”

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An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial report. The procedures selected depend on the auditor's judgement, including the assessment of the risks of material misstatement of the financial report, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation¹⁶ of the financial report 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.¹⁷ An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial report.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our unmodified opinion on the financial position and our qualified audit opinion on the financial performance and cash flows.

Basis for Qualified Opinion on the Financial Performance and Cash Flows

We were appointed as auditors of the company on 31 December 20X0 and thus did not observe the counting of the physical inventories at the beginning of the year. We were unable to satisfy ourselves by alternative means concerning inventory quantities held at 30 June 20X0. Since opening inventories enter into the determination of the financial performance and cash flows, we were unable to determine whether adjustments might have been necessary in respect of the profit for the year reported in the statement of comprehensive income and the net cash flows from operating activities reported in the statement of cash flows.

¹⁶ In the case of footnote 15, this may read: "In making those risk assessments, the auditor considers internal control relevant to the entity's preparation of the financial report that gives a true and fair view in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control."

¹⁷ In circumstances when the auditor also has responsibility to express an opinion on the effectiveness of internal control in conjunction with the audit of the financial report, this sentence would be worded as follows: "In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial report in order to design audit procedures that are appropriate in the circumstances." In the case of footnote 15, this may read: "In making those risk assessments, the auditor considers internal control relevant to the entity's preparation of the financial report that gives a true and fair view in order to design audit procedures that are appropriate in the circumstances."

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Qualified Opinion on the Financial Performance and Cash Flows

In our opinion, except for the possible effects of the matter described in the Basis for Qualified Opinion paragraph, the Statement of Comprehensive Income and Statement of Cash Flows present fairly, in all material respects (or “give a true and fair view of”) the financial performance and cash flows of ABC entity for the year ended 30 June 20X1 in accordance with Australian Accounting Standards.

Opinion on the Financial Position

In our opinion, the Statement of Financial Position presents fairly, in all material respects (or “gives a true and fair view of) the financial position of ABC entity as at 30 June 20X1 in accordance with Australian Accounting Standards.

Other Matter

The financial report of ABC entity for the year ended 30 June 20X0 was audited by another auditor who expressed an unmodified opinion on the financial report dated 30 September 20X0.

Report on Other Legal and Regulatory Requirements

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

[Auditor’s signature]

[Date of the auditor’s report]

[Auditor’s address]