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Explanatory Guide: *Opening Balances*

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

Draft

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Auditing and Assurance Standards Board

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Explanatory Guide: *Opening Balances*

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This Explanatory Guide:

1. Is not an AUASB Guidance Statement that provides guidance to assist auditors and assurance practitioners to fulfil the objectives of the audit or assurance engagement; and
2. Does not itself establish or extend requirements for the performance of audit, review, or other assurance engagements under the AUASB Standards.

Disclaimer:

Explanatory Guide: *Opening Balances* has been developed by the Auditing and Assurance Standards Board to provide information to auditors who are required under the Australian Auditing Standards to modify their audit opinions in relation to opening balances. No responsibility is taken for the results of actions or omissions to act on the basis of any information contained in this document or for any errors or omissions in it.

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EXPLANATORY GUIDE

Opening Balances

Purpose

1. The purpose of this explanatory guide is to provide information to auditors who are required under the Australian Auditing Standards to modify their audit opinions in relation to opening balances in an initial audit engagement.

Introduction

2. The information in this explanatory guide relates primarily to reporting under ASA 510 *Initial Audit Engagements – Opening Balances* and ASA 705 *Modifications to the Opinion in an Independent Auditor’s Report*. Reference is also made to ASA 710 *Comparative Information–Corresponding Figures and Comparative Financial Reports*.
3. In performing an initial audit engagement, it is not uncommon for the auditor to be faced with difficulties in obtaining sufficient appropriate audit evidence in relation to opening balances. Such difficulties may be due to the following circumstances:
 - (a) The auditor was appointed after the commencement of the current financial reporting period and accordingly was unable to attend the physical counting of inventory or other assets.
 - (b) The prior financial reporting period was not audited.
 - (c) The prior financial reporting period was audited and the predecessor auditor:
 - (i) Qualified the opinion.
 - (ii) Issued an adverse opinion.
 - (iii) Disclaimed an opinion.
 - (d) The predecessor auditor does not, or cannot, provide access to the audit working papers for the previous reporting period.

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- (e) The auditor cannot obtain sufficient appropriate audit evidence through:
 - (i) audit procedures performed in the current year; or
 - (ii) specific procedures designed to obtain audit evidence regarding opening balances.
- 4. In the circumstances listed in paragraph 3 above, the auditor is required to determine the effect that the issue has on the current period financial report.
- 5. It is important to emphasise that:
 - (a) The current period audit engagement does not extend to an *audit* (per se) of opening balances or comparative figures. The current period audit engagement is to form, and express, an opinion on:
 - (i) the performance for the current period; and
 - (ii) the financial position at the end of the current financial reporting period.
 - (b) The overall objectives of the auditor include obtaining reasonable assurance about whether the financial report as a whole is free from material misstatement. That includes whether the opening balances contain misstatements that materially affect the current period's financial report.

Background

- 6. The term “split opinion” relates only to opening balances in an initial audit engagement and refers to the format of the auditor's report where the opinion is expressed in two separate opinion paragraphs, namely:
 - (a) An opinion which is qualified or disclaimed, as appropriate, regarding the results of operations, and cash flows, where relevant; and
 - (b) An unmodified opinion regarding the financial position.
- 7. The (implicit) purpose of a split-opinion format is to help readers of the auditor's report to understand that:

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- (a) the lack of sufficient appropriate audit evidence over opening balances affects only the current period financial performance statements (profit and loss and cash flows); and
 - (b) the auditor has obtained sufficient appropriate evidence over the financial position statement (period end balance sheet) to express an unmodified opinion on that period end balance sheet.
8. Prior to the current clarity versions of both the International Standards on Auditing (ISAs) and the equivalent Australian Auditing Standards, split-opinion formats were referred to in the requirements and guidance of the auditing standards.
9. The current clarity version of the ISAs refers to split-opinion formats only in the application and other explanatory material and appendices.
10. The equivalent Australian standards do not refer to split-opinion formats on the basis that single form opinion paragraphs:
- (a) provides a concise expression of opinion, or disclaimer of opinion, on the financial report as a whole;
 - (b) provides the reader with the same information as in a split-opinion format;
 - (c) avoids potential inconsistencies in interpreting the requirements of other Auditing Standards and the *Corporations Act 2001* (the Act); and
 - (d) avoids unnecessary reporting complexity and potential inconsistent application when the auditor is faced with a wide range of circumstances such as:
 - (i) differing underlying reasons for insufficient or inappropriate audit evidence regarding opening balances; and
 - (ii) how to report when modifying the opinion on both opening balances and current period balances.

Fundamental Audit Requirements

11. Under ASA 510 paragraph 6:

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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:

- (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** (emphasis added)*
 - (c) *Performing one or more of the following:*
 - (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.*
12. When the auditor is unable to obtain sufficient appropriate audit evidence as required by ASA 510 paragraph 6, a modified opinion or disclaimer of opinion in relation to the opening balances is issued.
13. When the opening balances have not been previously audited or the previous auditor has issued a disclaimer of opinion, the auditor is still required to comply with ASA 510 paragraph 6. The associated application and other explanatory material, especially from paragraphs A3 to A7, provides useful suggestions on the audit procedures an auditor may undertake.
14. It is incumbent on the auditor to exercise professional judgement and to explore all reasonable avenues in obtaining sufficient appropriate audit evidence as to whether the opening balances contain misstatements that materially affect the current period's financial report.
15. It is important to remember that all relevant requirements in the Auditing Standards are also to be complied with in conducting the initial engagement. It is not appropriate for an auditor to by-pass the

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requirements of the Auditing Standards and rely only on a modified opinion as sufficient compliance with the Auditing Standards.

Subsequent Audits

16. The audits of subsequent reporting periods are conducted in accordance with all relevant Auditing Standards.

Modifications to the Auditor's Opinion

17. The type of modification to the auditor's opinion under the Australian Auditing Standards (particularly ASA 705), is a direct result of the specific circumstances of the engagement and the audit procedures undertaken by the auditor.
18. Using the basic formats of a modified auditor's report under the Act (see examples in ASA 705), the appendices to this explanatory guide provide examples of audit reports relating to opening balances.
19. Example auditor's reports that are modified in regard to opening balances, are set out in the appendices as shown in the following table:

| Appendix 1 Qualified Opinion | |
|---|---|
| Example 1 | Previous auditor issued an unmodified opinion |
| Example 1.1 | Previous auditor issued a qualified opinion |
| Example 1.2 | No previous auditor |
| Appendix 2 Adverse Opinion | |
| Example 2 | Previous auditor issued an adverse opinion |
| Appendix 3 Disclaimer of Opinion | |
| Example 3 | Previous auditor issued a disclaimer of opinion |
| Example 3.1 | No previous auditor |

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20. Following each example report in the appendices, there is a brief description of the type of auditor's report that would ordinarily be issued in the subsequent reporting period (Year 2); and the supporting reason(s)/auditor work.

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Appendix 1

EXAMPLE 1: QUALIFIED OPINION

PERIOD 1: INITIAL ENGAGEMENT

Circumstances:

- Previous auditor issued an unmodified opinion.
- Auditor appointed *after* commencement of current reporting period.
- 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 report.
- With the exception of the matter described above, the financial report presents fairly.
- The auditor decides to refer to the previous auditor's report in an Other Matter paragraph (ASA 710 paragraph 13).
- The financial report is prepared under the *Corporations Act 2001*.

Audit Work Performed:

- Audit conducted in accordance with Auditing Standards. Opening balances audited in accordance with ASA 510. Sufficient appropriate audit evidence obtained with the exception of opening inventory quantities (see qualification).

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INDEPENDENT AUDITOR'S REPORT

[Appropriate Addressee]

Report on the Financial Report

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

Directors' Responsibility for the Financial Report

The directors of the company are responsible for the preparation of the financial report that gives a true and fair view in accordance with Australian Accounting Standards and the *Corporations Act 2001*, and for such internal control as the directors determine 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.

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 company'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 company's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by the directors, 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.

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Independence

In conducting our audit, we have complied with the independence requirements of the *Corporations Act 2001*. We confirm that the independence declaration required by the *Corporations Act 2001*, which has been given to the directors of ABC Company Ltd., would be in the same terms if given to the directors as at the time of this auditor's report.

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 of ABC Company Ltd. is in accordance with the *Corporations Act 2001*, including:

- (a) giving a true and fair view of the company's financial position as at 30 June 20X1 and of its performance for the year ended on that date; and
- (b) complying with Australian Accounting Standards and the *Corporations Regulations 2001*.

Other Matter

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

Report on the Remuneration Report

We have audited the Remuneration Report included in paragraphs a to b of the directors' report for the year ended 30 June 20X1. The directors of the company are responsible for the preparation and presentation of the Remuneration Report in accordance with section 300A of the *Corporations Act 2001*. Our responsibility is to express an opinion on the Remuneration

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Report, based on our audit conducted in accordance with Australian Auditing Standards.

Opinion

In our opinion the Remuneration Report of ABC Company Ltd. for the year ended 30 June 20X1, complies with section 300A of the *Corporations Act 2001*.

[Auditor's signature]

[Date of the auditor's report]

[Auditor's address]

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EXAMPLE 1 continued...

PERIOD 2: SUBSEQUENT ENGAGEMENT

Circumstances:

- The auditor did not observe the counting of the physical inventory at the beginning of the initial engagement [i.e. the *prior* period (Period 1)] and issued a qualified auditor's report. [See above]
- With this exception, the financial report for the initial engagement (Period 1) was fairly presented.
- No other matters required modification to the opinion.

Audit Work Performed:

- Audit of Period 2 conducted in accordance with Auditing Standards. Sufficient appropriate audit evidence obtained.
- Under ASA 510 and ASA 710 auditor determines if comparatives include a misstatement that affects the current period. As the auditor attended the inventory count at the end of Period 1, the auditor concludes that the basis for qualification in Period 1 does not result in an unacceptable risk of material misstatement in Period 2.

Period 2 Auditor's Report:

- Unmodified opinion.

EXAMPLE 1.1: QUALIFIED OPINION

PERIOD 1: INITIAL ENGAGEMENT

Circumstances:

- Same as in Example 1, however, previous auditor issued a qualified opinion - qualification *not* related to inventory.

Audit Work Performed:

- Audit conducted in accordance with Auditing Standards. Opening balances audited in accordance with ASA 510.
- Auditor obtains sufficient appropriate evidence to determine the effect, if any, that the matter causing the previous auditor to qualify has on the Period 1 (initial engagement) financial report.

Auditor's Report:

- If the matter causing the previous auditor to qualify is *not* resolved and the auditor determines that the matter affects the Period 1 financial performance or position, the auditor must decide (in accordance with ASA 705) whether to:
 - repeat the qualification; or
 - issue an adverse opinion or a disclaimer of opinion, depending on the circumstances and taking into consideration the additional qualification arising from non-attendance at the physical count of inventories.
- If the matter causing the previous auditor to qualify *is* resolved, the auditor qualifies only on non-attendance at the physical count of inventories (as per Example 1).
- The auditor considers inclusion of an emphasis of matter paragraph where the financial report contains disclosures of the resolution of the matter.

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EXAMPLE 1.1 continued...

PERIOD 2: SUBSEQUENT ENGAGEMENT

Audit Work Performed:

- Audit of Period 2 conducted in accordance with Auditing Standards. Sufficient appropriate audit evidence obtained.
- Under ASA 510 and ASA 710 auditor determines if comparatives include a misstatement that affects the current period. As the auditor attended the inventory count at the end of Period 1, the auditor concludes that the basis for qualification in Period 1 does not result in an unacceptable risk of material misstatement in Period 2.
- The auditor determines the status of the matter causing the previous auditor to qualify and which was *not* resolved in the initial engagement and resulted in a modification to the auditor's report in Period 1.

Period 2 Auditor's Report:

- Unmodified opinion; or
- Modified opinion under ASA 705 - dependent on the status of the unresolved matter(s) carried over from Period 1.

EXAMPLE 1.2: QUALIFIED OPINION

PERIOD 1: INITIAL ENGAGEMENT

Circumstances:

- Same as in Example 1, however, no previous audit.

Audit Work Performed:

- Audit conducted in accordance with Auditing Standards. Opening balances audited in accordance with ASA 510.
- In accordance with ASA 510 paragraph 6, the auditor obtains sufficient appropriate evidence to determine whether the opening balances contain misstatements that materially affect the current financial report.

Auditor's Report:

- The auditor performs procedures required by ASA 510 paragraph 6. If the auditor is unable to obtain sufficient appropriate audit evidence about an opening balance matter that the auditor considers to be material but not pervasive, the auditor issues a qualified opinion (as per Example 1 above).
- If the auditor obtains sufficient appropriate audit evidence, an unmodified opinion is issued.
- As the previous financial report was not audited, ASA 710 paragraph 14 requires the auditor to include an Other Matter paragraph stating that the corresponding figures are unaudited.

Appendix 2

EXAMPLE 2: ADVERSE OPINION

PERIOD 1: INITIAL ENGAGEMENT

Circumstances:

- Previous auditor issued an adverse opinion.
- The matter that caused the previous auditor to issue an adverse opinion remains unresolved.
- The auditor determines that the unresolved matter in the opening balances is a misstatement that materially affects the current period (Period 1) financial report.
- The auditor decides to refer to the previous auditor's report in an Other Matter paragraph (ASA 710 paragraph 13).
- The financial report is prepared under the *Corporations Act 2001*.

Audit Work Performed:

- Audit conducted in accordance with Auditing Standards. Opening balances audited in accordance with ASA 510. Sufficient appropriate audit evidence obtained to support the auditor's expression of an adverse opinion.

INDEPENDENT AUDITOR'S REPORT

[Appropriate Addressee]

Report on the Financial Report

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

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consolidated entity comprising the company and the entities it controlled at the year's end or from time to time during the financial year.

Directors' Responsibility for the Financial Report

The directors of the company are responsible for the preparation of the financial report that gives a true and fair view in accordance with Australian Accounting Standards and the *Corporations Act 2001* and for such internal control as the directors determine is necessary to enable the preparation of the financial report that gives a true and fair view and 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.

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 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 company's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by the directors, 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 adverse audit opinion.

Independence

In conducting our audit, we have complied with the independence requirements of the *Corporations Act 2001*. We confirm that the independence declaration required by the *Corporations Act 2001*, which has been given to the directors of ABC Company Ltd., would be in the same terms if given to the directors as at the time of this auditor's report.

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Basis for Adverse Opinion

As explained in Note X, the entity has not consolidated the financial statements of subsidiary XYZ Company it acquired during the previous financial year to 30 June 20X0, because it has not yet been able to ascertain the fair values of certain of the subsidiary's material assets and liabilities at the acquisition date. This investment is therefore accounted for on a cost basis. Under Australian Accounting Standards, the subsidiary should have been consolidated because it is controlled by the company. Had XYZ Company been consolidated, many elements in the accompanying financial report would have been materially affected. The effects on the financial report of the failure to consolidate have not been determined.

Adverse Opinion

In our opinion, because of the significance of the matter discussed in the Basis for Adverse Opinion paragraph, the financial report is not in accordance with the *Corporations Act 2001* including:

- (i) Giving a true and fair view of the company's and consolidated entity's financial positions as at 30 June 20X1 and of their performance for the year ended on that date; and
- (ii) Complying with Australian Accounting Standards and the *Corporations Regulations 2001*.

Other Matter

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

Report on the Remuneration Report

We have audited the Remuneration Report included in paragraphs a to b of the directors' report for the year ended 30 June 20X1. The directors of the company are responsible for the preparation and presentation of the Remuneration Report in accordance with section 300A of the *Corporations Act 2001*. Our responsibility is to express an opinion on the Remuneration Report, based on our audit conducted in accordance with Australian Auditing Standards.

Opinion

In our opinion the Remuneration Report of ABC Company Ltd. for the year ended 30 June 20X1, complies with section 300A of the *Corporations Act 2001*.

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[Auditor's signature]

[Date of the auditor's report]

[Auditor's address]

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EXAMPLE 2 continued...

PERIOD 2: SUBSEQUENT ENGAGEMENT

Audit Work Performed:

- The auditor determines the status of the matter causing the adverse opinion in the prior period.
- Audit of Period 2 conducted in accordance with Auditing Standards.

Period 2 Auditor's Report:

- If the matter causing the auditor to issue an adverse opinion in the previous period is *not* resolved, the auditor issues an adverse opinion.
- If the matter causing the auditor to issue an adverse opinion in Period 1 *is* resolved; and there are no other unresolved matters arising from the Period 2 audit, the auditor issues an unmodified opinion.
- The auditor considers including an emphasis of matter paragraph where the financial report contains disclosures of the resolution of the matter.

Appendix 3

EXAMPLE 3: *DISCLAIMER OF OPINION*

PERIOD 1: INITIAL ENGAGEMENT

Circumstances:

- Previous auditor issued a disclaimer of opinion. The reasons given were accidental loss of accounting records and difficulties with the completeness and accuracy of subsequent processing under a new accounting system.
- The possible effects of the inability to obtain sufficient appropriate audit evidence regarding opening balances are considered by the auditor to be material and pervasive to the entity's current financial report.
- Auditor unable to obtain sufficient appropriate audit evidence regarding the collectability of overseas debts.
- The auditor decides to refer to the previous auditor's report in an Other Matter paragraph (ASA 710 paragraph 13).
- The financial report is prepared under the *Corporations Act 2001*.

Audit Work Performed:

- Auditor engaged to, and, conducts an audit in accordance with Auditing Standards. Opening balances audited in accordance with ASA 510. Current year transactions and balances audited.
- Following ASA 510 paragraph 6 and determining the status of the matter(s) causing the disclaimer of opinion given by the previous auditor, the auditor applies professional judgement in endeavouring to obtain sufficient appropriate audit evidence as to whether the opening balances contain misstatements that materially affect the current period's financial report.
- Auditor's endeavours are unsuccessful and the auditor is therefore unable to obtain sufficient appropriate audit evidence on the opening balances.

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Auditor's Report:

- As the auditor is unable to obtain sufficient appropriate audit evidence over all, or a significant number of, opening balances, a disclaimer of opinion is appropriate.
- Under ASA 705 paragraph 21, even when the auditor has expressed a disclaimer of opinion, the auditor is required to describe the reasons for any other matter of which the auditor is aware that would have required a modification to the opinion. In this case, the auditor is unable to obtain sufficient appropriate audit evidence over the collectability of material export debts from customers in a country experiencing civil war.

INDEPENDENT AUDITOR'S REPORT

[Appropriate Addressee]

Report on the Financial Report

We were engaged to audit the accompanying financial report of ABC Company Ltd., which comprises the statement of financial position as at 30 June 20X1, the statement of comprehensive income, statement of changes in equity and statement of cash flows for the year then ended, notes comprising a summary of significant accounting policies and other explanatory information, and management's assertion statement.

The Directors' Responsibility for the Financial Report

The Directors are responsible for the preparation of the financial report that presents a true and fair view in accordance with Australian Accounting Standards and the *Corporations Act 2001* and for such internal control as the Directors 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 conducting the audit in accordance with Australian Auditing Standards. Because of the matter(s) described in the Basis for Disclaimer of Opinion paragraph, however, we were not able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion.

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Independence

In conducting our audit, we have complied with the independence requirements of the *Corporations Act 2001*. We confirm that the independence declaration required by the *Corporations Act 2001*, which has been given to the directors of ABC Company Ltd., would be in the same terms if given to the directors as at the time of this auditor's report.

Basis for Disclaimer of Opinion

Due to the accidental destruction of financial records and the subsequent introduction of a new computerised system in the previous financial year to 30 June 20X0, we were unable to obtain sufficient appropriate audit evidence in regard to opening balances. We were unable to satisfy ourselves by alternative means concerning a number of opening balances disclosed in the statements of financial performance and cash flows and the statement of financial position as at that date. Accordingly, we were unable to determine whether adjustments might have been necessary in respect of the financial performance, cash flows and financial position for the year to 30 June 20X1.

In addition, we were unable to obtain sufficient appropriate audit evidence regarding the collectability of export debts to customers in the Republic of XXXX, a country currently suffering from civil war. These debts are included in Trade Receivables at 30 June 20X1 in the amount of \$zzzzz. We were unable to determine whether any adjustments to these amounts were necessary.

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 report.

Other Matter

The financial report of ABC Company Ltd. for the year ended 30 June 20X0 was audited by another auditor who disclaimed an opinion on that financial report on 30 September 20X0.

Report on the Remuneration Report

We have audited the Remuneration Report included in paragraphs a to b of the directors' report for the year ended 30 June 20X1. The directors of the company are responsible for the preparation and presentation of the Remuneration Report in accordance with section 300A of the *Corporations Act 2001*. Our responsibility is to express an opinion on the Remuneration

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Report, based on our audit conducted in accordance with Australian Auditing Standards.

Opinion

In our opinion the Remuneration Report of ABC Company Ltd. for the year ended 30 June 20X1, complies with section 300A of the *Corporations Act 2001*.

[Auditor's signature]

[Date of the auditor's report]

[Auditor's address]

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EXAMPLE 3 continued...

PERIOD 2: SUBSEQUENT ENGAGEMENT

Audit Work Performed:

- The auditor determines the status of the matter(s) causing the disclaimer of opinion in the prior period.
- Audit of Period 2 conducted in accordance with Auditing Standards. In particular, if the auditor becomes aware of a possible misstatement in the comparative information while performing the current year audit, the auditor is required to obtain sufficient appropriate audit evidence to determine whether a material misstatement exists (ASA 710 paragraph 8).

Period 2 Auditor's Report:

- If the matters causing the auditor to issue a disclaimer of opinion in the previous period are *not* resolved, the auditor issues a disclaimer of opinion.
- If one of the matters causing the auditor to issue a disclaimer of opinion in Period 1 *is* resolved but the matter that would have resulted in a modification to the opinion (in this case, the collectability of overseas debts) remains, the auditor issues a modified opinion (in this case a *qualification* over the continuing issue of collectability of overseas debts).
- If the matters causing the auditor to issue a disclaimer of opinion in Period 1 *is* resolved; and there are no other unresolved matters arising from the Period 2 audit, the auditor issues an unmodified opinion.

EXAMPLE 3.1: *DISCLAIMER OF OPINION*

PERIOD 1: INITIAL ENGAGEMENT

Circumstances:

- No previous audit.
- The possible effects of the inability to obtain sufficient appropriate audit evidence regarding opening balances are considered by the auditor to be material and pervasive to the entity's financial report.
- The financial report is prepared under the *Corporations Act 2001*.

Audit Work Performed:

- Audit conducted in accordance with Auditing Standards. Opening balances audited in accordance with ASA 510. Current year transactions and balances audited.
- In accordance with ASA 510 paragraph 6, the auditor seeks to obtain sufficient appropriate evidence to determine whether the opening balances contain misstatements.
- The auditor applies professional judgement in endeavouring to obtain sufficient appropriate audit evidence as to whether the opening balances contain misstatements that materially affect the current period's financial report.
- Auditor's endeavours are unsuccessful and the auditor is therefore unable to obtain sufficient appropriate audit evidence on the opening balances.

Auditor's Report:

- The auditor issues a disclaimer of opinion.
- As the previous financial report was not audited, ASA 710 paragraph 14 requires the auditor to include an Other Matter paragraph stating that the corresponding figures are unaudited.

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INDEPENDENT AUDITOR'S REPORT

[Appropriate Addressee]

Report on the Financial Report

We were engaged to audit the accompanying financial report of ABC Company Ltd., which comprises the statement of financial position as at 30 June 20X1, the statement of comprehensive income, statement of changes in equity and statement of cash flows for the year then ended, notes comprising a summary of significant accounting policies and other explanatory information, and management's assertion statement.

The Directors' Responsibility for the Financial Report

The Directors are responsible for the preparation of the financial report that presents a true and fair view in accordance with Australian Accounting Standards and the *Corporations Act 2001* and for such internal control as the Directors 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 conducting the audit in accordance with Australian Auditing Standards. Because of the matter(s) described in the Basis for Disclaimer of Opinion paragraph, however, we were not able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion.

Independence

In conducting our audit, we have complied with the independence requirements of the *Corporations Act 2001*. We confirm that the independence declaration required by the *Corporations Act 2001*, which has been given to the directors of ABC Company Ltd., would be in the same terms if given to the directors as at the time of this auditor's report.

Basis for Disclaimer of Opinion

The previous financial report was not audited. We were unable to satisfy ourselves by alternative means concerning a number of opening balances disclosed in the statements of financial performance and cash flows and the statement of financial position, as comparative figures. Accordingly, we were unable to determine whether adjustments might have been necessary in respect of the financial performance, cash flows and financial position for the year to 30 June 20X1.

Explanatory Guide: *Opening Balances*

Disclaimer of Opinion

Because of the significance of the matter(s) 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.

Report on the Remuneration Report

We have audited the Remuneration Report included in paragraphs a to b of the directors' report for the year ended 30 June 20X1. The directors of the company are responsible for the preparation and presentation of the Remuneration Report in accordance with section 300A of the *Corporations Act 2001*. Our responsibility is to express an opinion on the Remuneration Report, based on our audit conducted in accordance with Australian Auditing Standards.

Opinion

In our opinion the Remuneration Report of ABC Company Ltd. for the year ended 30 June 20X1, complies with section 300A of the *Corporations Act 2001*.

[Auditor's signature]

[Date of the auditor's report]

[Auditor's address]

Explanatory Guide: *Opening Balances*

EXAMPLE 3.1 continued...

PERIOD 2: SUBSEQUENT ENGAGEMENT

Audit Work Performed:

- The auditor conducted an audit of Period 1 in accordance with Auditing Standards and disclaimed on the opening balances.
- The auditor determines the status of the matter(s) causing the disclaimer of opinion in the prior period.
- The audit of Period 2 is conducted in accordance with Auditing Standards. If the auditor becomes aware of a possible misstatement in the comparative information while performing the current year audit, the auditor is required to obtain sufficient appropriate audit evidence to determine whether a material misstatement exists (ASA 710 paragraph 8).

Period 2 Auditor's Report:

- In the absence of identified material misstatements, the auditor issues an unmodified opinion because Period 1 has been audited. Balances and transactions have been audited; and the disclaimer was due only to the inability to obtain sufficient appropriate audit evidence regarding the opening balances.
- The Period 1 profit and loss transactions have been audited as well as the balance sheet, including the closing inventory. Accordingly, the risk of a material misstatement in the Period 1 comparatives shown in the Period 2 financial report is likely to be low and the auditor will issue an unmodified opinion for Period 2.