

**PROPOSED INTERNATIONAL STANDARD ON AUDITING 701 MODIFICATIONS TO
THE OPINION IN THE INDEPENDENT AUDITOR'S REPORT****CONTENTS**

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International Standard on Auditing (ISA) 701, "Modifications to the Opinion in the Independent Auditor's Report" should be read in the context of the "Preface to the International Standards on Quality Control, Auditing, Assurance and Related Services," which sets out the application and authority of ISAs.

Introduction

1. This International Standard on Auditing (ISA) establishes standards and provides guidance on (a) circumstances that may result in a modification of the auditor's opinion on the financial statements, (b) the type of opinion appropriate in the circumstances, and (c) the content of the auditor's report when the auditor's opinion is modified.
2. ISA 700 (Revised), "The Independent Auditor's Report on a Complete Set of General Purpose Financial Statements," establishes standards and provides guidance on the independent auditor's report issued as a result of an audit of a complete set of general purpose financial statements prepared in accordance with a financial reporting framework that is designed to achieve fair presentation. ISA 700 (Revised) addresses circumstances when the auditor is able to express an unmodified opinion and no changes to the auditor's report are necessary. The illustrative reports in this ISA (see Appendix) are based on the form and content of the auditor's report on a complete set of general purpose financial statements.
3. The standards and guidance in this ISA also apply to modifications to the opinion in the auditor's report on historical financial information other than a complete set of general purpose financial statements, as described in proposed ISA 800 (Revised), "The Independent Auditor's Report on Other Historical Financial Information."
4. In contrast to this standard, which addresses modifications to the auditor's opinion, proposed ISA 702 establishes standards and provides guidance when the auditor considers including an emphasis of matter paragraph or an other matters paragraph in the auditor's report.
5. As ISA 200, "Objective and General Principles Governing an Audit of Financial Statements," states, the objective of an audit of financial statements is to enable the auditor to express an opinion whether the financial statements are prepared, in all material respects, in accordance with an applicable financial reporting framework. The auditor evaluates the conclusions drawn from the audit evidence obtained as a basis for forming an opinion on the financial statements.
6. **The auditor should modify the opinion in the auditor's report when:**
 - a) **The auditor concludes that, based on the audit evidence obtained, the financial statements are not free from material misstatement and accordingly are not prepared, in all material respects, in accordance with an applicable financial reporting framework; or**
 - b) **The auditor is unable to obtain sufficient appropriate audit evidence to conclude that the financial statements are free from material misstatement.**

Circumstances Resulting in a Modification of the Auditor's Opinion

7. In forming the opinion on the financial statements, as described in paragraph 5, the auditor evaluates whether the financial statements have been prepared and presented in accordance with the specific requirements of the applicable financial reporting

framework. The auditor expresses a modified opinion in the auditor's report on the financial statements when:

- a) The auditor concludes that, based on the audit evidence obtained, the financial statements are not free from material misstatement due to a disagreement with management¹ about (i) the acceptability of selected accounting policies, (ii) the application of the selected accounting policies, or (iii) the adequacy of disclosures in the financial statements;
 - b) The auditor is unable to obtain sufficient appropriate audit evidence to conclude that the financial statements are free from material misstatement (also referred to as a limitation on the scope of the audit).
8. This ISA establishes three types of modified opinions, an *except for opinion*, an *adverse opinion*, and a *disclaimer of opinion*, the choice of which will depend upon the materiality and pervasiveness of the matter giving rise to the modification:
- (a) The auditor expresses an *except for opinion* (see paragraph 24) when the auditor concludes that the effect of any disagreement with management, while material, is not pervasive; therefore the financial statements taken as a whole are not misleading and thus do not require an adverse opinion.
 - (b) The auditor expresses an *adverse opinion* (see paragraph 27) when the auditor concludes that the effect of a disagreement with management is material and pervasive to the financial statements such that an except for opinion is not adequate to disclose the misleading nature of the financial statements.
 - (c) The auditor expresses an *except for opinion* (see paragraph 24) when the auditor concludes that the possible effect of any inability to obtain sufficient appropriate audit evidence, while material, could not be pervasive; therefore the financial statements taken as a whole are not misleading and do not require a *disclaimer of opinion*.
 - (d) The auditor expresses a *disclaimer of opinion* (see paragraph 31) when the possible effect of an inability to obtain sufficient appropriate audit evidence is material and pervasive to the financial statements such that the auditor is unable to express an opinion on the financial statements.

See paragraph 22 for a discussion of materiality and paragraphs 23, 28-30 for a discussion of pervasiveness.

¹ The term *management* used in this ISA describes those responsible for the preparation and presentation of the financial statements. Other terms may be appropriate depending on the legal framework in the particular jurisdiction. For example, in some jurisdictions, the appropriate reference may be to those charged with governance (for example, the directors).

9. The table below illustrates how the nature, materiality and pervasiveness of the matter giving rise to the modification affect the type of opinion to be used.

Affects or Possibly Affects the Financial Statements	Materially	Materially and Pervasively
Nature of Matter Giving Rise to the Modification		
Disagreement With Management	A Except for Opinion (See paragraph 24)	B Adverse Opinion (See paragraph 27)
Inability to Obtain Sufficient Appropriate Audit Evidence	C Except for Opinion (See paragraph 24)	D Disclaimer of Opinion (See paragraph 31)

Disagreement with Management

10. The auditor should express an *except for opinion* or an *adverse opinion* when disagreements with management are material to the financial statements. As discussed in paragraph 7(a), the auditor may disagree with management about the following matters:

- The acceptability of selected accounting policies;
- The application of the selected accounting policies; or
- The adequacy of disclosures in the financial statements.

ACCEPTABILITY OF SELECTED ACCOUNTING POLICIES

11. Disagreements with management about the acceptability of the selected accounting policies may arise when:

- (a) The selected accounting policies are not consistent with the applicable financial reporting framework;
- (b) The selected accounting policies are not appropriate in the circumstances and accordingly the overall presentation of and disclosures in the financial statements are not consistent with the auditor's understanding of the entity and its environment;
- (c) Because of the accounting policies selected by management, the financial statements, including the note disclosures, do not faithfully represent the underlying transactions and events in a manner that gives a true and fair view of or presents fairly, in all material respects, the information in the financial statements.

12. Where the entity has changed its selection of significant accounting policies, the auditor considers the reasons for the change and whether it is appropriate in the entity's circumstances. Financial reporting frameworks often contain requirements for accounting for, and disclosure of, changes in accounting policies. Where the entity has not complied with these requirements, the auditor considers whether this constitutes a material departure from the requirements of the applicable financial reporting framework, and the effect that such departure may have on the auditor's opinion.

APPLICATION OF THE SELECTED ACCOUNTING POLICY

13. Disagreements with management about the application of selected accounting policies may arise when:
 - (a) Management has not applied the selected accounting policies consistently with the financial reporting framework or has not applied the selected accounting policies consistently between periods and to similar transactions and events (consistency in application), or
 - (b) Based on the audit evidence obtained, the auditor has identified a misstatement of the financial statements due to the method of application of a selected accounting policy (error in application). This may arise when there is a disagreement with management about the underlying facts and circumstances to which the selected accounting policies are applied.
14. Misstatements due to the method of application of selected accounting policies may arise from (see ISA 320, "Materiality in the Identification and Evaluation of Misstatements"):
 - (a) Known misstatements, separately identifying:
 - (i) Misstatements of fact: These are specific misstatements identified during the audit including, for example, those arising from mistakes in gathering or processing data and the overlooking or misinterpretation of facts; and
 - (ii) Misstatements involving subjective decisions: These arise from differences between management's and the auditor's judgments concerning accounting estimates (e.g., because an estimate included in the financial statements by management is outside of the reasonable range of outcomes the auditor has determined) or the selection and application of accounting policies that the auditor considers to give rise to misstatements; and
 - (b) Likely misstatements: These are misstatements that the auditor considers likely to exist based on an extrapolation from audit evidence obtained, for example, the amount obtained by projecting known misstatements identified in an audit sample to the entire population from which the sample was drawn.

ADEQUACY OF DISCLOSURES IN THE FINANCIAL STATEMENTS

15. Disagreements with management about the adequacy of disclosures in the financial statements may arise when the financial statements (a) do not include all of the disclosures required by the applicable financial reporting framework or (b) do not provide sufficiently clear disclosures to enable users to understand the effect of material transactions and events on the information conveyed in the financial statements, for example, in the case of financial statements prepared in accordance with International

Financial Reporting Standards (IFRSs), the effect on the entity's financial position, financial performance, and cash flows.

Inability to Obtain Sufficient Appropriate Audit Evidence

16. **The auditor should express an *except for opinion* or a *disclaimer of opinion* when the auditor is unable to obtain sufficient appropriate audit evidence about one or more matters that are or could be material to the financial statements to conclude whether the financial statements are free from material misstatement.**
17. The auditor's inability to obtain sufficient appropriate audit evidence may be imposed by circumstances. For example,
 - (a) When the timing of the auditor's appointment is such that the auditor is unable to observe the counting of the physical inventories;
 - (b) When the entity's accounting records have been destroyed due to a fire.

The auditor considers whether it is possible to perform alternate procedures to obtain sufficient appropriate audit evidence on which to base an unmodified opinion. If performing alternate procedures is not possible, the auditor will not be able to obtain sufficient appropriate audit evidence and accordingly modifies the audit opinion.
18. The auditor's inability to obtain sufficient appropriate audit evidence may also be imposed by management, for example, when management precludes the auditor from observing the counting of the physical inventory or from requesting external confirmation of specific account balances.
19. After accepting an engagement, the auditor may become aware that management has imposed a limitation on the scope of the audit which the auditor considers likely to result in the need to express a modified opinion on the financial statements. Under those circumstances, the auditor requests the removal of that limitation. If management does not remove the limitation, the auditor considers the implications for the risk assessment and whether it is possible to perform alternative procedures to obtain sufficient appropriate audit evidence on which to base an unmodified opinion. If performing alternative procedures is not possible, the auditor will not be able to obtain sufficient appropriate audit evidence and accordingly modifies the audit opinion.

Determining the Type of Opinion

20. Where there is a disagreement with management or an inability to obtain sufficient appropriate audit evidence, the auditor determines whether a modified opinion is necessary and, if so, what type of opinion (an *except for opinion*, an *adverse opinion*, or a *disclaimer of opinion*) is appropriate in the circumstances.
21. In deciding on the type of opinion, the auditor considers the materiality and pervasiveness of the matter giving rise to the modification to the auditor's opinion.
22. ISA 320 discusses the factors the auditor considers in determining the materiality of a matter and the importance of considering not only the financial magnitude but also the

qualitative aspects of the matter. The circumstances related to some misstatements may cause the auditor to evaluate them as material, individually or when considered together with other identified misstatements, even if they are of a lower level than the auditor had determined to be material when establishing the overall audit strategy. Circumstances that may affect the evaluation include, for example, the extent to which the misstatement affects compliance with regulatory requirements and debt covenants, or other contractual requirements.

23. In determining the pervasiveness of the effect of the disagreement with management or the inability to obtain sufficient appropriate audit evidence, the auditor considers the following:
- (a) The degree to which the disagreement with management or inability to obtain sufficient appropriate audit evidence impairs the usefulness of the financial statements (see paragraphs 26, 30 and 32)
 - (b) The extent to which the disagreement with management or inability to obtain sufficient appropriate audit evidence can be (i) related to specific items in the financial statements and (ii) quantified (see paragraph 28).
 - (c) Whether the effect of the disagreement with management on the financial statements can be clearly described in the auditor's report so that the modification can address the incomplete or misleading nature of the financial statements (see paragraphs 25, 29-30, 32 and 39).

The effect of a disagreement with management would ordinarily be considered to be pervasive when it affects the amounts and presentation of numerous financial statement items.

Except For Opinion

24. **The auditor should express an *except for opinion* when the auditor concludes that an unmodified opinion cannot be expressed, but the effect of any disagreement with management or inability to obtain sufficient appropriate audit evidence, while material, is not pervasive to the financial statements so as to require an *adverse opinion* or a *disclaimer of opinion*.** (See report example 1 in the Appendix for an example of an *except for opinion* due to a disagreement with management and examples 4, 5 and 6 for examples of an *except for opinion* due to an inability to obtain sufficient appropriate audit evidence.)
25. The auditor ordinarily expresses an *except for opinion* when the effect of a disagreement with management (a) can be clearly described in the auditor's report and (b) does not result in financial statements that are misleading as a whole.
26. The auditor ordinarily expresses an *except for opinion* when the possible effect of an inability to obtain sufficient appropriate audit evidence can be clearly described in the auditor's report and the possible effect does not impair the overall true and fair view of the financial statements.

Adverse Opinion

27. **The auditor should express an *adverse opinion* when the auditor concludes that the effect of a disagreement with management is material and pervasive to the financial statements and accordingly an *except for opinion* is not adequate to disclose the misleading or incomplete nature of the financial statements.** (See report examples 2 and 3 in the Appendix.)
28. When a disagreement with management clearly relates to specific financial statement line items and is readily quantifiable, for example, an overstatement of cash, revenues or equity, the auditor is able to clearly describe in the auditor's report the effect of the disagreement with management on the financial statements. When it is not possible to determine which financial statement line items are affected or may be affected by a disagreement with management or, when it is not possible to quantify the effect thereof, it may be difficult or impossible for the auditor to describe in the auditor's report the effect of the disagreement with management on the financial statements. In such situations, the auditor ordinarily expresses an *adverse opinion*.
29. In certain circumstances, a single line item of the financial statements may comprise such a large percentage of the balance sheet, income statement or cash flow statement or otherwise be so fundamental to the true and fair view of the financial statements that a misstatement of that single line item may cause the auditor to conclude that an *adverse opinion* is necessary.
30. When a disagreement with management relates to multiple departures from the applicable financial reporting framework and those departures affect multiple financial statements line items, the financial statements may be misleading because of the cumulative effect of the departures. Furthermore, as the number of financial statement line items affected by the disagreements with management increases, the more difficult it becomes to clearly describe in the auditor's report the effects of the disagreements. In such situations, the auditor ordinarily expresses an *adverse opinion*.

Disclaimer of Opinion

31. **The auditor should express a *disclaimer of opinion* when the possible effect of an inability to obtain sufficient appropriate audit evidence is material and pervasive to the financial statements and accordingly the auditor is unable to express an *except for opinion* on the financial statements.** (See report examples 7 and 8 in the Appendix.)
32. The auditor ordinarily expresses a *disclaimer of opinion* when it is not possible to determine which financial statement line items are or may be affected by an inability to obtain sufficient appropriate audit evidence and accordingly it may be difficult or impossible for the auditor to clearly describe in the auditor's report the effect on the financial statements.

Piecemeal Opinions

33. When the auditor has expressed an *adverse opinion* or a *disclaimer of opinion* on the financial statements *taken as a whole*, the auditor does not express an unmodified opinion

as to specific elements, accounts or line items of a financial statement as such a piecemeal opinion tends to overshadow or contradict the *adverse opinion* or the *disclaimer of opinion*.

Communication with Those Charged with Governance

34. **The auditor should communicate circumstances that lead to expected modifications to the opinion in the auditor's report to those charged with governance.** This helps to ensure that
- (a) Those charged with governance are aware of the expected modification(s) and the reasons (or circumstances) for the modification(s) before the financial statements are finalized;
 - (b) There are no disputed facts in respect of the matter(s) giving rise to the expected modification(s), or that matters of disagreement with management are confirmed as such; and
 - (c) Those charged with governance have an opportunity, where appropriate, to provide the auditor with further information and explanations in respect of the matter(s) giving rise to the expected modification(s).

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

Basis for Modified Opinion Paragraph

35. Consistency in the auditor's report helps to promote the reader's understanding and to identify unusual circumstances when they occur. Accordingly, although uniformity in the wording of a modified opinion and in the description of the basis for the modification may not be possible, consistency in both the form and content of the auditor's report is desirable.
36. ISA 700 (Revised) requires the auditor to include certain specific elements in the auditor's report when the auditor's opinion is unmodified. **In addition to those specific elements, whenever the auditor expresses a modified opinion on the financial statements, the auditor should include a paragraph that provides:**
- (a) **A clear description of all the substantive reasons for the modification; and**
 - (b) **In the case of a disagreement with management, a quantification of the principal effects on the financial statements of the matter giving rise to the modification, unless impracticable.**
 - (c) **In the event of an inability to obtain sufficient appropriate audit evidence, a description of the reason for the inability (see paragraphs 16–19).**

This paragraph should precede the opinion paragraph in the auditor's report and should have the heading "Basis for Modified Opinion," "Basis for Adverse Opinion," and "Basis for Disclaimer of Opinion," as appropriate.

37. If the modification arises from a known or likely misstatement (see paragraph 13), the consequences of the misstatement are described in the Basis for Modified Opinion paragraph. For example, if inventory is overstated, tax, net income and equity will be

affected as a consequence. When there is an inability to obtain sufficient appropriate audit evidence, the auditor may not be able to quantify the possible effects on the financial statements, and thus may not be able to include such information in the Basis for Modified Opinion paragraph.

38. The auditor describes the effects of all matters that require modification to the opinion. For example, even when the auditor expresses an *adverse opinion* because the auditor concludes that the entity is not a going concern, the *adverse opinion* does not justify the omission of specific modifications for specific disagreements with management about the recognition, measurement, or disclosure of certain assets and liabilities, for example, the existence of inventory. The auditor describes all of the reasons for modifications in the Basis for Modified Opinion paragraph of the auditor's report.
39. The auditor's responsibility to include a description of all the substantive reasons for the modification of the opinion and a quantification of the possible effect on the financial statements does not extend to that of management or result in a responsibility to include disclosures that management is responsible for including in the financial statements.

Opinion Paragraph

40. **When the opinion is modified, the opinion paragraph should have the heading "Modified Opinion," "Adverse Opinion," or "Disclaimer of Opinion," as appropriate.** Inclusion of this paragraph heading makes it clear to the user that the auditor's opinion is modified and the type of modification.
41. **When the auditor expresses an *except for opinion*, the opinion paragraph should state that, "In our opinion, except for the effect of the matter described in the preceding paragraph, the financial statements give a true and fair view (or 'present fairly, in all material respects') in accordance with the applicable financial reporting framework."** Other qualifying phrases such as "with the foregoing explanation" or "subject to" are not sufficiently clear or forceful and are not to be used. When the modification arises from an inability to obtain sufficient appropriate audit evidence, the opinion states "Except for the *possible* effect of the matter ..."
42. **When the auditor expresses an *adverse opinion*, the opinion paragraph should state that, "In our opinion, because of the significance of the matters described in the preceding paragraph, the financial statements do not give a true and fair view (or 'present fairly, in all material respects') in accordance with the applicable financial reporting framework."**
43. **When the auditor expresses a *disclaimer of opinion*, the opinion paragraph should state that "Because of the significance of the matters described in the preceding 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."**

Description of Auditor's Responsibility When Expressing a Disclaimer of Opinion

44. When the auditor expresses a *disclaimer of opinion*, the auditor should amend the description of the auditor's responsibility and the description of the scope of the audit to state only, "Because of the matter(s) described in the following paragraph(s) we were not able to perform an audit in accordance with ISAs."

Effective Date

45. This ISA is effective for auditor's reports dated on or after December 31, 2006.

Examples of Auditor's Reports with Modified Opinions

No. 1: Auditor's report with except for opinion due to a disagreement with management – overstatement of inventories; the effect of this disagreement with management is deemed to be material but not pervasive to the financial statements

INDEPENDENT AUDITOR'S REPORT

[Appropriate Addressee]

Report on the Financial Statements²

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

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

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

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of

² The subheading "Report on the Financial Statements" is unnecessary in circumstances when the second subheading "Report on Other Legal and Regulatory Requirements" is not applicable.

expressing an opinion on the effectiveness of the entity's internal control.³ An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

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

Basis for Modified Opinion

The Company's inventories, which are recognized in the balance sheet at 16 million EUR, are overstated by 5 million EUR due to missing write downs of slow moving items. The tax effect hereof is 1.5 million EUR. Accordingly, shareholders' equity and profit for the year are overstated by 3.5 million EUR.

Modified Opinion

In our opinion, except for the effects of the matters described in the preceding paragraph, the financial statements give a true and fair view of (*or "present fairly, in all material respects"*) the financial position of ABC Company as of December 31, 20X1, and of its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards. On this basis we modify our opinion as described below.

Report on Other Legal and Regulatory Requirements—Republic of Ireland

Auditors' responsibilities

In addition to reporting on the financial statements, Republic of Ireland legal and regulatory requirements also require us to:

- (a) Report to you our opinion as to whether the financial statements have been properly prepared in accordance with the Companies Acts 1963 to 2001.
- (b) Report to you only if, in our opinion, any information specified by law or the Listing Rules of the Irish Stock Exchange regarding directors' remuneration and directors' transactions is not given and, where practicable, include such information in our report.
- (c) Review whether the Corporate Governance Statement reflects the company's compliance with the seven provisions of the Combined Code specified for our review by the Listing Rules of the Irish Stock Exchange, and we report only if it does not. We are not required to consider whether the board's statements on internal control cover all risks and controls, or form an opinion on the effectiveness of the [company's] [group's] corporate governance procedures or its risk and control procedures.

³ In circumstances when the auditor also has responsibility to express an opinion on the effectiveness of internal control in conjunction with the audit of the financial statements, this sentence would be worded as follows: "In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements as a basis in order to design audit procedures that are appropriate in the circumstances."

- (d) Report to you whether, in our opinion, proper books have been kept by the company and, whether the information given in the Directors' Report is consistent with the financial statements. In addition, we state whether we have obtained all the information and explanations necessary for the purposes of our audit and whether the company's financial statements are in agreement with the books of account.
- (e) Report to you whether, in our opinion at the balance sheet date, there exists a financial situation under Section 40(1) of the Companies (Amendment) Act, 1983 which requires the convening of an extraordinary general meeting of the company.

Opinion

In our opinion, having regard to the work undertaken during the audit, the financial statements have been properly prepared in accordance with the Companies Acts, 1963 to 2001.

In our opinion, proper books of account have been kept by the company and the information given in the Directors' Report is consistent with the financial statements. We have obtained all the information and explanations we consider necessary for the purposes of our audit and the financial statements are in agreement with the books of account.

In our opinion, the net assets of the company, as stated in the balance sheet, are more than half of the amount of its called-up share capital and, in our opinion, on that basis there did not exist at 31 December 20xx a financial situation which under Section 40(1) of the Companies (Amendment) Act 1983, would require the convening of an extraordinary general meeting of the company.

[Auditor's signature]

[Date of the auditor's report]

[Auditor's address]

No. 2: Auditor's report with an adverse opinion due to a disagreement with management related to the going concern assumption; the effect of the disagreement with management is deemed to be both material and pervasive to the financial statements

INDEPENDENT AUDITOR'S REPORT

[Appropriate Addressee]

Report on the Financial Statements⁴

We have audited ... *(remaining words are the same as illustrated in the introductory paragraph – see report example 1 above).*

Management's Responsibility for the Financial Statements

Management is responsible for ... *(remaining words are the same as illustrated in the management's responsibility paragraph – see report example 1 above).*

Auditor's Responsibility

Our responsibility is ... *(remaining words are the same as illustrated in the paragraphs describing the auditor's responsibility – see example 1).*

Basis for Adverse Opinion

As discussed in Note X to the financial statements, ABC Company's financing arrangements expired and the amount outstanding was payable on December 31, 20X1. The Company has been unable to re-negotiate or obtain replacement financing and is considering filing for bankruptcy but management has still prepared the financial statements on a going concern basis. We do not believe the Company will be able to obtain replacement financing and accordingly we disagree that the financial statements should have been prepared on a going concern basis. On this basis we modify our opinion as described below.

Adverse Opinion

In our opinion, because of the significance of the matter discussed in the preceding paragraph, the financial statements do not give a true and fair view of *(or "present fairly, in all material respects")* the financial position of ABC Company as of December 31, 20X1, and of its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards.

⁴ The subheading "Report on the Financial Statements" is unnecessary in circumstances when the second subheading "Report on Other Legal and Regulatory Requirements" is not applicable.

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]

No. 3: Auditor's report with an adverse opinion due to a disagreement with management related to losses of 20 million EUR arising from long-term contracts of a total base of 30 million EUR; the effect of this disagreement with management is deemed to be both material and pervasive to the financial statements

INDEPENDENT AUDITOR'S REPORT

[Appropriate Addressee]

Report on the Financial Statements⁵

We have audited ... *(remaining words are the same as illustrated in the introductory paragraph – see report example 1 above).*

Management's Responsibility for the Financial Statements

Management is responsible for ... *(remaining words are the same as illustrated in the management's responsibility paragraph – see report example 1 above).*

Auditor's Responsibility

Our responsibility is ... *(remaining words are the same as illustrated in the paragraphs describing the auditor's responsibility – see example 1).*

Basis for Adverse Opinion

As discussed in Note X to the financial statements, no provision has been made for losses expected to arise from certain long-term contracts currently in progress, as the directors consider that such losses should be offset against amounts recoverable on other long-term contracts. We believe that a provision should be made for foreseeable losses on individual contracts as required by International Accounting Standard (IAS) 11, *Construction Contracts*, in the amount of 20 million EUR. The tax effect thereof would be 6 million EUR. Accordingly, shareholders equity and profit for the year are overstated by 14 million EUR. On this basis we modify our opinion as described below.

Adverse Opinion

In our opinion, because of the significance of the matters discussed in the preceding paragraph, the financial statements do not give a true and fair view of *(or "present fairly, in all material respects")* the financial position of ABC Company as of December 31, 20X1, and of its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards.

⁵ The subheading "Report on the Financial Statements" is unnecessary in circumstances when the second subheading "Report on Other Legal and Regulatory Requirements" is not applicable.

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]

Example Report 4: Auditor's report with except for opinion due to the auditor's inability to obtain sufficient appropriate audit evidence regarding an investment in a foreign affiliate; the possible effect of the inability to obtain sufficient appropriate audit evidence can be clearly described in the auditor's report and does not impair the overall true and fair view of the financial statements

INDEPENDENT AUDITOR'S REPORT

[Appropriate Addressee]

Report on the Financial Statements⁶

We have audited ... *(remaining words are the same as illustrated in the introductory paragraph – see report example 1 above).*

Management's Responsibility for the Financial Statements

Management is responsible for ... *(remaining words are the same as illustrated in the management's responsibility paragraph – see report example 1 above).*

Auditor's Responsibility

Our responsibility is ... *(remaining words of the first two paragraphs are the same as in the first two paragraphs describing the auditor's responsibility – see example 1)*

Except for the matter described in the following paragraph, we believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Basis for Modified Opinion

We were unable to obtain audited financial statements supporting the Company's investment in a foreign affiliate stated at 15 million EUR as at December 31, 20X1, which is included in the net income for the year then ended as described in Note X to the financial statements; nor were we able to satisfy ourselves as to the carrying value of the investment in the foreign affiliate or the equity in its earnings by other auditing procedures. On this basis we modify our opinion as described below.

⁶ The subheading "Report on the Financial Statements" is unnecessary in circumstances when the second subheading "Report on Other Legal and Regulatory Requirements" is not applicable.

Modified Opinion

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

Report on Other Legal and Regulatory Requirements

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

[Auditor's signature]

[Date of the auditor's report]

[Auditor's address]

No. 5: Auditor's report with except for opinion due to the auditor's inability to obtain sufficient appropriate audit evidence; the possible effect of the inability to obtain sufficient appropriate audit evidence can be clearly described in the auditor's report and does not impair the overall true and fair view of the financial statements

INDEPENDENT AUDITOR'S REPORT

[Appropriate Addressee]

Report on the Financial Statements⁷

We have audited ... *(remaining words are the same as illustrated in the introductory paragraph – see report example 1 above).*

Management's Responsibility for the Financial Statements

Management is responsible for ... *(remaining words are the same as illustrated in the management's responsibility paragraph – see report example 1 above).*

Auditor's Responsibility

Our responsibility is ... *(remaining words of the first two paragraphs are the same as in the first two paragraphs describing the auditor's responsibility – see example 1).*

Except for the matter described in the following paragraph, we believe that the audit evidence that we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Basis for Modified Opinion

The company's accounting records for cash sales were not adequate for purposes of our audit and therefore there were no satisfactory audit procedures that we could perform to obtain reasonable assurance that all cash sales have been properly recorded. The Company's recorded sales included 50,000 EUR in cash sales. On this basis we modify our opinion as described below.

Modified Opinion

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

⁷ The subheading "Report on the Financial Statements" is unnecessary in circumstances when the second subheading "Report on Other Legal and Regulatory Requirements" is not applicable.

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]

No. 6: Auditor's report with except for opinion due to the auditor's inability to obtain sufficient appropriate audit evidence with regard to the opening balance for inventory; the possible effect of the inability to obtain sufficient appropriate audit evidence can be clearly described in the auditor's report and does not impair the overall true and fair view of the financial statements

INDEPENDENT AUDITOR'S REPORT

[*Appropriate Addressee*]

Report on the Financial Statements⁸

We have audited ... (*remaining words are the same as illustrated in the introductory paragraph – see report example 1 above*).

Management's Responsibility for the Financial Statements

Management is responsible for ... (*remaining words are the same as illustrated in the management's responsibility paragraph – see report example 1 above*).

Auditor's Responsibility

Our responsibility is ... (*remaining words of the first two paragraphs are the same as in the first two paragraphs describing the auditor's responsibility – see example 1*).

Except for the matter described in the following paragraph, we believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Basis for Modified Opinion

We did not observe the counting of the physical inventories at the previous year end, since that date was prior to our appointment as auditors for the Company. Due to the nature of the Company's records, we were unable to satisfy ourselves as to opening inventory quantities by other audit procedures. On this basis we modify our opinion as described below.

Modified Opinion

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

⁸ The subheading "Report on the Financial Statements" is unnecessary in circumstances when the second subheading "Report on Other Legal and Regulatory Requirements" is not applicable.

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]

No. 7: Auditor's report with a disclaimer of opinion due to the auditor's inability to obtain sufficient appropriate audit evidence with respect to inventory and accounts receivable; the auditor was unable to obtain sufficient appropriate audit evidence because management restricted the scope of the auditor's procedures; the report also identifies a disagreement with management related to interest-bearing borrowings; the effect of this disagreement with management is deemed to be both material and pervasive to the financial statements

INDEPENDENT AUDITOR'S REPORT

[Appropriate Addressee]

Report on the Financial Statements⁹

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

Management's Responsibility for the Financial Statements

Management is responsible for ... *(remaining words are the same as illustrated in the management's responsibility paragraph – see report example 1 above).*

Auditor's Responsibility

Because of the matter described in the following paragraph we were not able to perform an audit in accordance with ISAs.

Basis for Disclaimer of Opinion

The company's management restricted us from observing the counting of the physical inventories and sending out requests for confirmation of accounts receivable to certain customers. The company's records did not permit the application of alternative auditing procedures regarding the inventories and accounts receivable. Consequently, we were unable to obtain all the information and explanations we considered necessary to satisfy ourselves as to the existence of inventories and accounts receivable.

Furthermore, included in interest bearing borrowings, under non-current liabilities, are amounts totaling 5 million EUR that are due for settlement within the forthcoming fiscal year. International Accounting Standard No. 1, Presentation of Financial Statements, requires separate disclosure of amounts that are to be settled before and after the forthcoming fiscal year. Based on the latter, interest-bearing borrowings would have been stated at 15 million EUR, short-term borrowings at 10 million EUR and current liabilities at 25 million EUR. On this basis we modify our opinion as described below.

⁹ The subheading "Report on the Financial Statements" is unnecessary in circumstances when the second subheading "Report on Other Legal and Regulatory Requirements" is not applicable.

Disclaimer of Opinion

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

Report on Other Legal and Regulatory Requirements

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

[Auditor's signature]

[Date of the auditor's report]

[Auditor's address]

No. 8: Auditor's report with a disclaimer of opinion due to the auditor's inability to obtain sufficient appropriate audit evidence; completeness of accounting records cannot be substantiated due to lack of control over sales; the possible effect of this inability to obtain sufficient appropriate audit evidence is deemed to be material and pervasive to the financial statements

INDEPENDENT AUDITOR'S REPORT

[Appropriate Addressee]

Report on the Financial Statements¹⁰

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

Management's Responsibility for the Financial Statements

Management is responsible for ... *(remaining words are the same as illustrated in the management's responsibility paragraph – see report example 1 above).*

Auditor's Responsibility

Because of the matter described in the following paragraph we were not able to perform an audit in accordance with ISAs.

Basis for Disclaimer of Opinion

The Company's accounting records for cash sales were not adequate for purposes of our audit therefore there were no satisfactory audit procedures that we could perform to obtain reasonable assurance that all cash sales have been properly recorded. The Company's sales were made entirely on a cash basis. On this basis we modify our opinion as described below.

Disclaimer of Opinion

Because of the significance of the matter described in the preceding 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.

¹⁰ The subheading "Report on the Financial Statements" is unnecessary in circumstances when the second subheading "Report on Other Legal and Regulatory Requirements" is not applicable.

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]