



## Agenda Item 1H (705)

### Proposed SAS, Modifications to the Opinion in the Independent Auditor’s Report

ISA 705 (Revised)	Extant AU-C 705	Proposed SAS
<b>Illustrations of Auditor’s Reports with Modifications to the Opinion</b>	<b>Exhibit—Illustrations of Auditor’s Reports With Modifications to the Opinion</b>	
Illustration 1: An auditor’s report containing a qualified opinion due to a material misstatement of the financial statements.	Illustration 1 — An Auditor’s Report Containing a Qualified Opinion Due to a Material Misstatement of the Financial Statements	Illustration 1 — An Auditor’s Report Containing a Qualified Opinion Due to a Material Misstatement of the Financial Statements
	Illustration 2 — An Auditor’s Report Containing a Qualified Opinion for Inadequate Disclosure	Illustration 2 — An Auditor’s Report Containing a Qualified Opinion for Inadequate Disclosure
Illustration 2: An auditor’s report containing an adverse opinion due to a material misstatement of the consolidated financial statements.	Illustration 3 — An Auditor’s Report Containing an Adverse Opinion Due to a Material Misstatement of the Financial Statements	Illustration 3 — An Auditor’s Report Containing an Adverse Opinion Due to a Material Misstatement of the Financial Statements

Illustrative Reports – Proposed SAS Modifications  
ASB Meeting, July 17-20, 2017

<b>ISA 705 (Revised)</b>	<b>Extant AU-C 705</b>	<b>Proposed SAS</b>
Illustration 3: An auditor’s report containing a qualified opinion due to the auditor’s inability to obtain sufficient appropriate audit evidence regarding a foreign associate.	Illustration 4 — An Auditor’s Report Containing a Qualified Opinion Due to the Auditor’s Inability to Obtain Sufficient Appropriate Audit Evidence	Illustration 4 — An Auditor’s Report Containing a Qualified Opinion Due to the Auditor’s Inability to Obtain Sufficient Appropriate Audit Evidence
Illustration 4: An auditor’s report containing a disclaimer of opinion due to the auditor’s inability to obtain sufficient appropriate audit evidence about a single element of the consolidated financial statements.	Illustration 5 — An Auditor’s Report Containing a Disclaimer of Opinion Due to the Auditor’s Inability to Obtain Sufficient Appropriate Audit Evidence About a Single Element of the Financial Statements	Illustration 5 — An Auditor’s Report Containing a Disclaimer of Opinion Due to the Auditor’s Inability to Obtain Sufficient Appropriate Audit Evidence About a Single Element of the Financial Statements
Illustration 5: An auditor’s report containing a disclaimer of opinion due to the auditor’s inability to obtain sufficient appropriate audit evidence about multiple elements of the financial statements.	Illustration 6 — An Auditor’s Report Containing a Disclaimer of Opinion Due to the Auditor’s Inability to Obtain Sufficient Appropriate Audit Evidence About Multiple Elements of the Financial Statements	Illustration 6 — An Auditor’s Report Containing a Disclaimer of Opinion Due to the Auditor’s Inability to Obtain Sufficient Appropriate Audit Evidence About Multiple Elements of the Financial Statements
	Illustration 7 — An Auditor’s Report in Which the Auditor Is Expressing an Unmodified Opinion in the Prior Year and a Modified Opinion (Qualified Opinion) in the Current Year	Illustration 7 — An Auditor’s Report in Which the Auditor Is Expressing an Unmodified Opinion in the Prior Year and a Modified Opinion (Qualified Opinion) in the Current Year
	Illustration 8 — An Auditor’s Report in Which the Auditor Is Expressing an Unmodified Opinion in the Current Year and a Disclaimer of Opinion on the Prior-Year	Illustration 8 — An Auditor’s Report in Which the Auditor Is Expressing an Unmodified Opinion in the Current Year and a Disclaimer of Opinion on the Prior-Year

Illustrative Reports – Proposed SAS Modifications  
ASB Meeting, July 17-20, 2017

<b>ISA 705 (Revised)</b>	<b>Extant AU-C 705</b>	<b>Proposed SAS</b>
	Statements of Income, Changes in Stockholders' Equity, and Cash Flows	Statements of Income, Changes in Stockholders' Equity, and Cash Flows

**Exhibit—Illustrations of Auditor’s Reports With Modifications to the Opinion**

Illustration 1 — An Auditor’s Report Containing a Qualified Opinion Due to a Material Misstatement of the Financial Statements

Illustration 2 — An Auditor’s Report Containing a Qualified Opinion for Inadequate Disclosure

Illustration 3 — An Auditor’s Report Containing an Adverse Opinion Due to a Material Misstatement of the Financial Statements

Illustration 4 — An Auditor’s Report Containing a Qualified Opinion Due to the Auditor’s Inability to Obtain Sufficient Appropriate Audit Evidence

Illustration 5 — An Auditor’s Report Containing a Disclaimer of Opinion Due to the Auditor’s Inability to Obtain Sufficient Appropriate Audit Evidence About a Single Element of the Financial Statements

Illustration 6 — An Auditor’s Report Containing a Disclaimer of Opinion Due to the Auditor’s Inability to Obtain Sufficient Appropriate Audit Evidence About Multiple Elements of the Financial Statements

Illustration 7 — An Auditor’s Report in Which the Auditor Is Expressing an Unmodified Opinion in the Prior Year and a Modified Opinion (Qualified Opinion) in the Current Year

Illustration 8 — An Auditor’s Report in Which the Auditor Is Expressing an Unmodified Opinion in the Current Year and a Disclaimer of Opinion on the Prior-Year Statements of Income, Changes in Stockholders’ Equity, and Cash Flows

*Note: In the following illustrations, the Opinion section has been positioned first in accordance with proposed SAS, Forming an Opinion and Reporting on Financial Statements, and the Basis for Opinion section is positioned immediately after the Opinion section. Also, the first sentence of the second paragraph and last sentence that was included in the extant auditor’s responsibilities section is now subsumed as part of the new Basis for Opinion section.*

### **Illustration 1 — An Auditor’s Report Containing a Qualified Opinion Due to a Material Misstatement of the Financial Statements**

Circumstances include the following:

- Audit of a complete set of general purpose financial statements (comparative). The audit is not a group audit.
- The financial statements are prepared by management of the company in accordance with accounting principles generally accepted in the United States of America.
- The terms of the audit engagement reflect the description of management’s responsibility for the financial statements in AU-C section 210.
- Inventories are misstated. The misstatement is deemed to be material but not pervasive to the financial statements. Accordingly, the auditor’s report contains a qualified opinion.
- Based on the audit evidence obtained, the auditor has concluded that there are no conditions or events, considered in the aggregate, that raise substantial doubt about the entity’s ability to continue as a going concern for a reasonable period of time in accordance with AU-C section 570.
- The auditor has obtained all of the other information prior to the date of the auditor’s report and the matter giving rise to the qualified opinion on the financial statements also affects the other information.
- The auditor is not communicating key audit matters in the auditor’s report.
- Those responsible for oversight of the financial statements differ from those responsible for the preparation of the financial statements.

**Independent Auditor's Report**

[Appropriate Addressee]

**Report on the Audit of the Financial Statements<sup>1</sup>**

***Qualified Opinion***

We have audited the ~~accompanying~~ financial statements of ABC Company, which comprise the balance sheets as of December 31, 20X1 and 20X0, and the related statements of income, changes in stockholders' equity, and cash flows for the years then ended, and the related notes to the financial statements.

In our opinion, except for the effects of the matter described in the *Basis for Qualified Opinion* section of our report, paragraph, the accompanying financial statements ~~referred to above~~ present fairly, in all material respects, the financial position of ABC Company as of December 31, 20X1 and 20X0, and the results of its operations and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

***Basis for Qualified Opinion***

The Company has stated inventories at cost in the accompanying balance sheets. Accounting principles generally accepted in the United States of America require inventories to be stated at the lower of cost or market. If the Company stated inventories at the lower of cost or market, a write down of \$XXX and \$XXX would have been required as of December 31, 20X1 and 20X0, respectively. Accordingly, cost of sales would have been increased by \$XXX and \$XXX, and net income, income taxes, and stockholders' equity would have been reduced by \$XXX, \$XXX, and \$XXX, and \$XXX, \$XXX, and \$XXX, as of and for the years ended December 31, 20X1 and 20X0, respectively.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Our responsibilities under those standards are further described in the *Auditor's Responsibilities for the Audit of the Financial Statements* section of our report. We are independent of ABC Company in accordance with ethical requirements that are relevant to our audit of the financial statements, and we have fulfilled our other ethical responsibilities in accordance with these requirements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our qualified audit opinion.

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<sup>1</sup>The subtitle "Report on the Financial Statements" is unnecessary in circumstances when the second subtitle, "Report on Other Legal and Regulatory Requirements," is not applicable.

*Other Information for another title if appropriate such as “Information other than the Financial Statements and Auditor’s Report Thereon”]*

*[Reporting in accordance with the reporting requirements in proposed SAS, The Auditor’s Responsibilities Relating to Other Information Included in Annual Reports – see Illustration 3 in appendix of proposed SAS, The Auditor’s Responsibilities Relating to Other Information Included in Annual Reports. The last paragraph of the Other Information section in Illustration 3 would be customized to describe the specific matter giving rise to the qualified opinion that also affects the other information.]*

*Responsibilities of Management’s Responsibility and Those Charged With Governance for the Financial Statements*

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

*In preparing the financial statements, management is responsible for assessing ABC Company’s ability to continue as a going concern in accordance with accounting principles generally accepted in the United States of America, and using the going concern basis of accounting unless management either intends to liquidate ABC Company or to cease operations, or has no realistic alternative but to do so.*

*Those charged with governance are responsible for overseeing ABC Company’s financial reporting process.*

*~~Auditor’s Responsibilities for the Audit of the Financial Statements~~ Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.*

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

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

- 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 Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of In making those risk assessments, the auditor considers internal control relevant to the audit 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 expressing an opinion on the effectiveness of ABC Company's the entity's internal control.<sup>2</sup> Accordingly, we express no such opinion is expressed.
- Evaluate An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.
- Conclude on ABC Company's ability to continue as a going concern and conclude on the appropriateness of management's use of the going concern basis of accounting.

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

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

### **Report on Other Legal and Regulatory Requirements**

~~[The form and content of this section of the auditor's report would vary depending on the nature of the auditor's other reporting responsibilities.]~~

~~[Auditor's signature of the auditor's firm]~~

~~[Auditor's city and state]~~

~~[Date of the auditor's report]~~

<sup>2</sup> 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 in order to design audit procedures that are appropriate in the circumstances." In addition, the next sentence, "Accordingly, we express no such opinion." would not be included.



## Illustration 2 — An Auditor’s Report Containing a Qualified Opinion for Inadequate Disclosure

Circumstances include the following:

- Audit of a complete set of general purpose financial statements (comparative). [The audit is not a group audit.](#)
- The financial statements are prepared [by management of the Company](#) in accordance with accounting principles generally accepted in the United States of America.
- The terms of the audit engagement reflect the description of management’s responsibility for the financial statements in [AU-C section 210.](#)
- The financial statements have inadequate disclosures. The auditor has concluded that (a) it is not practicable to present the required information and (b) the effects are such that an adverse opinion is not appropriate. Accordingly, the auditor’s report contains a qualified opinion.
- Based on the audit evidence obtained, the auditor has concluded that there are no conditions or events, considered in the aggregate, that raise substantial doubt about the entity’s ability to continue as a going concern for a reasonable period of time in accordance with [AU-C section 570.](#)
- The auditor has obtained all of the other information prior to the date of the auditor’s report and the matter giving rise to the qualified opinion on the financial statements also affects the other information.
- Key audit matters have been communicated in accordance with proposed SAS, [Communicating Key Audit Matters in the Independent Auditor’s Report.](#)
- Those responsible for oversight of the financial statements differ from those responsible for the preparation of the financial statements.

### **Independent Auditor’s Report**

[Appropriate Addressee]

#### **Report on the [Audit of the Financial Statements](#)<sup>3</sup>**

<sup>3</sup>The subtitle "Report on the Financial Statements" is unnecessary in circumstances when the second subtitle, "Report on Other Legal and Regulatory Requirements," is not applicable.

### ***Qualified Opinion***

We have audited the ~~accompanying~~ financial statements of ABC Company, which comprise the balance sheets as of December 31, 20X1 and 20X0, and the related statements of income, changes in stockholders' equity, and cash flows for the years then ended, and the related notes to the financial statements.

In our opinion, except for the omission of the information described in the *Basis for Qualified Opinion section of our report*~~paragraph~~, the ~~accompanying~~ financial statements ~~referred to above~~ present fairly, in all material respects, the financial position of ABC Company as of December 31, 20X1 and 20X0, and the results of its operations and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

### ***Basis for Qualified Opinion***

The Company's financial statements do not disclose [*describe the nature of the omitted information that is not practicable to present in the auditor's report*]. In our opinion, disclosure of this information is required by accounting principles generally accepted in the United States of America.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Our responsibilities under those standards are further described in the *Auditor's Responsibilities for the Audit of the Financial Statements* section of our report. We are independent of ABC Company in accordance with ethical requirements that are relevant to our audit of the financial statements, and we have fulfilled our other ethical responsibilities in accordance with these requirements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our qualified audit opinion.

### ***Key Audit Matters***

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

[Description of each key audit matter in accordance with proposed SAS, Communicating Key Audit Matters in the Independent Auditor's Report]

### ***Other Information [or another title if appropriate such as "Information other than the Financial Statements and Auditor's Report Thereon"]***

[Reporting in accordance with the reporting requirements in proposed SAS, The Auditor's Responsibilities Relating to Other Information Included in Annual Reports – see Illustration 3 in appendix of proposed SAS, The Auditor's Responsibilities Relating to Other Information Included in Annual Reports. The last paragraph of the Other Information section in Illustration 3 would be customized to describe the specific matter giving rise to the qualified opinion that also affects the other information.]

**Responsibilities of Management's Responsibility and Those Charged With Governance for the Financial Statements**

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, management is responsible for assessing ABC Company's ability to continue as a going concern in accordance with accounting principles generally accepted in the United States of America, and using the going concern basis of accounting unless management either intends to liquidate ABC Company or to cease operations, or has no realistic alternative but to do so.

Those charged with governance are responsible for overseeing ABC Company's financial reporting process.

**Auditor's Responsibilities for the Audit of the Financial Statements**

~~Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.~~

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

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

- 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 Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.

- Obtain an understanding of ~~In making those risk assessments, the auditor considers~~ internal control relevant to the audit 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 expressing an opinion on the effectiveness of ABC Company's ~~the entity's~~ internal control.<sup>4</sup> Accordingly, ~~we express~~ no such opinion is expressed.
- Evaluate ~~An audit also includes evaluating~~ the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.
- Conclude on ABC Company's ability to continue as a going concern and conclude on the appropriateness of management's use of the going concern basis of accounting.

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

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

### Report on Other Legal and Regulatory Requirements

~~[The form and content of this section of the auditor's report would vary depending on the nature of the auditor's other reporting responsibilities.]~~

~~[Auditor's Signature of the auditor's firm]~~

~~[Auditor's city and state]~~

~~[Date of the auditor's report]~~

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<sup>4</sup> 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 in order to design audit procedures that are appropriate in the circumstances." In addition, the next sentence, "Accordingly, we express no such opinion." would not be included.

### **Illustration 3 — An Auditor’s Report Containing an Adverse Opinion Due to a Material Misstatement of the Financial Statements**

Circumstances include the following:

- Audit of a complete set of consolidated general purpose financial statements (single year). The audit is not a group audit.
- The consolidated financial statements are prepared by management of the Company in accordance with accounting principles generally accepted in the United States of America.
- The terms of the audit engagement reflect the description of management’s responsibility for the financial statements in AU-C section 210.
- The consolidated financial statements are materially misstated due to the nonconsolidation of a subsidiary. The material misstatement is deemed to be pervasive to the consolidated financial statements. Accordingly, the auditor’s report contains an adverse opinion. The effects of the misstatement on the financial statements have not been determined because it was not practicable to do so.
- Based on the audit evidence obtained, the auditor has concluded that there are no conditions or events, considered in the aggregate, that raise substantial doubt about the entity’s ability to continue as a going concern for a reasonable period of time in accordance with AU-C section 570.
- The auditor has obtained all of the other information prior to the date of the auditor’s report and the matter giving rise to the adverse opinion on the consolidated financial statements also affects the other information.
- The auditor is precluded from communicating key audit matters in the auditor’s report ~~when issuing an adverse opinion.~~
- Those responsible for oversight of the financial statements differ from those responsible for the preparation of the financial statements.

**Independent Auditor's Report**

[Appropriate Addressee]

**Report on the Audit of the Consolidated Financial Statements<sup>5</sup>**

***Adverse Opinion***

We have audited the ~~accompanying~~ consolidated financial statements of ABC Company and its subsidiaries, which comprise the consolidated balance sheet as of December 31, 20X1, and the related consolidated statements of income, changes in stockholders' equity, and cash flows for the year then ended, and the related notes to the financial statements.

In our opinion, because of the significance of the matter discussed in the *Basis for Adverse Opinion* section of our report~~paragraph~~, the ~~accompanying~~ consolidated financial statements ~~referred to above~~ do not present fairly the consolidated financial position of ABC Company and its subsidiaries as of December 31, 20X1, or the results of their operations or their cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America.

***Basis for Adverse Opinion***

As described in Note X, the Company has not consolidated the financial statements of subsidiary XYZ Company that it acquired during 20X1 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 by the Company. Under accounting principles generally accepted in the United States of America, the subsidiary should have been consolidated because it is controlled by the Company. Had XYZ Company been consolidated, many elements in the accompanying consolidated financial statements would have been materially affected. The effects on the consolidated financial statements of the failure to consolidate have not been determined.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Our responsibilities under those standards are further described in the *Auditor's Responsibilities for the Audit of the Consolidated Financial Statements* section of our report. We are independent of ABC Company in accordance with ethical requirements that are relevant to our audit of the consolidated financial statements, and we have fulfilled our other ethical responsibilities in accordance with these requirements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our adverse audit opinion.

<sup>5</sup> The subtitle "Report on the Financial Statements" is unnecessary in circumstances when the second subtitle, "Report on Other Legal and Regulatory Requirements," is not applicable.

*Other Information for another title if appropriate such as “Information other than the Financial Statements and Auditor’s Report Thereon”]*

*[Reporting in accordance with the reporting requirements in proposed SAS, The Auditor’s Responsibilities Relating to Other Information Included in Annual Reports – see Illustration 4 in appendix of proposed SAS, The Auditor’s Responsibilities Relating to Other Information Included in Annual Reports. The last paragraph of the Other Information section in Illustration 4 would be customized to describe the specific matter giving rise to the adverse opinion that also affects the other information.]*

*Responsibilities of Management’s Responsibility and Those Charged With Governance for the Consolidated Financial Statements*

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

*In preparing the consolidated financial statements, management is responsible for assessing ABC Company’s ability to continue as a going concern in accordance with accounting principles generally accepted in the United States of America, and using the going concern basis of accounting unless management either intends to liquidate ABC Company or to cease operations, or has no realistic alternative but to do so.*

*Those charged with governance are responsible for overseeing ABC Company’s financial reporting process.*

*Auditor’s Responsibilities for the Audit of the Consolidated Financial Statements*

*Our responsibility is to express an opinion on these consolidated financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement. Our objectives are to obtain reasonable assurance about whether the consolidated financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor’s report that includes our opinion. Reasonable assurance is a high level of assurance, but is not absolute assurance and therefore is not a guarantee that an audit conducted in accordance with GAAS will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these consolidated financial statements.*

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



- ~~An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgment, including the assessment of Identify and assess the risks of material misstatement of the consolidated financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.~~
- ~~Obtain an understanding of In making those risk assessments, the auditor considers internal control relevant to the audit entity's preparation and fair presentation of the consolidated financial statements 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 ABC Company's the entity's internal control.<sup>6</sup> Accordingly, ~~we express~~ no such opinion is expressed.~~
- ~~Evaluate An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.~~
- ~~Conclude on ABC Company's ability to continue as a going concern and conclude on the appropriateness of management's use of the going concern basis of accounting.~~

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

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

## Report on Other Legal and Regulatory Requirements

~~[The form and content of this section of the auditor's report would it vary depending on the nature of the auditor's other reporting responsibilities.]~~

~~[Auditor's sSignature of the auditor's firm]~~

~~[Auditor's city and state]~~

~~[Date of the auditor's report]~~

<sup>6</sup> 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 in order to design audit procedures that are appropriate in the circumstances." In addition, the next sentence, "Accordingly, we express no such opinion." would not be included.



**Illustration 4 — An Auditor’s Report Containing a Qualified Opinion Due to the Auditor’s Inability to Obtain Sufficient Appropriate Audit Evidence**

Circumstances include the following:

- Audit of a complete set of general purpose financial statements (single year). [The audit is not a group audit.](#)
- The ~~consolidated~~ financial statements are prepared by management of the Company in accordance with accounting principles generally accepted in the United States of America.
- The terms of the audit engagement reflect the description of management’s responsibility for the financial statements in AU-C section 210.
- The auditor was unable to obtain sufficient appropriate audit evidence regarding an investment in a foreign affiliate. The possible effects of the inability to obtain sufficient appropriate audit evidence are deemed to be material but not pervasive to the financial statements. Accordingly, the auditor’s report contains a qualified opinion.
- Based on the audit evidence obtained, the auditor has concluded that there are no conditions or events, considered in the aggregate, that raise substantial doubt about the entity’s ability to continue as a going concern for a reasonable period of time in accordance with AU-C section 570.
- The auditor has obtained all of the other information prior to the date of the auditor’s report and the matter giving rise to the qualified opinion on the financial statements also affects the other information.
- The auditor is not communicating key audit matters in the auditor’s report.
- Those responsible for oversight of the financial statements differ from those responsible for the preparation of the financial statements.

**Independent Auditor’s Report**

[Appropriate Addressee]

**Report on the Audit of the Financial Statements<sup>7</sup>**

***Qualified Opinion***

We have audited the ~~accompanying~~ financial statements of ABC Company, which comprise the balance sheet as of December 31, 20X1, and the related statements of income, changes in stockholders’ equity, and cash flows for the year then ended, and the related notes to the financial statements.

In our opinion, except for the possible effects of the matter described in the *Basis for Qualified Opinion section of our report*~~paragraph~~, the ~~accompanying~~ financial statements ~~referred to above~~ present fairly, in all material respects, the financial position of ABC Company as of December 31, 20X1, and the results of its operations and its cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America.

***Basis for Qualified Opinion***

ABC Company’s investment in XYZ Company, a foreign affiliate acquired during the year and accounted for under the equity method, is carried at \$XXX on the balance sheet at December 31, 20X1, and ABC Company’s share of XYZ Company’s net income of \$XXX is included in ABC Company’s net income for the year then ended. We were unable to obtain sufficient appropriate audit evidence about the carrying amount of ABC Company’s investment in XYZ Company as of December 31, 20X1 and ABC Company’s share of XYZ Company’s net income for the year then ended because we were denied access to the financial information, management, and the auditors of XYZ Company. Consequently, we were unable to determine whether any adjustments to these amounts were necessary.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Our responsibilities under those standards are further described in the *Auditor’s Responsibilities for the Audit of the Financial Statements* section of our report. We are independent of ABC Company in accordance with ethical requirements that are relevant to our audit of the financial statements, and we have fulfilled our other ethical responsibilities in accordance with these requirements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our qualified audit opinion.

*Other Information for another title if appropriate such as “Information other than the Financial Statements and Auditor’s Report Thereon”*

<sup>7</sup> The subtitle "Report on the Financial Statements" is unnecessary in circumstances when the second subtitle, "Report on Other Legal and Regulatory Requirements," is not applicable.

[Reporting in accordance with the reporting requirements in proposed SAS, The Auditor's Responsibilities Relating to Other Information Included in Annual Reports – see Illustration 3 in appendix of proposed SAS, The Auditor's Responsibilities Relating to Other Information Included in Annual Reports. The last paragraph of the Other Information section in Illustration 3 would be customized to describe the specific matter giving rise to the qualified opinion that also affects the other information.]

**Responsibilities of Management's Responsibility and Those Charged With Governance for the Financial Statements**

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, management is responsible for assessing ABC Company's ability to continue as a going concern in accordance with accounting principles generally accepted in the United States of America, and using the going concern basis of accounting unless management either intends to liquidate ABC Company or to cease operations, or has no realistic alternative but to do so.

Those charged with governance are responsible for overseeing ABC Company's financial reporting process.

**Auditor's Responsibilities for the Audit of the Financial Statements**

~~Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.~~

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

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

- 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 Identify and assess the risks of material misstatement of the financial

statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.

- Obtain an understanding of ~~In making those risk assessments, the auditor considers~~ internal control relevant to the audit 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 expressing an opinion on the effectiveness of the ABC Company's entity's internal control.<sup>8</sup> Accordingly, ~~we express no such opinion~~ is expressed.
- Evaluate ~~An audit also includes evaluating~~ the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.
- Conclude on ABC Company's ability to continue as a going concern and conclude on the appropriateness of management's use of the going concern basis of accounting.

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

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

### Report on Other Legal and Regulatory Requirements

~~[The form and content of this section of the auditor's report would vary depending on the nature of the auditor's other reporting responsibilities.]~~

~~[Auditor's Signature of the auditor's firm]~~

~~[Auditor's city and state]~~

~~[Date of the auditor's report]~~

<sup>8</sup> 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 in order to design audit procedures that are appropriate in the circumstances." In addition, the next sentence, "Accordingly, we express no such opinion." would not be included.

**Illustration 5 — An Auditor’s Report Containing a Disclaimer of Opinion Due to the Auditor’s Inability to Obtain Sufficient Appropriate Audit Evidence About a Single Element of the Financial Statements**

Circumstances include the following:

- Audit of a complete set of general purpose financial statements (single year). The audit is not a group audit.
- The financial statements are prepared by management of the Company in accordance with accounting principles generally accepted in the United States of America.
- The terms of the audit engagement reflect the description of management’s responsibility for the financial statements in AU-C section 210.
- The auditor was unable to obtain sufficient appropriate audit evidence about a single element of the financial statements. That is, the auditor was unable to obtain audit evidence about the financial information of a joint venture investment accounted for under the proportionate consolidation approach. The investment represents over 90 percent of the Company’s net assets. The possible effects of this inability to obtain sufficient appropriate audit evidence are deemed to be both material and pervasive to the financial statements. Accordingly, the auditor’s report contains a disclaimer of opinion.
- The auditor concluded that it was unnecessary to include in the auditor’s report specific amounts for the Company’s proportional share of the assets, liabilities, income, and expenses of the joint venture investment because the investment represents over 90 percent of the Company’s net assets, and that fact is disclosed in the auditor’s report.
- Based on the audit evidence obtained, the auditor has concluded that there are no conditions or events, considered in the aggregate, that raise substantial doubt about the entity’s ability to continue as a going concern for a reasonable period of time in accordance with AU-C section 570.
- The auditor is precluded from communicating key audit matters in the auditor’s report.
- Those responsible for oversight of the financial statements differ from those responsible for the preparation of the financial statements.
- A more limited description of the auditor’s responsibilities section is required because of the disclaimer of opinion.

**Independent Auditor's Report**

[Appropriate Addressee]

**Report on the Audit of the Financial Statements<sup>9</sup>**

***Disclaimer of Opinion***

We were engaged to audit the ~~accompanying~~ financial statements of ABC Company, which comprise the balance sheet as of December 31, 20X1, and the related statements of income, changes in stockholders' equity, and cash flows for the year then ended, and the related notes to the financial statements.

We do not express an opinion on the accompanying financial statements of ABC Company. Because of the significance of the matter described in the *Basis for Disclaimer of Opinion* section of our report~~paragraph~~, we have not been able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion on these financial statements. ~~Accordingly, we do not express an opinion on these financial statements.~~

***Basis for Disclaimer of Opinion***

The Company's investment in XYZ Company, a joint venture, is carried at \$XXX on the Company's balance sheet, which represents over 90 percent of the Company's net assets as of December 31, 20X1. We were not allowed access to the management and the auditors of XYZ Company. As a result, we were unable to determine whether any adjustments were necessary relating to the Company's proportional share of XYZ Company's assets that it controls jointly, its proportional share of XYZ Company's liabilities for which it is jointly responsible, its proportional share of XYZ Company's income and expenses for the year, and the elements making up the statements of changes in stockholders' equity and cash flows.

**Responsibilities of Management and Those Charged With Governance's Responsibility for the Financial Statements**

Management is responsible for the preparation and fair presentation of ~~these~~ financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, management is responsible for assessing ABC Company's ability to continue as a going concern in accordance with accounting principles generally accepted in the United

<sup>9</sup> The subtitle "Report on the Financial Statements" is unnecessary in circumstances when the second subtitle, "Report on Other Legal and Regulatory Requirements," is not applicable.

States of America, and using the going concern basis of accounting unless management either intends to liquidate ABC Company or to cease operations, or has no realistic alternative but to do so.

Those charged with governance are responsible for overseeing ABC Company's financial reporting process.

***Auditor's Responsibilities for the Audit of the Financial Statements***

Our responsibility is to conduct an audit of ABC Company's financial statements ~~express an opinion on these financial statements based on conducting the audit~~ in accordance with auditing standards generally accepted in the United States of America and to issue an auditor's report. ~~However, b~~Because of the matter described in the *Basis for Disclaimer of Opinion* section of our report~~paragraph~~, ~~however,~~ we were not able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion on these financial statements.

We are independent of ABC Company in accordance with ethical requirements that are relevant to our audit of the financial statements, and we have fulfilled our other ethical responsibilities in accordance with these requirements.

**Report on Other Legal and Regulatory Requirements**

*[The ~~f~~Form and content of this section of the auditor's report ~~would~~ vary depending on the nature of the auditor's other reporting responsibilities.]*

*[~~Auditor's~~Signature of the auditor's firm]*

*[Auditor's city and state]*

*[Date of the auditor's report]*



**Illustration 6 — An Auditor’s Report Containing a Disclaimer of Opinion Due to the Auditor’s Inability to Obtain Sufficient Appropriate Audit Evidence About Multiple Elements of the Financial Statements**

Circumstances include the following:

- Audit of a complete set of general purpose financial statements (single year). [The audit is not a group audit.](#)
- The financial statements are -prepared [by management of the Company](#) in accordance with accounting principles generally accepted in the United States of America.
- The terms of the audit engagement reflect the description of management’s responsibility for the [financial statements in AU-C section 210.](#)
- The auditor was unable to obtain sufficient appropriate audit evidence about multiple elements of the financial statements. That is, the auditor was unable to obtain audit evidence about the entity’s inventories and accounts receivable. The possible effects of this inability to obtain sufficient appropriate audit evidence are deemed to be both material and pervasive to the financial statements. Accordingly, the auditor’s opinion contains a disclaimer of opinion.
- Based on the audit evidence obtained, the auditor has concluded that there are no conditions or events, considered in the aggregate, that raise substantial doubt about the entity’s ability to continue as a going concern for a reasonable period of time in accordance with [AU-C section 570.](#)
- The auditor is precluded from communicating key audit matters in the auditor’s report.
- Those responsible for oversight of the financial statements differ from those responsible for the [preparation of the financial statements.](#)
- A more limited description of the auditor’s responsibilities section is required because of the [disclaimer of opinion.](#)



**Independent Auditor's Report**

[Appropriate Addressee]

**Report on the Audit of the Financial Statements<sup>10</sup>**

***Disclaimer of Opinion***

We were engaged to audit the ~~accompanying~~ financial statements of ABC Company, which comprise the balance sheet as of December 31, 20X1, and the related statements of income, changes in stockholders' equity, and cash flows for the year then ended, and the related notes to the financial statements.

We do not express an opinion on the accompanying financial statements of ABC Company. Because of the significance of the matters described in the *Basis for Disclaimer of Opinion* section of our report~~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 these financial statements.~~

***Basis for Disclaimer of Opinion***

We were not engaged as auditors of the Company until after December 31, 20X1, and, therefore, did not observe the counting of physical inventories at the beginning or end of the year. We were unable to satisfy ourselves by other auditing procedures concerning the inventory held at December 31, 20X1, which is stated in the balance sheet at \$XXX. In addition, the introduction of a new computerized accounts receivable system in September 20X1 resulted in numerous misstatements in accounts receivable. As of the date of our audit report, management was still in the process of rectifying the system deficiencies and correcting the misstatements. We were unable to confirm or verify by alternative means accounts receivable included in the balance sheet at a total amount of \$XXX at December 31, 20X1. As a result of these matters, we were unable to determine whether any adjustments might have been found necessary in respect of recorded or unrecorded inventories and accounts receivable, and the elements making up the statements of income, changes in stockholders' equity, and cash flows.

**Responsibilities of Management and Those Charged With Governance's Responsibility for the Financial Statements**

Management is responsible for the preparation and fair presentation of ~~these~~ financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

<sup>10</sup> The subtitle "Report on the Financial Statements" is unnecessary in circumstances when the second subtitle, "Report on Other Legal and Regulatory Requirements," is not applicable.

In preparing the financial statements, management is responsible for assessing ABC Company’s ability to continue as a going concern in accordance with accounting principles generally accepted in the United States of America, and using the going concern basis of accounting unless management either intends to liquidate ABC Company or to cease operations, or has no realistic alternative but to do so.

Those charged with governance are responsible for overseeing ABC Company’s financial reporting process.

***Auditor’s Responsibilities for the Audit of the Financial Statements***

Our responsibility is to conduct an audit of ABC Company’s ~~express an opinion on these~~ financial statements ~~based on conducting the audit~~ in accordance with auditing standards generally accepted in the United States of America and to issue an auditor’s report. ~~However, b~~Because of the matters described in the *Basis for Disclaimer of Opinion* ~~section of our report~~ paragraph, ~~however,~~ we were not able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion on these financial statements.

We are independent of ABC Company in accordance with ethical requirements that are relevant to our audit of the financial statements, and we have fulfilled our other ethical responsibilities in accordance with these requirements.

**Report on Other Legal and Regulatory Requirements**

~~[The f~~*Form and content of this section of the auditor’s report would* ~~vary depending on the nature of the auditor’s other reporting responsibilities.]~~

~~[~~*Auditor’s*~~s~~*Signature of the auditor’s firm]*

~~[~~*Auditor’s city and state]*

~~[~~*Date of the auditor’s report]*

**Illustration 7 — An Auditor’s Report in Which the Auditor Is Expressing an Unmodified Opinion in the Prior Year and a Modified Opinion (Qualified Opinion) in the Current Year**

Circumstances include the following:

- Audit of a complete set of general purpose financial statements (comparative).
- -The financial statements are prepared by management of the Company in accordance with accounting principles generally accepted in the United States of America.
- The terms of the audit engagement reflect the description of management’s responsibility for the financial statements in AU-C section 210.
- Certain lease obligations have been excluded from the financial statements in the current year. The effect of the exclusion is material but not pervasive. The auditor expressed an unmodified opinion in the prior year and is expressing a modified opinion (qualified opinion) in the current year.
- Based on the audit evidence obtained, the auditor has concluded that there are no conditions or events, considered in the aggregate, that raise substantial doubt about the entity’s ability to continue as a going concern for a reasonable period of time in accordance with AU-C section 570.
- The auditor is not communicating key audit matters in the auditor’s report.
- Those responsible for oversight of the financial statements differ from those responsible for the preparation of the financial statements.

**Independent Auditor's Report**

[Appropriate Addressee]

**Report on the Audit of the Financial Statements<sup>11</sup>**

***Qualified Opinion***

We have audited the ~~accompanying~~ financial statements of ABC Company, which comprise the balance sheets as of December 31, 20X1 and 20X0, and the related statements of income, changes in stockholders' equity, and cash flows for the years then ended, and the related notes to the financial statements.

In our opinion, except for the effects on the ~~accompanying~~ 20X1 financial statements of not capitalizing certain lease obligations as described in the *Basis for Qualified Opinion* ~~section of our report~~ paragraph, the financial statements ~~referred to above~~ present fairly, in all material respects, the financial position of ABC Company as of December 31, 20X1 and 20X0, and the results of its operations and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

***Basis for Qualified Opinion on the 20X1 Financial Statements***

The Company has excluded, from property and debt in the accompanying 20X1 balance sheet, certain lease obligations that were entered into in 20X1 which, in our opinion, should be capitalized in accordance with accounting principles generally accepted in the United States of America. If these lease obligations were capitalized, property would be increased by \$XXX, long-term debt by \$XXX, and retained earnings by \$XXX as of December 31, 20X1, and net income and earnings per share would be increased (decreased) by \$XXX and \$XXX, respectively, for the year then ended.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Our responsibilities under those standards are further described in the *Auditor's Responsibilities for the Audit of the Financial Statements* section of our report. We are independent of ABC Company in accordance with ethical requirements that are relevant to our audit of the financial statements, and we have fulfilled our other ethical responsibilities in accordance with these requirements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our qualified opinion on the 20X1 financial statements and for our opinion on the 20X0 financial statements.

***Responsibilities of Management's Responsibility and Those Charged With Governance for the Financial Statements***

<sup>11</sup> The subtitle "Report on the Financial Statements" is unnecessary in circumstances when the second subtitle, "Report on Other Legal and Regulatory Requirements," is not applicable.

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, management is responsible for assessing ABC Company's ability to continue as a going concern in accordance with accounting principles generally accepted in the United States of America, and using the going concern basis of accounting unless management either intends to liquidate ABC Company or to cease operations, or has no realistic alternative but to do so.

Those charged with governance are responsible for overseeing ABC Company's financial reporting process.

### ***Auditor's Responsibilities for the Audit of the Financial Statements***

~~Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.~~

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

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

- ~~• Identify and assess, 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, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.~~
- ~~• Obtain an understanding of In making those risk assessments, the auditor considers internal control relevant to the audit 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 expressing an opinion on the effectiveness of ABC Company's ~~the entity's~~ internal control.<sup>12</sup> Accordingly, ~~we express~~ no such opinion is expressed.

- Evaluate ~~An audit also includes evaluating~~ the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.
- Conclude on ABC Company's ability to continue as a going concern and conclude on the appropriateness of management's use of the going concern basis of accounting.

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

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

### **Report on Other Legal and Regulatory Requirements**

~~[The f~~Form and content of this section of the auditor's report would ~~it~~ vary depending on the nature of the auditor's other reporting responsibilities.]

~~[Auditor's s~~Signature of auditor's firm]

~~[Auditor's city and state]~~

~~[Date of the auditor's report]~~

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<sup>12</sup> 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 in order to design audit procedures that are appropriate in the circumstances." In addition, the next sentence, "Accordingly, we express no such opinion." would not be included.

**Illustration 8 — An Auditor’s Report in Which the Auditor Is Expressing an Unmodified Opinion in the Current Year and a Disclaimer of Opinion on the Prior-Year Statements of Income, Changes in Stockholders’ Equity, and Cash Flows**

Circumstances include the following:

- Audit of a complete set of general purpose financial statements (comparative).
- -The financial statements are prepared by management of the Company in accordance with accounting principles generally accepted in the United States of America.
- The terms of the audit engagement reflect the description of management’s responsibility for the financial statements in AU-C section 210.
- The auditor was unable to observe the physical inventory as ~~of~~ December 31, 20X0, as at that time the auditor had not been engaged. Accordingly, the auditor was unable to obtain sufficient appropriate audit evidence regarding the net income and cash flows for the year ended December 31, 20X1. The effects of the inability to obtain sufficient appropriate audit evidence are deemed material and pervasive.
- The auditor expressed an unmodified opinion on December 31, 20X1 and 20X0 balance sheets and a disclaimer of opinion on the 20X0 statements of income, changes in stockholders’ equity, and cash flows.
- Based on the audit evidence obtained, the auditor has concluded that there are no conditions or events, considered in the aggregate, that raise substantial doubt about the entity’s ability to continue as a going concern for a reasonable period of time in accordance with AU-C section 570.
- The auditor is not communicating key audit matters in the auditor’s report.
- Those responsible for oversight of the financial statements differ from those responsible for the preparation of the financial statements.

**Independent Auditor’s Report**

*[Appropriate Addressee]*

**Report on the -Audit of the Financial Statements<sup>13</sup>**

<sup>13</sup> The subtitle "Report on the Financial Statements" is unnecessary in circumstances when the second subtitle, "Report on Other Legal and Regulatory Requirements," is not applicable.



**Opinion**

We have audited the ~~accompanying~~ financial statements of ABC Company, which comprise the balance sheets as of December 31, 20X2 and 20X1, and the related statements of income, changes in stockholders' equity, and cash flows for the years then ended, and the related notes to the financial statements.

In our opinion, the ~~accompanying~~ balance sheets of ABC Company as of December 31, 20X2 and 20X1, and the statements of income, changes in stockholders' equity, and cash flows for the year ended December 31, 20X2, present fairly, in all material respects, the financial position of ABC Company as of December 31, 20X2 and 20X1, and the results of its operations and its cash flows for the year ended December 31, 20X2 in accordance with accounting principles generally accepted in the United States of America.

***Disclaimer of Opinion on 20X1 Operations and Cash Flows***

~~We do not express an opinion on the accompanying results of operations and cash flows for the year ended December 31, 20X1. Because of the significance of the matter described in the *Basis for Disclaimer of Opinion* section of our report paragraph, we have not been able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion on the results of operations and cash flows for the year ended December 31, 20X1. Accordingly, we do not express an opinion on the results of operations and cash flows for the year ended December 31, 20X1.~~

**Basis for Opinion**

~~We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Our responsibilities under those standards are further described in the *Auditor's Responsibilities for the Audit of the Financial Statements* section of our report. We are independent of ABC Company in accordance with ethical requirements that are relevant to our audit of the financial statements, and we have fulfilled our other ethical responsibilities in accordance with these requirements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinions on the balance sheets as of December 31, 20X2 and 20X1, and the statements of income, changes in stockholders' equity, and cash flows for the year ended December 31, 20X2.~~

***Basis for Disclaimer of Opinion on 20X1 Operations and Cash Flows***

We did not observe the taking of the physical inventory as of December 31, 20X0, since that date was prior to our engagement as auditors for the Company, and we were unable to satisfy ourselves regarding inventory quantities by means of other auditing procedures. Inventory amounts as of December 31, 20X0 enter into the determination of net income and cash flows for the year ended December 31, 20X1.

***Responsibilities of Management's Responsibility and Those Charged With Governance for the Financial Statements***



Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, management is responsible for assessing ABC Company's ability to continue as a going concern in accordance with accounting principles generally accepted in the United States of America, and using the going concern basis of accounting unless management either intends to liquidate ABC Company or to cease operations, or has no realistic alternative but to do so.

Those charged with governance are responsible for overseeing ABC Company's financial reporting process.

### **Auditor's Responsibilities for the Audit of the Financial Statements**

~~Our responsibility is to express an opinion on these financial statements based on our audits. Except as explained in the Basis for Disclaimer of Opinion paragraph, we conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.~~

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

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

- Identify and assess ~~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,~~ design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of ~~In making those risk assessments, the auditor considers~~ internal control relevant to the audit 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 expressing an opinion on the effectiveness of ABC Company's internal control.<sup>14</sup> Accordingly, ~~we express~~ no such opinion is expressed.

- Evaluate ~~An audit also includes evaluating~~ the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.
- Conclude on ABC Company's ability to continue as a going concern and conclude on the appropriateness of management's use of the going concern basis of accounting.

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

~~We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinions on the balance sheets as of December 31, 20X2 and 20X1, and the statements of income, changes in stockholders' equity, and cash flows for the year ended December 31, 20X2.~~

### Report on Other Legal and Regulatory Requirements

~~[The f~~Form and content of this section of the auditor's report would ~~it~~ vary depending on the nature of the auditor's other reporting responsibilities.]

~~[~~Auditor's ~~s~~Signature of the auditor's firm]

~~[~~Auditor's city and state]

~~[~~Date of the auditor's report]

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<sup>14</sup>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 in order to design audit procedures that are appropriate in the circumstances." In addition, the next sentence, "Accordingly, we express no such opinion." would not be included.