

Standards on Auditing SA 700,705 and 706

Primarily dealing with Issuance of Audit Reports.

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Standards pertaining to Audit Reports

SA 700	Forming an Opinion and Reporting on Financial Statements - to be used only in case of unmodified opinion.
SA 705	Modifications to the Opinion in the Independent Auditor's Report - to be used only in case of modified opinion.
SA 706	Emphasis of Matter Paragraphs and Other Matter paragraphs in the Independent Auditor's Report - to be used if there is an emphasis of matter and it also deals with Other Matters

Applicable for Audit reports for periods beginning on or after April 1, 2018.

SA – 700 (Revised)

Forming an Opinion and Reporting on Financial Statements

Changes in SA 700 (Revised)

- * The flow of the reporting has been changed substantially from the earlier SA-700
- * The new Standard is applicable for audits of all the financial statement for accounting periods beginning on and after April 1, 2018
- * SA700 (R) applies only to a complete set of General Purpose Financial Statement.

Flow of the report as per Revised SA-700

- * Title
- * Addressee
- * Auditors' Opinion
- * Basis for Opinion (to be given even for unmodified opinion)
- * Going Concern (SA-570 - Revised)
- * Key Audit Matter (SA-701 Revised)
- * Emphasis of Matter (SA-706 Revised)
- * Management Responsibility for Financial Statements
- * Auditors' Responsibilities for the audit of financial statements
- * Other Information (SA720 Revised)
- * Reporting on other legal and regulatory matters (SA-706 Revised)
- * Signature block
- * Place and Date of Signing

Audit opinion

- * In order that the reader does not have to search for the opinion paragraph in the report, the first reporting paragraph is the opinion paragraph
- * This is true whether it is in an unmodified opinion or a modified opinion
- * The basis for the opinion now follows the opinion paragraph.
- * The Auditor's responsibility is now a more detailed paragraph detailing in a more specific manner the responsibilities of the Auditor

Forming a Clean (Unmodified) Opinion

- The financial statements are prepared, in all material respects, in accordance with the applicable financial reporting framework including qualitative aspects of entity's accounting policies and possible bias in management's judgments.
- Has obtained reasonable assurance about whether the financial statements are free of material misstatements due to Fraud or Error based on : Sufficient and appropriate audit evidence;
- Whether uncorrected misstatements are material, Individually or in aggregate in accordance with SA 450.
- Requirements of the reporting framework (eg., the Accounting Standards) have been materially complied with

Contd....

- Disclose the accounting policies selected and applied and Consistency and appropriateness of those policies
- Reasonable estimates are used by the management
- Information presented in relevant, reliable, comparable and understandable
- Disclosures are adequate to enable users to understand the effect of material transactions
- Terminology used is appropriate.

SA-705

Modification to the Opinion in the
Independent Auditor's Report

Introduction and Scope

- Deals with circumstances when the auditor concludes modification to the report is necessary.
- Types of modified opinions
 - ✓ **Qualified Opinion**
 - ✓ **Adverse Opinion**
 - ✓ **Disclaimer of Opinion**
- The decision on the type of opinion depends upon:
 - ✓ The **nature of the matter** giving rise to the modification i.e. whether the financial statements are materially misstated
 - ✓ **Inability to obtain** sufficient and appropriate audit evidence
 - ✓ Auditor's judgment about the **pervasiveness** of the effects or possible effects of the matter
- The auditor shall modify the opinion when:
 - He concludes that, **based on audit evidence, the financial statements as a whole are NOT free of material misstatements**; or
 - The auditor is **UNABLE to obtain sufficient appropriate audit evidence to conclude** that the financial statements are free of material misstatements

QUALIFIED OPINION

QUALIFIED OPINION

The auditor shall express qualified opinion when :

He concludes that the misstatements, individually or in aggregate , are MATERIAL , BUT NOT PERVASIVE to the financial statements

He is unable to obtain sufficient appropriate audit evidence but also concludes that the possible effects of undetected misstatements could be MATERIAL, BUT NOT PERVASIVE

Adverse Opinion

ADVERSE OPINION

When the auditor concludes that having obtained sufficient appropriate audit evidence, the misstatements, individually or in aggregate, are BOTH MATERIAL AND PERVASIVE, he issues an adverse opinion.

Disclaimer of Opinion

DISCLAIMER OF OPINION

- ❑ When the auditor is unable to obtain sufficient appropriate audit evidence and concludes that the possible effects of undetected misstatements are **BOTH MATERIAL AND PERVASIVE**, he issues an disclaimer of opinion .
- ❑ In extremely rare circumstances , having obtained sufficient appropriate audit evidence, BUT due to multiple uncertainties , the auditor is not able to form an opinion , due to possible interaction of those uncertainties and their possible cumulative outcomes , he issues a disclaimer of opinion.

Modifications in the Report(Contd..)

Auditors ' Report Modification Matrix:

Nature of matter giving rise to the modification	Auditor's Judgment about the Pervasiveness of the Effects or Possible Effects on the Financial Statements	
	Material but not pervasive	Material and Pervasive
Financial statements are materially misstated	Qualified opinion	Adverse opinion
Inability to obtain sufficient appropriate audit evidence	Qualified opinion	Disclaimer of opinion

Material Misstatements

A misstatement is the difference between the amount of classification, presentation, or disclosure reported in the financial statements and the classification, presentation, or disclosure required as per the applicable financial reporting framework.

This may arise in relation to :

- 1. Appropriateness of the selected accounting policies**
 - ✓ **Selected accounting policies are not consistent with the applicable financial reporting framework ;**
 - ✓ **Financial statements , including notes thereon , do not represent underlying transactions and events that achieves fair presentation**
- 2. Application of selected accounting policies**
 - ✓ **When accounting policies are not applied consistently , including consistency between periods , similar transactions and events ;**
 - ✓ **Method of application is erroneous**

Material Misstatements (Contd..)

3. Appropriateness or adequacy of disclosures in the financial statements :

- ✓ Financial statements **do not include all disclosures** required by the applicable financial reporting framework
- ✓ Disclosures are **not presented in accordance with the applicable financial reporting frame work**
- ✓ The financial statements **do not provide the disclosures necessary to achieve fair presentation**

Inability to obtain Sufficient Appropriate Audit Evidence

- Auditor's inability to obtain sufficient appropriate audit evidence may arise from :
 - ✓ Circumstances beyond the control of the entity; eg. Where records have been destroyed by fire, or seizure by government authority, etc.
 - ✓ Circumstances relating to nature or timing of the Auditor's work eg. When auditor is appointed on such date that he cannot observe the physical count
 - ✓ Limitation imposed by the management Eg: Management prevents auditors from inventory counting / obtaining external confirmations.
- In case limitation is imposed by the management, **the auditor shall request the management to remove the limitation**
- If the management still persists, Auditor **shall communicate it to those charged with governance** and determine if alternative audit procedures are possible.

Inability to obtain Sufficient Appropriate Audit Evidence

- If the auditor is unable to obtain sufficient appropriate audit evidence, he shall:
 - ✓ Resign from the engagement, where practicable and not prohibited by law
 - ✓ If resignation is not possible due to stage of the auditor legal or professional restriction, the auditor shall give a disclaimer of opinion
- Where the auditor decides to resign, he shall inform to those charged with the governance any matters regarding misstatements identified during the audit that would have given rise to modification in the report

Revision in SA 705

- * The only change is that the basis of Qualified opinion, basis of adverse opinion or basis of disclaimer of opinion will follow the Opinion paragraph
- * The opinion paragraph will be the first paragraph which will be titled “Qualified opinion”, “adverse Opinion” or “disclaimer of opinion”
- * There are no changes as compared to the previous SA-705 in
 - what constitutes misstatements,
 - what situation requires qualification,
 - what situation requires adverse opinion and
 - what situation requires disclaimer of opinion

SA-706

Emphasis of Matter Paragraphs and
Other Matters Paragraphs in the
Independent Auditor's Report

Updation in the Audit Report

Types of paragraph

Emphasis of Matter

- **Paragraph** in the Audit Report
- On a matter that is appropriately **presented or disclosed** in Financial Statements.
- Insertion of an emphasis of matter paragraph in the Auditor's Report **does not make the opinion "modified"**
- An Emphasis of Matter paragraph **is not a substitute for either the auditor expressing a qualified opinion or an adverse opinion, or disclaiming an opinion**
- An emphasis of matter **is not a part of the audit opinion at all**. It is a separate, independent paragraph designed to provide **"additional communication"** to the users

Other paragraphs

- Paragraph in the Audit Report that refers to a matter other than those presented or disclosed in Financial Statements.

Revision in SA 706

- * Similarly excepting for the reporting of Going concern paragraph separately in a paragraph titled “material uncertainty relating to going concern” as per SA570 (R) there are no other changes.
- * The other reporting of “Emphasis of Matter” and “Other Matters” or the “other legal and regulatory requirements” paragraphs are substantially the same as the previous SA-706 except that there are some rules to be followed relating to Key Audit Matters which is dealt with separately

Emphasis of Matter Paragraph

- ❑ An emphasis of matter paragraph is useful when the auditor, having formed an opinion, intends to draw the attention of the users to :
 - ✓ A matter, though **appropriately presented** and disclosed, is of fundamental importance to the users to understand the financial statements;
 - ✓ Any other matter relevant to the **users' understanding** of the audit, auditor's responsibility or Auditor's Report.
 - ✓ Where an emphasis of matter paragraph **is required by any other auditing standard**, the disclosure shall be as per this SA.

- ❑ Such a paragraph shall refer **to information presented and disclosed in financial statements.**

- ❑ The auditor should have **obtained sufficient appropriate audit evidence** that the matter is not materially misstated.

Emphasis of Matter Paragraph (Contd..)

- ❑ The emphasis of matter paragraph shall be **placed immediately after the Opinion (basis of opinion)** paragraph in the Auditor's Report under the heading "Emphasis of Matter Paragraph" provided there are no Going concern issue and Key audit matters. Else it is placed after that.
- ❑ Include a **clear reference** to the matter being emphasized and to the relevant disclosures
- ❑ Indicate that the **Auditor's opinion is NOT modified by using words like "Without qualifying our opinion" or "Our report is not qualified on this account"**

Issues to be considered under Covid19 Situations

- * Improper Accounting and/or Inadequate Disclosures.
- * Inability to obtain sufficient and appropriate audit evidence.
- * Inability to complete audit procedures to enable forming an opinion.
- * Going Concern Considerations [SA570 (revised)].
- * Including an emphasis of Matter Paragraph in the Audit Report.
- * Inclusion of information in other matters.

Covid 19 contd..

- * The ICAI has come out with guidance related to possible impacts of Covid 19.
- * The ICAI guidance is like a refresher of all standards which needs to be perused to obtain guidance on procedure to be followed.
- * The ICAI guidance does not state possible examples of drafting etc.
- * This has to be done by the Auditor.
- * There are a number of Companies who have made some comments and others are expected to follow.

Some Presentations

Name of Company	Audit Report Modifications/ EOM
HDFC Bank Ltd	EOM
Adani Enterprises Ltd	EOM
Adani Power Ltd	EOM
Axis Bank	EOM
Bajaj Auto Ltd	EOM
BPCL	EOM
Infosys, HCL Tech, TCS, Mindtree, Wipro	No Comments
Lemon Tree	EOM
Reliance	No Comments
Interglobe Aviation	EOM
JSW Steel	No comments
Trent Ltd.	No Comments

Questions ??

Thank You!!