

# KAEG-I [INTL VERSION 2024]: ISA 510 Initial Audit Engagements - Opening Balances

## Contents

## KAEG-I [INTL VERSION]: ISA 510 Initial Audit Engagements - Opening Balances [ISA | KAEGISA510]

ISA 510 Initial Audit Engagements - Opening Balances

### **Introduction, Objective and Definitions**

International Standards on Auditing: ISA 510.01-04

### **Audit procedures, conclusions and reporting**

International Standards on Auditing: ISA 510.05-13

ISA Application and Other Explanatory Material: ISA 510.A1-A9

How do we comply with the standards?

[1 Initial Audit | Perform procedures for an initial audit](#)

[1.1 Initial Audit | Obtain evidence to support our opinion on the financial statements](#)

[1.1.1 Initial Audit | Read the most recent financial statements and the predecessor auditor's report](#)

[1.1.2 Initial Audit | Review the predecessor auditor's audit documentation](#)

[1.1.2.1 Initial Audit | Request authorization to review predecessor auditor's documentation](#)

[1.1.2.2 Initial Audit | Review the predecessor auditor's documentation](#)

[1.1.3 Initial Audit | Perform procedures over opening balances](#)

[1.1.3.1 Initial Audit | Obtain evidence that the opening balances were brought forward correctly](#)

[1.1.3.2 Initial Audit | Obtain evidence that the opening balances reflect appropriate accounting policies or principles](#)

[1.1.3.3 Initial Audit | Obtain evidence over the opening balances](#)

[1.1.3.4 Initial Audit | Do not make reference to or assume responsibility of the predecessor auditor](#)

[1.1.4 Initial Audit | Assess prior and current period financial statements for consistency](#)

[1.1.5 Initial Audit | Perform additional procedures when a possible misstatement is identified](#)

[1.1.5.1 Initial Audit | Determine the effect of misstatements on the current period financial statements](#)

[1.1.5.2 Initial Audit | Request the client to communicate items determined to be misstatements to the predecessor auditor](#)

[1.1.5.3 Initial Audit | Communicate misstatements to management and those charged with governance](#)

**Illustrations of Auditors' Reports with Modified Opinions**

International Standards on Auditing: ISA 510.Appendix

# ISA 510 Initial Audit Engagements - Opening Balances

[View the Full Chapter for this Standard](#)

## ISA 510 *Initial Audit Engagements - Opening Balances*

(Effective for audits of financial statements for periods beginning on or after December 15, 2009)

International Standard on Auditing (ISA) 510, *Initial Audit Engagements - Opening Balances*, should be read in conjunction with ISA 200, *Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with International Standards on Auditing*.

## Introduction, Objective and Definitions

### International Standards on Auditing: ISA 510.01-04

#### Introduction

#### Scope of this ISA

1. This International Standard on Auditing (ISA) deals with the auditor's responsibilities relating to opening balances in an initial audit engagement. In addition to financial statement amounts, opening balances include matters requiring disclosure that existed at the beginning of the period, such as contingencies and commitments. When the financial statements include comparative financial information, the requirements and guidance in ISA 710<sup>1</sup> also apply. ISA 300<sup>2</sup> includes additional requirements and guidance regarding activities prior to starting an initial audit.

---

<sup>1</sup> ISA 710, *Comparative Information - Corresponding Figures and Comparative Financial Statements*

<sup>2</sup> ISA 300, *Planning an Audit of Financial Statements*

#### Effective Date

2. This ISA is effective for audits of financial statements for periods beginning on or after December 15, 2009.

#### Objective

3. In conducting an initial audit engagement, the objective of the auditor with respect to opening balances is to obtain sufficient appropriate audit evidence about whether:

- (a) Opening balances contain misstatements that materially affect the current period's financial statements; and
- (b) Appropriate accounting policies reflected in the opening balances have been consistently applied in the current period's financial statements, or changes thereto are appropriately accounted for and adequately presented and disclosed in accordance with the applicable financial reporting framework.

## Definitions

4. For the purposes of the ISAs, the following terms have the meanings attributed below:

- (a) Initial audit engagement - An engagement in which either:
  - (i) The financial statements for the prior period were not audited; or
  - (ii) The financial statements for the prior period were audited by a predecessor auditor.
- (b) Opening balances - Those account balances that exist at the beginning of the period. Opening balances are based upon the closing balances of the prior period and reflect the effects of transactions and events of prior periods and accounting policies applied in the prior period. Opening balances also include matters requiring disclosure that existed at the beginning of the period, such as contingencies and commitments.
- (c) Predecessor auditor - The auditor from a different audit firm, who audited the financial statements of an entity in the prior period and who has been replaced by the current auditor.

## Audit procedures, conclusions and reporting

### International Standards on Auditing: ISA 510.05-13

## Requirements

### Audit Procedures

#### *Opening Balances*

5. The auditor shall read the most recent financial statements, if any, and the predecessor auditor's report thereon, if any, for information relevant to opening balances, including disclosures.

6. The auditor shall obtain sufficient appropriate audit evidence about whether the opening balances contain misstatements that materially affect the current period's financial statements by: (Ref: Para. A1 - A2)

- (a) Determining whether the prior period's closing balances have been correctly brought forward to the current period or, when appropriate, have been restated;
- (b) Determining whether the opening balances reflect the application of appropriate accounting policies; and
- (c) Performing one or more of the following: (Ref: Para. A3 - A7)

- (i) Where the prior year financial statements were audited, reviewing the predecessor auditor's working papers to obtain evidence regarding the opening balances;
- (ii) Evaluating whether audit procedures performed in the current period provide evidence relevant to the opening balances; or
- (iii) Performing specific audit procedures to obtain evidence regarding the opening balances.

7. If the auditor obtains audit evidence that the opening balances contain misstatements that could materially affect the current period's financial statements, the auditor shall perform such additional audit procedures as are appropriate in the circumstances to determine the effect on the current period's financial statements. If the auditor concludes that such misstatements exist in the current period's financial statements, the auditor shall communicate the misstatements with the appropriate level of management and those charged with governance in accordance with ISA 450.<sup>3</sup>

---

<sup>3</sup> ISA 450, *Evaluation of Misstatements Identified during the Audit*, paragraphs 8 and 12

### *Consistency of Accounting Policies*

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

### *Relevant Information in the Predecessor Auditor's Report*

9. If the prior period's financial statements were audited by a predecessor auditor and there was a modification to the opinion, the auditor shall evaluate the effect of the matter giving rise to the modification in assessing the risks of material misstatement in the current period's financial statements in accordance with ISA 315 (Revised).<sup>4</sup>

---

<sup>4</sup> ISA 315 (Revised), *Identifying and Assessing the Risks of Material Misstatement through Understanding the Entity and Its Environment*

## **Audit Conclusions and Reporting**

### *Opening Balances*

10. If the auditor is unable to obtain sufficient appropriate audit evidence regarding the opening balances, the auditor shall express a qualified opinion or disclaim an opinion on the financial statements, as appropriate, in accordance with ISA 705 (Revised).<sup>5</sup> (Ref: Para. A8)

---

<sup>5</sup> ISA 705 (Revised), *Modifications to the Opinion in the Independent Auditor's Report*

11. If the auditor concludes that the opening balances contain a misstatement that materially affects the current period's financial statements, and the effect of the misstatement is not appropriately accounted for or not adequately presented or disclosed, the auditor shall express a qualified opinion or an adverse opinion, as appropriate, in accordance with ISA 705.

### *Consistency of Accounting Policies*

12. If the auditor concludes that:

- (a) the current period's accounting policies are not consistently applied in relation to opening balances in accordance with the applicable financial reporting framework; or
- (b) a change in accounting policies is not appropriately accounted for or not adequately presented or disclosed in accordance with the applicable financial reporting framework,

the auditor shall express a qualified opinion or an adverse opinion as appropriate in accordance with ISA 705 (Revised).

### *Modification to the Opinion in the Predecessor Auditor's Report*

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

## ISA Application and Other Explanatory Material: ISA 510.A1-A9

### Application and Other Explanatory Material

#### **Audit Procedures**

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

A1. In the public sector, there may be legal or regulatory limitations on the information that the current auditor can obtain from a predecessor auditor. For example, if a public sector entity that has previously been audited by a statutorily appointed auditor (for example, an Auditor General, or other suitably qualified person appointed on behalf of the Auditor General) is privatized, the amount of access to working papers or other information that the statutorily appointed auditor can provide a newly-appointed auditor that is in the private sector may be constrained by privacy or secrecy laws or regulations. In situations where such communications are constrained, audit evidence may need to be obtained through other means and, if sufficient appropriate audit evidence cannot be obtained, consideration given to the effect on the auditor's opinion.

A2. If the statutorily appointed auditor outsources an audit of a public sector entity to a private sector audit firm, and the statutorily appointed auditor appoints an audit firm other than the firm that audited the financial statements of the public sector entity in the prior period, this is not usually regarded as a change in auditors for the statutorily appointed auditor. Depending on the nature of the outsourcing arrangement, however, the audit engagement may be considered an initial audit engagement from the perspective of the private sector auditor in fulfilling the auditor's responsibilities, and therefore this ISA applies.

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

A3. The nature and extent of audit procedures necessary to obtain sufficient appropriate audit evidence regarding opening balances depend on such matters as:

- The accounting policies followed by the entity.

- The nature of the account balances, classes of transactions and disclosures and the risks of material misstatement in the current period's financial statements.
- The significance of the opening balances relative to the current period's financial statements.
- Whether the prior period's financial statements were audited and, if so, whether the predecessor auditor's opinion was modified.

A4. If the prior period's financial statements were audited by a predecessor auditor, the auditor may be able to obtain sufficient appropriate audit evidence regarding the opening balances by reviewing the predecessor auditor's working papers. Whether such a review provides sufficient appropriate audit evidence is influenced by the professional competence and independence of the predecessor auditor.

A5. Relevant ethical and professional requirements guide the current auditor's communications with the predecessor auditor.

A6. For current assets and liabilities, some audit evidence about opening balances may be obtained as part of the current period's audit procedures. For example, the collection (payment) of opening accounts receivable (accounts payable) during the current period will provide some audit evidence of their existence, rights and obligations, completeness and valuation at the beginning of the period. In the case of inventories, however, the current period's audit procedures on the closing inventory balance provide little audit evidence regarding inventory on hand at the beginning of the period. Therefore, additional audit procedures may be necessary, and one or more of the following may provide sufficient appropriate audit evidence:

- Observing a current physical inventory count and reconciling it to the opening inventory quantities.
- Performing audit procedures on the valuation of the opening inventory items.
- Performing audit procedures on gross profit and cutoff.

A7. For non-current assets and liabilities, such as property, plant and equipment, investments and long-term debt, some audit evidence may be obtained by examining the accounting records and other information underlying the opening balances. In certain cases, the auditor may be able to obtain some audit evidence regarding opening balances through confirmation with third parties, for example, for long-term debt and investments. In other cases, the auditor may need to carry out additional audit procedures.

## **Audit Conclusions and Reporting**

### *Opening Balances (Ref: Para. 10)*

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

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

The Appendix includes illustrative auditors' reports.

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

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

## How do we comply with the Standards?

[ISA | KAEGHDWC]

## 1 Initial Audit | Perform procedures for an initial audit [ISA | 741]

### What do we do?

IF the audit is an initial audit THEN perform the appropriate procedures.

### Why do we do this?

In an initial audit, we may have little or no experience with the entity, so we perform incremental procedures as part of conducting our initial audit. We perform incremental procedures during an initial audit to help us obtain the evidence in order to conclude on our current audit.

## Execute the Audit

[What procedures do we perform for an initial audit?](#) [ISA | 741.10722]

We perform the following procedures for an initial audit:

- [Consult if specific circumstances apply](#)
- [Obtain evidence to support our opinion on the financial statements](#)

[What is an initial audit?](#) [ISA | 741.1300]

An initial audit is an engagement to audit the financial statements in which:

- the financial statements for the prior period were not audited; or
- the financial statements for the prior period were audited by a different auditor (i.e. predecessor auditor).

[When do initial audits arise?](#) [ISA | 741.10723]

There are different scenarios that lead to initial audits, including:

Type of Initial Audit	Scenario
-----------------------	----------

If the financial statements for the prior period were not audited	<b>Newly established entity</b>  This is the first year the entity is in existence (e.g. Start-up company or a newly formed business venture). Since this is a new entity, there is no predecessor auditor and no opening balances or comparative financial figures to consider.
---	--

### What additional procedures do we perform for an initial audit? [ISA | 741.1500]

In addition to the audit procedures we perform for all audits, during an initial audit, there are certain incremental procedures we perform including:

Incremental procedure for an initial audit	Newly established entity	Initial audit of an existing entity, not previously audited	Initial audit of an existing entity, previously audited
<a href="#">Perform incremental client and engagement acceptance procedures</a>	✓	✓	✓
<a href="#">Communicate with the predecessor auditor</a>	N/A - no predecessor auditor	N/A - no predecessor auditor	✓
<a href="#">Consult if specific circumstances apply</a>	N/A - no financial statements or predecessor auditor report	N/A - no financial statements or predecessor auditor report	✓
<a href="#">Obtain evidence to support our opinion on the financial statements</a> by performing the following:			
<a href="#">Reading the financial statements and predecessor auditor's report(s)</a>	N/A - no financial statements or predecessor auditor report	✓  Read financial statements/ management reports, if available, but there will be no	✓



		predecessor auditor report	
<a href="#">Reviewing predecessor auditor audit documentation</a>	N/A - no predecessor auditor nor audit documentation	N/A - no predecessor auditor nor audit documentation	✓
<a href="#">Performing procedures over opening balances</a>	N/A - No opening balances	✓	✓
<a href="#">Assessing prior financial statements, if applicable, and current period financial statements for consistency</a>	N/A - No comparative application of accounting policies or principles	✓	✓
<a href="#">Performing additional procedures when a possible misstatement is identified</a>	N/A - no financial statements	✓  Read financial statements/ management reports, if available, but there will be no predecessor auditor report	✓

When do we perform the incremental procedures for an initial audit? [ISA | 741.1600]

There are certain inquiries we make and firm policies we follow before we accept a client engagement. Other procedures, such as review of the predecessor auditor's audit documentation, can occur before or after we accept the engagement.

## 1.1 Initial Audit | Obtain evidence to support our opinion on the financial statements [ISA | 747]

### What do we do?

Perform incremental procedures - including procedures over opening balances - to obtain sufficient appropriate audit evidence to support our audit opinion on the initial audit

## Why do we do this?

Since we did not audit the prior period closing balances, we perform audit procedures to obtain evidence over the current year opening balances, including the appropriateness and application of accounting policies or principles over the opening balances to determine the effect on the current-year financial statements.

## Execute the Audit

### What procedures do we perform for an initial audit? [ISA | 747.1300]

In addition to following the other audit standards, we perform audit procedures to obtain evidence about whether:

- opening balances contain misstatements that materially affect the current period's financial statements; and
- appropriate accounting policies or principles and the application of accounting policies or principles over the opening balances have been consistently applied in the current period's financial statements or changes have been appropriately accounted for and adequately presented and disclosed in accordance with the applicable financial reporting framework.

### What incremental procedures do we perform? [ISA | 747.10802]

The incremental audit procedures we perform to obtain audit evidence over opening balances, and the consistency of the application of accounting policies or principles include:

- [Reading](#) the financial statements and predecessor auditor's report(s), if any
- [Reviewing](#) predecessor auditor audit documentation if we chose to
- [Performing](#) procedures over opening balances
- [Assessing](#) prior and current period financial statements for consistency
- [Performing additional procedures when a possible misstatement is identified](#)

## 1.1.1 Initial Audit | Read the most recent financial statements and the predecessor auditor's report [ISA |

748]

## What do we do?

Read the most recent financial statements and the predecessor auditor's report(s), if any, for specific information.

## Why do we do this?

We read the financial statements to obtain evidence about whether the accounting policies or principles have been consistently applied, and whether changes in the accounting policies or principles have been appropriately accounted for, adequately presented and disclosed. We also do this to obtain evidence about the appropriateness of the significant accounting policies or principles selected by management.

We read the predecessor auditor's report to see if it included a modification and, if so, whether that modification is still relevant and material to the current period's financial statements.

## Execute the Audit

When we read the financial statements and predecessor auditor's report(s) what specific items do we consider? [ISA | 748.1300]

We read for items that we may consider further during risk assessment or in designing audit procedures, such as:

- information relevant to the appropriateness of the opening balances, including disclosures;
- information about any possible policies that depart from the financial reporting framework (i.e. non-GAAP);
- information about significant issues and judgments, including the consistency of the application of accounting policies or principles; and/or modifications of the auditor's report.

### How might we interpret this information?

When we read the financial statements and predecessor auditor's report(s) we may identify important information that we may have to interpret such as:

- Information relevant to the appropriateness of the opening balances, including disclosures.
  - For example, you may find that the some of the disclosures are not in-line with your expectations of the industry standard, knowledge of the entity, or not consistent with the account balances.
- Information about any possible policies or principles that depart from the financial reporting framework (i.e. non-GAAP)
  - For example, in the summary of significant accounting policies or principles, entities may discuss these departures and note that they are not material to the annual financial statements such as "The impact of recognizing an expense ratably over the length of a contract is not materially different on a quarterly and annual basis from a method of recognizing costs as incurred."
- Information about significant issues, including application of accounting policies or principles
  - For example, new accounting standards that are anticipated to have a significant impact on the entity as these are often disclosed in the year before the effective date.
- Information about changes in the overall market/economic factors and the impact to management's plan.
  - For example, an entity that operates in the oil and gas industry where there is a significant decline in oil price could indicate a risk of material misstatement exists related to impairment.
- Modification to the predecessor auditor's opinion and that modification continues to remains relevant and material in the current period
  - For example, the predecessor auditor may have a modification to their auditor's report related to a scope limitation as there was a fire and not all records were available to the auditor. The lack of records still has an impact on the opening balances so this modification is likely to continue to be relevant to the current period audit.

### What if there is a modification in the prior period auditor's report(s)? [ISA | 748.1400]

We evaluate the possible effects on our current audit. This is particularly relevant when the matter(s) that led to the modification may have a continuing impact on the current period financial statements.

We think about how these matters might inform us about possible risks of misstatement (RM) in the current period, which may lead to us identifying and assessing a risk of misstatement as part of our risk assessment procedures. If there is a continuing impact on the current period financial statements, we also consider whether similar modifications are necessary in our report on the current period's financial statements.

### What if there is no prior period financial statements and/or predecessor auditor's report(s)? [ISA | 748.1500]

We may read internal management or financial reports, which can provide us similar information.

## 1.1.2 Initial Audit | Review the predecessor auditor's audit documentation [ISA | 749]

### What do we do?

Review the predecessor auditor's audit documentation AND consider the impact on our audit.

### Why do we do this?

By reviewing the predecessor auditor's audit documentation, we can learn information that will help us to identify and assess risks of material misstatement (RMMs), as well as consider the impacts to our overall audit strategy and plan.

## Execute the Audit

### What are the steps we undertake when reviewing predecessor audit documentation? [ISA | 749.1300]

We:

- [request client authorization to allow us to review the predecessor auditor's audit documentation,](#) and
- [perform our review of the predecessor auditor's audit documentation and consider the impacts on our audit.](#)

## 1.1.2.1 Initial Audit | Request authorization to review predecessor auditor's documentation [ISA | 750]

### What do we do?

Request that management authorize us to review the predecessor auditor's audit documentation and make further inquiries

### Why do we do this?

Audit documentation includes confidential client information that is typically subject to confidentiality laws of the local jurisdictions. Because of such laws, we generally obtain the entity's consent before we request information about the audit from the predecessor auditor.

## Execute the Audit

If we chose to review predecessor auditor workpapers, how do we request access? [ISA | 750.10814]

If we chose to review the prior period audit documentation of the predecessor auditor, we follow local laws and regulations in regards to the process to be followed.

Are there examples to assist us in drafting a letter requesting access to review the predecessor auditor's audit documentation? [ISA | 750.10815]

Example letters are located on [Alex](https://alex.kpmg.com/AROWeb/bridge/18152/18153?d=CN,INTL,AU,NL,SG,UK,US) <https://alex.kpmg.com/AROWeb/bridge/18152/18153?d=CN,INTL,AU,NL,SG,UK,US>.

What if management declines or limits our access to the predecessor auditor? [ISA | 750.1400]

If management refuses to provide authorization, or attempts to limit our access to the predecessor auditor, then we:

- inquire about the reasons for the refusal/limitation; and
- consider the effect on our audit approach.

Depending on the reason for the refusal/limitation, we may consult with DPP, or other appropriate parties, as there may be risk management considerations to address.

What predecessor auditor information might we expect to have access to? [ISA | 750.1600]

In some cases, the predecessor auditor may agree to provide us with copies of certain information included in the audit documentation. We follow two general principles when requesting access to audit documentation, copies or determining what other information to ask for:

- consider whether the entity itself could provide that information; and
- consider whether we would provide access, copies or other information if we were the predecessor auditor.

There are also relevant standards, laws and regulations in specific jurisdictions that may cover these matters. The extent to which the predecessor auditor permits access to the audit documentation is a matter of the predecessor auditor's judgment.

Are we expected to provide anything to the predecessor auditor when reviewing their audit documentation? [ISA | 750.1700]

The predecessor auditor ordinarily asks us to sign an acknowledgement letter.

Before complying with this request, we ordinarily first compare their requested letter to the standard acknowledgement letter we ask successor auditors to sign. By comparing to our standard letter, we can see if the acknowledgement letter contains anything that is outside or missing from our standard acknowledgement letter.

If the letter contains terms and conditions that we do not find acceptable, we respond back to the predecessor auditor to discuss our suggested updates.

## 1.1.2.2 Initial Audit | Review the predecessor auditor's documentation [ISA | 751]

### What do we do?

Review the predecessor auditor's audit documentation AND consider the impact on our audit.

### Why do we do this?

Reviewing the predecessor auditor's audit documentation can provide insights into a variety of matters that can affect the nature and extent of the additional audit procedures we perform over opening balances, as well as help us in performing our risk assessment and planning the current year audit.

### Execute the Audit

**How might we prepare before reviewing the predecessor auditor's audit documentation?** [ISA | 751.1300]

Before we review predecessor auditor's audit documentation, it is helpful to gain a broad understanding of the entity to increase the efficiency and effectiveness of the review and our ability to identify and assess risks of misstatement. This broad understanding may include reading previous financial statements and auditor's reports, as well as information gained through our initial inquiries with management and client acceptance procedures.

**How does obtaining an understanding of the entity before reviewing the predecessor auditor's audit documentation help?** [ISA | 751.1400]

Obtaining an understanding of the entity helps us identify specific matters we may consider and discuss with the predecessor auditor during our reviews. In addition, it can help us better identify and assess risks of misstatements where we will want to devote more attention during our reviews.

**What other information is relevant to building our understanding of the entity in addition to the predecessor auditor's audit documentation?** [ISA | 751.1500]

Relevant information that may be available at this stage includes:

- key issues discussed with management or those charged with governance as part of the proposal/tender process;
- information included in documents obtained from the entity that are relevant to the audit - e.g. the entity may be able to provide copies of audit committee reports, audit misstatement schedules, management representation letters, management letters etc.;
- information presented in the most recent financial statements that allows us to assess the appropriateness of the accounting policies or principles and disclosures;
- information contained in the auditor's report (including the form of opinion issued) on the most recent financial statements; and
- information related to the entity obtained as part of the client acceptance process.

**What are we focused on learning during our review of the predecessor auditor's audit documentation?** [ISA | 751.1600]

We are focused on identifying information that may have significance in our current audit and information that can help us determine whether the balances from the prior period financial statements are brought forward into the current period financial statements correctly. We also focus on areas that could influence the nature and extent of work we will perform over opening balances and to evaluate the consistency of the application of accounting policies or principles.

More significant items that could impact the audit might include information about:

Type of predecessor audit documentation	How the information may impact our audit planning
Planning of the audit	We may obtain information that provides us insight into the timing of the audit, key audit focus areas and prior year audit issues that we can prioritize in the current year.
Business understanding and risk assessment	We may obtain information to enhance our understanding of the entity and its environment, including internal control. If we use this information, this can be a starting point for us to have inquiries with management, inspect key business documents and consider our understanding of the industry in which the entity operates and other relevant external factors to corroborate the information.
Risks of material misstatement, significant risks and estimates	We may obtain information about risks of material misstatement, significant risks and significant estimates. We use this information as a starting point to help inform our risk assessment. However, for each process that is relevant to the audit, we still perform our own risk assessment procedures in the current period audit.
Audit differences	<p>We evaluate the treatment and effects of uncorrected audit differences on both opening and closing balances of the period under audit.</p> <p>We have no obligation to accept previous methods of evaluating audit differences or any agreements between the entity and the predecessor auditor about their treatment.</p> <p>We evaluate the effects of any audit differences, including those that exist at the beginning of the period under audit such that we are satisfied that the financial statements being audited are free from material misstatement.</p>
Responses to confirmations with third parties	We may consider responses to confirmation requests received by the predecessor auditor, provided we are able to

	<p>review the confirmations during our predecessor workpaper review.</p> <p>These responses may relate to, for example, accounts receivable, debt and other balance and transaction confirmations, related party questionnaires, and responses to inquiries from attorneys. We evaluate the process used by the predecessor auditor in controlling the confirmation process and in selecting the accounts (items) for confirmation and the persons or entities for inquiry.</p>
Key stakeholders	Predecessor audit documentation helps us have a starting point for identifying key stakeholders, which may help us make our materiality assessments and perform other risk assessment procedures.
Applicable laws and regulations	Predecessor audit documentation helps us have a starting point for identifying the applicable laws and regulations for our consideration in performing our risk assessment procedures.

#### Who performs the review of the predecessor auditor's audit documentation? [ISA | 751.1800]

Engagement team members with the appropriate level of experience and knowledge to review the predecessor auditor's audit documentation perform the review. When assigning engagement team members for this purpose, we may also consider including specific team members (i.e. tax and IT Audit) as well as employed KPMG specialists (i.e. Valuations) on the review team.

From our preliminary understanding of the client, we will likely understand those audit areas with higher complexity and can consider that understanding when deciding whether to involve others. For example, if an entity has a sophisticated and complex IT system, we might involve an IT Audit specific team member with the appropriate system's experience and knowledge to assist in reviewing the audit documentation.

## Example

#### Example audit documentation review template [ISA | 751.2100]

The purpose of this template is to illustrate how our review of the predecessor auditor's audit documentation in the context of an initial audit may be documented. The template should be tailored to the specific circumstances of the engagement.

<b>Name of Client</b>	[Insert name]
<b>File for period end</b>	[Insert period end date]



<b>Entities covered</b>	[Insert entities or business units covered]
<b>Financial reporting framework</b>	[Insert financial reporting framework]
<b>Reporting approach for comparative information</b>	[Corresponding figures or comparative financial statements]

**Key stakeholders**

<b>Stakeholder</b>	<b>Comments</b>

**Applicable laws and regulations**

<b>Law or regulation</b>	<b>Impact to the audit</b>

**Identified risks of material misstatements** *[complete for each RMM]*

<b>Risk of material misstatement</b>	[List identified risks of material misstatement]
<b>Accounts</b>	[List key accounts where risks of material misstatements were identified]
<b>Key estimates</b>	[List key estimates]
<b>Controls tested</b>	[List controls tested and any deficiencies noted]
<b>Substantive procedures performed</b>	[Describe procedures performed]
<b>Involvement of specific team members and/or specialists</b>	[List specific team members and/or specialists involved and describe their involvement]

<b>Significant accounting issue memorandums</b>	[Describe accounting issues discussed in any memorandums including consultations with national office]
---	--

**Materiality**

<b>Materiality</b>	[Insert \$ value]
<b>Basis for determining materiality</b>	[e.g. x% of profit before tax]
<b>Other considerations noted</b>	[Any other relevant information]

**Business risks that may result in material misstatements, including significant risks**

<b>Business risks identified</b>	[List]
----------------------------------	--------

**Estimates identified as giving rise to a significant risk**

<b>Description</b>	[Describe the estimates]
<b>Key accounts affected</b>	
<b>Procedures performed</b>	[Describe procedures performed]
<b>Involvement of specific team members and/or specialists</b>	[List specific team members and/or specialists involved and describe their involvement]

**Going concern**

<b>Going concern issues identified</b>	[Describe any going concern issues identified]
<b>If yes describe procedures performed</b>	[Describe procedures performed, in order to determine whether there was material uncertainty related to going concern issues and mitigating factors identified]

**Discussions with Management and Those Charged With Governance**

<b>Person</b>	Issues noted
<b>[Name and title]</b>	[Describe significant items discussed]

**CERAMIC**

<b>Understanding of CERAMIC</b>	[Describe understanding of CERAMIC components]
<b>Procedures performed</b>	[Describe procedures performed]
<b>Significant deficiencies noted</b>	[Describe any significant deficiencies noted]

**IT Environment**

<b>Key systems identified</b>	[List]
<b>Was a specific team member and/or specialist involved in the audit?</b>	[Y/N]
<b>Key IT general controls identified and tested</b>	[Describe controls tested and any significant issues noted]

**Related Parties**

<b>Related party relationships and transactions</b>	[List relationships and transactions identified]
<b>Procedures performed</b>	[Describe procedures performed]

**Loan Agreements**

<b>Agreement</b>	[Description of key terms]
<b>[Insert name]</b>	[List details including covenant details if any]

**Other significant agreements**

<b>Agreement</b>	Description of key terms
<b>[e.g. leases, supply, sales]</b>	[List details including covenant details if any]

**Significant Unusual Transactions**

<b>Description</b>	[Describe the transaction - e.g. Acquisition of X]
<b>Procedures performed</b>	[Describe procedures performed]
<b>Key judgements</b>	[Note key judgements]
<b>Involvement of specific team members and/or specialists</b>	[List specific team members and/or specialists involved and describe their involvement]

**Confirmations**

<b>Lawyer</b>	[List solicitors contacted and any significant issues noted]
<b>Bank</b>	[List banks]
<b>Investments</b>	[Note any issues identified]
<b>Debtor</b>	[Note any issues identified]
<b>Supplier</b>	[Note any issues identified]
<b>[Other - insert as required]</b>	

**Fraud**

<b>Fraud risks</b>	[List risks]
<b>Procedures to test the appropriateness of journal entries</b>	[Describe procedures performed]

<b>Procedures performed to address the other fraud risks</b>	[Describe procedures performed]
<b>Instances of fraud noted</b>	[Note any instances of fraud or suspected fraud]
Instances of management bias	[Note any instances of management bias]

**Other significant risks identified**

<b>Description</b>	[Describe the risks]
<b>Key accounts affected</b>	
<b>Procedures performed</b>	[Describe procedures performed]
<b>Involvement of specific team members and/or specialists</b>	[List specific team members and/or specialists involved and describe their involvement]

**Financial statements**

<b>Referenced financial statements on file</b>	[Y/N]
<b>Disclosure checklist or equivalent</b>	[Y/N]
<b>Supporting work papers for amounts not directly from the general ledger</b>	[Describe areas where additional papers included]

**Misstatements**

<b>Uncorrected misstatements</b>	[List significant misstatements]
----------------------------------	----------------------------------

<b>Corrected misstatements</b>	[List areas in which misstatements were made]
--------------------------------	---

**Does the predecessor auditor's file include the following?**

Item	Included?	Comments
<b>Signed auditor's report</b>	[Y/N]	[Any qualification, other matters etc.]
<b>Signed engagement letter</b>	[Y/N]	[Any unusual terms or general terms omitted]
<b>Signed representation letter</b>	[Y/N]	[Any unusual terms or general terms omitted]
<b>Audit misstatement schedule</b>	[Y/N]	
<b>Modifications to the auditor's report</b>	[Y/N]	[Describe modifications]

## 1.1.3 Initial Audit | Perform procedures over opening balances [ISA | 752]

### What do we do?

Perform procedures over the opening balances to identify possible material misstatements in the current period's financial statements.

### Why do we do this?

We perform procedures to obtain sufficient appropriate audit evidence about whether the opening balances contain a material misstatement because of the possible effect such a misstatement could have on the current period's financial statements and consequently our audit approach.

## Execute the Audit

**What procedures do we perform over opening balances?** [ISA | 752.1300]

The procedures we perform over opening balances are:

- (1) [Obtain evidence that the opening balances were brought forward correctly](#);
- (2) [Obtain evidence that the opening balances reflect appropriate accounting policies or principles](#);
- and
- (3) [Obtain evidence over the opening balances](#).

[We also consider the impact of the work of the predecessor auditor on our report.](#)

What might affect the nature and extent of our audit procedures? [ISA | 752.1400]

The level of testing can be influenced by:

- the results of our review of the predecessor auditor's audit documentation;
- the complexity of the accounting policies or principles followed by the entity;
- the nature of the significant accounts and disclosures and risks of material misstatement;
- the significance of opening balances and the ongoing impact of opening balances on the current period financial statements (e.g. deferred revenue, lease agreements that span multiple years, litigation accruals, and acquisitions and the related purchase price allocation);
- the input from other procedures performed in the current period, where we have obtained some evidence over the opening balances, then we may take that into account when determining the nature and extent of additional procedures; and/or
- the prior period's financial statements were audited and, if so, whether the predecessor auditor's opinion was modified.

## 1.1.3.1 Initial Audit | Obtain evidence that the opening balances were brought forward correctly <sup>[ISA</sup>

| 753]

### What do we do?

Obtain sufficient appropriate audit evidence about whether the opening balances have been brought forward correctly

### Why do we do this?

We obtain evidence that the prior period's closing balances have been brought forward to the current period, as the opening balances make up the basis for the current period's financial statements. A misstatement in the opening balances may have a material effect on the current period's financial statements. An entity may use a change in auditor as an opportunity to inappropriately correct errors in prior period financial statements.

## Execute the Audit

[How might we obtain evidence over whether the opening balances are correctly brought forward?](#) [ISA | 753.1300]

Example procedures performed to determine whether prior period balances have been correctly brought forward, or where appropriate, have been restated may include:

Procedure	Evidence obtained
Reconcile current period opening balances to the prior period closing balances	<p>This will help us identify any differences between the closing and opening balances in the general ledger. This may include errors in transferring the numbers from the prior period to the current period within the system, highlight when the entity may have changed how they map their general ledger accounts to the financial statements and/or include instances where the entity may inappropriately be correcting errors from prior periods.</p> <p>We perform these procedures at the detailed general ledger level.</p>
Agree the opening balances to the prior period audited financial statements	<p>This will help us identify any differences between the values in the audited financial statements and the opening general ledger balances. This may identify errors in the prior period mapping of account balances, and/or can also include instances where the entity may inappropriately be correcting errors in prior period financial statements.</p> <p>It also allows us to identify if the information is obtained from within or outside of the general and subsidiary ledgers.</p> <p>We perform these procedures at the financial statement level.</p>
Agree the opening balances to the predecessor auditor's audit documentation	<p>We may also want to obtain information from the entity before we go to review the predecessor auditor's audit documentation, so we can perform a reconciliation of the opening balances to the predecessor auditor's audit documentation.</p> <p>This can be done by area or in total, by obtaining information from the client about the opening balances and agreeing them to the information in the predecessor auditor's audit documentation.</p> <p>Areas of the audit that we may want to focus in reconciling the opening balances to the predecessor auditor's audit documentation include accounts where we typically test roll-forward schedules such as debt, equity, trade receivables, financial assets, taxes, pensions, inventory, intangible assets or property, plant and equipment.</p>



## 1.1.3.2 Initial Audit | Obtain evidence that the opening balances reflect appropriate accounting policies or principles [ISA | 754]

### What do we do?

Obtain sufficient appropriate audit evidence that the opening balances reflect the application of appropriate accounting policies or principles

### Why do we do this?

We determine if the opening balances reflect the application of appropriate accounting policies or principles as the opening balances establish the starting position for the current period's financial statements. Since this is our first year auditing the entity, the inappropriate application of accounting policies or principles may have a material effect on the current period's financial statements. An entity may also use a change of auditor, as an opportunity to inappropriately change to an alternative accounting policy or principle.

### Execute the Audit

How might we obtain evidence over the application of appropriate accounting policies or principles? [ISA | 754.1300]

We are focused on the opening balances and not the consistency between application of accounting policies or principles period over period. Some example procedure to determine if the application of appropriate accounting policies or principles are reflected in the opening balances may include:

What do we do?	What do we look for?
Review the financial statement disclosures and the entity's accounting memos from the prior period	<p>We evaluate whether the entity's accounting policies or principles are appropriate for its business/relevant industry and consistent with the applicable financial reporting framework.</p> <p>To make this evaluation we determine whether:</p> <ul style="list-style-type: none"> <li>• accounting policies or principles selected and applied are consistent with the applicable financial reporting framework and are appropriate;</li> <li>• the accounting policies or principles, including any changes / effective accounting pronouncements, are appropriately disclosed in the financial statements; and</li> <li>• accounting estimates made by management are reasonable</li> </ul>

Review the predecessor auditor's audit documentation that supports the accounting policy or principle elections or memos containing considerations for alternative positions

We evaluate the qualitative aspects of the entity's accounting practices, including indicators of possible bias in management's judgments and their rational for the accounting policy or principle elections.

## 1.1.3.3 Initial Audit | Obtain evidence over the opening balances [ISA | 755]

### What do we do?

Obtain sufficient appropriate audit evidence over the opening balances AND qualify or disclaim an opinion if such evidence is not available.

### Why do we do this?

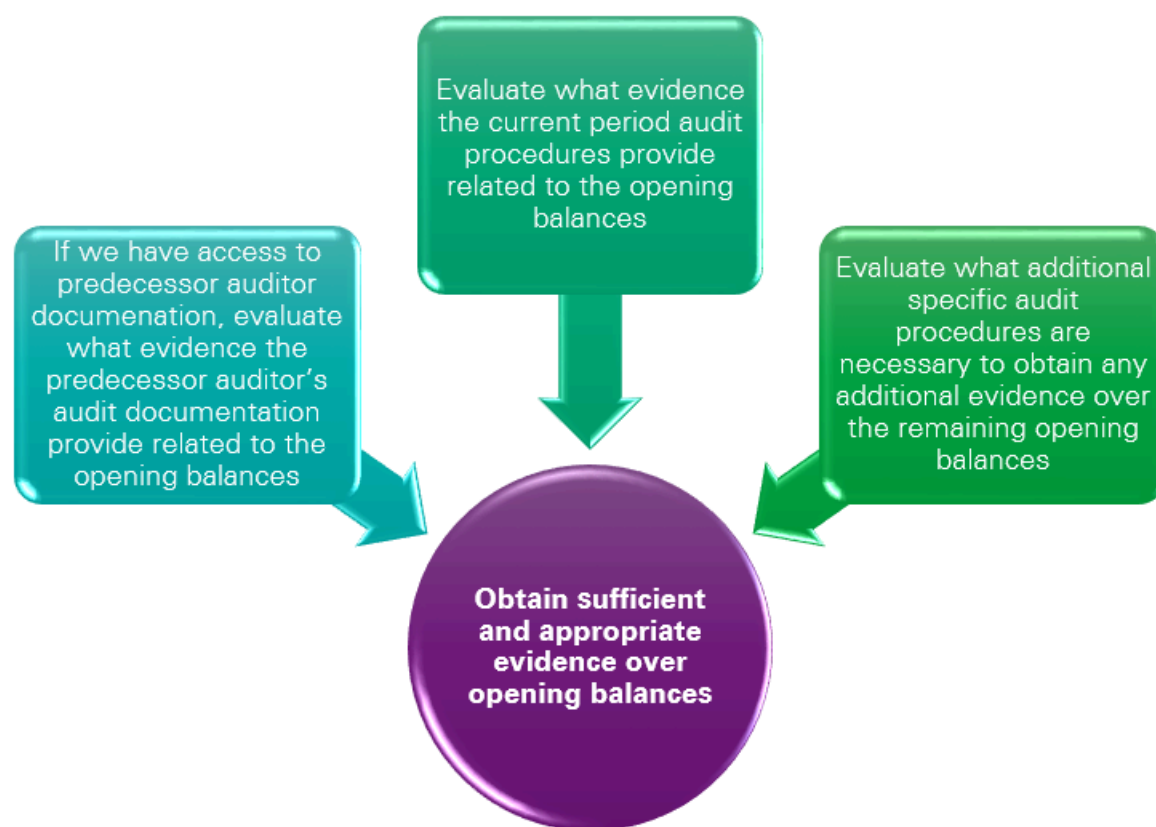
Opening balances can impact the current period financials statements. Since we did not audit the prior year financial statements, we obtain evidence over the opening balances to support our audit opinion. If we are unable to obtain sufficient appropriate evidence, we determine whether we issue a qualified opinion or disclaim an opinion.

## Execute the Audit

[How do we obtain sufficient appropriate audit evidence over the opening balances?](#) [ISA | 755.1300]

We consider what evidence can be used to obtain sufficient appropriate audit evidence over the opening balances. We look to one or more of these three sources that might be used to obtain sufficient audit evidence:

- (1) Review of predecessor auditor's documentation, if allowed under local rules and regulations;
- (2) Audit procedures performed over the current period financial statements that provide evidence related to the opening balances;
- (3) Additional specific audit procedures over opening balances



How might the predecessor auditor's audit documentation impact our procedures over the opening balances? [ISA | 755.1400]

The predecessor auditor's audit documentation may impact the procedures we perform in a number of ways, some of which are outlined below:

Scenario	Impact on our procedures
We identify areas where the predecessor auditor's audit documentation highlighted areas of risk or judgement from the prior period over which it may be necessary for us to obtain further evidence during the current year audit.	We might obtain further evidence in the current year over transactions that have continuing relevance, such as a business combination.
We identify areas where the predecessor auditor's audit documentation may have identified issues or previous errors that could impact the current year, which may cause us to want to test the issue ourselves	The prior period audit may have identified cut-off issues or issues in ending balances of certain accounts that may cause us to want to perform cut-off procedures related to opening balances or other specific test work to confirm or determine existence of opening balances.

We identify areas where the predecessor auditor's work may not be sufficient for our purposes or where we believe we may perform additional work.	In a situation where a business combination was still "provisional" at prior period-end; we obtain our own audit evidence when the final accounting related to the business combination happens in the current period.
---	--

How might we evaluate the predecessor auditor's audit documentation and determine the extent of additional procedures to perform? [ISA | 755.10862]

Below are examples of how we might evaluate the predecessor's audit documentation:

Evaluation of predecessor audit documentation	Impact on our procedures over opening balances
The predecessor auditor sent accounts receivable confirmations by haphazardly selecting a sample of 5 accounts receivables, instead of a statistical sample. One of the confirmation responses identified a difference, but the difference was resolved by the predecessor auditor.	We decide to send our own confirmations or perform subsequent receipt testing over a statistical sample of balances that comprise accounts receivable at the beginning of the period.
The predecessor auditor sent accounts receivable confirmations by selecting a statistical sample of accounts receivables. All responses were received and there were no differences identified.	We decide that the evidence expected to be obtained through our current period audit procedures examining write-offs/adjustments to accounts receivable during the period is sufficient.

How do we evaluate what evidence the current period audit procedures will provide related to the opening balances when performing an initial audit? [ISA | 755.1500]

We use our existing audit knowledge and understanding to identify the procedures we can perform in the current year that might provide us evidence over the opening balances. Certain procedures being performed in the current period audit in response to a current risks of material misstatement may provide evidence relevant to opening balances.

For example, if we had a valuation of a property and there were no issues with the valuation in the current period and circumstances have not changed in the current period, this may provide evidence about possible impairments in the prior period. A contrasting example, is if the property was impaired in the current year, we consider the implications to the opening balances and perhaps that the prior year balance could have been impaired.

What are examples of procedures in the current year that may provide evidence related to the opening balances? [ISA | 755.1700]

Types of procedures that may provide evidence about opening balances include:

- revenue transaction testing in current period (e.g. auditing revenue transactions and determining there were no cut-off errors or timing issues with transactions recorded in prior periods);
- inventory observation (e.g. rollback an inventory observation to the opening period and testing the intervening transactions) as well as the procedures over inventory adjustments, write-offs, etc. during the period.
- valuation test work (e.g. if there was no significant changes from prior period, we could leverage the valuation test work in the current period and apply it to the opening balance by obtaining sufficient and appropriate evidence over the prior period inputs)
- procedures testing the appropriateness of the release of a material legal accrual;
- retrospective review of the outcome of an accounting estimate included in the prior period financial statements as part of our current period audit procedures, including evaluating the consistency of the application of accounting policies or principles (e.g. indicators of the appropriateness of management's estimates and estimation process);
- testing collections (payment) of accounts receivable (accounts payable) during the current period and write-offs of uncollectible accounts;
- confirmation with third parties (e.g. long-term debt and investments)

How might the predecessor auditor's professional competence and independence impact us? [ISA | 755.1750]

To the extent there are significant concerns with the level of work performed or conclusions reached in the prior period (based on our review of the audit documentation) and/or the professional competence and independence of the predecessor firm, it may impact our ability to obtain sufficient audit evidence in the current period and over the opening balances.

Why might we consider evaluating the predecessor auditor's professional competence and independence?

Our evaluation of the predecessor auditor's professional competence and independence can influence how we use the information resulting from our review of the predecessor auditor's audit documentation. When the predecessor auditor does not display an appropriate level of competence and/or independence, this may result in us performing additional procedures to obtain more persuasive evidence over opening balances and appropriateness of the accounting policies or principles.

How do we evaluate the predecessor auditor's professional competence and independence?

We make inquiries to assess the professional competence and independence of the predecessor auditor. These may include:

- evaluating the predecessor auditor's professional qualifications;
- understanding their experience in the entity's sector; and
- determining whether they have been subject to any regulatory investigations or audit inspections, and reviewing any publicly available inspection reports.
- understanding their assessment of independence as it relates to the entity

How do we evaluate what additional specific audit procedures to perform, to obtain any additional evidence over the remaining opening balances when performing an initial audit? [ISA | 755.10865]

Additional procedures related to the opening balances are designed and performed like any other procedure in our audit; however, they are targeted at gaining evidence specifically related to the opening balances.

These procedures could range from testing specific prior period transactions that accumulate into the opening balances, specifically testing opening balance amounts, or applying current period cutoff procedures to opening balance amounts. We may also be able to incorporate additional procedures to current period work to gain evidence over the opening balance (for instance rolling back observation of inventory).

#### What if we are unable to obtain sufficient appropriate audit evidence or if we identify a material misstatement related to opening balances? [ISA | 755.1800]

If we are unable to obtain evidence over the opening balances, we may modify our auditor's opinion. For example, there is an unsupported material accrual in the prior period that was released in the current period. If we were unable to obtain evidence about the appropriateness of the accrual and its release, then a misstatement may exist in both the current period and prior period.

When we are unable to obtain evidence see the chapter on modifications to the audit opinion ([AS 3105](#); [ISA 705](#); [AU-C 705](#)).

#### What if we conclude the predecessor auditor's audit documentation is lacking or incomplete? [ISA | 755.10867]

We perform additional procedures over these areas determined to be lacking or incomplete to obtain sufficient appropriate audit evidence regarding the opening balances on the current period's financial statements. For instance, through our review of predecessor auditor's audit documentation, we conclude that the predecessor auditor did not document sufficient audit procedures or evidence relating to a valuation of an asset. When we identify a deficiency in the predecessor auditor's audit documentation, we take this into consideration and perform procedures to obtain the evidence in order to assess the impact of the opening balance on the current-year financial statements.

## 1.1.3.4 Initial Audit | Do not make reference to or assume responsibility of the predecessor auditor [ISA

| 7611]

### What do we do?

Do not make reference to the report or the work of the predecessor, assume responsibility for the predecessor auditor's work or issue a report that reflects divided responsibility.

### Why do we do this?

In reporting on the audit, the successor auditor does not make reference to or assume responsibility for the work of the predecessor auditor, nor does the successor auditor issue a report that reflects divided responsibility. To do otherwise might introduce risks that audit procedures are not performed by

either auditor. If this were to occur, the successor auditor's opinion would not be supported by the work performed.

## Execute the audit

[Can we divide responsibility for the opening balances with the predecessor auditor?](#) [ISA | 7611.11163]

In general no. However, we may refer to the predecessor auditor's report on the corresponding figures, in an Other Matters paragraph in our auditor's report in accordance with ISA 710 Comparative Information - Corresponding Figures and Comparative Financial Statements.

## 1.1.4 Initial Audit | Assess prior and current period financial statements for consistency [ISA | 756]

### What do we do?

Assess the consistency between the prior period's and current period's financial statements and their application of accounting policies or principles

### Why do we do this?

We evaluate the consistency of the application of accounting policies or principles to the opening balances and to the current period's financial statements as the entity may use a change of auditor as an opportunity to inappropriately change to an alternative accounting policy or principle.

## Execute the Audit

[What procedures do we perform to assess the consistency between prior period and current period's financial statements and the application of accounting policies or principles for an initial audit?](#) [ISA | 756.1300]

We have already determined that the [application of the accounting policies or principles are appropriate](#), and are now focused on the consistency between application of accounting policies or principles period over period.

What do we do?	What do we look for?
Evaluate the consistency of the basis of presentation and accounting policies or principles in the current period as compared with comparative periods	The accounting policies or principles reflected in the prior period financial statements or comparative information are consistent with those applied in the current period or, if there have been changes in accounting policies or principles, whether those changes have been properly accounted for and adequately presented and disclosed.

	Discuss with management any newly implemented or changed accounting policies or principles that took effect in the current period including determining whether management's justification for the change is reasonable and the change is appropriate for the entity, as well as the effect, if any, of these policies on prior period balances, reclassifications or restatements that have been made to conform to current period accounting and presentation.
Evaluate whether comparative financial statements are consistent with previously issued financial statements for respective periods.	The comparative financial statements or comparative information agrees with the amounts and other disclosures presented in the prior period or, when appropriate, have been restated for the correction of a material misstatement or adjusted for the retrospective application of an accounting policy or principle.

What if we conclude accounting policies or principles are not consistently applied and/or change in accounting policies or principles are not appropriately accounted for or not adequately presented or disclosed in an initial audit? [ISA | 756.1400]

We follow the guidance related to modifications to the auditor's opinion on the financial statements in the [ISRM](https://alex.kpmg.com/AROWeb/document/lfo/UN_IISRM_ISRM2018_1/toc/UN_IISRM_ISRM2018_1?tocref=UN_IISRM_ISRM2018_1) [https://alex.kpmg.com/AROWeb/document/lfo/UN\\_IISRM\\_ISRM2018\\_1/toc/UN\\_IISRM\\_ISRM2018\\_1?tocref=UN\\_IISRM\\_ISRM2018\\_1](https://alex.kpmg.com/AROWeb/document/lfo/UN_IISRM_ISRM2018_1/toc/UN_IISRM_ISRM2018_1?tocref=UN_IISRM_ISRM2018_1) Chapters 4 & 5, which discuss modifications to the auditor's opinion.

## 1.1.5 Initial Audit | Perform additional procedures when a possible misstatement is identified [ISA | 757]

### What do we do?

IF we discover a possible misstatement in the financial statements reported on by the predecessor auditor or the opening balances THEN perform additional audit procedures

### Why do we do this?

During an initial audit, we may discover a possible misstatement in the prior period financial statements that were reported on by the predecessor auditor. We investigate these possible misstatements to obtain the facts so that we can appropriately determine the impact to the prior period financial statements, the opening balances and the current period audit.

## Execute the Audit



What if we discover a possible misstatement in the financial statements reported on by predecessor auditor? [ISA | 757.1300]

There are several steps we follow when we discover a misstatement in order to resolve the matter identified and provide the predecessor auditor the information they need as they consider a possible misstatement in the prior period financial statements ([AS 2905](#); [ISA 560](#); [AU-C 560](#)). This includes:

- (1) [determining the effect of misstatements on the current period financial statements](#);
- (2) [requesting the client to communicate items determined to be misstatements to the predecessor auditor](#), and
- (3) [communicating material misstatements to those charged with governance](#).

What if we discover a possible misstatement in the prior year financial statements but there is no predecessor auditor? [ISA | 757.1400]

When there is no predecessor auditor and we discover a possible misstatement in prior year financial statements, we still perform additional procedures. We still determine the effects on the current period's financial statements, as well as communicating with management and possibly those charged with governance.

## 1.1.5.1 Initial Audit | Determine the effect of misstatements on the current period financial statements [ISA | 758]

### What do we do?

IF the opening balances contain misstatements that could materially affect the current period's financial statements, THEN perform additional audit procedures to determine their effect. IF a restatement of the prior period financial statements is necessary, THEN consult if applicable.

### Why do we do this?

While we are obtaining audit evidence related to the opening balances, we may identify misstatements that could materially affect the current period financial statements. As this is an initial audit and we were not involved in the prior period audit, we usually have limited information on the potential misstatement, so we investigate further to determine if there is an impact on the opening balances and current period financial statements.

## Execute the Audit

How do we determine the effect of possible misstatements in the opening balances on the current period financials when performing an initial audit? [ISA | 758.1300]

We start by inquiring of management to gather more information about the facts and circumstances of the possible misstatement. After we have a better understanding, we plan and perform procedures to determine the actual impact of the matter in the current period.

Through our procedures we may determine that a misstatement does exist. In this instance, we treat this as a misstatement in the current period and evaluate the materiality to the current period like any other misstatement. Any items that are not clearly trivial are accumulated on our Summary of Audit Misstatements.

As part of the evaluation of misstatements, we obtain management's evaluation of the issue and the impacts to both the current and prior period.

[In what circumstances do we consult when considering a restatement of previously issued financial statements when performing an initial audit? \[ISA | 758.1400\]](#)

If we plan to issue the auditor's report on financial statements of the current year when the corresponding figures or comparative financial statements that were audited by a predecessor auditor contain a material misstatement, we consult with risk management partner if:

- the predecessor auditor does not agree with the proposed amendment to the financial statements; or
- the predecessor auditor refuses to reissue the auditor's report on the prior period financial statements

## 1.1.5.2 Initial Audit | Request the client to communicate items determined to be misstatements to the predecessor auditor [ISA | 759]

### What do we do?

When we identified items that are determined to be misstatements we request the client to communicate those misstatements to the predecessor auditor AND determine the effect on our audit

### Why do we do this?

When misstatements are identified in the prior period financial statements that were reported on by the predecessor auditor, we meet with the client and predecessor auditor to gather more information on the misstatements. We request management to inform the predecessor auditor so that they can make their own assessment of the impact and consider the need for a revision to either the auditor's report or ICFR report.

## Execute the Audit

[Why do we meet with the client and predecessor auditor when we become aware of misstatements in prior periods? \[ISA | 759.1300\]](#)

It can be complicated to determine the appropriate reporting or impact to our audit without discussing the information we are aware of with both the client and predecessor auditor.

In some cases, the client and the predecessor auditor may already be aware of the misstatement and may have further information or may have made certain judgements when they were considering the

impact of the misstatement in the prior period. We gather these facts so that we can assess the impact on the current period financial statements.

In other cases, the client and the predecessor auditor may not be aware of the error and will consider the impact on the financial statements, such as restatement.

**Why do we first communicate with management prior to them contacting the predecessor auditor when we become aware of misstatements in prior periods?** [ISA | 759.1400]

Management may be able to provide additional insights into the error that we are considering for restatement, for example providing their analysis as to why they do not consider the difference to be an error. After we obtain their insights and confirm if there is an issue, we request the client to contact the predecessor auditor to inform them. Because restating financial statements is a sensitive topic and management is responsible for the accuracy of the financial statements, the client informs the predecessor auditor of the issue.

**What circumstances might arise where we determine a restatement or modification to prior period auditor's reports might be needed?** [ISA | 759.10884]

There are certain circumstances where the misstatement we discovered may result in a restatement of the prior period financial statements and/or modification of predecessor's auditor's reports. Examples include:

- a material misstatement that affects the prior period financial statements on which the predecessor auditor had previously reported without modification; or
- comparative information presented in current period financial statements that is derived from prior period financial statements that were audited by a predecessor auditor, is restated for retrospective adjustments.

**What information might we request management to communicate to the predecessor auditor when we become aware of misstatements in prior periods?** [ISA | 759.1700]

We inform management and request that they communicate any information that the predecessor auditor may consider in accordance with the subsequent events standards. This includes the significant new information related to the previously issued financial statements or interim financial information, including:

- description of the misstatement and how it was identified
- primary cause of the misstatement, including specific considerations of whether the misstatement was due to fraud
- description of how management has addressed (or is addressing) the primary cause of the misstatement
- identification of any deficiency(ies) in internal control that failed to prevent, or detect and correct, the misstatement and our assessment of their severity

**How might a restatement impact our auditor's reports?** [ISA | 759.1800]

Our report may be affected by the predecessor auditor's willingness to be involved in auditing any required adjustments to the prior period financial statements, as well as any standards, laws and regulations requiring them to do so. Therefore, to avoid problems later in the audit, we may wish to discuss with the predecessor auditor as early as possible how to address any such reporting issues.

You can find more information about this in [ISRM Section 6.190 - Prior period financial statements audited by a predecessor auditor](https://alex.kpmg.com/AROWeb/document/lfc/find/UN_IISRM_ISRM2018_6_190) [https://alex.kpmg.com/AROWeb/document/lfc/find/UN\\_IISRM\\_ISRM2018\\_6\\_190](https://alex.kpmg.com/AROWeb/document/lfc/find/UN_IISRM_ISRM2018_6_190).

**What if we are not satisfied with the resolution of the matter or the client refuses to inform the predecessor auditor of the misstatement?** [ISA | 759.1900]

If we are not satisfied with the resolution of the matter or if the client refuses to inform the predecessor auditor, we consult with the appropriate parties to evaluate the possible implications on the current year engagement and in determining the appropriate next course of action. This could include evaluating whether to withdraw from the engagement or when withdrawal is not possible under applicable law or regulation, disclaiming an opinion of the financial statements.

Type of Audit	Who do we consult with?
PCAOB (US)	<ul style="list-style-type: none"> <li>• RPPP;</li> <li>• DPP; and</li> <li>• OGC</li> </ul>
AICPA (US) Global Accounts / U.S firm serves as Component/Participating auditor for a Group/Multi-firm engagement	<ul style="list-style-type: none"> <li>• RPPP; and</li> <li>• OGC</li> </ul>
AICPA (US) All other engagements	<ul style="list-style-type: none"> <li>• BUPPP; and</li> <li>• OGC</li> </ul>
INTL engagements	<ul style="list-style-type: none"> <li>• RMP</li> </ul>

## 1.1.5.3 Initial Audit | Communicate misstatements to management and those charged with governance [ISA | 760]

### What do we do?

IF a misstatement exists in the opening balances that affects the current period's financial statements, THEN communicate it with the appropriate level of management and those charged with governance

### Why do we do this?

When misstatements are identified in the opening balances that affect the current period's financial statements, we communicate these to management and those charged with governance (TCWG) so that they are properly informed to carry out their responsibilities.

## Execute the Audit

What do we communicate to management or Those Charged With Governance when performing an initial audit? [ISA | 760.1300]

If a misstatement exists in the opening balances that affects the current period's financial statements, we communicate this to management and those charged with governance ([AS 1301](#), [ISA 450](#), [AU-C 260](#)).

When do we perform these communications? [ISA | 760.10921]

We make our communications as soon as possible after we reach a conclusion about the misstatement.

Are there limitations that would prohibit us from making these communications? [ISA | 760.10922]

There may be local jurisdictions that prohibit or limit our communications with those charged with governance due to local law or regulation. If our communications are prohibited or limited, we consider local risk management policies.

## Illustrations of Auditors' Reports with Modified Opinions

### International Standards on Auditing: ISA 510. Appendix Appendix Illustrations of Auditors' Reports with Modified Opinions

(Ref: Para. A8)

Note: Throughout these illustrative auditor's reports, the Opinion section has been positioned first in accordance with ISA 700 (Revised), and the Basis for Opinion section is positioned immediately after the Opinion section. Also, the first 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:

**For purposes of this illustrative auditor's report, the following circumstances are assumed:**

- **Audit of a complete set of financial statements of an entity other than a listed entity using a fair presentation framework. The audit is not a group audit (i.e., ISA 600 (Revised) <sup>6</sup> does not apply).**
- **The financial statements are prepared by management of the entity in accordance with International Financial Reporting Standards (IFRSs) (a general purpose framework).**
- **The terms of the audit engagement reflect the description of management's responsibility for the financial statements in ISA 210.7**

- The auditor did not observe the counting of the physical inventory at the beginning of the current period and was unable to obtain sufficient appropriate audit evidence regarding the opening balances of inventory.
- The possible effects of the inability to obtain sufficient appropriate audit evidence regarding opening balances of inventory are deemed to be material but not pervasive to the entity's financial performance and cash flows.<sup>8</sup>
- The financial position at year end is fairly presented.
- In this particular jurisdiction, law and regulation prohibit the auditor from giving an opinion which is qualified regarding the financial performance and cash flows and unmodified regarding financial position.
- The relevant ethical requirements that apply to the audit are those of the jurisdiction.
- Based on the audit evidence obtained, the auditor has concluded that a material uncertainty does not exist related to events or conditions that may cast significant doubt on the entity's ability to continue as a going concern in accordance with ISA 570 (Revised).<sup>9</sup>
- The auditor is not required, and has otherwise not decided, to communicate key audit matters in accordance with ISA 701.<sup>10</sup>
- The auditor has obtained all of the other information prior to the date of the auditor's report and has not identified a material misstatement of the other information.
- Corresponding figures are presented, and the prior period's financial statements were audited by a predecessor auditor. The auditor is not prohibited by law or regulation from referring to the predecessor auditor's report on the corresponding figures and has decided to do so.
- Those responsible for oversight of the financial statements differ from those responsible for the preparation of the financial statements.
- In addition to the audit of the financial statements, the auditor has other reporting responsibilities required under local law.

6 ISA 600, *Special Considerations-Audits of Group Financial Statements (Including the Work of Component Auditors)*

7 ISA 210, *Agreeing the Terms of Audit Engagements*

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

9 ISA 570 (Revised), *Going Concern*

10 ISA 701, *Communicating Key Audit Matters in the Independent Auditor's Report*

## INDEPENDENT AUDITOR'S REPORT

To the Shareholders of ABC Company [or Other Appropriate Addressee]

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

#### Qualified Opinion

We have audited the financial statements of ABC Company (the Company), which comprise the statement of financial position as at December 31, 20X1, and the statement of comprehensive income, statement of changes in equity and statement of cash flows for the year then ended, and notes to the financial statements, including a summary of significant accounting policies.

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

### **Basis for Qualified Opinion**

We were appointed as auditors of the company on June 30, 20X1 and thus did not observe the counting of the physical inventories at the beginning of the year. We were unable to satisfy ourselves by alternative means concerning inventory quantities held at December 31, 20X0. Since opening inventories enter into the determination of the financial performance and cash flows, we were unable to determine whether adjustments might have been necessary in respect of the profit for the year reported in the statement of comprehensive income and the net cash flows from operating activities reported in the statement of cash flows.

We conducted our audit in accordance with International Standards on Auditing (ISAs). 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 the Company in accordance with the ethical requirements that are relevant to our audit of the financial statements in [jurisdiction], 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.

### **Other Matter**

The financial statements of the Company for the year ended December 31, 20X0 were audited by another auditor who expressed an unmodified opinion on those statements on March 31, 20X1.

### **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 ISA 720 (Revised) - see Illustration 1 in Appendix 2 of ISA 720 (Revised).]

### **Responsibilities of Management and Those Charged with Governance for the Financial Statements**<sup>12</sup>

[Reporting in accordance with ISA 700 (Revised)<sup>13</sup> - see Illustration 1 in ISA 700 (Revised).]

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

[Reporting in accordance with ISA 700 (Revised) - see Illustration 1 in ISA 700 (Revised).]

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

[Reporting in accordance with ISA 700 (Revised) - see Illustration 1 in ISA 700 (Revised).]

[Signature in the name of the audit firm, the personal name of the auditor, or both, as appropriate for the particular jurisdiction]

[Auditor Address]

[Date]

---

11 The sub-title "Report on the Audit of the Financial Statements" is unnecessary in circumstances when the second sub-title "Report on Other Legal and Regulatory Requirements" is not applicable.

12 Throughout these illustrative auditor's reports, the terms management and those charged with governance may need to be replaced by another term that is appropriate in the context of the legal framework in the particular jurisdiction.

13 ISA 700 (Revised), *Forming an Opinion and Reporting on Financial Statements*

## **Illustration 2:**

**For purposes of this illustrative auditor's report, the following circumstances are assumed:**

- **Audit of a complete set of financial statements of an entity other than a listed entity using a fair presentation framework. The audit is not a group audit (i.e., ISA 600 (Revised) does not apply).**
- **The financial statements are prepared by management of the entity in accordance with IFRSs (a general purpose framework).**
- **The terms of the audit engagement reflect the description of management's responsibility for the financial statements in ISA 210.**
- **The auditor did not observe the counting of the physical inventory at the beginning of the current period and was unable to obtain sufficient appropriate audit evidence regarding the opening balances of inventory.**
- **The possible effects of the inability to obtain sufficient appropriate audit evidence regarding opening balances of inventory are deemed to be material but not pervasive to the entity's financial performance and cash flows.<sup>14</sup>**
- **The financial position at year end is fairly presented.**
- **An opinion that is qualified regarding the financial performance and cash flows and unmodified regarding financial position is considered appropriate in the circumstances.**
- **The relevant ethical requirements that apply to the audit are those of the jurisdiction.**
- **Based on the audit evidence obtained, the auditor has concluded that a material uncertainty does not exist related to events or conditions that may cast significant doubt on the entity's ability to continue as a going concern in accordance with ISA 570 (Revised).**
- **The auditor is not required, and has otherwise not decided, to communicate key audit matters in accordance with ISA 701.**
- **The auditor has obtained all of the other information prior to the date of the auditor's report and has not identified a material misstatement of the other information.**
- **Corresponding figures are presented, and the prior period's financial statements were audited by a predecessor auditor. The auditor is not prohibited by law or regulation from referring to the predecessor auditor's report on the corresponding figures and has decided to do so.**
- **Those responsible for oversight of the financial statements differ from those responsible for the preparation of the financial statements.**
- **In addition to the audit of the financial statements, the auditor has other reporting responsibilities required under local law.**
- 

<sup>14</sup> If the possible effects, in the auditor's judgment, are considered to be material and pervasive to the entity's financial performance and cash flows, the auditor would disclaim the opinion on the financial performance and cash flows.



**INDEPENDENT AUDITOR'S REPORT**

To the Shareholders of ABC Company [or Other Appropriate Addressee]

**Report on the Audit of the Financial Statements** <sup>15</sup>**Opinions**

We have audited the financial statements of ABC Company (the Company), which comprise the statement of financial position as at December 31, 20X1, and the statement of comprehensive income, statement of changes in equity and statement of cash flows for the year then ended, and notes to the financial statements, including a summary of significant accounting policies.

**Qualified Opinion on the Financial Performance and Cash Flows**

In our opinion, except for the possible effects of the matter described in the Basis for Qualified Opinion section of our report, the accompanying statement of comprehensive income and statement of cash flows present fairly, in all material respects (or give a true and fair view of), the financial performance and cash flows of the Company for the year ended December 31, 20X1 in accordance with International Financial Reporting Standards (IFRSs).

**Opinion on the Financial Position**

In our opinion, the accompanying statement of financial position presents fairly, in all material respects (or gives a true and fair view of), the financial position of the Company as at December 31, 20X1 in accordance with IFRSs.

**Basis for Opinions, Including Basis for Qualified Opinion on the Financial Performance and Cash Flows**

We were appointed as auditors of the Company on June 30, 20X1 and thus did not observe the counting of the physical inventories at the beginning of the year. We were unable to satisfy ourselves by alternative means concerning inventory quantities held at December 31, 20X0. Since opening inventories enter into the determination of the financial performance and cash flows, we were unable to determine whether adjustments might have been necessary in respect of the profit for the year reported in the statement of comprehensive income and the net cash flows from operating activities reported in the statement of cash flows.

We conducted our audit in accordance with International Standards on Auditing (ISAs). 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 the Company in accordance with the ethical requirements that are relevant to our audit of the financial statements in [jurisdiction], 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 unmodified opinion on the financial position and our qualified audit opinion on the financial performance and cash flows.

**Other Matter**

The financial statements of the Company for the year ended December 31, 20X0 were audited by another auditor who expressed an unmodified opinion on those statements on March 31, 20X1.

**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 ISA 720 (Revised) - see Illustration 1 in Appendix 2 of ISA 720 (Revised)]*

## **Responsibilities of Management and Those Charged with Governance for the Financial Statements**<sup>16</sup>

*[Reporting in accordance with ISA 700 (Revised) - see Illustration 1 in ISA 700 (Revised).]*

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

*[Reporting in accordance with ISA 700 (Revised) - see Illustration 1 in ISA 700 (Revised).]*

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

*[Reporting in accordance with ISA 700 (Revised) - see Illustration 1 in ISA 700 (Revised).]*

*[Signature in the name of the audit firm, the personal name of the auditor, or both, as appropriate for the particular jurisdiction]*

*[Auditor Address]*

*[Date]*

---

<sup>15</sup> The sub-title "Report on the Audit of the Financial Statements" is unnecessary in circumstances when the second sub-title "Report on Other Legal and Regulatory Requirements" is not applicable.

<sup>16</sup> Or other terms that are appropriate in the context of the legal framework in the particular jurisdiction

# Copyright

---

This document includes extracts from materials owned and published by the International Federation of Accountants (IFAC) in 2023, and is used with permission of IFAC.

International Standards on Auditing and their respective logos are trademarks or registered trademarks of the International Federation of Accountants (IFAC).