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*International Standard  
on Auditing  
(UK and Ireland)*

700 (Revised)

THE AUDITOR'S REPORT ON FINANCIAL  
STATEMENTS

The Auditing Practices  
Board

## THE AUDITING PRACTICES BOARD

The Auditing Practices Board (APB), which is part of the Financial Reporting Council (FRC), prepares for use within the United Kingdom and the Republic of Ireland:

- Standards and guidance for auditing;
- Standards and guidance for reviews of interim financial information performed by the auditor of the entity;
- Standards and guidance for the work of reporting accountants in connection with investment circulars; and
- Standards and guidance for auditor's and reporting accountant's integrity, objectivity and independence

with the objective of enhancing public confidence in the audit process and the quality and relevance of audit services in the public interest.

The APB comprises individuals who are not eligible for appointment as company auditors, as well as those who are so eligible. Those who are eligible for appointment as company auditors may not exceed 40% of the APB by number.

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# INTERNATIONAL STANDARD ON AUDITING (UK AND IRELAND) 700 (REVISED)

## THE AUDITOR'S REPORT ON FINANCIAL STATEMENTS

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<sup>1</sup> The illustrative auditor's reports do not form part of ISA (UK and Ireland) 700 (Revised).

# **An explanation of APB's approach to revising ISA (UK and Ireland) 700 to facilitate more concise auditor's reports**

## **Background**

In December 2007 the Auditing Practices Board (APB) issued the Discussion Paper "The Auditor's Report: A time for change?" In this APB sought views on what steps it should take to reflect, in the standard auditor's report, the coming into force of the Companies Act 2006, and also on whether more wide ranging changes should be made to the content of the auditor's report.

Institutional investors, preparer organizations, public sector bodies and some auditing firms expressed strong support for a shorter auditor's report. They observed that there were opportunities for streamlining the current report especially in relation to the current descriptions of the auditor's and directors' responsibilities and the summarised description of the scope of an audit.

Many of the institutional investors also called for the auditor's report to be made more informative. Views on how this could be achieved varied. Some called for the auditor's report to provide more of an insight into the quality of the work which the auditor has carried out; others suggested much greater use of emphasis of matter paragraphs.

## **How ISA (UK and Ireland) 700 (Revised) will facilitate more concise auditor's reports**

Improving the conciseness of the auditor's report is the first phase of APB's work to respond to these views. The requirements of the attached revision of ISA (UK and Ireland) 700 will enable auditors to provide shorter auditor's reports as illustrated by the illustrative examples provided on pages 24 to 31.

A significant change relates to what was previously described as the "basis of opinion". ISA (UK and Ireland) 700 (Revised) changes the heading of this section to "Scope of the audit" and allows three alternatives. In the case of UK companies, the report can:

- cross refer to a "Statement of the Scope of an Audit" that is maintained on APB's web site (See Example 1 on page 24 and Example 3 on page 28); or
- cross refer to a "Statement of the Scope of an Audit" that is included elsewhere within the Annual Report (See Example 1 on page 24 and Example 3 on page 28); or
- include a prescribed description of the scope of an audit (See Example 2 on page 26 and Example 4 on page 30).

Where auditors decide to include a description of the scope of the audit within the auditor's report, APB believes the description should be as short as possible and use the prescribed words.

A further significant change relates to the description of the auditor's responsibilities which has been both reduced in length and in part re-distributed to the second part of the auditor's report that addresses other reporting matters.

### **Making auditor's reports more informative**

The second phase is for APB to undertake research to better understand what can realistically be done to make auditor's reports more informative. APB believes that this work is best coordinated on an international basis and wishes to support work that the International Auditing and Assurance Standards Board (IAASB) may undertake.

In the short term, pending future possible changes to the standards in this area, APB wishes to make clear that ISA (UK and Ireland) 700 (Revised) does not preclude auditors from including additional comment in the auditor's report to highlight matters which they regard as relevant to a proper understanding of their work. To facilitate the inclusion of such additional comments in the auditor's report APB has introduced into the revised ISA (UK and Ireland) the requirement relating to "Other Matter Paragraphs in the Auditor's Report" from ISA 706 "Emphasis of Matter Paragraphs and Other Matter Paragraphs in the Independent Auditor's Report" (see paragraph 55 of ISA (UK and Ireland) 700 (Revised)).

Based on comments received in response to the Discussion Paper, APB also believes that providing a fuller description of the scope of an audit on its website will be informative to users.

### **Discussing the alternatives with those charged with governance**

APB encourages auditors to discuss the proposed content of the auditor's report with those charged with governance. The following matters in particular might usefully be the subject of such discussions:

- the advantages and disadvantages of the various alternative approaches to the description of the scope of the audit, permitted by ISA (UK and Ireland) 700 (Revised); and
- matters that auditors may wish to include in the auditor's report under the heading "Other Matter".

APB believes that those charged with governance have a legitimate interest in understanding why an auditor has chosen a particular approach to describing the scope of the audit and why the auditor considers it necessary to report the "Other Matter".

### **A window of opportunity to influence international developments**

The form and content of the auditor's report is a matter of active consideration internationally. In particular, the European Commission has yet to decide on the form and content of auditor's reports within the EU and the IAASB has agreed to consider recent research and

developments with regard to the auditor's report. APB continues to believe that there is a "window of opportunity" during which it can influence international decisions on the auditor's report, especially if its ideas are implemented in practice and are found to be beneficial by the investor community.

APB will therefore monitor reaction to the changes it has made to ISA (UK and Ireland) 700 and, in particular, the extent to which:

- reference is made to the longer version of the Scope of an Audit on APB's web-site;
- reference is made to the Scope of an Audit elsewhere within the annual report; and
- auditors decide to provide additional comment in the auditor's report to highlight matters which they regard as relevant to a proper understanding of their work in 'Other Matter' paragraphs.

### **Focus on UK companies**

The catalyst for change was the implementation of the Companies Act 2006 and APB is also responding, in part, to the views of institutional investors. It therefore seems appropriate to focus, initially, on UK companies. Consequently APB has established a two-stage implementation plan:

- The effective date of ISA (UK and Ireland) 700 (Revised) for UK companies will be for accounting periods ending on or after 5 April 2009.
- For other UK entities the effective date is for periods ending on or after 15 December 2010 (ie the same effective date as will apply to the clarified ISAs (UK and Ireland)).

Consistent with this approach APB will initially provide descriptions of the scope of an audit on APB's web-site with respect to UK companies only. If there is a strong take up of cross referring to its web site APB will, in due course, consider the need to provide examples applicable to other types of entity.

### **Republic of Ireland**

With respect to Irish companies and entities APB is monitoring developments in Irish Law which may have an effect on the content or structure of auditor's reports issued in accordance with Irish legal requirements. APB will make an announcement concerning the applicability of ISA (UK and Ireland) 700 (Revised) in the Republic of Ireland when there is more certainty about the legal position. In the meantime the version of ISA (UK and Ireland) 700 that was effective for periods commencing on or after 15 December 2004 remains in effect with respect to Irish auditor's reports.

# INTERNATIONAL STANDARD ON AUDITING (UK AND IRELAND) 700 (REVISED)

## THE AUDITOR'S REPORT ON FINANCIAL STATEMENTS

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International Standard on Auditing (UK and Ireland) (ISA (UK and Ireland)) 700 "The Auditor's Report on Financial Statements" (Revised) should be read in the context of the Auditing Practices Board's Statement "The Auditing Practices Board - Scope and Authority of Pronouncements (Revised)" which sets out the application and authority of ISAs (UK and Ireland).

## Introduction

1. This International Standard on Auditing (UK and Ireland) (ISA (UK and Ireland)) establishes standards and provides guidance on the form and content of the auditor's report issued as a result of an audit performed by an independent auditor of the financial statements of:
  - (a) UK companies, except for those that are charities, for periods commencing on or after 6 April 2008 and ending on or after 5 April 2009<sup>1</sup>; and
  - (b) all other UK entities for periods ending on or after 15 December 2010.

For earlier accounting periods and for audits carried out in the Republic of Ireland the previous version of ISA (UK and Ireland) 700 is applicable<sup>2</sup>.

2. This ISA (UK and Ireland) is written to address both "true and fair frameworks"<sup>3</sup> and "compliance frameworks". A "true and fair framework" is one that requires compliance with the framework but which acknowledges that to achieve a true and fair view:
  - (a) it may be necessary to provide disclosures additional to those specifically required by the framework<sup>4</sup>; and
  - (b) it may be necessary to depart from a requirement of the framework<sup>5</sup>.

A "compliance framework" is one that requires compliance with the framework and does not contain the acknowledgements in (a) or (b) above.

3. In this ISA (UK and Ireland) the term "those charged with governance" is defined as: The person(s) or organization(s) (e.g., a corporate trustee) with responsibility for overseeing the strategic direction of the entity and obligations related to the accountability of the entity. This includes overseeing the financial reporting process. For some entities in some jurisdictions, those charged with governance may include management personnel, for example, executive members of a governance board of a private or public sector entity, or an owner-manager. In the UK and Ireland, those

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<sup>1</sup> For UK Companies issuing financial statements for periods commencing on or after 6 April 2008 and ending before 5 April 2009 guidance on the wording of auditor's reports is provided by Bulletin 2008/8 "Auditor's Reports for Short Accounting Periods in Compliance with the United Kingdom Companies Act 2006".

<sup>2</sup> That version was effective for periods commencing on or after 15 December 2004.

<sup>3</sup> True and fair frameworks are sometimes referred to as "fair presentation frameworks".

<sup>4</sup> In the IFRS Framework this is acknowledged in paragraph 17(c) of IAS 1. In UK GAAP this is acknowledged in Sections 396(4) and 404(4) of the Companies Act 2006.

<sup>5</sup> This is sometimes referred to as the "true and fair override". In the IFRS Framework this is acknowledged in paragraph 19 of IAS 1. In UK GAAP this is acknowledged in Sections 396(5) and 404(5) of the Companies Act 2006.

charged with governance include the directors (executive and non-executive) of a company or other body, the members of an audit committee where one exists, the partners, proprietors, committee of management or trustees of other forms of entity, or equivalent persons responsible for directing the entity's affairs and preparing its financial statements.

4. **The auditor's report on the financial statements should contain a clear written expression of opinion on the financial statements taken as a whole, based on the auditor evaluating the conclusions drawn from the audit evidence obtained, including evaluating whether.**
  - (a) **sufficient appropriate audit evidence has been obtained;**
  - (b) **uncorrected misstatements are material, individually or in aggregate;**
  - (c) **in respect of a true and fair framework, the financial statements, including the related notes, give a true and fair view; and**
  - (d) **in respect of all frameworks, the financial statements have been prepared in all material respects in accordance with the framework, including the requirements of applicable law.**
  
5. **In particular, the auditor should evaluate whether:**
  - (a) **the financial statements adequately refer to or describe the relevant financial reporting framework;**
  - (b) **the financial statements adequately disclose the significant accounting policies selected and applied;**
  - (c) **the accounting policies selected and applied are consistent with the applicable financial reporting framework, and are appropriate in the circumstances;**
  - (d) **accounting estimates are reasonable;**
  - (e) **the information presented in the financial statements is relevant, reliable, comparable and understandable;**
  - (f) **the financial statements provide adequate disclosures to enable the intended users to understand the effect of material transactions and events on the information conveyed in the financial statements; and**
  - (g) **the terminology used in the financial statements, including the title of each financial statement, is appropriate.**

## Basic Elements of the Auditor's Report

### ***Title***

6. **The auditor's report should have an appropriate title.**
7. The term "Independent Auditor" is usually used in the title in order to distinguish the auditor's report from reports that might be issued by others, such as by those charged with governance, or from the reports of other auditors who may not have to comply with the Auditing Practices Board's (APB's) Ethical Standards for Auditors.

### ***Addressee***

8. **The auditor's report should be appropriately addressed as required by the circumstances of the engagement.**
9. The Companies Acts<sup>6</sup> require the auditor to report to the company's members because the audit is undertaken on their behalf. Such auditor's reports are, therefore, typically addressed to either the members or the shareholders of the company. The auditor's report on financial statements of other types of reporting entity is addressed to the appropriate person or persons, as defined by statute or by the terms of the individual engagement.

### ***Introductory Paragraph***

10. **The auditor's report should identify the financial statements of the entity that have been audited, including the date of, and period covered by, the financial statements.**

### ***Respective responsibilities of those charged with governance and the auditor***

11. **The auditor's report should include a statement that those charged with governance are responsible for the preparation of the financial statements and a statement that the responsibility of the auditor is to audit and express an opinion on the financial statements in accordance with applicable legal requirements and International Standards on Auditing (UK and Ireland). The report should also state that those standards require the auditor to comply with the APB's Ethical Standards for Auditors.**

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<sup>6</sup> In the United Kingdom the Companies Act 2006 establishes this requirement. In the Republic of Ireland the Companies Acts 1963 to 2005 establish this requirement.

12. An appreciation of the interrelationship between the responsibilities of those who prepare financial statements and those who audit them facilitates an understanding of the nature and context of the opinion expressed by the auditor.
13. The preparation of financial statements requires those charged with governance to make significant accounting estimates and judgments, as well as to determine the appropriate accounting principles and methods used in preparation of the financial statements. This determination will be made in the context of the financial reporting framework that those charged with governance choose, or are required, to use. In contrast, the auditor's responsibility is to audit the financial statements in order to express an opinion on them.

### ***Scope of the audit of the financial statements***

14. **The auditor's report should either:**
  - (a) **cross refer to a "Statement of the Scope of an Audit" that is maintained on the APB's web site; or**
  - (b) **cross refer to a "Statement of the Scope of an Audit" that is included elsewhere within the Annual Report; or**
  - (c) **include the following description of the scope of an audit.**

**"An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of: whether the accounting policies are appropriate to the [*describe nature of entity*] circumstances and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by [*describe those charged with governance*]; and the overall presentation of the financial statements".**

15. The APB maintains on its web site example descriptions of the scope of an audit of the financial statements of various categories of United Kingdom company.<sup>7</sup>
16. Where the scope of the audit is described within the Annual Report but not in the auditor's report, such description includes the prescribed text set out in paragraph 14. The content of the description of the scope of the audit is determined by the auditor

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<sup>7</sup> A description of the scope of an audit of the financial statements of a UK publicly traded company or group can be found at [www.frc.org.uk/apb/scope/UKP](http://www.frc.org.uk/apb/scope/UKP). The description for a UK non-publicly traded company or group can be found at [www.frc.org.uk/apb/scope/UKNP](http://www.frc.org.uk/apb/scope/UKNP).

regardless of whether it is incorporated into the auditor's report or published as a separate statement elsewhere in the annual report.

### ***Opinion on the financial statements***

17. **The opinion paragraph of the auditor's report should clearly state the auditor's opinion as required by the relevant financial reporting framework used to prepare the financial statements, including applicable law.**
18. **When expressing an unqualified opinion on financial statements prepared in accordance with a true and fair framework the opinion paragraph should clearly state that the financial statements give a true and fair view. It is not sufficient for the auditor to conclude that the financial statements give a true and fair view solely on the basis that the financial statements were prepared in accordance with accounting standards and any other applicable legal requirements.**
19. Although the "true and fair" concept has been central to accounting and auditing practice in the UK and Ireland for many years it is not defined in legislation. In 2008, the Financial Reporting Council published a legal opinion, that it had commissioned, entitled "The true and fair requirement revisited" (The Opinion)<sup>8</sup>. The Opinion confirms the overarching nature of the true and fair requirement to the preparation of financial statements in the United Kingdom, whether they are prepared in accordance with international or national accounting standards.
20. The Opinion states that "The preparation of financial statements is not a mechanical process where compliance with relevant accounting standards will automatically ensure that those financial statements show a true and fair view, or a fair presentation. Such compliance may be highly likely to produce such an outcome; but it does not guarantee it".
21. To advise the reader of the context in which the auditor's opinion is expressed, the auditor's opinion indicates the financial reporting framework upon which the financial statements are based. In the UK and Ireland subject to certain restrictions, these normally comprise:
  - "International Financial Reporting Standards (IFRSs) as adopted by the European Union", and the national law that is applicable when using IFRSs and, in the case of consolidated financial statements of publicly traded companies<sup>9</sup>, Article 4 of the IAS Regulation (1606/2002/EC); or

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<sup>8</sup> The Opinion can be downloaded from the FRC website at [www.frc.org.uk/about/trueandfair.cfm](http://www.frc.org.uk/about/trueandfair.cfm)

<sup>9</sup> A publicly traded company is one whose securities are admitted to trading on a regulated market in any Member State in the European Union".

- “UK Generally Accepted Accounting Practice”, which comprises applicable UK company law and UK Accounting Standards as issued by the Accounting Standards Board (ASB); or
- “Generally Accepted Accounting Practice in Ireland”, which comprises applicable Irish company law and the Accounting Standards issued by the ASB and promulgated by the Institute of Chartered Accountants in Ireland.

### ***Opinion in respect of an additional financial reporting framework***

22. **When an auditor is engaged to issue an opinion on the compliance of the financial statements with an additional financial reporting framework the second opinion should be clearly separated from the first opinion on the financial statements, by use of an appropriate heading.**
23. The financial statements of some entities may comply with two financial reporting frameworks (for example “IFRSs as issued by the IASB” and “IFRSs as adopted by the European Union”) and those charged with governance may engage the auditor to express an opinion in respect of both frameworks. If the auditor is satisfied that there are no differences between the two financial reporting frameworks that affect the financial statements being reported on, the auditor states a second separate opinion with regard to the other financial reporting framework.

### ***Requirement specific to public sector entities where an opinion on regularity is given***

24. For the audit of certain public sector entities the audit mandate may require the auditor to express an opinion on regularity<sup>10</sup>. Regularity is the requirement that financial transactions are in accordance with the legislation authorising them.
25. **Where the auditor has a reporting responsibility with respect to regularity the opinion arising from this responsibility should be set out in a separate section of the auditor’s report following the opinion[s] on the financial statements.**

### ***Opinion on other matters***

26. **The auditor should address other reporting responsibilities in [a] separate section[s] of the auditor’s report following the opinion[s] on the financial statements and, where there is one, the opinion on regularity.**

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<sup>10</sup> Guidance for auditors of public sector bodies in the UK and Ireland is given in Practice Note 10 “Audit of Financial Statements of Public Sector Bodies in the United Kingdom (Revised)” and Practice Note 10(I) “Audit of Central Government Financial Statements in the Republic of Ireland (Revised)”.

27. The auditor sets out its opinion[s] on these other reporting responsibilities in [a] separate section[s] of the report in order to clearly distinguish it from the auditor's opinion[s] on the financial statements.
28. Other reporting responsibilities may be determined by specific statutory requirements applicable to the reporting entity, or, in some circumstances, by the terms of the auditor's engagement<sup>11</sup>. Such matters may be required to be dealt with by either:
- (a) a positive statement in the auditor's report; or
  - (b) by exception.

An example of (a) arises in the United Kingdom where the auditor of a company is required to state whether, in the auditor's opinion, the information given in the directors' report for the financial year for which the accounts are prepared is consistent with those accounts<sup>12</sup>. An example of (b) arises in the United Kingdom where company legislation requires the auditor of a company to report if a company has not maintained adequate accounting records<sup>13</sup>.

29. **If the auditor is required to report on certain matters by exception the auditor should describe its responsibilities under the heading "Matters on which we are required to report by exception" and incorporate a suitable conclusion in respect of such matters.**
30. Where the auditor has discharged such responsibilities and has nothing to report in respect of them, the conclusion could be expressed in the form of the following phrase: "We have nothing to report in respect of the following:".
31. Where the auditor expresses a modified conclusion in respect of other reporting responsibilities (including those on which they are required to report by exception) this may give rise to a modification of the auditor's opinion on the financial statements. For example, if adequate accounting records have not been maintained and as a result it proves impracticable for the auditor to obtain sufficient appropriate evidence concerning material matters in the financial statements, the auditor's report on the financial statements includes a qualified opinion or disclaimer of opinion arising from that limitation.

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<sup>11</sup> An example of a reporting responsibility determined by the terms of the auditor's engagement is where the directors of a listed company are required by the rules of a Listing Authority to ensure that the auditor reviews certain statements made by the directors before the annual report is published.

<sup>12</sup> Section 496 of the Companies Act 2006.

<sup>13</sup> Section 498(2)(a) of the Companies Act 2006.

**Date of Report**

32. **The date of an auditor's report on a reporting entity's financial statements should be the date on which the auditor signed the report expressing an opinion on those statements.**
33. This informs the reader that the auditor has considered the effect on the financial statements and on the auditor's report of events and transactions of which the auditor became aware and that occurred up to that date.
34. **The auditor should not sign, and hence date, the report earlier than the date on which all other information contained in a report of which the audited financial statements form a part have been approved by those charged with governance and the auditor has considered all necessary available evidence.**
35. The auditor is not in a position to form the opinion until the financial statements (and any other information contained in a report of which the audited financial statements form a part) have been approved by those charged with governance and the auditor has completed the assessment of all the evidence the auditor considers necessary for the opinion or opinions to be given in the auditor's report. This assessment includes events occurring up to the date the opinion is expressed. The auditor, therefore, plans the conduct of an audit to take account of the need to ensure, before expressing an opinion on financial statements, that those charged with governance have approved the financial statements and any accompanying other information and that the auditor has completed a sufficient review of post balance sheet events.
36. The date of the auditor's report is, therefore, the date on which the auditor signs the auditor's report expressing an opinion on the financial statements for distribution with those financial statements, following:
- (a) receipt of the financial statements and accompanying documents in the form approved by those charged with governance for release;
  - (b) review of all documents which the auditor is required to consider in addition to the financial statements (for example the directors' report, chairman's statement or other review of an entity's affairs which will accompany the financial statements); and
  - (c) completion of all procedures necessary to form an opinion on the financial statements (and any other opinions required by law or regulation) including a review of post balance sheet events.
37. The form of the financial statements and other information approved by those charged with governance, and considered by the auditor when signing a report expressing the auditor's opinion, may be in the form of final drafts from which printed documents will be

prepared. Subsequent production of printed copies of the financial statements and the auditor's report does not constitute the creation of a new document. Copies of the report produced for circulation to shareholders or others may, therefore, reproduce a printed version of the auditor's signature showing the date of actual signature.

38. If the date on which the auditor signs the report is later than that on which those charged with governance approved the financial statements, the auditor takes such steps as are appropriate:
- (a) to obtain assurance that those charged with governance would have approved the financial statements on that later date (for example, by obtaining confirmation from specified individual members of the board to whom authority has been delegated for this purpose); and
  - (b) to ensure that their procedures for reviewing subsequent events cover the period up to that date.

### ***Location of Auditor's Office***

39. **The report should name the location of the office where the auditor is based.**

### ***Auditor's Signature***

40. **The auditor's report should state the name of the auditor and be signed and dated.**
41. The report is signed in the name of the audit firm, the personal name of the auditor or both, as required by law. In the case of a UK company, where the auditor is an individual the report is required to be signed by the individual. Where the auditor of a UK company is a firm the report is required to be signed by the senior statutory auditor<sup>14</sup> in his or her own name, for and on behalf of the auditor.

## **The Auditor's Report**

42. **With respect to compliance frameworks an unqualified opinion on the financial statements should be expressed only when the auditor concludes that they have been prepared in accordance with the identified financial reporting framework, including the requirements of applicable law.**
43. **With respect to true and fair frameworks, in addition to the requirement in paragraph 42, an unqualified opinion on the financial statements should be**

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<sup>14</sup> See Bulletin 2008/6 "The "Senior Statutory Auditor" under the United Kingdom Companies Act 2006". This Bulletin, at paragraphs 8-10 also explains the meaning of "signing the auditor's report" in a UK context.

**expressed only when the auditor concludes that the financial statements give a true and fair view.**

44. Illustrative examples of auditor’s reports tailored for use with audits conducted in accordance with ISAs (UK and Ireland) are given in various Bulletins and Practice Notes issued by the APB. With respect to companies examples are provided in the most recent versions of the APB Bulletins, “Auditor’s Reports on Financial Statements in the United Kingdom”/“Auditor’s Reports on Financial Statements in the Republic of Ireland”.

## **Modified Reports**

45. An auditor’s report is considered to be modified in the following situations:

### *Matters That Do Not Affect the Auditor’s Opinion*

- (a) Emphasis of matter

### *Matters That Do Affect the Auditor’s Opinion*

- (b) Qualified opinion,  
 (c) Disclaimer of opinion, or  
 (d) Adverse opinion.

The APB Bulletins referred to in paragraph 44 include examples of modified auditor’s reports illustrating each of these situations.

### ***Matters That Do Not Affect the Auditor’s Opinion***

46. An auditor’s report may be modified by adding an emphasis of matter paragraph to highlight a matter affecting the financial statements which is included in a note to the financial statements that more extensively discusses the matter. The addition of such an emphasis of matter paragraph does not affect the auditor’s opinion. The emphasis of matter paragraph usually follows the opinion paragraph on the financial statements and refers to the fact that the auditor’s opinion is not qualified in this respect. Communication with the reader is enhanced by the use of an appropriate sub-heading.
47. **The auditor should consider modifying the auditor’s report by adding a paragraph if there is a significant uncertainty, the resolution of which is dependent upon future events and which may affect the financial statements. In accordance with the requirements of ISA (UK and Ireland) 570 “Going Concern” the auditor should always modify the auditor’s report by adding a paragraph to highlight a material uncertainty relating to an event or condition that may cast significant doubt on the entity’s ability to continue as a going concern.**

48. An uncertainty is a matter whose outcome depends on future actions or events not under the direct control of the entity but that may affect the financial statements.
49. The emphasis of matter paragraph describes the matter giving rise to the significant uncertainty and its possible effects on the financial statements, including (where practicable) quantification. Where it is not possible to quantify the potential effects of the resolution of the uncertainty, the auditor includes a statement to that effect. Reference may be made to notes in the financial statements but such a reference is not a substitute for sufficient description of the significant uncertainty so that a reader can appreciate the principal points at issue and their implications.
50. In determining whether an uncertainty is significant, the auditor considers:
- (a) the risk that the estimate included in financial statements may be subject to change;
  - (b) the range of possible outcomes; and
  - (c) the consequences of those outcomes on the view shown in the financial statements.
51. Uncertainties are regarded as significant when they involve a significant level of concern about the validity of the going concern basis or other matters whose potential effect on the financial statements is unusually great. An example of a significant uncertainty may be the outcome, either beneficial or detrimental, of major litigation.
52. An unqualified opinion indicates that the auditor considers that appropriate estimates and disclosures relating to significant uncertainties are made in the financial statements. It remains unqualified notwithstanding the inclusion of an emphasis of matter paragraph describing a significant uncertainty.
53. When the auditor concludes that the estimate of the outcome of a significant uncertainty is materially misstated or that the disclosure relating to it is inadequate, the auditor issues a qualified opinion.
54. The addition of a paragraph emphasising a going concern problem or other significant uncertainty is ordinarily adequate to meet the auditor's reporting responsibilities regarding such matters. However, in extreme cases, such as situations involving multiple uncertainties that are significant to the financial statements, the auditor may consider it appropriate to express a disclaimer of opinion instead of adding an emphasis of matter paragraph.
55. **If the auditor considers it necessary to communicate a matter other than those that are presented or disclosed in the financial statements that, in the auditor's judgment, is relevant to users' understanding of the audit, the auditor's**

**responsibilities or the auditor’s report and this is not prohibited by law or regulation, the auditor should do so in a paragraph in the auditor’s report, with the heading “Other Matter,” or other appropriate heading.**

56. “Other Matter” paragraphs may be used by the auditor in an number of different circumstances, for example:
- To provide further explanation of the auditor’s responsibilities in the audit of the financial statements or of the auditor’s report thereon.
  - Where reporting by exception on corporate governance matters<sup>15</sup>.
  - If an amendment to other information in a document containing audited financial statements is necessary to correct a material inconsistency and the entity refuses to make the amendment, the auditor would consider including in the auditor’s report an emphasis of matter paragraph describing the material inconsistency.

### ***Matters That Do Affect the Auditor’s Opinion***

57. An auditor may not be able to express an unqualified opinion when either of the following circumstances exist and, in the auditor’s judgment, the effect of the matter is or may be material to the financial statements:
- (a) there is a disagreement with those charged with governance regarding the acceptability of the accounting policies selected, the method of their application or the adequacy of financial statement disclosures; or
  - (b) there is a limitation on the scope of the auditor’s work

The circumstances described in (a) could lead to a qualified opinion or an adverse opinion. The circumstances described in (b) could lead to a qualified opinion or a disclaimer of opinion. These circumstances are discussed more fully in paragraphs 66–76.

58. The three financial reporting frameworks described in paragraph 21 (which are all true and fair frameworks) recognise that a departure from an accounting standard may be necessary where compliance with that standard would produce a result so misleading that it would conflict with the objective of financial statements. IAS 1 states that the circumstances in which there should be such a conflict are “extremely rare”, FRS 18 uses the word “exceptional”. As discussed in The Opinion described in paragraph 19, both of these terms contemplate departures from a relevant standard in circumstances that compliance therewith would be inconsistent with the basic objective of fair

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<sup>15</sup> See Bulletin 2006/5 paragraph 55.

presentation or the true and fair view. Against this background, therefore, the circumstances in which departure from an accounting standard is appropriate are very limited.

59. In almost all cases, therefore, a departure from accounting standards will result in the issuance of a qualified or adverse opinion on the view given by the financial statements. When the auditor concludes that the financial statements of a company do not comply with accounting standards, the auditor assesses whether:

- (a) the departure is necessary in order to show a true and fair view; and
- (b) adequate disclosure has been made concerning the departure from accounting standards.

60. Where an explanation is not given for a departure from accounting standards, its absence may of itself impair the ability of the financial statements to give a true and fair view of the company's state of affairs and profit or loss. When the auditor concludes that this is so, a qualified or adverse opinion on the view given by the financial statements is appropriate, in addition to a reference (where appropriate) to the departure from accounting standards and the reasons for the departure.

61. **A qualified opinion should be expressed when the auditor concludes that an unqualified opinion cannot be expressed but that the effect of any disagreement with those charged with governance, or limitation on scope is not so material and pervasive as to require an adverse opinion or a disclaimer of opinion. A qualified opinion should be expressed as being "except for" the effects of the matter to which the qualification relates.**

62. **A disclaimer of opinion should be expressed when the possible effect of a limitation on scope is so material and pervasive that the auditor has not been able to obtain sufficient appropriate audit evidence and accordingly is unable to express an opinion on the financial statements.**

63. **An adverse opinion should be expressed when the effect of a disagreement is so material and pervasive to the financial statements that the auditor concludes that a qualification of the report is not adequate to disclose the misleading or incomplete nature of the financial statements.**

64. **Whenever the auditor expresses an opinion that is other than unqualified, a clear description of all the substantive reasons should be included in the report and, unless impracticable, a quantification of the possible effect(s) on the financial statements.** Ordinarily, this information would be set out in a separate paragraph preceding the opinion or disclaimer of opinion and may include a reference to a more extensive discussion, if any, in a note to the financial statements.

65. Whilst reference may be made to relevant notes in the financial statements, such reference is not a substitute for sufficient description of the circumstances in the auditor's report so that a reader can appreciate the principal points at issue and their implications for an understanding of the financial statements.

### ***Disagreement with Those Charged with Governance***

66. The auditor may disagree with those charged with governance about matters such as the acceptability of accounting policies selected, the method of their application, or the adequacy of disclosures in the financial statements. **If such disagreements are material to the financial statements, the auditor should express a qualified or an adverse opinion.**

### ***Limitation on Scope***

67. A limitation on the scope of the auditor's work may sometimes be imposed by the entity (for example, when the terms of the engagement specify that the auditor will not carry out an audit procedure that the auditor believes is necessary). However, when the limitation in the terms of a proposed engagement is such that the auditor believes the need to express a disclaimer of opinion exists; the auditor would ordinarily not accept such a limited engagement as an audit engagement, unless required to by statute. Also, a statutory auditor would not accept such an audit engagement when the limitation infringes on the auditor's statutory duties.

#### *Limitation on scope imposed by the entity before accepting an audit engagement*

68. **If the auditor is aware, before accepting an audit engagement, that those charged with governance of the entity, or those who appoint its auditor, will impose a limitation on the scope of the audit work which the auditor considers likely to result in the need to issue a disclaimer of opinion on the financial statements, the auditor should not accept that engagement, unless required to do so by statute<sup>16</sup>.**
69. Agreeing to such a restriction on the scope of the audit work would seriously threaten the auditor's independence and make it impossible for the auditor to meet with integrity and rigour the requirements of ISAs (UK and Ireland). The acceptance of such a limited engagement as an audit engagement would be incompatible with the auditor's obligations to conduct any audit of financial statements in accordance with:

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<sup>16</sup> There are certain circumstances in which (regardless of any limitation imposed on the scope of the audit work) the auditor is required by statute to accept an audit engagement, for example the majority of appointments of the national audit agencies to audit the accounts of certain public sector bodies. However, in general, there is no such requirement in the private sector; there may be a statutory requirement for the entity to appoint an auditor, but this does not create an obligation for any auditor to accept appointment.

- (a) applicable legislation; and
- (b) Auditing Standards contained in the ISAs (UK and Ireland).

Furthermore, the auditor, by accepting the engagement on such restricted terms, might be regarded as complicit in an arrangement to enable the entity to observe the form of any legal or regulatory audit requirements but to evade complying with the substance of those obligations.

*Limitation on scope imposed by the entity after accepting an audit engagement*

70. **If the auditor becomes aware, after accepting an audit engagement, that those charged with governance of the entity, or those who appointed them as its auditor, have imposed a limitation on the scope of the audit work which they consider likely to result in the need to issue a disclaimer of opinion on the financial statements, the auditor should request the removal of the limitation. If the limitation is not removed, the auditor should consider resigning from the audit engagement.**
71. If the limitation is not removed, the auditor considers the factors discussed in paragraph 69 above and may often decide that resignation from the audit engagement is appropriate. If, after careful consideration of all the circumstances (for example, where third party interests are involved), the auditor concludes that it is appropriate to continue with the engagement, the auditor includes in the audit report a full description of the events which led to the disclaimer. On completion of the audit for that year, however, the auditor will follow the requirements of paragraph 68 when deciding whether to undertake the audit for the following period<sup>17</sup>.
72. In cases where the auditor resigns immediately, or continues with the audit for that year but does not seek reappointment, the auditor needs to comply with any statutory, regulatory or professional requirements for a statement of the circumstances of ceasing to hold office.<sup>18</sup> The fact that such a limitation has been imposed on the scope of the auditor's work may be a matter to which the auditor refers in both cases.
73. Where a significant limitation on scope has arisen during the course of the audit work the auditor considers whether an obligation arises under statute, as discussed in ISA (UK and Ireland) 250, Section B, to make a report to the appropriate regulators.

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<sup>17</sup> Auditors in the Republic of Ireland are required by the Companies Act 1963 (section 160, para 2(c)) to give the company notice in writing of their unwillingness to be re-appointed, where this is the case.

<sup>18</sup> For example, in the case of a quoted company incorporated in the United Kingdom, on ceasing to hold office for any reason, the auditor is required under section 519(3) Companies Act 2006 to make '... a statement of the circumstances connected with his ceasing to hold office.' Similar requirements exist in the Republic of Ireland (section 185 Companies Act, 1990).

*Limitation on scope imposed by circumstances*

74. A scope limitation may be imposed by circumstances (for example, when the timing of the auditor's appointment is such that the auditor is unable to observe the counting of physical inventories). It may also arise when, in the opinion of the auditor, the entity's accounting records are inadequate or when the auditor is unable to carry out an audit procedure believed to be desirable. In these circumstances, the auditor would attempt to carry out reasonable alternative procedures to obtain sufficient appropriate audit evidence to support an unqualified opinion.
75. **When there is a limitation on the scope of the auditor's work that requires expression of a qualified opinion or a disclaimer of opinion, the auditor's report should describe the limitation and indicate the possible adjustments to the financial statements that might have been determined to be necessary had the limitation not existed.**
76. In considering whether a limitation on scope results in a lack of evidence necessary to form an opinion, the auditor assesses:
- (a) the quantity and type of evidence which may reasonably be expected to be available to support the particular figure or disclosure in the financial statements; and
  - (b) the possible effect on the financial statements of the matter for which insufficient evidence is available. When the possible effect is, in the opinion of the auditor, material to the financial statements, there will be insufficient evidence to support an unqualified opinion.

**Effective Date**

77. This ISA (UK and Ireland) is effective for audits of financial statements of:
- (a) UK companies, except for those that are charities, for periods commencing on or after 6 April 2008 and ending on or after 5 April 2009; and
  - (b) all other UK entities for periods ending on or after 15 December 2010.

For earlier accounting periods and for audits carried out in the Republic of Ireland the previous version of ISA (UK and Ireland) 700 is applicable<sup>19</sup>.

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<sup>19</sup> That version was effective for periods commencing on or after 15 December 2004.



## **ILLUSTRATIVE AUDITOR'S REPORTS**

The four Illustrative auditor's reports set out on the following pages do not form part of ISA (UK and Ireland) 700 (Revised).

## UK PUBLICLY TRADED COMPANY USING IFRSS AS ADOPTED BY THE EUROPEAN UNION, WHERE THE SCOPE OF THE AUDIT IS DESCRIBED ON THE APB WEB-SITE OR ELSEWHERE IN THE ANNUAL REPORT

- *Group and parent company financial statements not presented separately*
- *IFRSs as adopted by the European Union used for both group and parent company financial statements*
- *Company does meet the Companies Act definition of a quoted company*
- *Section 408 exemption relating to parent company's own income statement not taken*

### INDEPENDENT AUDITOR'S REPORT TO THE MEMBERS OF XYZ PLC

We have audited the financial statements of (name of entity) for the year ended ... which comprise [specify the financial statements, such as the Group and Parent Company Statements of Financial Position, the Group and Parent Company Statements of Comprehensive Income, the Group and Parent Company Statements of Cash Flows, the Group and Parent Company Statements of Changes in Equity,] and the related notes<sup>1</sup>. The financial reporting framework that has been applied in their preparation is applicable law and International Financial Reporting Standards (IFRSs) as adopted by the European Union.

### Respective responsibilities of directors and auditors

As explained more fully in the Directors' Responsibilities Statement [set out [on pages...]], the directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view. Our responsibility is to audit the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's (APB's) Ethical Standards for Auditors.

### Scope of the audit of the financial statements

A description of the scope of an audit of financial statements is [provided on the APB's web-site at [www.frc.org.uk/apb/scope/UKP](http://www.frc.org.uk/apb/scope/UKP)] / [set out [on page x] of the Annual Report].

### Opinion on financial statements

In our opinion the financial statements:

- give a true and fair view of the state of the group's and the parent company's affairs as at ... and of the group's and the parent company's profit [loss] for the year then ended;

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<sup>1</sup> Auditor's reports of entities that do not publish their financial statements on a web site or publish them using "PDF" format may refer to the financial statements by reference to page numbers.

- have been properly prepared in accordance with IFRSs as adopted by the European Union; and
- have been prepared in accordance with the requirements of the Companies Act 2006 and, as regards the group financial statements, Article 4 of the IAS Regulation.

### **Opinion on other matters prescribed by the Companies Act 2006**

In our opinion:

- the part of the Directors' Remuneration Report to be audited has been properly prepared in accordance with the Companies Act 2006; and
- the information given in the Directors' Report for the financial year for which the financial statements are prepared is consistent with the financial statements.

### **Matters on which we are required to report by exception**

We have nothing to report in respect of the following:

Under the Companies Act 2006 we are required to report to you if, in our opinion:

- adequate accounting records have not been kept, or returns adequate for our audit have not been received from branches not visited by us; or
- the parent company financial statements and the part of the Directors' Remuneration Report to be audited are not in agreement with the accounting records and returns; or
- certain disclosures of directors' remuneration specified by law are not made; or
- we have not received all the information and explanations we require for our audit.

Under the Listing Rules we are required to review:

- the directors' statement, [set out [on page]], in relation to going concern; and
- the parts of the Corporate Governance Statement relating to the company's compliance with the nine provisions of the [2006] [June 2008]<sup>2</sup> Combined Code specified for our review.

*[Signature]*

*John Smith (Senior statutory auditor)*

*for and on behalf of ABC LLP, Statutory Auditor*

*Address*

*Date*

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<sup>2</sup> The June 2008 Combined Code applies to accounting periods beginning on or after 29 June 2008: the 2006 Combined Code applies before that date.

## UK PUBLICLY TRADED COMPANY USING IFRSS AS ADOPTED BY THE EUROPEAN UNION, WHERE THE SCOPE OF THE AUDIT IS DESCRIBED WITHIN THE AUDITOR'S REPORT

- *Group and parent company financial statements not presented separately*
- *IFRSs as adopted by the European Union used for both group and parent company financial statements*
- *Company does meet the Companies Act definition of a quoted company*
- *Section 408 exemption relating to parent company's own income statement not taken*

### INDEPENDENT AUDITOR'S REPORT TO THE MEMBERS OF XYZ PLC

We have audited the financial statements of (name of entity) for the year ended ... which comprise [specify the financial statements, such as the Group and Parent Company Statements of Financial Position, the Group and Parent Company Statements of Comprehensive Income, the Group and Parent Company Statements of Cash Flows, the Group and Parent Company Statements of Changes in Equity,] and the related notes<sup>1</sup>. The financial reporting framework that has been applied in their preparation is applicable law and International Financial Reporting Standards (IFRSs) as adopted by the European Union.

### Respective responsibilities of directors and auditors

As explained more fully in the Directors' Responsibilities Statement [set out [on pages...]], the directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view. Our responsibility is to audit the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

### Scope of the audit

An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of: whether the accounting policies are appropriate to the group's and the parent company's circumstances and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by the directors; and the overall presentation of the financial statements.

### Opinion on financial statements

In our opinion the financial statements:

- give a true and fair view of the state of the group's and the parent company's affairs

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<sup>1</sup> Auditor's reports of entities that do not publish their financial statements on a web site or publish them using "PDF" format may refer to the financial statements by reference to page numbers.

as at ... and of the group's and the parent company's profit [loss] for the year then ended;

- have been properly prepared in accordance with IFRSs as adopted by the European Union; and
- have been prepared in accordance with the requirements of the Companies Act 2006 and, as regards the group financial statements, Article 4 of the IAS Regulation.

### **Opinion on other matters prescribed by the Companies Act 2006**

In our opinion:

- the part of the Directors' Remuneration Report to be audited has been properly prepared in accordance with the Companies Act 2006; and
- the information given in the Directors' Report for the financial year for which the financial statements are prepared is consistent with the financial statements.

### **Matters on which we are required to report by exception**

We have nothing to report in respect of the following:

Under the Companies Act 2006 we are required to report to you if, in our opinion:

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- the parent company financial statements and the part of the Directors' Remuneration Report to be audited are not in agreement with the accounting records and returns; or
- certain disclosures of directors' remuneration specified by law are not made; or
- we have not received all the information and explanations we require for our audit.

Under the Listing Rules we are required to review:

- the directors' statement, [set out [on page]], in relation to going concern; and
- the parts of the Corporate Governance Statement relating to the company's compliance with the nine provisions of the [2006] [June 2008]<sup>2</sup> Combined Code specified for our review.

*[Signature]*

*John Smith (Senior statutory auditor)*

*for and on behalf of ABC LLP, Statutory Auditor*

*Address*

*Date*

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<sup>2</sup> The June 2008 Combined Code applies to accounting periods beginning on or after 29 June 2008: the 2006 Combined Code applies before that date.

## UK NON-PUBLICLY TRADED COMPANY USING UK GAAP, WHERE THE SCOPE OF THE AUDIT IS DESCRIBED ON THE APB WEB-SITE OR ELSEWHERE IN THE ANNUAL REPORT

- *Group and parent company financial statements not presented separately*
- *Company prepares group financial statements*
- *Company is not a quoted company*
- *UK GAAP used for group and parent company financial statements*
- *Section 408 exemption taken for parent company's own profit and loss account*

### INDEPENDENT AUDITOR'S REPORT TO THE MEMBERS OF XYZ LIMITED

We have audited the financial statements of (name of entity) for the year ended ... which comprise [specify the financial statements, such as the Group Profit and Loss Account, the Group and Parent Company Balance Sheets, the Group Cash Flow Statement, the Group Statement of Total Recognised Gains and Losses,] and the related notes<sup>1</sup>. The financial reporting framework that has been applied in their preparation is applicable law and United Kingdom Accounting Standards (United Kingdom Generally Accepted Accounting Practice).

#### Respective responsibilities of directors and auditors

As explained more fully in the Directors' Responsibilities Statement [set out [on pages...]], the directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view. Our responsibility is to audit the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's (APB's) Ethical Standards for Auditors.

#### Scope of the audit

A description of the scope of an audit of financial statements is [provided on the APB's web-site at [www.frc.org.uk/apb/scope/UKNP](http://www.frc.org.uk/apb/scope/UKNP)] / [set out [on page x] of the Annual Report].

#### Opinion on financial statements

In our opinion the financial statements:

- give a true and fair view of the state of the group's and the parent company's affairs as at ... and of the group's profit [loss] for the year then ended;
- have been properly prepared in accordance with United Kingdom Generally Accepted Accounting Practice; and

<sup>1</sup> Auditor's reports of entities that do not publish their financial statements on a web site or publish them using "PDF" format may refer to the financial statements by reference to page numbers.

- have been prepared in accordance with the requirements of the Companies Act 2006.

**Opinion on other matter prescribed by the Companies Act 2006**

In our opinion the information given in the Directors' Report for the financial year for which the financial statements are prepared is consistent with the financial statements.

**Matters on which we are required to report by exception**

We have nothing to report in respect of the following matters where the Companies Act 2006 requires us to report to you if, in our opinion:

- adequate accounting records have not been kept, or returns adequate for our audit have not been received from branches not visited by us; or
- the parent company financial statements are not in agreement with the accounting records and returns; or
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### Opinion on financial statements

In our opinion the financial statements:

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- have been prepared in accordance with the requirements of the Companies Act 2006.

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- certain disclosures of directors' remuneration specified by law are not made; or
- we have not received all the information and explanations we require for our audit.

*[Signature]*

*John Smith (Senior statutory auditor)*

*for and on behalf of ABC LLP, Statutory Auditor*

*Address*

*Date*

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