

INTERNATIONAL STANDARD ON AUDITING 510
INITIAL ENGAGEMENTS—OPENING BALANCES

(Effective for audits of financial statements for periods
beginning on or after December 15, 2004)*

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International Standard on Auditing (ISA) 510, “Initial Engagements—Opening Balances” should be read in the context of the “Preface to the International Standards on Quality Control, Auditing, Review, Other Assurance and Related Services,” which sets out the application and authority of ISAs.

* ISA 315, “Understanding the Entity and Its Environment and Assessing the Risks of Material Misstatement,” ISA 330, “The Auditor’s Procedures in Response to Assessed Risks,” and ISA 500, “Audit Evidence” gave rise to conforming amendments to ISA 510. The conforming amendments are effective for audits of financial statements for periods beginning on or after December 15, 2004 and have been incorporated in the text of ISA 510.

Introduction

1. The purpose of this International Standard on Auditing (ISA) is to establish standards and provide guidance regarding opening balances when the financial statements are audited for the first time or when the financial statements for the prior period were audited by another auditor. This ISA would also be considered when the auditor becomes aware of contingencies and commitments existing at the beginning of the period. Guidance on the audit and reporting requirements regarding comparatives is provided in ISA 710, “Comparatives.”
2. **For initial audit engagements, the auditor should obtain sufficient appropriate audit evidence that:**
 - (a) **The opening balances do not contain misstatements that materially affect the current period’s financial statements;**
 - (b) **The prior period’s closing balances have been correctly brought forward to the current period or, when appropriate, have been restated; and**
 - (c) **Appropriate accounting policies are consistently applied or changes in accounting policies have been properly accounted for and adequately presented and disclosed.**
3. “Opening balances” means those account balances which exist at the beginning of the period. Opening balances are based upon the closing balances of the prior period and reflect the effects of:
 - (a) Transactions of prior periods; and
 - (b) Accounting policies applied in the prior period.

In an initial audit engagement, the auditor will not have previously obtained audit evidence supporting such opening balances.

Audit Procedures

4. The sufficiency and appropriateness of the audit evidence the auditor will need to obtain regarding opening balances depends on such matters as the following:
 - The accounting policies followed by the entity.
 - Whether the prior period’s financial statements were audited, and if so whether the auditor’s report was modified.
 - The nature of the accounts and the risk of material misstatement in the current period’s financial statements.
 - The materiality of the opening balances relative to the current period’s financial statements.

5. The auditor will need to consider whether opening balances reflect the application of appropriate accounting policies and that those policies are consistently applied in the current period's financial statements. When there are any changes in the accounting policies or application thereof, the auditor would consider whether they are appropriate and properly accounted for and adequately presented and disclosed.
6. When the prior period's financial statements were audited by another auditor, the current auditor may be able to obtain sufficient appropriate audit evidence regarding opening balances by reviewing the predecessor auditor's working papers. In these circumstances, the current auditor would also consider the professional competence and independence of the predecessor auditor. If the prior period's auditor's report was modified, the auditor would pay particular attention in the current period to the matter which resulted in the modification.
7. Prior to communicating with the predecessor auditor, the current auditor will need to consider the *Code of Ethics for Professional Accountants* issued by the International Federation of Accountants.
8. When the prior period's financial statements were not audited or when the auditor is not able to be satisfied by using the audit procedures described in paragraph 6, the auditor will need to perform other audit procedures such as those discussed in paragraphs 9 and 10.
9. For current assets and liabilities some audit evidence can ordinarily 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, it is more difficult for the auditor to be satisfied as to inventory on hand at the beginning of the period. Therefore, additional audit procedures are ordinarily necessary such as observing a current physical inventory taking and reconciling it back to the opening inventory quantities, performing audit procedures on the valuation of the opening inventory items, and performing audit procedures on gross profit and cutoff. A combination of these audit procedures may provide sufficient appropriate audit evidence.
10. For noncurrent assets and liabilities, such as fixed assets, investments and long-term debt, the auditor will ordinarily examine the accounting records and other information underlying the opening balances. In certain cases, the auditor may be able to obtain confirmation of opening balances 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

11. **If, after performing audit procedures including those set out above, the auditor is unable to obtain sufficient appropriate audit evidence concerning opening balances, the auditor’s report should include:**
- (a) **A qualified opinion**, for example:
- “We did not observe the counting of the physical inventory stated at XXX as at December 31, 19X1, since that date was prior to our appointment as auditors. We were unable to satisfy ourselves as to the inventory quantities at that date by other audit procedures.
- In our opinion, except for the effects of such adjustments, if any, as might have been determined to be necessary had we been able to observe the counting of physical inventory and satisfy ourselves as to the opening balance of inventory, the financial statements give a true and fair view of (present fairly, in all material respects,) the financial position of ... as at December 31, 19X2 and the results of its operations and its cash flows for the year then ended in accordance with ...;”
- (b) **A disclaimer of opinion; or**
- (c) **In those jurisdictions where it is permitted, an opinion which is qualified or disclaimed regarding the results of operations and unqualified regarding financial position**, for example:
- “We did not observe the counting of the physical inventory stated at XXX as at December 31, 19X1, since that date was prior to our appointment as auditors. We were unable to satisfy ourselves as to the inventory quantities at that date by other audit procedures.
- Because of the significance of the above matter in relation to the results of the Company’s operations for the year to December 31, 19X2, we are not in a position to, and do not, express an opinion on the results of its operations and its cash flows for the year then ended.
- In our opinion, the balance sheet gives a true and fair view of (or ‘presents fairly in all material respects,’) the financial position of the Company as at December 31, 19X2, in accordance with ...”
12. If the opening balances contain misstatements which could materially affect the current period’s financial statements, the auditor would inform management and, after having obtained management’s authorization, the predecessor auditor, if any. **If the effect of the misstatement is not properly accounted for and adequately presented and disclosed, the auditor should express a qualified opinion or an adverse opinion, as appropriate.**
13. **If the current period’s accounting policies have not been consistently applied in relation to opening balances and if the change has not been**

properly accounted for and adequately presented and disclosed, the auditor should express a qualified opinion or an adverse opinion as appropriate.

14. If the entity's prior period auditor's report was modified, the auditor would consider the effect thereof on the current period's financial statements. For example, if there was a scope limitation, such as one due to the inability to determine opening inventory in the prior period, the auditor may not need to qualify or disclaim the current period's audit opinion. **However, if a modification regarding the prior period's financial statements remains relevant and material to the current period's financial statements, the auditor should modify the current auditor's report accordingly.**