

IAASB Public Consultation

Proposals to amend and improve independent auditor reports

1. Positioning

The public consultation document presented a number of questions related to the proposals, but given the limited time available and highly specific and technical nature of this issue, we attempted to focus on the basic and wider aspects discussed in the report to which the IBGC is better able to contribute.

Therefore, the issues were divided into five themes, set out as questions below:

- Are the proposed changes sufficient to add value to the audit report in terms of possible barriers (including costs)?
- What practical aspects, feasibility and challenges of implementation? Is it applicable in Brazil? Does it apply to SMEs and privately held companies?
- Will the responsibilities of "preparers" of financial statements change?
- Will the relationship between preparers and auditors change?
- Are there other issues that should be considered individually or as a whole to improve the audit report (or reporting on the audit in a wider sense)?

1.1. Are the proposed changes sufficient to add value to the audit report in terms of possible barriers (including costs)?

There is a belief that current auditors' reports need to change. There is a sense that current reports are incomplete and very similar to one another, therefore they are unable to clearly differentiate diverse situations at different companies using the same type of report. There is an impression that the information currently available is fairly poor and the general public, including boards and audit committees, want more information, greater detail and more data on the impact that critical accounting issues may have on companies.

The IFRS is highly dependent on estimates, fair values, judgments and substance taking precedence over the format of information and whether it can be understood. Reports should assure users that the auditor did indeed take all these issues into account and how he or she did so.

The IAASB review is timely and it would seem that the current model does need to change.

The proposals presented seem very well thought out, however moderation is needed to ensure the auditor's report does not become overly large, confusing the roles played by auditors and preparers of the financial statements. The report should therefore concentrate on essential issues: (i) consistency between the management report and the financial statements; (ii) going concern issues; and (iii) other relevant issues, especially discretionary matters, such as how estimates, fair values, assumptions and accounting decisions based on judgments are defined.

Note that the report from the board of directors (and the MD&A¹, required in one way or another on the Reference Form²) must already present some of the information it has been suggested the new auditor's report should include. However, we should tread carefully to ensure reports do not become repetitive and offer users little value.

IAASB should also take care to ensure that the report does not become alarmist or becomes a source of concern for corporations and the capital markets.

As far as the wider improvements proposed by the IAASB are concerned, we believe the following should be adopted. Please see the following table.

¹ Management Discussion and Analysis

² It's the Brazilian version of the 20-F (requested by the SEC). According to a CVM (Brazilian market regulator) regulation, Companies must fill in their Reference Form with a huge set of information about the company annually, including corporate governance and management analysis on relevant information.

IAASB Proposal	Does the IBGC recommend keeping it?	IBGC reasons
Additional information in the auditor's report to highlight matters that, in the auditor's judgment, are likely to be most important to users' understanding of the audited financial statements or the audit.	Yes	Comments should be restricted to specific areas of the financial statements. Although users should be ready to understand financial statements and the opinion on the accuracy of the financial statements, the audit report would, for example, be more informative if it highlighted areas in which there are significant assumptions made by management and whether or not there are significant or unusual transactions.
Auditor conclusion on the appropriateness of management's use of the going concern assumption in preparing the financial statements and an explicit statement as to whether material uncertainties in relation to going concern have been identified.	Yes with care	We should make sure that disclosure of going concern problems does not come too late, but we should also take care that the report does not become alarmist or a source of concern for corporations and the capital markets.
Auditor statement as to whether any material inconsistencies between the audited financial statements and other information have been identified	Yes	Auditors can inform users of the focal points where they should pay greater attention and analyze the report in greater detail.
Prominent placement of the auditor's opinion and other entity-specific information in the auditor's report	Yes	Highlight the most relevant information in the report.

Provide more transparency about the audits and explain the responsibilities of auditors, management and others responsible for corporate governance	Yes	This may help avoid future attempts by any of the parties involved to shirk their responsibilities.
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Regarding the specific IAASB proposals to include certain information, we recommend evaluating and keeping only information that is truly essential, to avoid the report becoming too unwieldy, jejune and ineffective.

Also, the information asymmetry between management and will persist and auditors are unlikely to have the same level of information as management auditors (managers will always have more information than the one that's available to or are requested by the auditors). As such, an important recommendation for users would be to avoid judging published material as definitive - whatever the source - however trustworthy it may be. In other words, users need to be aware that they are responsible for supplementing their appreciation, consideration and knowledge of the company's performance and equity when analyzing the financial statements, in spite of any information provided by the company or the auditors.

Basically, we believe that changes are needed but they should be prudent and sparing.

**1.2. What practical aspects, feasibility and challenges of implementation? Is it applicable in Brazil?
Does it apply to SMEs and privately held companies?**

We believe it is feasible to adopt the new reporting model in Brazil, because it is more a matter of changing the format, quantity and quality of disclosure rather than pushing for additional information.

However, we would like to point out certain challenges implementing these reporting changes.

The main hurdle would be overcoming the current cultural barriers within companies (especially SMEs and privately-held corporations), that in most cases are fearful of disclosing information, and possible resistance to change among auditors.

Another major difficulty in Brazil could be the difficulty transforming this information into a more user-friendly format for the general public.

We do not foresee an increase in the complexity (or cost) of auditors' work, as most of the information that would be disclosed in the reports is already known by the auditor and only needs to be organized, structured and disclosed.

1.3. Will the responsibilities of "preparers" of financial statements change?

It is our opinion that the proposed change will not increase the responsibilities of those responsible for preparing financial statements (preparers) as they are already expected to fulfill their disclosure role/duty as properly, transparently and fully as possible.

1.4. Will the relationship between preparers and auditors change?

We do not believe the relationship between preparers - company executives - and auditors will change. This relationship already involves a significant amount of discussion and debate that includes the criteria used. With the new report, details of these discussions will be presented to the public.

1.5. Are there other issues that should be considered individually or in concert to improve the audit report (or reporting on the audit in a wider sense)?

Other relevant issues we have identified that could improve reporting involve:

- Auditors taking on more responsibility, showing more of their work and substantiating it (without excessive disclaimers related to their work of the responsibilities of management);
- Encouraging management and auditors to present shareholders and other stakeholders with full, transparent, accurate and relevant information;
- Disclosing evaluation of the internal control system/environment, stating whether the control tools present any relevant weaknesses and report on any significant deficiencies discovered (as already required to an extent in the Reference Form);
- Disclosing information on the way auditors define criteria to assess the material relevance of issues and evidence of the fragility of internal controls that could allow or lead to fraud;
- Rational balance of the use of the Principles of Prudence and Neutrality, avoiding indiscriminate usage of one or the other;
- Improve the way companies' financial statements and explanatory notes are prepared, turning them into a real informative (and not misleading) piece of data;
- Discuss the need of creating a body in Brazil to oversee audits, along the lines of the PCAOB in the US.