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# Federative Republic of Brazil

# Brazil: Report on the Observance of Standards and Codes (ROSC): Accounting & Auditing

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Financial Management Unit, Operations Services Department
Brazil Country Management Unit
Latin America and the Caribbean Region
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# Main Abbreviations and Acronyms

| | |
|---|---|
| AQRB | Audit Quality Review Board |
| BCB | Central Bank of Brazil |
| BM&F Bovespa | Brazilian Securities, Commodities and Futures Exchange |
| BNDES | Brazilian Economic and Social Development Bank |
| CFC | Federal Accounting Council |
| IPSAS | International Public Sector Accounting Standards |
| CNE | National Council on Education |
| CNPC | National Council for Complementary Pension |
| CNSP | National Council for Private Insurance |
| COSIF | Chart of Accounts for Financial Institutions |
| CPA | Certified Professional Accountant |
| CPC | Brazilian Accounting Pronouncements Committee (issues pronouncements known as CPCs) |
| CPD | Continuing Professional Development |
| CRC | Regional Accounting Council |
| CVM | Securities and Exchange Commission |
| GDP | Gross Domestic Product |
| IAASB | International Auditing and Assurance Standards Board |
| IASB | International Accounting Standards Board |
| IBRACON | Institute of Independent Auditors |
| IES | International Education Standards for Professional Accountants |
| IFAC | International Federation of Accountants |
| IFRS | International Financial Reporting Standards |
| ISA | International Standards on Auditing |
| ISQC | International Standard on Quality Control |
| MEC | Ministry of Education |
| MoF | Ministry of Finance |
| NYSE | New York Stock Exchange |
| PREVIC | National Superintendency for Complementary Pension |
| ROSC A&A | Reports on the Observance of Standards and Codes for Accounting and Auditing |
| RTT | *Regime Tributário de Transição* |
| SESu | Higher Education Secretariat in the Ministry of Education |
| SINREM | National System of Commercial Registry |
| SRF | Brazilian Internal revenue Service |
| SUSEP | Private Insurance Superintendency |

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|---|---|
| Vice-President | Hasan Tuluy |
| Country Director | Deborah L. Wetzel |
| Sector Director | Elizabeth Adu |
| Sector Manager | Daniel Boyce (Acting) |
| Task Manager | Joseph Mubiru Kizito |

# TABLE OF CONTENTS

# EXECUTIVE SUMMARY

This Report on the Observance of Standards and Codes: Accounting and Auditing (ROSC A&A) has been prepared under the Financial Sector Assessment Program in Brazil. This report assesses the status of implementation of policy recommendations contained in the 2005 ROSC A&A, which is summarized in Appendix B. It also highlights recent improvements in Brazil's corporate financial reporting framework, and sheds light on emerging issues regarding institutional underpinnings of accounting and auditing practices that require further strengthening in line with international good practices.

Following a recommendation of the 2005 ROSC A&A, amendments to the corporation law and the law relating to accountancy profession have resulted in significant improvements in the statutory framework for accounting and auditing. The CFC has also undertaken a number of efforts to improve the quality of accounting, particularly in working towards convergence with international accounting standards and towards improvement in the standard of accounting education in the country. These actions have provided a strong foundation on which further improvements should be built.

The Central Bank (BCB) and Securities Commission (CVM) have significantly improved their institutional capacity to monitor and enforce financial reporting and auditing requirements in the case of regulated entities. However, the insurance and pension regulators (SUSEP and PREVIC) still lack capacity in this regard.

The introduction of a strong oversight body, independent from the accountancy profession, to monitor and enforce accounting and auditing requirements in general and not just in regulated sectors is considered by key stakeholders as necessary for enhancing the institutional framework for corporate financial reporting in the country. The BCB and the CVM carry out accounting and auditing monitoring activities as part of their supervision activities. However, there remains a need to enhance the capacity of these institutions, and challenges in ensuring compliance with IFRS and other financial reporting obligations. There is recognition that the establishment of an independent oversight body independent from the profession and the oversight role played by the CFC, would be helpful to address these challenges and to deploy adequate resources for carrying out monitoring and enforcement activities with efficiency and effectiveness.

Legally backed arrangements have been adopted to mandate the application of *International Financial Reporting Standards* (IFRS) for consolidated financial reporting by listed companies, banks and other financial institutions. This is in addition to the requirements for individual entity financial statements of financial institutions to be prepared in accordance with the chart of accounts for financial institutions (COSIF) issued by the BCB. For the purposes of preparing individual legal entity financial statements, Brazilian accounting technical pronouncements issued by the CPC are followed once they have been endorsed by Brazilian regulatory bodies (including CFC, CVM, BCB and SUSEP). In the recent past, arrangements have been put in place for full convergence of Brazilian accounting standards (CPC) with IFRS.

The requirements of *International Standards on Auditing* (ISAs), *International Standard on Quality Control* (ISQC-1) and related procedures have been made mandatory in Brazil. A

Committee is working on full convergence of the *Code of Ethics for Professional Accountants* with the standard in this regard issued by IFAC's International Ethics Standards Board for Accountants (IESBA).

At present, only the practicing auditors are required to comply with Continuing Professional Development (CPD) requirements. The CFC does not require its non-auditor members—about 500,000 accountants—to comply with any Continuing Professional Development (CPD) requirements.

The requirements for professional accountancy qualification in Brazil do not currently meet the requirements of *International Education Standards* (IESs) issued by IFAC's International Accounting Education Standards Board (IAESB). From this perspective, there is a need to upgrade arrangements for professional qualification examination and practical training of the future members of the accountancy profession.

**The table below summarizes the policy recommendations made in this report:**

| | Policy Recommendation | Responsible |
|---|---|---|
| 1 | **Further strengthen the technical capability of CFC to support development of a strong accountancy profession**:<br>■ build modern professional skills and enhance technical knowledge of CFC staff and committee members<br>■ make arrangements (amendment of law, if needed) for complying with all the requirements of International Education Standards<br>■ put in place necessary arrangements for introduction of monitored practical training<br>■ assist members all over the country to have access to high quality continuing professional development (CPD) activities<br>■ provide value added services for professional development of its members | CFC |
| 2 | **Strengthen CFC's capacity in line with international good practices to:**<br>■ support those who aspire to membership (its students) through:<br>• A rigorous and future-oriented program of professional learning and development<br>• Comprehensive and credible assessment procedures that serve to demonstrate the competences required of a professional accountant<br>• A range of services and resources to prepare students for membership<br>■ support its members, through:<br>• Ongoing access to relevant continuing professional development or education<br>• Identifying and providing access to relevant professional support services<br>• Maintaining and supporting networks of active members<br>• Provision of technical guidance and advice in support of member roles<br>• Access to up-to-date accounting information resources<br>• Access to relevant career planning and development resources | CFC |
| 3 | **On a pilot basis, introduce a voluntary Certified Professional Accountant (CPA) qualification program in line with international good practices.** | CFC, CVM |
| 4 | **Establish a strong "Audit Quality Review Board (AQRB)" under the auspices of CVM.** | CVM |

| | Policy Recommendation | Responsible |
|---|---|---|
| 5 | **Strengthen accounting curriculum and teaching in higher education institutions**<br>■ Strengthen collaboration arrangement between the Ministry of Education, the accountancy profession, and academia<br>■ Consider the introduction of an "accreditation program," in collaboration with other interested parties, for universities/colleges that offer a bachelor's degree in accounting.<br>■ Put in place arrangements for designing, developing and implementing a "train the trainers" program, focusing on practical aspects of IFRS, IPSAS and ISA for accounting academics in higher educational institutions throughout the country –<br>■ Develop a collaboration arrangement with higher educational institutions to provide access to latest learning materials on practical aspects of IFRS, IPSAS and ISA | Higher education institutes, CFC |
| 6 | **Take steps to further update the regulatory framework of accounting and auditing:**<br>■ Amend the Corporations Law<br>■ Streamline the current accounting standard setting process and develop a three-tier accounting and financial reporting structure<br>■ Continue to promote the full adoption of the CPCs by the regulatory authorities<br>■ Support various forward looking initiatives for enhanced corporate reporting<br>■ Ensure tax neutrality of corporate financial reporting | Congresso Nacional, CFC |

# PREFACE

This Report on the Observance of Standards and Codes: Accounting and Auditing (ROSC A&A) has been prepared in parallel with the update of the Financial Sector Assessment Program (FSAP) for Brazil. This is a reassessment of accounting and auditing practices in Brazil, with the previous report having been prepared in June 2005. The ROSC A&A is a part of the joint World Bank and International Monetary Fund initiative on Standards and Codes. The Standards and Codes Initiative was launched in the wake of the Asian economic and financial crisis in the late 1990s. It was one of several building blocks in the post-crisis efforts to strengthen the global financial architecture. Standards and codes in twelve policy areas were selected as key for sound financial systems, and these standards and codes are covered by the twelve ROSC modules prepared by the World Bank and IMF.[1]

The ROSC A&A review focuses on the strengths and weaknesses of the institutional underpinnings of accounting and auditing practices in the country. International Financial Reporting Standards (IFRS)[2] and International Standards on Auditing (ISA)[3], as well as international good practices are used as benchmarks for this review exercise. An overview of the ROSC A&A Program, including rationale and detailed methodology are available at http://www.worldbank.org/ifa/rosc_aa.html

The ROSC A&A exercise was carried out in Brazil in 2012 through a participatory process involving in-country stakeholders, including the Ministry of Finance, BCB, CVM, SUSEP, PREVIC, CFC, IBRACON, BM&F Bovespa, banks, insurance companies, audit firms, academics, and financial analysts.

The Brazil ROSC A&A review exercise was conducted by a World Bank team comprising Joseph Mubiru Kizito (Senior Financial Management Specialist and Task Leader), Susana Amaral (Senior Financial Management Specialist and Co-Task Leader), Regis Cunningham (Senior Financial Management Specialist), Ana Monteiro (Consultant), Ricardo Lopes Cardoso (Consultant).

The ROSC review exercise and report preparation was carried out under the overall supervision of Trichur K. Balakrishnan (Manager, LCSFM) and Daniel Boyce (Acting Manager, LCSFM). M. Zubaidur Rahman (Program Manager, OPSOR) participated as an Advisor.

[1] The current ROSC modules as approved by the Boards of the World Bank and IMF are (i) monetary and financial policy transparency, (ii) fiscal policy transparency, (iii) data dissemination, (iv) banking supervision, (v) securities regulation, (vi) insurance supervision, (vii) crisis resolution and deposit insurance, (viii) insolvency, (ix) corporate governance, (x) accounting and auditing, (xi) payment, clearing and settlement, and (xii) market integrity.

[2] IFRSs are issued by the International Accounting Standards Board (IASB). Many of the standards forming part of IFRS are known by the older name of International Accounting Standards (IAS) issued by IASB's predecessor International Accounting Standards Committee (IASC). All the standards and related official interpretations adopted by the IASB are referred as IFRS in this report.

[3] ISAs are issued by the International Auditing and Assurance Standards Board (IAASB), which is an independent standard setting organ of the International Federation of Accountants (IFAC).

# I. INTRODUCTION

1. This Report on the Observance of Standards and Codes: Accounting and Auditing (ROSC A&A) has been prepared under the Financial Sector Assessment Program in Brazil. The report assesses the status of implementation of 2005 ROSC A&A policy recommendations, highlights recent improvements in Brazil's corporate financial reporting framework, and sheds light on emerging issues regarding the institutional underpinnings of accounting and auditing practices that require further upgrading in line with international good practices

2. **Brazil's robust growth performance has led to a widespread improvement in economic and social indicators over the last decade.** Brazil is not only one of the largest countries in terms of area[4] and population,[5] but has also become one of the largest economies in the world; —Brazil's economy became the world's sixth largest economy,[6] overtaking that of the UK at the end of 2011. From 2006 up to 2011, Brazil was among the countries with the best performance in terms of the United Nations' Human Development Index; however, it still ranks in 84th place among 187 countries. Underpinned by the three pillars of macroeconomic policy—fiscal responsibility, inflation targeting, and flexible exchange rates—hyperinflation was finally contained in the late 1990s and the economy started a new period of higher growth. GDP expanded by 4½ percent a year between 2004 and 2010, more than doubling the average over the previous two decades, while real per capita income grew by more than 25 percent. Unemployment has fallen to historical lows. The rising real wages, increased financial deepening, and successful social programs, led to a sharp fall in both income inequality and poverty rates. The country's sovereign credit ratings reflect these improvements, having reached investment grade status.

3. **The Brazilian economy has rebounded quickly from the 2008-09 international financial crisis, partly reflecting the prompt and effective actions of the country authorities.** Improved public finances, low external debt, and large foreign exchange reserves allowed Brazil to adopt countercyclical policies in response to the crisis, including cutting interest rates, promoting credit growth, and undertaking a fiscal stimulus package. As a result of these policies, together with rising prices of commodity exports, Brazil was one of the first economies to rebound strongly from the 2008-09 global crisis. While Brazil is not immune to the unsettled external investment environment, it is in a better position than in the past to manage the potential fallout of increased distress in Europe and falling commodity prices. Given the relatively low net public debt (37 percent of GDP), the government has increased fiscal stimulus. Moreover, Brazil has benefited from record high foreign direct investments flowing mostly into the manufacturing and service sectors.

[4] Brazil covers 8,456,510 sq km area, which is roughly half of South America.
[5] Population was 196,655,014 in 2011.
[6] GDP was $2,476,652,189,879 in 2011.

## Banking Sector

4. **Brazil's banking sector has expanded significantly in recent years as a result of the macroeconomic stability the country enjoyed during this period.** There are about 160 banks operating in Brazil, more than one thousand credit cooperatives and dozens of leasing companies. Domestic private sector banks accounted for close to 40 percent of outstanding banking loans in 2011, with foreign banks' share at 17 percent. Public sector banks play a leading role in several segments, namely credit for investment, agriculture, and housing. The four largest banks in the country held 73 percent of the total deposits and are responsible for 70 percent of the total outstanding credit. Bank credit has expanded on average slightly above 20 percent per year since 2005, reaching R$2 trillion at the end of 2011, equivalent to 49 percent of GDP (up from 28 percent of GDP in 2005).[7] Brazil is also making inroads towards further developing domestic markets for long-term finance for corporations and real estate loans for households, which remain a very small share of total credit.

## Capital Market

5. **The Brazilian Securities, Commodities and Futures Exchange (BM&F Bovespa) is a leader in Latin America and one of the largest exchanges in the world.** It was formed in 2008 following the merger of BM&F (derivatives) and Bovespa (equities). In recent years, the BM&F Bovespa has made remarkable strides towards becoming a world-class equity market. In 2011, the daily volume of transactions in the equity market remained broadly stable (R$6.5 billion), repeating the historical record achieved in 2010. The equity market capitalization (373 publicly traded companies) reached R$2.3 trillion[8] at end 2011. Out of this total, 33 companies are also listed in the US, in the form of American Depositary Receipts.[9]

6. **In recent years, the domestic equity market has been impacted by the unsettled international financial markets, high volatility in commodity prices, and weak global growth.** The global financial crisis in 2008-09 and, more recently, the heightened risks associated with the sovereign debt crisis in the Euro area have hit asset prices and capital markets hard in general. In addition, Brazil's stock market has also not been immune to financial uncertainty, especially as it is heavily exposed to commodities, and has seen wide fluctuations in valuations. Equity public offerings have also been affected by the increased market volatility, totaling R$19.2 billion in 2011, the lowest level in the past five years. However, the issuances of other types of domestic securities (e.g. debentures, commercial paper) reached new record highs in 2011 (close to R$100 billion).[10] Likewise, Brazilian corporations have been increasingly able to access foreign markets, with issuances abroad reaching new highs in 2010-11.

[7] Source: BCB: Relatório de Economia Bancária e Crédito
[8] Source: Monthly, BM&FBOVESPA.
[9] Source: NYSE.
[10] Source: ANBIMA, Capital Markets Bulletin, 2012.

## Insurance and Pension Funds Sectors

7. **Brazil is the largest insurance market in Latin America and has large growth potential given its population size (and low coverage rates), rising incomes and robust credit.** The insurance sector more than doubled in size since the last ROSC A&A in 2005, due to a combination of factors, ranging from greater economic stability, rising credit, the deregulation process, and the opening of the market to foreign insurers.[11] The insurance companies and open pension funds market are supervised by the Superintendency of Private Insurance (*Superintendência de Seguros Privados* or SUSEP). The sector has 167 companies, with seven large groups playing a dominant role, spread across the following segments: insurance (69 percent), open pension funds [12] (15 percent), capitalization plans (11 percent), and local reinsurance companies (5 percent). Additionally, 121 foreign-owned reinsurance companies and reinsurance brokers were operating in the market. In 2011, as a whole, the market continued to grow at a faster pace than GDP. Since 2007, the revenues in the sector expanded at an average rate of 15 percent per year, reaching R$132 billion (to 3.2 percent of GDP) in 2011.

8. **The closed pension funds[13], with a significant presence of funds associated with state-owned companies, are among the largest investors in the domestic capital and debt markets.** At the time of the previous ROSC A&A exercise in 2005, there were about 350 closed pension funds holding total assets just under R$300 billion. At the end of 2011, there were 368 closed pension funds with R$574 billion assets under management (14 percent of GDP), with 2.3 million active members. The closed pension fund market is a highly concentrated sector, with a large presence of pension funds from state-owned enterprises/banks—the three largest closed pension funds in the country represent close to 50 percent of the total investments.[14] The vast majority of the pension funds' plans have defined benefits, and these face increased challenges to meet their targets in an environment of falling interest rates.

## Strategic Objective of ROSC A&A

9. **Notwithstanding the remarkable progress, Brazil still faces important challenges to sustain a high level of growth and achieve further progress.** In addition to maintaining appropriate macroeconomic policies, there is an extensive agenda to implement wide ranging structural reforms to promote growth, increase productivity, and raise living standards. Brazil's low domestic savings and limited domestic long-term financing markets remain a major impediment to the investment in infrastructure that is required to sustain high economic growth. Given the increased role played by the financial system—especially as more families and

[11] A positive change from open competition was achieved by the elimination of the monopolistic status of the state-controlled reinsurer IRB Brazil Re. However, Resolutions 225 and 232 of March 2011 issued by the regulator (CNSP) appear to put new limitations on the extent to which local re-insurance companies can re-insure risks through their international networks.

[12] Open pension funds (*Entidades Abertas de Previdência Complementar* or EAPC) are accessible to the general public and are managed by insurance companies, bank subsidiaries, and non-profit organizations.

[13] Closed pension funds (*Entidades Fechadas de Previdência Complementar* or EFPC) are accessible only to employees and retirees of a specific institution.

[14] Source: Brazilian Pension Fund Association (ABRAPP), December 2011.

businesses have access to banking credit and capital markets—it will also be necessary to further develop and strengthen Brazil's financial markets and institutions, to help to ensure macroeconomic stability and sustainable growth. In this context, one of the strategic objectives of the ROSC A&A is to help consolidate the institutional framework for accounting and auditing in Brazil in order to support improvements in business conditions in general, and facilitate access to more abundant and cheaper domestic and foreign financial resources.

# II. INSTITUTIONAL FRAMEWORK

10. Since the previous ROSC A&A review exercise was conducted in 2005, Brazil has made significant strides in strengthening the institutional framework for corporate accounting, auditing, and financial reporting. The framework, salient features of which are discussed below, appears to be of higher quality than that of 2005. However, there is room for further improvement. Moreover, in order to meet future challenges in the strengthening of the accounting profession, there is a need to further enhance the statutory and institutional underpinnings in line with international good practices. This would allow Brazil to emerge as a role model of accountancy profession development both regionally and internationally.

## A. Statutory Framework

11. **In recent years, some important legislative changes have been made to improve the regulatory framework for accounting and auditing.** During this period, the legislative and regulatory regime applicable to accounting and auditing of corporate entities, banks, and similar financial institutions in Brazil has changed significantly. The 1976 Corporations Law was amended in 2007. The amendment (Law No. 11638/07) was intended to align financial reporting requirements with international good practices. The legal amendments helped to adjust the 1976 Corporations Law (No. 6404/76) to the social and economic changes resulting from the evolution of market practices. It also contributed to strengthening the Brazilian public capital markets by requiring the use of internationally accepted accounting standards. Considering that Law No. 11638/07 significantly amended the 1976 Law, Brazilian corporate entities have been left the challenge of understanding the implications of these changes and measuring their impact on financial accounting and reporting matters. This has important implications for the institutional underpinnings of accounting and auditing practices in the country.

12. **Various regulatory bodies play a key role with regard to accounting, auditing and financial reporting for corporate entities within their regulatory purview**. In addition to complying with the requirements of the Corporations Law, the regulated entities are under the legal obligation to follow accounting, auditing and reporting requirements issued by the respective regulatory body. These regulatory bodies include:

- the Federal Accounting Council (*Conselho Federal de Contabilidade* –CFC) which has authority to issue accounting standards and to conduct oversight over the accounting profession in the country[15].
- the Securities and Exchange Commission (CVM) which supervises listed companies and investment funds;
- the Central Bank of Brazil (BCB) which oversees the banking sector and financial institutions;
- the Superintendency of Private Insurance (SUSEP) which monitors the insurance sand open pension funds markets,

[15] Law 12.249/10 and Decree 9.295/46

- the PREVIC (National Superintendency for Complementary Pension) which supervises the closed pension funds (EFPC).

Other companies operate under general laws and norms, without a regulatory body formally supervising their accounting and auditing practices. All the corporate entities are required to comply with the filing requirements set by the National Commercial Registry System (SINREM), and are required to file important corporate documents[16] with the commercial registry (*Junta Comercial*)[17]. It is worth noting that Brazilian corporate entities are generally organized as either *Sociedade por Ações* (S/A), a corporation limited by shares that can be privately held (closed corporations) or publicly held (open corporations); or as a *Limitada*, which is a limited liability partnership. A summary of accounting, auditing and reporting requirements for corporate entities under the prevailing statutory framework in Brazil is presented in Table 1 below

**Table 1 – Summary of Legal Requirements on Financial Reporting and Auditing by Types of Entities**

| Type of Entity | | | Regulatory Agency | Accounting and Financial Reporting Requirements[1] | Publication Requirement | Auditing Requirement |
|---|---|---|---|---|---|---|
| Listed companies (S/A) | | | CVM (under the umbrella of CMN[2]) | Corporations Law[3, 4]<br>CVM rules[4] | Yes | Yes<br>▪ By CVM-registered auditor<br>▪ Audit firm rotation every 5 years; cooling-off period of 3 years. If audit committee active, rotation every 10 years. |
| Non-listed companies | S/A | SME[5] | - | Corporations Law[3]<br>CVM rules (optional)[6] | Yes[12] | Not required |
| | | Large-size[5] | - | | Yes | Yes<br>▪ By CVM-registered auditor[13] |
| | Limitadas | Micro & small[17] | - | Civil Code[7]<br>Simplified version of the IFRS for SMEs[18] | Not required | Not required |
| | | SME[5] | - | Civil Code[7]<br>IFRS for SMEs[16] | Not required | Not required |
| | | Large-size[5] | - | Civil Code[7]<br>Corporations Law[8] | Not required | Yes<br>▪ By CVM-registered auditor[13] |
| Banks and non-banking financial institutions | | | BCB (under the umbrella of CMN[2]) | Corporations Law[3, 9]<br>COSIF[9]<br>CVM rules[9]<br>BCB Regulations[16] | Yes | Yes<br>▪ By CVM-registered auditor<br>▪ Rotation of managerial participants in the team, including audit partner in-charge, directors and managers every 5 years; cooling-off period of 3 years<br>▪ Audit committee mandatory for relevant financial institutions[14] |
| Insurance companies and open pension funds | | | SUSEP (under the umbrella of CNSP[10]) | Corporations Law[3, 10]<br>CNSP rules[10] | Yes | Yes<br>▪ By CVM-registered auditor<br>▪ Rotation of managerial participants in the team, including audit partner in- |

[16] These include the minutes of the Annual General Meeting (AGM) of shareholders, including the approved financial statements of the corporate entity.
[17] Art. 2, Law 8934/94.

| | | | | |
|---|---|---|---|---|
| | | | | charge, directors and managers every 5 years; cooling-off period of 3 years<br>▪ Audit committee mandatory for large-sized entities[15] |
| Closed pension funds | PREVIC (under the umbrella of CNPC[11]) | CNPC rules[11] | Not required | Yes<br>▪ Rotation of the audit partner in-charge every 5 years; cooling-off period of 3 years |

Notes

[1] The accounting, financial reporting and auditing requirements of the professional bodies, CFC and IBRACON, are also applied. However, they are legally binding to accounting professionals and are only mandatory for companies when explicitly endorsed by the respective regulators.
[2] National Monetary Council.
[3] Law 6404/76 (as amended) is commonly known as Corporations Law and sets the dispositions to be followed by joint stock companies (*sociedades por ações*), either open (listed) or closed (non-listed).
[4] Art. 26 of CVM Instruction 480/09 and art. 177, para. 3 of Law 6404/76 establish that the financial statements of listed companies must follow both the requirements of the Corporations Law and the rules issued by CVM.
[5] Threshold criteria are defined in Law 11638/07: large-sized entities encompass a company or group of companies under common control, independently of their legal structure, which had total assets > R$ 240 million or total gross revenues > R$ 300 million in the previous fiscal year. Small and medium-sized entities are all the other companies, by default.
[6] Art 177, para. 6 of Law 6404/76 establishes that closed *sociedades por ações* (which follow the Corporations Law) can also opt to follow CVM rules.
[7] The Civil Code is established in Law 10406/02.
[8] Law 11638/07 subjects large-sized *limitadas* to the Corporations Law for the preparation of their financial statements.
[9] Financial institutions follow the Central Bank's Accounting Plan for Financial Institutions (COSIF). The Corporations Law also applies to banks organized as *sociedades por ações* and CVM rules also apply to listed banks. Wherever a bank is also a listed company, the rules applicable to financial institutions prevail.
[10] Insurance companies and open pension funds are legally structured as *sociedades por ações* and thus must follow the Corporations Law, besides the rules set by CNSP – National Council of Private Insurance.
[11] Closed pension funds are structured as non-profit entities and follow the dispositions set by CNPC – National Council of Private Welfare.
[12] Art. 294 of the Corporations Law exempts closed corporations (fewer than twenty shareholders and net equity below $R 1 million) from publication requirements. However, they are still required to file their corporate acts with the company registry.
[13] Law 11638/07 requires that the financial statements of large-sized entities (independently of their legal structure) be audited by a CVM-registered auditor.
[14] Relevant financial institutions are those that have reference equity≥ R$ 1 billion or resources managed by third parties ≥ R$ 1 billion or third parties' resources + resources managed by third parties ≥ R$ 5 billion in the previous two fiscal years (CMN Resolution 3198/04).
[15] Large-sized insurance companies and open pension funds are those with adjusted equity≥ R$ 500 million or technical provisions ≥ R$ 700 million in the previous two fiscal years (CNSP Resolution 118/04).
[16]Resolution 3,786/09 requires that the reporting be prepared based on IASB's pronouncements, and not IASB's.[16] The IFRS for SMEs published by the IASB in July 2009 was translated by the CPC (CPC-PME) and endorsed by CFC (Resolução CFC 1255/09 and 1285/10). The IFRS for SMEs adoption is mandatory for entities not listed-companies and are not classified as large-sized entities.
[17] Threshold criteria are defined in Complimentary Law 123/06: micro-sized entities encompass a company which total gross revenues > R$ 360 thousand in the previous fiscal year; small-sized encompass a company which total gross revenues > R$ 3,6 million in the previous fiscal year.
[18] In 2012 the CFC issued Resolução 1418, presenting a simplified version of the IFRS for SMEs that micro and small-sized entities can choose to adopt instead of the IFRS for SMEs.

13. **Amendments to the Corporations Law of 1976 have resulted in significant improvements to the statutory framework for corporations, but the law still contains some provisions that the 2005 ROSC A&A had recommended to remove**. These provisions relate to accounting standards and financial reporting rules. This law prescribes the structure of financial statements, and enumerates the categories (and sub-categories) of accounts that each financial statement should include and how they should be classified and presented. From a practical point of view, the accounting standards and financial reporting rules may be included in sub legislative acts, in order to facilitate potential future revisions and additions needed to reflect the dynamic nature and complexity of business transactions. In place of emphasizing prescriptive rules, the Corporations Law should focus on more long-lasting general principles, especially in light of the fact that generally a lengthy process is needed for changing the law in line with new international developments on accounting and financial reporting standards. Some examples of financial reporting standards and rules in the Corporations Law and differences with international standards are as follows:

- Article 176: does not include the Statement of Other Comprehensive Income in the list of statements to be presented as components of financial statements. However, this is a requirement of IAS 1.
- Article 176: does not require Non-listed S/A with equity capital less than R$ 2,000,000 to present the Statement of Cash Flows. However, full IFRS and the IFRS for SMEs require any entity to present the Statement of Cash Flows.
- Article 183: establishes classification and measurement criteria for financial instruments, based on IAS 39. It is worth mentioning that the requirements of IAS 39 are in the process of being changed under IFRS 9.
- Article 183: establishes criteria to determine fair value; it could more directly draw on IFRS 13, which is dedicated to this issue.
- Article 187: requires presentation of gross revenue on the face of the Income Statement.
- Article 248: requires the application of the equity method to account for investments in associates, joint ventures and subsidiaries. However, IAS 27 does not allow the equity method in separate financial statements.

14. **According to the Corporations Law and CVM's regulations,[18] financial reporting requirements of the publicly traded companies include, amongst others, the following:**

- Preparation of the following financial statements on an annual basis[19]: balance sheet, statement of retained earnings, income statement, statement of cash flows, and statement of value added[20]. These are prepared, along with the explanatory notes, the opinion of the external auditor, the report of the *conselho fiscal* (when active), and the Directors' report.[21] These standardized financial statements must be submitted electronically to the CVM within three months of the end of the year[22]. In addition, they must be published in the official gazette, and in a widely circulated newspaper at least five days before the annual general meeting (AGM)[23]. When applicable, consolidated financial statements must also follow the filing and publication requirements established by CVM[24].
- The listed companies must electronically send quarterly information to CVM, along with a report prepared by the external auditor on the review of financial statements. This must be done within forty five days after the end of the quarter[25].
- The financial statements of listed companies must be audited by a CVM-registered independent auditor, as established in the Corporations Law[26].

[18] Art. 26 of CVM Instruction 480/09, and art. 177, para. 3 of Law 6404/76.
[19] Article 176 of Law 6404/76, as amended.
[20] The statement of cash flows and the statement of value added were changes brought in by Law 11638/07. The statement of cash flows replaces the statement of sources and applications of funds (DOAR).
[21] Acknowledging the auditor's opinion and assuming responsibility for the probity of the financial statements.
[22] Art. 25 of CVM Instruction 480/09.
[23] Arts. 133 and 289 of Law 6404/76.
[24] Arts. 249-250 of Law 6404/76.
[25] Arts. 29 and 65 of CVM Instruction 480/09.
[26] Art. 177, para. 3 of Law 6404/76, an amendment introduced by Law 11941/09.

15. **New provisions of the Corporations Law require the large-sized non-publicly traded business enterprises to follow the same accounting, auditing and reporting requirements as in the case of publicly traded companies**. This represents a significant improvement in the corporate financial reporting regime of Brazil. The large-sized companies are defined as a company or group of companies under common control, whose total assets, in the previous year, amounted to over R$240 million, or whose total gross annual revenues exceeds R$300 million. This threshold applies to all non-publicly traded business enterprises including limited liability partnerships and closed corporations. The new legal requirement has brought large-sized limited liability partnerships (*limitadas*) and closed corporations under the purview of high quality accounting and auditing requirements. It is worth noting that the threshold criteria of large-sized companies appear to be very high in the context of individual legal entities in Brazil. In practice, many economically significant group companies in the country establish a number of legal entities that do not individually meet the above thresholds, and thus avoid having to comply with the stringent financial reporting requirements. Since there is no enforcement regime for financial reporting by the large-sized limited liability partnerships and non-publicly traded companies, the group companies mentioned above do not necessarily comply with the requirements to prepare and present consolidated financial statements for the group of companies under common control.

16. **The new legislation has sparked a debate in regard to publication of audited financial statements by large-sized *limitadas***. Article 3 of Law 11.638/07 (that amended the Corporations Law) requires large-sized companies to prepare financial statements and have them audited by CVM-registered auditors. The digest of the law refers to "preparation and disclosure" of the financial statements. However, there is no clearly stated requirement to publish these financial statements. Some argue that a systematic interpretation of the Law leads to the conclusion that publication is required, since preparation of financial statements necessarily results in their publication, pursuant to articles 176 and 289 of the Brazilian Corporations Law. Others believe that Article 3 merely makes large-sized companies subject to the provisions of the Brazilian Corporations Law on preparation of financial statements (including the requirement for an independent audit), without addressing the issue of publication. This school of thought argues that if the legislator wanted to impose an obligation to publish financial statements on large companies, they would have done so expressly. The ambiguity about publication requirements has in some cases resulted in legal processes. Under such circumstances, it is necessary to take steps to add clarity in the law. Strengthening the requirement for publication of financial statements would also help to enhance the quality of financial reporting in Brazil and the effectiveness of audits. Since the Law already requires the preparation of the financial statements and their audit, additional provisions for their publication would ensure the comprehensiveness of the Law .

17. **Regardless of legal form and size, financial institutions must follow the Central Bank's rules for accounting and financial reporting purposes.** These rules are embodied in the standard Chart of Accounts for Financial Institutions (COSIF), which includes a compulsory chart of accounts, accounting methods, and standard formats of reporting. All banks and financial institutions[27] under supervision of the BCB,[28] are required to prepare and disclose financial

[27] Including, among others, commercial, investment, and development banks, leasing companies, savings and loans, securities companies, money exchange, mortgage companies, consortium companies, and micro credit entities.

statements on the basis of the COSIF. The COSIF already reflects many of the accounting policies and practices set out in IFRS. However, the BCB and CMN are working to narrow the gap between these two accounting standards, resulting in the adoption of 7 of the 41 CPCs up to March 2012. The financial reporting requirements of the COSIF include the following:

- Semi-annual and annual audited financial statements of banks and non-banking financial institutions must be published in the official gazette and in a widely circulated newspaper within 60 days and 90 days after the end of the respective reporting period. A full set of financial statements includes the balance sheet, income statement, statement of cash flows, statement of changes in equity, and explanatory notes;
- On a quarterly basis, banks must submit to BCB financial information containing financial statements reviewed by the external auditor, explanatory notes, risk management policies, and statistical data, as well as some other regulatory reports;
- At the end of every month, banks must submit simplified financial statements and statistical data to the BCB.
- Financial statements of banks and non-banking financial institutions must be audited by an external auditor registered with CVM.

18. **The accounting and financial reporting obligations for insurance companies and open pension funds are prescribed by Superintendency of Private Insurance (SUSEP) which operates under the umbrella of National Council for Private Insurance (CNSP).**[29] Insurance companies and open pension funds are legally structured as *sociedades por ações* and thus must follow the requirements of the Corporations Law. They must prepare annually the following financial statements: balance sheet, income statement, statement of comprehensive income, statement of changes in equity, statement of cash flows, and explanatory notes. These, in conjunction with the Director's report assuming responsibility for the financial statements, as well as the opinion of the independent auditor, must be published in the official gazette and in a widely-circulated newspaper, besides being made available in SUSEP's website. Consolidated financial statements, along with the auditor's opinion, must be sent electronically to SUSEP as well. On a quarterly basis, entities send to SUSEP a form with financial information reviewed by the external auditor; on a semi-annual basis, the interim financial statements and the auditor's opinion are also made available in SUSEP's website (with optional publication)[30] Financial statements of SUSEP regulated entities must be audited by an external auditor registered with CVM.

19. **The regulator of closed pension funds has changed since the 2005 ROSC A&A**. Previously the Secretariat of Private Welfare was the regulator. Under the new institutional arrangement, the closed pension funds are regulated by the National Superintendency for Complementary Pension (PREVIC) under the umbrella of National Council for Complementary Pension (CNPC). Closed pension funds are structured as non-profit entities and require an

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[28] Art. 4, Law 4595/64.

[29] SUSEP's supervisory authority does not cover all segments of the insurance, reinsurance, private pension and capitalization industry. ANS - National Agency of Supplementary Health is the supervisory authority for the health insurance and PREVIC – National Superintendence for Complementary Pensions supervises the closed private pension funds.

[30] Annex 1, SUSEP Circular 430/12.

employment relationship between the entity and the participant. The presentation format as well as the number of financial statements to be prepared by the closed pension funds has changed substantially since 2010. They must prepare and send electronically (publication is not required) to the supervisory agency the following statements[31]:

- On a monthly basis, trial balance of each benefit plan and administrative management plan, as well as a consolidated balance sheet or statement of financial position. These are to be aggregated per quarter and sent to the supervisor by the last day of the following month.
- On an annual basis, by March 31 of the following year: balance sheet (consolidated), statement of changes of equity (per benefit plan and consolidated), statement of equity (per benefit plan), statement of administrative management plan (consolidated), statement of actuarial obligations (per benefit plan), along with related explanatory notes (on consolidated statements) and the opinions of the independent auditor (on consolidated and individual statements). Also required are a report of the fiscal council, as well as a statement of the advisory board approving the financial statements.
- The requirements for mandatory audit of closed pension funds fall short of those applicable to open pension funds. The auditors do not need to be CVM registered. Any recognized (CFC/CRC registered) auditor in the country may be appointed as external auditor.

20. **There has been an extensive discussion in Brazil about the role of the *conselho fiscal*, focused on whether it complements or conflicts with audit committee responsibilities that would be in line with international good practices.** Companies listed in BM&F Bovespa are not required by CVM to establish an audit committee. The US Securities and Exchange Commission determined that Brazilian companies listed in the US could choose between adopting an audit committee or electing their *conselho fiscal* to perform the functions of the audit committee. As a result, US-listed Brazilian companies have either created an audit committee that co-existed with their *conselho fiscal* or have increased the scope of responsibilities of what became known as "*turbinated conselho fiscal*". The traditional functions performed by the *conselho fiscal* seem to go in a direction that is different from that of the audit committee attributions, even if there is some degree of overlap and similarity between the two. Even if both bodies monitor some of the acts of management (for instance, the definition of the accounting policies, preparation of financial statements, and oversight of the internal and external auditors' work), the audit committee executes these activities in a supporting role to the Board of Directors, whereas the *conselho fiscal* performs this monitoring (in a less frequent and continuous manner) as part of its responsibilities[32] of supervising management and the Board of Directors. Its ultimate goal is to protect the interests of the minority shareholders. International best practices also indicate that audit committees should be constituted after carefully considering the qualifications of the members and ensuring that the specific attributions of the committee are suited to the needs of the company. In 2011, CVM issued *Instrução 509* allowing listed companies that have an active audit committee and that meet certain requirements to rotate their audit firm at least once every 10

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[31] CNPC Resolution 8/11, annex C and SPC Instruction 34/09.

[32] The attributions of the *conselho fiscal* are spelled out in art. 163 of the Corporations Law.

years, instead of at least once every 5 years. According to BCB and SUSEP regulations, an audit committee that is separate from the board of directors must be created by a shareholder's resolution. Notwithstanding the requirement for separate bodies, the members of the audit committee may be members of the board of directors, provided that they meet certain independence requirements. Under Brazilian law, the hiring of the independent auditor is a right that is reserved exclusively for the board of directors of a company.

**Box 1: Good Practices in the Constitution of Audit Committees**

Many countries have issued guidance on the constitution of audit committees. Amongst these is the United Kingdom, where the Financial Reporting Council, in its responsibility for promoting high quality corporate governance, issued its Guidance on Audit Committees in September 2012. This guidance is designed to assist company boards in making suitable arrangements for their audit committees and to assist directors serving on audit committees in performing their role. It mentions that audit committee arrangements need to be proportionate to the task, and will vary according to the size, complexity and risk profile of the company. According to the FRC, the audit committee has a role to ensure, independently from the executive, that the interests of shareholders are properly protected in relation to financial reporting and internal control. The Guidance sets out the key elements that should be considered in the establishment of an audit committee. These are summarized below.

- *Establishment and terms of reference*: The Committee should comprise at least three, or in the case of smaller companies, two people. The main role and responsibilities should be set out in its terms of reference.
- *Membership and appointment*: At least one member should have recent and relevant financial experience.
- *Meetings of the audit committee*: the frequency and timing of the meetings is decided by the Chairman, and sufficient time should be allowed for a full discussion.
- *Resources*: The audit committee should be provided with sufficient resources to undertake its duties.
- *Remuneration*: consideration should be given to the time members are required to give to audit committee business.
- *Skills experience and training*: It is desirable that the committee member whom the board considers to have recent and relevant financial experience should have a professional qualification from one of the professional accountancy bodies.
- *Relationship with the Board*: The audit committee should report to the board on how it has discharged its duties.

The Guidance highlights the key roles and responsibilities of the Audit Committee. These include:

- Reviewing the Financial Reports and Annual Company reports;
- Ensuring the availability of arrangements for the independent investigation of possible improprieties in matters of financial reporting or other matters;
- Reviewing internal controls and risk management systems;
- Monitoring and reviewing the effectiveness of the company's internal audit function;
- Overseeing the company's relations with the external auditor, including appointment and tendering. terms and remuneration, facilitating the planning and implementation of the annual audit cycle; and
- Ensuring independence of the external auditor.

*Source: https://www.frc.org.uk/Our-Work/Publications/Corporate-Governance/Guidance-on-Audit-Committees-September-2012.aspx*

21. **A new law in 2010 has strengthened the legal mandate of the accountancy profession's regulator, but there are areas that still require additional upgrading.** The Federal Accounting Council (*Conselho Federal de Contabilidade* – CFC) is a self-regulatory professional organization established by law. The Law 12249/2010 amended Decree-Law 9295/1946 (which creates the CFC and defines the accounting professionals' competencies). The new legal provisions specifically:

- state that the monitoring of the accounting practice is under the mandate of the CFC/CRC;
- establish CFC's responsibilities as including setting accounting standards, and regulating the professional examination, requirements for technical qualifications, and CPD programs;
- determine that in order to qualify as a professional accountant, a person needs to obtain a Bachelor's degree in accounting offered by an institution recognized by the Ministry of Education, successfully complete the professional examination, and obtain registration at the CRC; and
- indicate sanctions applicable for violation of the legal requirements to practice as a professional accountant.

The CFC has undertaken a number of efforts to strengthen the accounting profession in Brazil. As part of these efforts, the CFC: (i) provides financial support to educational institutions that offer master and/or doctoral programs in accounting; (ii) under an agreement with the Ministry of Education (SESU/MEC), evaluates the curriculum of undergraduate courses in Accounting offered by colleges and universities; (iii) suggests the structure and content of a standard curriculum for an undergraduate course in Accounting; (iv) in collaboration with its regional offices (CRCs), organizes annual meetings and forums with coordinators and lecturers of accounting. In order to build on these achievements and further upgrade CFC's powers and functions, it would be valuable to review all relevant legal provisions concerning CFC, and enact a modern law in this regard. In addition to dealing with CFC's operational matters, such a comprehensive modern law would provide legal backing for stronger arrangements for the professional accountancy examination and practical training for professional accountants and auditors in line with the international good practices. It would also support the issuance of high quality financial reporting and auditing standards consistent with the internationally accepted standards.

## B. The Accountancy Profession

22. **The CFC undertakes oversight of Brazil's accountancy profession on a self regulated basis.** The CFC, along with its regional arms—Regional Accounting Councils (*Conselhos Regionais da Contabilidade* or CRC)—carries out regulatory activities for overseeing the accountancy profession throughout the country[33]. Established in 1946, by Decree-Law 9695, the CFC is a special type of entity independent of the government. It is responsible for issuing the directives that govern the profession as well as for overseeing professional conduct. The Regional Accounting Councils (CRCs), subordinated to the CFC, are responsible for administering the CFC directives, as well as for registering accountants and providing support in the oversight of the profession. Accounting and auditing activities in Brazil can only be conducted by persons or firms registered with the CFC/CRC system.

23. **IBRACON is a private organization established in 1971 to promote advancement of the audit profession**. It cooperates with the CFC on technical and ethical issues of the auditing and accounting profession, assisting with the interpretation of the standards that regulate the profession and with the implementation of quality control standards, as well as working towards the enhancement of professional education. IBRACON has strong ties with the international professional community given its close involvement with the convergence process initiated in 2010—it is the Brazilian official translator of the IFRS issued by the IASB and of Brazil's version of IFRS for SMEs. It has also provided assistance with the process for CFC's issuance of Brazilian auditing standards that are fully equivalent to international standards on auditing (ISAs) as of 2010. As of mid-June 2012, IBRACON had 1,246 individual members and 104 firm members. The CFCs membership is comprised of 288,246 accountants, and 194,260 accounting technicians.

24. **Both the professional bodies have played a crucial role in developing Brazil's accountancy profession**. The CFC and the IBRACON set the accounting standards, primarily through the Brazilian Accounting Pronouncements Committee (CPC). The ethics and auditing standards result from the joint efforts of both organizations and are issued by CFC. In addition, CFC and IBRACON establish the education and qualification requirements for their members, develop and offer examinations as well as continuing professional development programs, and ensure quality control through a peer review program.

25. **Both CFC and IBRACON are members of the International Federation of Accountants (IFAC).** As such, they must make their best efforts to comply with IFAC's Statements of Membership Obligations (SMOs).[34] Even though improvements have taken place, full compliance with all SMOs has yet to be achieved. The main areas that need to be addressed in this regard, are the need to: (i) implement a process of independent oversight and supervision (SMO1); (ii) put in place arrangements for monitored practical training as an entry requirement to the profession, mandatory continuing professional development (CPD) for all accountants, and

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[33] Reference to CFC denotes the CFC/CRC system.

[34] The action plan for IFAC compliance was originally produced jointly by CFC and IBRACON July 2010 and was updated in July 2012. The SMOs were revised by IFAC in December 2012 with an overall clarification being made to the Applicability Framework and changes to requirements being applied to SMOs 1 and 6.

alignment to International Education Standards (IES) (SMO2); and to (iii) adopt IFAC's Code of Ethics (SMO4).

**Table 2 – Summary of Compliance with IFAC's SMOs**

| SMO | Issue | Comments | Compliance with SMO |
|---|---|---|---|
| 1 | Quality Assurance | • Formation of the Auditing Working Group for elaboration and revision of equivalent standards based on ISQC 1 and ISA 220—220—arrangements need to be put in place for ensuring effective implementation of these standards<br>• Peer review system for CVM-registered auditors<br>• BCB, in conjunction with its prudential supervision work, reviews external auditor's files and related documents<br>• CVM has developed a program for risk-based review of the quality of audit in publicly traded companies | Moderate |
| 2 | International Education Standards for Professional Accountants and Other IAESB Guidance | • College degree and a very basic proficiency examination are the only requirements to enter the profession<br>• Academic curriculum not up to IES<br>• No practical experience requirement for professional qualification<br>• CPD requirement only for independent auditors of entities regulated by CVM, BCB, and SUSEP; no such obligation for all other professional accountants including the auditors of non-listed companies and closed pension funds | Low |
| 3 | International Standards, Related Practice Statements and Other Papers Issued by the IAASB | • ISA adopted by CFC and IBRACON in 2010<br>• Training programs and implementation in progress<br>• Compliance with the standards varies among various audit firms | Substantial |

| | | | |
|---|---|---|---|
| 4 | IESBA Code of Ethics for Professional Accountants | • CFC/IBRACON's Code of Ethics date back to 1996 and is not as comprehensive as IFAC's current Code of Ethics for Professional Accountants<br>• A joint committee of CFC and IBRACON is working to harmonize Brazilian Code of Ethics with that of the IESBA | Low |
| 5 | International Public Sector Accounting Standards and Other IPSASB Guidance | • Arrangements have been made for gradual adoption of IPSAS: federal (2011), state (2012), and municipal (2013) levels<br>• Implementation slowed down by legal challenges | Moderate |
| 6 | Investigation and Discipline | • The CFC has put in place an arrangement for investigation and discipline, however its effective implementation is yet to come<br>• There is a legal impediment to implementing IFAC recommendation of including non-accountants in disciplinary tribunals<br>• There is no independent oversight of the profession | Low |
| 7 | International Financial Reporting Standards (IFRS) | • Creation of CPC to centralize standard-setting process; however, CPC-issued standards become applicable in regulated entities after endorsement by the respective regulators<br>• The CVM mandates the use of IFRS for consolidated financial statements for public interest companies<br>• New Brazilian GAAP substantially converged to IFRS<br>• Brazilian GAAP for SMEs essentially a translation of IFRS for SMEs<br>• Micro and small entities can choose to adopt ITG 1000 (*Resolução* CFC 1418/12), a simplified version of the IFRS for SMEs.<br>• Compliance with the standards varies among various corporate entities | Substantial |

26. **The current Code of Ethics issued by CFC[35], in force since 1996, needs to be reviewed to ensure alignment with the IESBA's Code.** The IESBA's Code is quite extensive and relies on a risk-based approach, including examples to help address various ethical challenges faced by the professional accountants. CFC's Code is considerably shorter and less comprehensive: it only covers very broadly the professional duties and excluded services, the

[35] CFC Resolution 803/96, as amended.

value of the services, professional conduct, and penalties. In addition, it does not contain implementation guidelines similar to the IESBA's Code. A Joint Committee of CFC and IBRACON is currently working to harmonize Brazilian ethical standards to the IESBA Code of Ethics for Professional Accountants.

27. **The four largest international audit firm networks dominate the market for provision of audit services to listed companies, banks, and insurance companies,[36] impacting positively on compliance with IFRS financial reporting requirements.** The audit requirement imposed on large private companies (*Limitadas*) by law 11638/07 has increased exponentially the potential demand for audit services. Medium-size audit firms have also established a significant presence, especially those associated with international networks. Benefiting from their affiliation with global audit networks, the Big Four audit firms have access to a wider pool of knowledge and experience with IFRS implementation, which they use to train preparers, regulators, and students. The perception of various stakeholders interviewed by the ROSC team is that there is a big gap in the quality of professional services provided by the major audit firms ("big-4" and "tier-2" audit firms) and smaller-size audit firms.

28. **There are no statutory provisions requiring an auditor or a licensed accountant to take on professional indemnity insurance.** However, auditors belonging to international network of firms are covered by international professional insurance policies under their networks. For independent auditors of listed companies, CVM Instruction 308/99 establishes individual and unlimited liability of the audit partners for obligations created while acting in a professional capacity, after the assets of the audit firm have been exhausted. Remaining mechanisms to deal with liability issues are on an after-the-fact basis.

29. **The CFC has put in place a regime of ethical and disciplinary sanctions that is broadly in line with IFAC guidelines, and this needs to be further strengthened and effectively enforced.** Law 12249/10 lists the sanctions to be applied which vary from fines and warnings to temporary suspension or even permanent loss of license for the more serious offenses. In this regard, the CFC undertook a number of supervisory actions in 2012, and 7,428 professionals were penalized with ethical and disciplinary sanctions. There is a need for further improvements that are necessary to implement these investigation and disciplinary mechanisms with more efficiency and effectiveness, such as the need for additional focus on compliance with IFRS for SMEs.

30. **With the objective of developing a model of self-regulation within the profession, CFC and IBRACON have established a quality assurance peer review program for CVM-registered independent auditors.[37]** A committee formed by members of the two professional bodies is responsible for administering all the aspects of the peer review program aimed at

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[36] With regard to the audit market share in 2011: About 80% of the listed companies were audited by the Big Four firms (source: CVM). For the banking sector, about 96% of all banks representing about 99% of total banking assets were audited by the Big Four (source: BCB). Non-bank financial institutions, also regulated by BCB (including leasing, finance, securities, consortium, savings and loans) gave about 35% of their audit business to the Big Four. The Big Four audited about 93% (in terms of percentage of total premiums earned) of the insurance undertakings (source: SUSEP).

[37] CFC Resolution 1323/11 and art. 33 of CVM Instruction 308/09

evaluating compliance with CFC-issued professional and technical standards. All CVM-registered independent auditors (firms and individuals) must submit themselves, at least once in a four-year cycle, to a quality assurance review by another CVM-registered auditor of comparable size. The report on findings prepared by the auditor-reviewer prompts the reviewed auditor to outline an action plan. The CFC analyzes both review reports and action plans, makes them available to the regulatory bodies that ask for peer review findings, and initiates appropriate proceedings, if needed. In 2012, a total of 27 individual auditors and 103 audit firms have been selected to take part in the peer review program. The peer review program mainly focuses on audit engagement file reviews and includes an assessment of the quality of the audit work performed. There are opportunities to strengthen this process, particularly through placing more focus on the assessment of the extent to which audit quality control standards (e.g. ISQC-1, and ISA 220) are being applied. There may be a shortcoming in the financing arrangement through which the peer reviews are financed by the audit firm subject to review and which also influences who conducts the review. Such an arrangement may allow conflicts of interest to arise and may compromise the independence of such reviews.

31. **The CVM has introduced a system of mandatory audit firm rotation for the listed companies**. The CVM requires audit firm rotation for listed companies every five years. After a cooling off period of three years, the same audit firm may again be engaged as an independent auditor. In 2011 CVM issued *Instrução 509* allowing listed-companies that have an active audit committee and that meet certain requirements to rotate their audit firm at least once every 10 years, instead of once every 5 years. The BCB and SUSEP require the rotation of the audit engagement managerial participants of the team every 5 years, including the partner, director and managers.

## C. Professional Education and Training

32. **While a lot of progress has been achieved in the last few years, the quality of accounting education and training needs to be further strengthened in order to support the overall progress of the profession.** There are about 1,238 officially recognized and active undergraduate programs, 19 master's degree programs and only 4 doctoral programs in accounting in the Brazilian universities and colleges. Generally, high quality undergraduate programs are offered by a handful of leading educational institutions in the country. The scarcity of qualified accounting instructors contributes to the deteriorating quality of undergraduate accounting programs offered by many higher educational institutions. In general, there is a low level of compliance among Universities with guidelines on accounting curriculum. At the federal level, these guidelines are issued by the Ministry of Education (MEC) and the National Council on Education (CNE). For accounting courses, the minimal content of the program is defined in the CNE/CES Resolution 10/04, which determines that "the curriculum must provide knowledge of the economic and financial environment, at the national and international levels, so as to promote the harmonization of the international accounting norms and standards." It leaves to colleges and universities the responsibility of organizing the format and programmatic content of accounting courses. There are a handful of universities that have incorporated IFRS and ISAs in their programs (located in the main urban areas of São Paulo and Rio de Janeiro). In most of the universities throughout the country, the academic accounting programs do not use modern

textbooks and teaching methodologies: the emphasis is more on memorization techniques rather than the use of analytical judgment and critical thinking skills. In 2008, CFC approached MEC and prepared a "Proposal for the Content of the Accounting Higher Education" with the objective of harmonizing the accounting education for all colleges and universities in Brazil. This proposal is yet to be implemented. In 2009, CFC and the Higher Education Secretariat in the Ministry of Education (SESu/MEC) signed a cooperation agreement under which CFC supports SESu/MEC in activities related to the regulation and supervision of higher education in Accounting.

33. **The requirements for registration within the CFC/CRC system as an "accountant (*contador*)" fall short of international good practices and pronouncements of the International Accounting Education Standards Board (IAESB) of IFAC.** It is worth noting that the proficiency examination for registration as an "accountant" started in 2000 in accordance with a regulation issued by the CFC. Prior to that, having a Bachelor's degree in accounting was the sole requirement for candidates to access the accountancy profession and become members of CFC. According to the international good practices, monitored practical training is an integral part of pre-qualification education and training, and registration as a member of a professional accountancy organization. Moreover, a prospective audit practitioner needs to have additional practical training in an audit environment under the supervision of an experienced practicing member of the profession. These requirements on monitored practical training are clearly recognized by IFAC and their implementation as precondition of CFC membership would represent an important enhancement of the standard of the accounting profession in Brazil.

34. **The introduction of the proficiency examination was a significant positive step towards development of the accountancy profession in Brazil**. To build on this achievement, the contents and focus of the proficiency examination need to be upgraded in order to make them comparable with international good practices.[38] During the period from its introduction in 2000 to 2004, the proficiency examination was held twice a year in all Brazilian states. In 2005, the exam was suspended due to legal challenges[39]. In 2010, the new law 12249, empowered CFC to regulate the accountancy profession's proficiency examination and CPD matters. Following this, the CFC reintroduced the proficiency examination as a prerequisite for its membership[40]. The examination lasts 4 hours and consists of fifty multiple-choice questions focusing on various accounting and business related subjects[41]. The ROSC Team carried out an analysis of the 50 multiple choice questions tested in the first proficiency examination of 2012. The purpose was to determine the level of rigor (easy, moderate, or difficult), and the focus of assessment (memorization, understanding and calculation, and judgment) of each of these questions. The result of this analysis is presented below:

| What is assessed \ Difficulty level (number of questions) | Easy | Medium | Difficult | Total |
|---|---|---|---|---|
| Memorization | 21 | 5 | 0 | **26** |
| Understanding and calculation | 10 | 8 | 3 | **21** |
| Judgment | 1 | 2 | 0 | **3** |
| Total | **32** | **15** | **3** | **50** |

In spite of the fact that the proficiency examination questions are very simple, the test results show poor performance. In 2011, the average success rate in two offerings of the proficiency examination was about 42%. In the first offering of proficiency exam during the first half of 2012, the performance of candidates improved to a pass rate of 47.19%.

35. **The current accounting technician scheme will be phased out**. As a requirement for registration within the CFC/CRCs system as an accounting technician (*técnico contábil*), each candidate is expected to: (i) have a high school diploma; (ii) pass a proficiency exam (*exame de suficiência* for *técnico contábil*); and (iii) complete a one year waiting period following graduation (without further proof of experience required). The scheme will be phased our starting from June 2015 through the termination of new registrations granted to fresh graduates of technical courses[42].

36. **The CFC-registered accountants who want to act as independent auditors of regulated entities are required to pass additional proficiency examinations.** These additional

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[38] IES 6, *Assessment of Professional Capabilities and Competence*, IAESB of IFAC.

[39] The argument advanced was that, since the exam was created by an administrative act and not by law, it barred the constitutional principle of free access to the profession and was therefore unconstitutional.

[40] CFC Resolution 1301/10, amended by Resolution 1373/11

[41] Subjects covered include accounting principles, cost accounting, business law, ethics, mathematical finance, Brazilian accounting standards, and Portuguese language for the proficiency exam for the accounting technician; accountants are tested additionally on public accounting, management accounting, controllership, accounting theory, auditing, forensic accounting, and statistics.

[42] Article 12, paragraph 2 of law 12249/10.

examination requirements thus apply only to those auditors who wish to practice in the regulated sectors. A CFC-member who wishes to act as an independent auditor of listed companies must take a general technical qualification examination.[43] The names of successful candidates are included in the national registry of independent auditors (CNAI). This examination is administered by CFC in collaboration with IBRACON. It is offered once a year. It is a 4-hour long test with 50 multiple-choice questions and 2 essay-type questions. Only the CNAI-registered audit practitioners with five years of practical experience of auditing listed companies are qualified to apply for CVM registration. It is worth noting that this practical experience requirement does not fully meet the stricter requirement of monitored practical training in line with international good practices.[44] If a CNAI registered audit practitioner wants to audit entities under the supervision of BCB or SUSEP, he/she needs to take additional examinations specific to these sectors. The format of the exam is similar but the content is adapted to the sector peculiarities.[45] These specific examinations are also administered by the CFC. The ROSC Team carried out an analysis of the 52 questions tested in CNAI examination held in the first half of 2012. It was found that about 79% of the questions were easy, and primarily assessed candidates' capacity to memorize standards. Table-3 below shows a summary of auditor examination results since its inception in 2001.

[43] Subjects covered: ethics, professional law, accounting principles, Brazilian accounting standards, auditing, company law, laws and regulations issued by the regulators, and Portuguese language.

[44] IES 5, *Practical Experience Requirements*, IAESB of IFAC.

[45] Specific exam for BCB covers: professional law, accounting principles, Brazilian accounting standards, auditing, laws and regulations issued by BCB, modus operandi of financial institutions, accounting for banks, and Portuguese language; specific exam for SUSEP covers: professional law, accounting principles, Brazilian accounting standards, auditing, laws and regulations issued by SUSEP, modus operandi of institutions regulated by SUSEP, accounting for banks, and Portuguese language.

## Table 3 - General Technical Qualification Exam and Specific Exams for Independent Auditors of CVM, BCB, and SUSEP

| Years | General Technical Qualification Exam (QTG) for becoming a CVM-registered auditor[1] | | | Specific Exam for becoming an auditor of BCB-regulated entities[2] | | | Specific Exam for becoming an auditor of SUSEP-regulated entities[2] | | |
|---|---|---|---|---|---|---|---|---|---|
| | Total Candidates | Successful Candidates | Passing Rate | Total Candidates | Successful Candidates | Passing Rate | Total Candidates | Successful Candidates | Passing Rate |
| **2001** | 234 | 186 | 79.5% | 363 | 271 | 74.7% | - | - | - |
| **2002** | 565 | 479 | 84.8% | 444 | 233 | 52.5% | - | - | - |
| **2003** | 456 | 113 | 24.8% | 222 | 32 | 14.4% | - | - | - |
| **2004** | 385 | 221 | 57.4% | 223 | 77 | 34.5% | - | - | - |
| **2005** | 388 | 113 | 29.1% | 188 | 58 | 30.9% | 145 | 75 | 51.7% |
| **2006** | 303 | 75 | 24.8% | 127 | 26 | 20.5% | 48 | 21 | 43.8% |
| **2007** | 390 | 81 | 20.8% | 142 | 46 | 32.4% | 46 | 23 | 50.0% |
| **2008** | 492 | 153 | 31.1% | 149 | 50 | 33.6% | 49 | 16 | 32.7% |
| **2009** | 766 | 220 | 28.7% | 377 | 133 | 35,3% | 121 | 47 | 38.8% |
| **2010** | 918 | 235 | 25.6% | 235 | 48 | 20.4% | 112 | 31 | 27.7% |
| **2011** | 998 | 491 | 49.2% | 220 | 82 | 37.3% | 110 | 44 | 40.0% |
| **TOTAL** | **5,895** | **2,367** | | **2,690** | **1,056** | | **631** | **257** | |

[1] An auditor who practices for an entity under CVM, BCB or SUSEP must pass the QTG exam which is a condition that must be met for registration in the National Registry of Independent Auditors (CNAI) of the CFC.

[2] An auditor of BCB or SUSEP-regulated entities must cumulatively pass the QTG exam and the Specific Exam for the respective field of practice.

37. **Accountancy education and training programs need to have increased content with respect to professional values and ethics.** Practical case-oriented learning programs and professional training can significantly contribute to enhancing awareness of professional ethical issues and influence the reasoning and judgment of aspiring accountants and auditors. From this perspective, the International Education Standards and IFAC guidelines recommend teaching professional ethics separately in the prequalifying education of professional accountants and auditors.[46] However, the higher educational institutions that prepare future accountants and auditors in Brazil, do not appear to provide adequate coverage on ethical dimensions in their curricula. In this regard, CFC and IBRACON should play an important role through the delivery of high quality CPD programs focusing on the practical dimensions of professional ethics.

38. **The CFC requires all CNAI-registered audit practitioners to comply with CPD requirements; however, this requirement needs to be extended to all accountants in line with international good practices.** According to the International Education Standard No. 7, IFAC's member bodies should require all professional accountants to develop and maintain competence relevant and appropriate to their work and professional responsibilities. From this perspective, all the members of CFC should be required to comply with CPD requirements. It is worth noting that CVM, BCB and SUSEP strictly require CPD compliance by the external auditors of their regulated entities. In order to support an effective CPD regime for the practicing auditors, CFC and IBRACON have established a technical committee to coordinate the CFC's program of continuing professional education (PEPC).[47] Since its implementation in 2003, the CFC's program has recognized about 400 CPD training provider institutions, and facilitated the continuing professional development of about 5,000 professionals in the country. In order to retain their CNAI registration, practicing auditors are required to complete at least 40 learning units of continuing professional education each year[48]. The CFC/CRC system maintains a registry of the auditors who have fulfilled their CPD requirements; non-compliance with this obligation leads to administrative procedures for violation of the professional accountant's code of ethics.

39. **It is widely believed in the profession that the quality of the CPD should be improved, and the main challenge of an efficient and effective CPD regime is the lack of consistency in the quality of training programs offered by CFC-accredited training providers.** This is due in part to the fact that CFC/CRC do not monitor the capability of these institutions in delivering high quality training programs. The CFC thus needs to put in place arrangements for making high quality CPD programs available throughout the country—specifically in regions outside the South East. In particular, the programs should focus more on practical implementation aspects of IFRS and ISAs. With the enactment of Law 12.249/10, the CFC constituted a working group to study effective means of making available CPD programs for professional accountants. It is expected that once developed, the new requirements will be applied initially to accountants working in regulated sectors.

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[46] IES 4, *Professional Values, Ethics, and Attitudes*, IAESB of IFAC.
[47] CFC Resolution 1146/08 (approves NBC PA 12), amended by CFC Resolution 1377/11.
[48] The CPD learning unit is calculated on the basis of the nature of CPD activities—e.g. formal training, conference participation, publication of articles, post-graduate education, etc.

## D. Setting Accounting and Auditing Standards

40. **In 2005, an important landmark was reached with the formal creation of the Brazilian Accounting Pronouncements Committee (CPC), with the goal of systematizing and centralizing the standard-setting process and promoting international convergence of accounting standards.** The CPC was created by CFC Resolution 1055/05 as a common effort of six entities: the Association of Listed Brazilian Companies (ABRASCA), the National Capital Market Investment Professionals and Analysts Association (APIMEC), the Financial and Accounting Research Institute Foundation (FIPECAFI), BM&F Bovespa, CFC, and IBRACON. In practice, CPC is independent of these sponsoring entities. It is composed of twelve members, mostly professional accountants. On a regular basis, BCB, CVM, SUSEP, and SRF are invited to get involved in CPC's work, which consists of issuance of technical pronouncements, guidelines, and interpretations on accounting standards. Technical pronouncements go through a thorough due process involving drafting, discussion within working groups, and mandatory public hearing before final approval and issuance. The technical pronouncements on accounting standards resemble current versions of IFRS. However, for historical reasons, some departures from IFRS are still found in the applicable accounting standards in Brazil. Moreover, if a particular IFRS allows application of alternative accounting policies, the technical pronouncement sometimes adopts one of the alternatives; the most common difference refers to the elimination of the standards for revaluation and early adoption when permitted. In December 2007, the Brazilian Congress passed legislation (law 11638/07) amending the Corporations Law, requiring that the applicable accounting standards in the country, and the accounting rules to be issued by the CVM, should be compatible with the international standards issued by the International Accounting Standards Board (IASB).

41. **Although the CPC issues accounting pronouncements in Brazil, these standards become mandatory only after the relevant regulatory bodies issue their own acts endorsing the CPC-issued pronouncements.** If a particular regulatory body does not endorse specific technical pronouncements (accounting standards), the entities covered by that regulatory body do not have an obligation to follow them. However, once the CFC endorses the CPC's pronouncements, their adoption becomes mandatory for professional accountants As of March 2012, there were 41 CPCs applicable in Brazil. However, only 7 of these CPCs have been adopted by the BCB for application in legal entity financial statements of the financial institutions that fall under its supervisory ambit. The CFC has endorsed all the CPCs and the CVM has endorsed all except that in respect of IFRS for SMEs. The SUSEP has adopted 38 CPCs. Detailed information in this regard is presented in Appendix A.

42. **The CFC has the legal authority to issue applicable auditing standards in Brazil**. In practice, IBRACON plays a very important role in collaboration with CFC in the process of issuing applicable auditing standards. When a decision was made in 2005 to converge Brazilian auditing standards with the International Standards on Auditing (ISA) issued by the International Auditing and Assurance Standards Board (IAASB), the responsibility of providing technical leadership on this matter was assumed by IBRACON. In this context, IBRACON translated all the clarified ISAs and these standards were issued by CFC as Brazilian auditing standards. These new standards became applicable to the audits of financial statements on or after December 31, 2010. In the process of adopting ISAs, the original ISA numbering system was maintained to

facilitate the subsequent revisions. The Brazilian auditing standards are classified as follows: (i) professional standards—includes the code of ethics which is not fully comparable with IESBA's code of ethics for professional accountants; and (ii) technical standards—International Standards on Auditing (ISA), International Standards on Assurance Engagements (ISAEs), International Standards on Related Services (ISRSs), and International Standards on Review Engagements (ISREs).

43. **The Transitory Tax Regime (*Regime Tributário de Transição – RTT*) was introduced by federal Law 11941, from May 2009**. Since old accounting standards were mainly tax-oriented and served the information needs of taxation authorities, the introduction of market-oriented new accounting standards (IFRS) from January 1, 2008 gave rise to concerns among the policy makers regarding potential distortions in tax calculations. Its main aim was to ensure 'tax neutrality' of the applicable IFRS-based accounting standards and related CVM regulations applied by corporate entities in accordance with the requirements of federal Law 11638/07. The RTT regime stipulates that the corporate entities that prepare general purpose financial statements in accordance with the new accounting standards, should take into consideration the accounting requirements in force on December 31, 2007 for purposes of calculating various taxes.[49] Therefore, whereas general purpose financial statements would be prepared on the basis of the standards introduced in 2008, tax liabilities would continue to be calculated as previously done. The RTT regime was originally scheduled to end in 2012. So far it is not clear whether tax neutrality of corporate financial reporting will become permanent, and whether it will be extended to other corporate taxes.[50]

[49] Corporate Income Tax *(IRPJ)*, Social Contribution on Net Profit *(CSLL)*, Employee's Profit Participation Program *(PIS)*, and Tax for Social Security Financing *(COFINS)*.
[50] Such as, taxes based on sale of goods and services *(ICMS and ISS)*.

## E. Ensuring Compliance with Accounting and Auditing Standards

44. **The recommendations of 2005 ROSC A&A regarding enhancement of the monitoring and enforcement capacity of regulatory agencies with respect to financial reporting have been substantially implemented in BCB and CVM**. However effective arrangements for monitoring and enforcing accounting standards for general purpose financial statements are yet to be put in place by SUSEP and PREVIC. The BCB and CVM have taken steps for building internal capacity on practical aspects of IFRS, with attendant effect on their ability to take actions for ensuring compliance with the applicable accounting and reporting requirements by the regulated entities. On the other hand, SUSEP and PREVIC have not established adequate capacity to carry out the proactive monitoring and enforcement of IFRS compliance with respect to general purpose financial statements of the regulated entities.

45. **Bank supervisors at BCB extensively use financial statement information for determining risks and carrying out inspection activities**. On-site supervisors, in the course of a bank examination, analyze: financial statements (both published and submitted to Central Bank); external auditors' reports (including mandatory complementary reports required by Central Bank); accounting reports presented to the boards of directors and senior management (budget and others); monitoring reports and other analyses prepared by off-site supervisors; and early warnings based on the cross-checking of relevant information and an analysis of trends. Off-site supervisors analyze accounting numbers in the financial statements of banks in order to identify mismatched information and variations from the industry average, and undertake varied cross checking exercises of numerical information. These exercises contribute to the determination of risks and provide relevant early warning signals..

46. **BCB on-site supervisors are supported by a specialized team responsible for financial accounting and auditing issues**. This team is a part of BCB's Department of Supervision of Banks and Banking Conglomerates. Most of the specialists of this team have participated in an IFRS "train the trainers" program for about two years. In the course of supervisory work, these specialists review financial statements in order to determine non-compliance with the reporting requirements that may have significant impact on capital adequacy, asset values, and loan loss provisioning of financial institutions. In regard to ensuring compliance with IFRS in the banking sector, this team provides analytical results on accounting and auditing matters to the on-site supervisors and their teams of examiners. The specialized team on accounting and auditing conducted a review of 31 sets of 2010 consolidated financial statements of banks. It is worth noting that these constitute the first set of consolidated financial statements prepared by banks under the new IFRS regime. The review mainly focused on compliance with IFRS disclosure requirements, especially for financial instruments (IFRS 7). The findings were communicated to the management and external auditors of the relevant financial institutions, with recommendations for improvements in future. The findings were also shared with IBRACON. This team has put in place an arrangement for reviewing bank financial statements on a regular basis from 2012, and to prepare analytical information based on the review findings, for supporting continuous monitoring of banks and banking conglomerates in Brazil.

47. **In addition to reviewing each bank's financial statements, the working papers of its external auditors are also reviewed by accounting and auditing specialists of the BCB's on-**

**site supervision Department**. Bank supervisors, by comparing their own findings with selected information in the audit working papers identify issues of concern regarding the audit work, and discuss these issues in a meeting with the external auditors. In addition, findings on systemic weaknesses in bank audits are discussed from time to time in meetings with the technical group on financial institutions of IBRACON. When auditing deficiencies are detected, the financial institution and/or its auditor are informed and encouraged to take the appropriate corrective actions. The Central Bank is vested with legal power to apply administrative sanctions to both the supervised institutions and to their auditors. Noncompliance with prescribed norms and regulations may subject the noncompliant entities to various penalties, [51] including warnings, fines, suspension of duties, temporary or permanent disqualification for the exercise of managerial positions, and cancellation of the authorization to operate. According to BCB regulations, the external auditor of a financial institution has a duty to provide to the BCB any information identified during the audit which results in material misstatements in financial statements. Such information should be provided within three days of its detection[52]. It may relate to the existence or evidence of fraud and/or error, breach of banking rules and laws, and a threat to the continued existence of the entity as a going concern.

48. **The Department of Supervision of Banks and Banking Conglomerates of BCB carried out research and related activities prior to first time mandatory application of IFRS in the preparation of 2010 financial statements.** These activities included; surveys on the preparedness of financial institutions for implementing IFRS; discussions with the management of financial institutions regarding the implications of various accounting policies in the context of complying with the requirements of IFRS; and meetings with the external auditors of financial institutions to discuss possible challenges of ensuring compliance with IFRS. In addition, arrangements were made for helping front-line bank examiners gain exposure to IFRS requirements.

49. **CVM is legally empowered to supervise listed companies and the activities of the professionals acting in the securities markets[53]**. It is entitled to request the financial statements and supporting documents of regulated companies and the working papers of CVM-registered independent auditors or any other information it deems necessary. In the event of noncompliance with the mandatory accounting, financial reporting, and auditing requirements set by applicable laws and regulations, CVM can demand the restatement of financial statements or impose administrative sanctions, including: warnings, fines, temporary prohibition, suspension or cancellation of registration. In the period from 2008 to 2011, CVM's Superintendency of Sanction Processes (SPS) issued a total of 52 warnings, 403 fines, 7 suspensions, 19 disqualifications, 1 prohibition, but no de-registrations.

50. **The CVM has considerably strengthened its monitoring and enforcement capacity with regard to accounting and financial reporting by the regulated entities; however, it still faces some challenges due to shortage of staff and the need to improve its management information systems.** CVM is contemplating actions to upgrade its information system controls

[51] CMN Resolution 3883/10.
[52] CMN Resolution 3198/2004
[53] Art. 8 of Law 6385/76.

in order to enhance effectiveness in protecting its financial and sensitive information. The review of financial statements of listed companies is carried out by the division of corporate monitoring under the Superintendency of Corporate Relations (*Superintendência de Relações com Empresas)*. This division has 6 staff, all of whom have an accounting education and training background. In 2010 and 2011, CVM reported a considerable deterioration in compliance with financial reporting requirements by listed companies , generating an increase in the number of alert messages sent by CVM to listed companies and in the amount of fines imposed by CVM. This was expected due to the first time adoption of all Brazilian accounting standards converged with IFRS. The CVM needs to further enhance its enforcement capacity to address more complex issues arising from implementation of fair value accounting principles and other highly sophisticated accounting treatments in financial reporting.

51. **In spite of the lack of adequate resources, CVM has introduced an audit quality review program.** The supervision of CVM-registered independent auditors is executed by the division of auditing standards under the Superintendency of Accounting and Auditing Standards. This division has 10 staff of varied backgrounds. The focus of CVM's efforts is twofold. First, it monitors the activities of independent auditors including: their compliance with certification (education and experience), continuing education and independence requirements; conformity of the auditing procedures applied; and adequacy of auditors' opinions with reference to the CFC and CVM rules. Secondly, it oversees the implementation of CFC's peer review program for independent auditors. Although the CVM's current staff are adequately qualified and experienced, their number does not appear to be sufficient to endow the CVM with sufficient monitoring and enforcement capabilities in regard to the application of auditing and quality control standards by the practicing auditors and audit firms. The recruitment of additional staff with appropriate qualifications and experience would enhance the capacity of the CVM in this regard.

52. **SUSEP needs to build its supervision and enforcement capabilities with respect to financial reporting in order to effectively address the challenges associated with the expansion of insurance and open funds markets**[54]. The Solvency Monitoring General Coordination Unit (CGSOA) within the Technical Directorate of SUSEP, is responsible for monitoring the assets, liabilities and net worth, and the risks relating to insurance operations. It is also responsible for adapting SUSEP's norms to international standards to ensure solvency of the supervised entities and transparency of operations. Although SUSEP has put in place arrangements for proactively detecting problems and deficiencies of the regulated entities, its capabilities with regard to monitoring and enforcing financial reporting requirements appear to be very limited. Its supervisors undertake efforts to determine infractions in financial statements in the course of regular supervision activities. In recent years, SUSEP's supervision staff have faced serious challenges arising from the increase in complexity of financial reporting as a result of the adoption of IFRS.

53. **PREVIC's inadequate capacity constrains its ability to monitor and enforce financial reporting requirements.** As part of its supervisory activities, the on-site and off-site supervisors of PREVIC analyze information contained in the financial statements of closed pension funds. In

[54] From 2008 to 2011, insurance and open pension funds markets' revenues grew by 77.5%, corresponding to a share of 3.2% of GDP in 2011 compared to 2.8% in 2007 (source: SUSEP's management report for 2011).

2010, PREVIC established new indicators with the objective of monitoring, on a systematic basis, the financial statements of closed pension funds, looking for potential inconsistencies and solvency issues with the funds and benefit plans. However, it does not proactively carry out reviews aimed at establishing the degree of compliance with applicable accounting standards.

54. **Financial reporting by large-sized non-listed corporate entities is not covered by any monitoring and enforcement regime.** Irrespective of the legal form, all large-sized corporate entities are under legal obligation to follow the same accounting and auditing requirements as in the case of listed companies. However, there is no regulatory body to ensure that these entities comply with the applicable accounting and auditing requirements. Since these entities do not publish their financial statements, there is no mechanism for imposing market discipline on the non-compliant large-sized corporate entities. It is worth noting that regulatory bodies enforcing the financial reporting obligations of closely-held companies are an uncommon feature of modern corporate financial reporting frameworks. Nonetheless, in addition to requirements for publication financial statements, effective audit practices are essential to ensure a high quality of financial reporting for large sized non-listed entities.

# III. ACCOUNTING STANDARDS AS DESIGNED AND AS PRACTICED

55. **Brazil has taken two distinct but related paths to the adoption of IFRS for financial reporting by the corporate entities**. First, the CVM and the BCB decided that IFRS should be used for preparing consolidated financial statements of listed companies and the financial institutions that fall under their regulatory ambit, from 2010 onwards, with early adoption being permitted. A similar decision was taken by SUSEP, requiring insurance companies to follow IFRS for consolidated financial reporting from 2010 onwards. Secondly, the new 2007 Corporations Law 11638 requires all Brazilian companies to prepare their financial statements in accordance with the new Brazilian GAAP (known as CPCs) which are closely based on IFRS. In fact, each CPC is generally a translation of the corresponding IFRS. This means that all listed and non-listed companies in Brazil are currently required to use local standards which are almost fully converged with IFRS. Brazil's commitment to IFRS is demonstrated through increased collaboration with the International Accounting Standards Board. On January 28, 2010, CFC and CPC signed a Memorandum of Understanding (MOU) with the IASB establishing principles for future cooperation aimed at supporting adoption of IFRS in Brazil and fostering the engagement of the Brazilian accounting standard-setter in the international accounting standard setting process. The CFC and CPC, in their MOU with IASB, made a commitment to eliminate all the differences between Brazilian GAAP and IFRS.

**IFRS For Consolidated Financial Reporting In Brazil**

**Banks**
In March 2006, the Central Bank of Brazil decided that any bank required by law or regulation to publish financial statements in Brazil (including domestic owned and foreign owned, listed and unlisted) will have to prepare and publish consolidated financial statements in full compliance with the IFRS requirements starting with year ending 31 December 2010. The BCB paved the way for full IFRS application for consolidated financial reporting in Brazil.

**Listed Companies**
In July 2007, the CVM required listed companies to prepare and publish their consolidated financial statements in accordance with the requirements of IFRS, starting with reporting periods ending in 2010. Application of IFRSs was optional for listed companies from 2007 through 2009.

**Insurance Companies**
In December 2007, the SUSEP decided that all the entities falling under the ambit of its supervision should prepare consolidated financial statements in compliance with the IFRS requirements starting with the year ending 31 December 2010.

56. As part of the convergence process, CPC adopted a Portuguese version of the IFRS for SMEs. By Resolution 1255 of 2009, the CPC for SMEs was endorsed by the CFC. However, application of these standards by SMEs is optional: a company that meets the SME criteria may opt to conform to the full IFRS rather than the CPC for SMEs. Micro and small-sized entities have an additional option to adopt the simplified version of the CPC for SMEs, the *Resolução* CFC 1418 of 2012 (also known as ITG 1000).

**Table 4– Summary of Applicable Accounting Standards by Type of Entity**

| Type of Entity | | Accounting Standards |
|---|---|---|
| Listed companies | | • Consolidated financial statements: IFRS[1]<br>• Individual company (legal entity) financial statements: CPCs[2] |
| Financial institutions | | • Consolidated financial statements: IFRS[3]and COSIF<br>• Individual financial institution (legal entity) financial statements: COSIF |
| Insurance companies and open pension funds | | • Consolidated financial statements: IFRS[4]<br>• Individual company (legal entity) financial statements: CPCs[2] |
| Closed pension funds | | • CNCP/PREVIC standards, converging with international standards[5] |
| Non-listed companies | Large-size | • Consolidated financial statements: IFRS[1]<br>• Individual company (legal entity) financial statements: CPCs[2] |
| | SME | • CPC for SMEs[6] (optional, the alternative is Full IFRS) |
| | Micro and small | • ITG 1000[7] (optional, alternatives are Full IFRS or the CPC for SMEs) |

Notes

[1]CVM Instruction 457/07 amended by CVM Instruction 485/10.

[2] CFC establishes in Resolution 1328/11 that the Brazilian accounting pronouncements converge to the international principles
and hence must follow similar preparation and format standards.

[3] CMN Resolution 3786/09.

[4] SUSEP Circulars 357/07 and 408/10.

[5] CFC Resolution 1334/11 and CNPC Resolution 8/11.

[6] CFC Resolution 1255/09 and CFC Resolution 1285/10.

[7] CFC Resolution 1418/12.

57. **Due to legal restrictions, a few gaps exist between the requirements of IFRS and CPCs as endorsed by the regulatory bodies**. The main difference between IFRS and CPCs arises from the fact that Brazilian law (11.638/07) requires that investments in associates should be accounted for in accordance with the equity method only. Other differences are with respect to Consolidated and individual company financial statements, where Brazilian law (11.638/07) does not allow the revaluation model for Property, Plant and Equipment (IAS 16, par. 31-42) or Intangible Assets (IAS 38, par.75-87), and the Income Statement and Statement of Other Comprehensive Income need to be presented separately (IAS 1, par. 81).

58. **Some compliance gaps exist in the published financial statements of corporate entities**. Interviews were conducted with a cross section of practicing auditors, corporate accountants, academics, investment analysts and regulators, and a review was undertaken of available research publications. From these, information on various instances of non-compliance with IFRS requirements was collected and corroborated with findings from a desk review of 15

sets of published financial statements[55] (2011) by the ROSC Team. The following are the instances of non-compliance identified in this exercise.

- *Boilerplate Disclosures*—In most cases, financial statement disclosures are found to be highly generic—not specific to the entity—in description, and include reproduction of sentences/paragraphs from the accounting standards, rather than a discussion regarding application of the requirements of relevant standards in the context of the entity's financial statement items.
- *Disclosures about share capital (IAS 1*.79)—Many companies did not present a reconciliation of the number of shares outstanding at the beginning and at the end of the period, for each class of share capital.
- *Investment Property (IAS 40)*—Some companies that presented investment properties in their balance sheets, did not disclose whether they applied the fair value model or the cost model; a number of other companies that presented investment properties in accordance with the cost model, did not disclose the respective fair value in the notes.
- *Agriculture (IAS 41)*—Many companies that presented biological assets on their balance sheets, failed to disclose some key information required by the standard.
- *Impairment of Assets (IAS 36)*—Many companies that disclosed that impairment tests of assets were performed, did not present one or more of the following information: whether the recoverable amount is assets' fair value less costs to sell or its value in use; if fair value less costs to sell, the basis used to determine fair value less costs to sell; if value in use, the discount rate used in the current estimate and previous estimate of value in use.
- *Inventories (IAS 2)*—A large number of companies did not disclose the carrying amount of inventories pledged as security for liability; also these companies did not disclose any information regarding the fact that none of the inventories were pledged as security for liability.
- *Property, Plant and Equipment (IAS 16)*—A large number of companies did not disclose items of property, plant and equipment pledged as security for liability; also these companies did not disclose any information regarding the fact that none of the items were pledged as security for liability.
- *Effects of Changes in Foreign Exchange Rate (IAS 21)*—Most of the companies that had foreign currency transactions, did not disclose judgment used to determine the functional currency.
- *Borrowing Costs (IAS 23)*—It was found to be a common practice to not disclose borrowing costs capitalized, and the capitalization rate.
- *Related Party Disclosures (IAS 24)*—Most of the companies did not disclose the relationships between parent and subsidiaries irrespective of whether there have been transactions between those related parties.
- *Provisions, Contingent Liabilities and Contingent Assets (IAS 37)*—Many companies did not comply with some of the key disclosure requirements of this standard. Moreover, one company that was found to have potential liabilities from a court case did not recognize any contingent liability in the financial statements.

[55] The sample was designed to select at least one set of financial statements audited by each of the audit firms that audit listed companies in Brazil.

- *Operating Segments (IFRS 8)*—Many companies did not comply with the requirements of disclosing segment information about assets and liabilities.

59. **BCB supervision teams conducted a review in 31 financial institutions of their IFRS-based Financial Statements for the year ended 31 December 2010, and the disclosure deficiencies identified are summarized below.** It is worth noting that 2010 was the first year of mandatory application of IFRS and for that reason a high level of non-compliance with disclosure requirements was expected by the BCB. Furthermore, the BCB supervision teams have found improvements in disclosure practices of the financial statements in 2011.

- *Financial Instruments: Disclosures (IFRS 7)*—various disclosure deficiencies were found in the financial statements of a number of financial institutions. These are:
  - Financial assets and financial liabilities not classified into the four categories defined in paragraph 9 of IAS 39.
  - No disclosure of items of income, expense, gains or losses into the four categories defined in IAS 39.
  - Lack of disclosures by class of financial assets and financial liabilities: impairment, fair value.
  - No description of methods and assumptions applied in determining fair values of financial assets and financial liabilities.
  - Regarding risk disclosure, the following disclosure deficiencies were found:

    **Credit risk disclosure deficiency**

    - Maximum exposure
    - Description of collateral held as security and other credit enhancements
    - Carrying amount of financial assets that would otherwise be past due or impaired whose terms have been renegotiated
    - Financial assets that are past due at the end of the reporting period but not impaired
    - Analysis of financial assets that are individually determined to be impaired
    - Estimate of the fair value of collateral held as security for past due or impaired financial assets
    - Financial assets that were transferred but do not qualify for derecognition: nature and carrying amount of the assets; nature of the risks and rewards of ownership

    **Liquidity risk disclosure deficiency**

    - Maturity analysis for financial liabilities

    **Market risk disclosure deficiency**

    - Sensitivity analysis for each type of market risk to which the entity is exposed

- *Disclosure deficiencies with reference to the requirements of various other standards.*
  - Low level of disclosure:
    - transactions with related parties
    - share-based payment transactions
  - Disclosure of interests in other entities:
    - lack of information relating to contingent liabilities of associates
    - use of inaccurate terms to define interests in entities of the same group

- Lack of detailed disclosure of assets presented as “Other assets” in the financial statements
- No disclosure of gain or loss recognized for discontinued operations
- Subsidiary not included in consolidated financial statements
- Transaction costs not included in the calculation of the effective interest rate
- Inaccurate fair value measurement
- Offsetting of court deposits and provisions
- Derecognition of goodwill without impairment test
- Assets that do not match the requirements of IFRS 5 classified as “non-current assets held for sale”

## IV. AUDITING STANDARDS AS DESIGNED AND AS PRACTICED

60. **CFC and IBRACON combined efforts in late 2009 to issue the new Brazilian Standards on Auditing, effective from 2010 onwards.** The CFC, through its Resolution 1201/09, has issued 38 new auditing standards. It is worth noting that the new auditing standards are essentially a translation of the international standards on auditing (ISAs) and on quality control (ISQC1). These standards are applicable with effect from January 1, 2010. However, for the audit of non-regulated small and medium-sized entities, CFC Resolution 1325/11 delayed mandatory application of the new auditing standards to January 1, 2012, mainly due to difficulties associated with the implementation of these new standards in the context of these entities. Standards for review and assurance engagements, related services, internal audits, and standards applicable to the work of specialists have also been issued by CFC. These standards are in convergence with internationally accepted standards. Training and related activities to support implementation of the new auditing standards are underway. However, these efforts need to be intensified in order to ensure proper application of the relevant auditing and quality control standards.

61. **Practicing auditors, except those belonging to the large international networks of firms, have faced challenges in implementing the new auditing standards**. The ROSC team interviewed regulators, practicing auditors, academics, and development bankers in the course of conducting a due diligence exercise for assessing the quality of auditing services provided by audit firms in the country. This exercise revealed some deficiencies that contribute to weak audits in many cases. These are summarized below:

- There is a tendency to give less emphasis to proper audit planning.
- There is a lack of adequate documentation to demonstrate that the auditor has performed procedures to obtain necessary audit evidence. In many cases, the auditors fail to gather sufficient audit evidence to support key audit judgments, including audit opinions.
- Many audit practitioners are not able to demonstrate appropriate levels of professional skepticism.
- Due to insufficient knowledge of the practical aspects of IFRS, many auditors find it difficult to properly judge appropriateness of the approach taken in applying some complicated financial reporting standards.
- In some cases, it appeared that the unqualified audit opinion was not properly justified by the audit work conducted, that information in the financial statements was contradicted by available evidence, and/or that conclusions were drawn on the basis of management representation without independent verification.
- Some audit firms determine the going concern basis to be appropriate without considering relevant events that might have occurred after the end of the reporting period but before the issuance of the audit reports.
- The International standard on audit quality control (ISQC-1) is yet to be fully implemented in most of the small and medium-sized audit practices.

## V. PERCEPTION OF THE QUALITY OF FINANCIAL REPORTING

62. **In general terms, the key stakeholders in corporate financial reporting appear to be relatively satisfied with the quality of financial statements prepared and presented by the listed companies**. Moreover, there is a general perception in the market that the financial statements that are audited by the members of international accounting firm networks provide relatively more reliable information than the others. Interviews with representatives of financial sector regulators, financial institutions, financial analysts, and other stakeholders revealed a consensus that the quality of audited financial statements of listed companies has significantly improved over the past five years; mainly due to the improvements in various institutional underpinnings of accounting and auditing practices in Brazil.

63. **There is a widespread belief that the Brazilian-based companies which are simultaneously traded on the Brazilian and the US stock markets prepare higher quality financial statements than other listed companies in the country.** This perception is backed by some empirical evidence produced in a 2009 Standard & Poor's (S&P) survey on disclosure practices of companies on the BM&F Bovespa Exchange.[56] The S&P survey of the transparency and disclosure (T&D) of Brazilian listed companies used a Transparency Index, calculated as the average score for the 56 companies which formed the basis for the Bovespa index as of August 31, 2009. It was found that the companies with a dual listing, i.e. on both the New York Stock Exchange (NYSE) and the Sao Paulo Stock Exchange (BM&F Bovespa) scored better transparency levels (72.4%) than those companies only listed on the BM&F Bovespa (59.8%). The analysis took into account financial statements, notes to the financial statements, web-based disclosure and public regulatory reporting.

64. **In the case of non-listed corporate borrowers, the bankers tend not to place high reliance on financial statements of the potential borrowers in determining whether to extend credit.** Although corporate borrowers are required to submit their financial statements as part of the loan application process, lending decisions to small and medium-sized enterprises are generally based on other factors, including the amount of collateral, management integrity, business forecasts, and site visits. This is mainly because there is a perception in the country that audited financial statements of most of the SMEs are rarely reliable and free from material misstatement.

65. **Investors express concerns about the quality of financial statements of the mid-size financial institutions**. In June 2012, after the Central Bank seized *Banco Cruzeiro do Sul SA*, the sixth intervention in two years, a London-based institutional investor commented, "At this point we cannot rely on the financial statements of the mid-size banks in Brazil."[57] During the past two years, a few other mid-size financial institutions were bailed out or liquidated. The audited

[56] "Disclosure Practices of the Companies Composing the Bovespa Index in Brazil—Reaping the Benefits of Exchange-Based Regulation," prepared by Standard & Poor's, November 16, 2009.
[57] Bloomberg breaking news, "Brazil's Cruzeiro Seizure Drives Investors to Big Banks," June 12, 2012.

financial statements of these troubled financial institutions, in the years immediately prior to the surfacing of financial trouble, did not provide any indication of "going concern" problems.

# VI. POLICY RECOMMENDATIONS

66. The policy recommendations outlined in this section emerge from the review of accounting and auditing practices in Brazil, as well as the valuable inputs received from the various stakeholders. A holistic approach is adopted to design the policy recommendations in order to strengthen the corporate financial reporting and auditing practices in Brazil. These primarily principles-based recommendations are expected to provide inputs in preparing a detailed Country Action Plan for Brazil geared toward a sustainable high-quality corporate financial regime. The recommendations are aimed at the country authorities and key stakeholders of accounting and auditing. The policy recommendations are focused on responding to the following overall findings:

- In the recent past, CFC has demonstrated significant improvements, but further strengthening of CFC capacity is necessary to enable them to fully comply with all the statements of membership obligations of IFAC.
- Although the BCB and the CVM have separately put in place arrangements for monitoring compliance with auditing requirements in respective regulated entities, efficiency and effectiveness of audit quality monitoring and enforcement may be further enhanced through establishment and operation of a comprehensive regulatory mechanism through joint collaboration of various regulatory bodies in the country;
- There is an urgent need for significantly strengthening accounting curriculum and teaching in higher educational institutions, mostly outside the metropolitan cities of Brazil; and
- The legal framework of accounting and auditing needs to be further improved in line with international good practices.

With these findings in mind, the ROSC recommends the following:

67. **Further strengthen the technical capability of CFC to support development of a strong accountancy profession with attendant effect on enhancing the quality of financial reporting in the country.** When a professional accountancy organization functions properly and fulfills its role in the economy, it holds the power to support the production of high-quality financial information. Given its responsibilities outlined above and the challenges it faces in fulfilling them, the CFC needs to strengthen its capacity. In addition to strengthening the secretariat, the CFC needs to bolster its technical capabilities. In addition, CFC is recommended to put in place arrangements for supporting a strong accountancy profession, and fully comply with all the statements of membership obligations of IFAC. In this context, the CFC should:

- continue to build the skills and enhance technical knowledge of the staff and committee members of CFC to enable them to keep abreast of modern developments in the profession;
- make arrangements (amendment of law, if needed) for complying with all the requirements of International Education Standards;

- put in place necessary arrangements for introduction of monitored practical training as a pre-condition of CFC membership;
- assist members all over the country to have access to high quality continuing professional development (CPD) activities;
- provide value added services for professional development of its members.

68. **The following issues need to be considered by CFC for strengthening its capacity in line with international good practices.**

- It should support those who aspire to membership (its students) through:
  - A rigorous and future-oriented program of professional learning and development
  - Comprehensive and credible assessment procedures that serve to demonstrate the competencies required of a professional accountant
  - A range of services and resources to prepare students for membership

- It should support its members through:
  - Ongoing access to relevant continuing professional development or education, including additional qualifications to enhance members' competitive advantage
  - Identifying and providing access to relevant professional support services, including professional indemnity insurance, IT support, etc
  - Maintaining and supporting networks of active members, as a basis for sharing information, problems and ideas
  - Provision of technical guidance and advice in support of member roles – whether in professional practice, business or the public services
  - Access to up-to-date accounting information resources e.g. professional library and associated databases
  - Access to relevant career planning and development resources, including advice, information, events, etc

69. **On a pilot basis, introduce a voluntary Certified Professional Accountant (CPA) qualification program in line with international good practices.** This program should not be mandatory for becoming a registered accountant under CFC, since such registration is governed by the law in Brazil. Instead, it should run side by side with the existing arrangements for proficiency examinations. The new pilot program may be organized through the collaboration of various relevant institutions—professional accountancy organizations, financial regulators, leading higher education institutions, and users of financial information—under the umbrella of a foundation. The requirements for obtaining the new qualification should be set in full compliance with the requirements of International Education Standards issued by the IAESB of IFAC. In addition, arrangements may be made to design and implement the program with the support of a strong professional accountancy organization, so that the new qualification receives international recognition from the beginning.

70. **As part of efforts to strengthen independent audit oversight, establish a strong "Audit Quality Review Board (AQRB)" under the auspices of CVM.** Such arrangements that are independent of the accounting profession are now recognized internationally as a key feature of modern audit oversight frameworks that are necessary to maintain public confidence. The current mandate of the CVM includes maintaining a list of approved auditors, and conducting reviews of the quality of the audits of entities regulated by CVM. However, due to resource constraints, CVM faces significant challenges in carrying out this quality review work. Banks and insurance companies in the country are required by their respective regulators to use CVM's list of approved auditors when considering the appointment of external auditors. Under such circumstances, it seems that effective functioning of an AQRB under the auspices of CVM would be enhanced through a collaboration arrangement with various regulatory agencies—e.g. BCB, SUSEP, PREVIC, etc. International experience suggests that independent regulatory bodies such as the proposed AQRB, once endowed with sufficient authority and resources, are effective in enhancing audit quality monitoring and enforcement. It would thus help to overcome the challenges faced by various regulators in the country. The main mission of the AQRB would be to oversee the auditors of public interest entities in order to protect the interests of investors and the public through ensuring that audit reports are informative, fair, and prepared in an independent manner. The audit firms registered with the Board would be permitted to be engaged as auditors of public interest entities. The establishment of the Board and its effective supervision and oversight of registered audit firms would promote investor confidence in audited financial statements of public interest entities, and contribute to enhancing financial stability in the economy. It would be necessary to put in place a strong secretariat with an adequate number of technical staff and audit inspectors at the AQRB.

71. **Once the AQRB's operations are effective, efforts should be made to enact an enabling law for putting in place a permanent independent oversight structure for monitoring and enforcing accounting, auditing and financial reporting requirements.** In this regard, a number of models for establishing legally backed oversight arrangements in other jurisdictions can be studied for relevant lessons and examples.[58] In this regard, a brief overview of Australian system is presented below.

**Australian Securities & Investments Commission (ASIC)**
**Audit inspection and surveillance programs**

The audit inspection program of ASIC commenced after the passing of the *Corporate Law Economic Reform Program (Audit Reform and Corporate Disclosure) Act 2004.* ASIC has responsibility for the surveillance, investigation and enforcement of the financial reporting and auditing requirements of the Corporations Act.

ASIC's audit inspection program reviews compliance with audit quality and auditor independence requirements. Registered company auditors and firms are required to comply with the Corporations Act and follow all auditing standards and other requirements that are relevant to each engagement. This helps to ensure that users of financial information can have greater confidence in financial statements. A strong audit profession helps maintain and promote confidence and integrity in the capital markets.

The inspection focuses on audit quality and promoting compliance with the requirements of the Corporations Act, Auditing Standards and Professional and Ethical Standards. Auditor surveillances generally arise through complaints from the public to ASIC or through media reports and intelligence from other areas of ASIC.

Audit firms to be inspected are selected based on a number of criteria, with an emphasis on firms auditing publicly listed or public interest entities. The inspection program captures all audit firms including small and medium-size practices (SMPs).

With auditing moving beyond national borders, there is a need for effective global auditor oversight. ASIC has sought to minimize the regulatory burden on Australian audit firms by seeking arrangements with other international audit oversight bodies, with the intention of conducting work either jointly with them or on their behalf.

[58] For example: Audit inspection and surveillance programs of the Australian Securities & Investments Commission; the Public Company Accounting Oversight Body in the United States; and the Financial Reporting Council in the United Kingdom.

72. **Strengthen accounting curriculum and teaching in higher educational institutions**.

- Deepen the existing strong collaboration arrangement between the Ministry of Education, the accountancy profession, and academia to ensure compatibility of academic curriculum and teaching with international good practices.
- The CFC may consider introduction of an "accreditation program," in collaboration with other interested parties, for universities/colleges that offer bachelor's degree in accounting.
- Put in place arrangements for designing, developing and implementing a "train the trainers" program, focusing on practical aspects of IFRS, IPSAS and ISA for accounting academics in higher educational institutions throughout the country – give preference to the academics outside major metropolitan centers. It is worth noting that training is the main challenge relating to implementation of international standards, because the adoption of principles-based standards requires a change of mindset and approach. For example, the previous Brazilian accounting system was mainly rules based, while the IFRS requirements are based on principles and are less detailed. As a result, compliance with IFRS requirements generally requires a higher level of professional judgment. Emphasis is given to the "substance" of transactions rather than simply the legal "form."
- CFC and IBRACON should develop a collaboration arrangement with higher educational institutions in order to further assist students and teachers to have access to the latest learning materials on practical aspects of IFRS, IPSAS and ISA.

73. **Take steps for further updating the regulatory framework of accounting and auditing**.

- Amend Corporations Law to:
  - Remove detailed accounting and financial reporting provisions
  - Clearly mandate publication of audited financial statements by large-size *Limitadas*—publication means making financial statements publicly available through a website and/or other electronic media.
- Continue to promote the full adoption of CPCs by regulatory bodies;
- Take steps for supporting various forward looking initiatives for enhanced corporate reporting; for example an "integrated corporate reporting" initiative.
- Take steps for ensuring tax neutrality of corporate financial reporting—arrangements should continue to ensure that tax rules do not have impact on the general purpose financial statements, and work of the accountants.

## Appendix A:
## CPC Technical Pronouncements and their adoption by the relevant Regulators

| Technical Pronouncement | | EQUIVALENT STANDARD/REQUIREMENT | | | | |
|---|---|---|---|---|---|---|
| | | Equivalent IFRS | CFC Adoption | CVM Adoption | BCB Adoption | SUSEP Adoption |
| CPC 00 | Conceptual Structure for the Preparation and Presentation of Financial Statements (12/02/11) | *Framework* | ✓ | ✓ | | ✓ |
| CPC 01 | Impairment of Assets (08/06/10) | IAS 36 | ✓ | ✓ | ✓ | ✓ |
| CPC 02 | The Effects of Changes in Foreign Exchange Rates and Conversion of Financial Statements (09/03/10) | IAS 21 | ✓ | ✓ | | ✓ |
| CPC 03 | Statement of Cash Flows (09/03/10) | IAS 7 | ✓ | ✓ | ✓ | ✓ |
| CPC 04 | Intangible Assets (11/05/10) | IAS 38 | ✓ | ✓ | | ✓ |
| CPC 05 | Related Party Disclosures (09/03/10) | IAS 24 | ✓ | ✓ | ✓ | ✓ |
| CPC 06 | Leases (11/05/10) | IAS 17 | ✓ | ✓ | | ✓ |
| CPC 07 | Accounting for Government Grants and Disclosure of Government Assistance (11/05/10) | IAS 20 | ✓ | ✓ | | ✓ |
| CPC 08 | Transaction Costs and Premiums in the Issuance of Securities (12/03/10) | IAS 39 (partial) | ✓ | ✓ | | ✓ |
| CPC 09 | Statement of Value Added (10/30/08) | - | ✓ | ✓ | | |
| CPC 10 | Share-based Payment (12/03/10) | IFRS 2 | ✓ | ✓ | ✓ | ✓ |
| CPC 11 | Insurance Contracts (12/05/08) | IFRS 4 | ✓ | ✓ | | ✓ |
| CPC 12 | Present Value Adjustment (12/05/08) | - | ✓ | ✓ | | ✓ |
| CPC 13 | Initial Adoption of Law 11638/07 and Provisional Measure 449/08 (12/05/08) | - | ✓ | ✓ | | ✓ |
| CPC 14 | Financial Instruments: Recognition, Measurement, and Disclosure | Replaced by subsequently issued CPCs | | | | |
| CPC 15 | Business Combinations (06/03/11) | IFRS 3 | ✓ | ✓ | | ✓ |
| CPC 16 | Inventories (05/08/09) | IAS 2 | ✓ | ✓ | | ✓ |
| CPC 17 | Construction Contracts (05/08/09) | IAS 11 | ✓ | ✓ | | ✓ |
| CPC 18 | Investments in Associates and Joint Ventures (11/06/09) | IAS 28 | ✓ | ✓ | | ✓ |
| CPC 19 | Interests in Joint Ventures (06/03/11) | IAS 31 | ✓ | ✓ | | ✓ |
| CPC 20 | Borrowing Costs (09/02/11) | IAS 23 | ✓ | ✓ | | ✓ |

| | | | | | | |
|---|---|---|---|---|---|---|
| CPC 21 | Interim Financial Reporting (09/02/11) | IAS 34 | ✓ | ✓ | | ✓ |
| CPC 22 | Operating Segments (06/26/09) | IFRS 8 | ✓ | ✓ | | ✓ |
| CPC 23 | Accounting Policies, Changes in Accounting. Estimates and Errors (06/26/09) | IAS 8 | ✓ | ✓ | ✓ | ✓ |
| CPC 24 | Events After the Reporting Period (07/17/09) | IAS 10 | ✓ | ✓ | ✓ | ✓ |
| CPC 25 | Provisions, Contingent Liabilities and Contingent Assets (06/26/09) | IAS 37 | ✓ | ✓ | ✓ | ✓ |
| CPC 26 | Presentation of Financial Statements (12/02/11) | IAS 1 | ✓ | ✓ | | ✓ |
| CPC 27 | Property, Plant and Equipment (06/26/09) | IAS 16 | ✓ | ✓ | | ✓ |
| CPC 28 | Investment Property (06/26/09) | IAS 40 | ✓ | ✓ | | ✓ |
| CPC 29 | Biological Assets and Agricultural Produce (08/07/09) | IAS 41 | ✓ | ✓ | | ✓ |
| CPC 30 | Revenue (08/07/09) | IAS 18 | ✓ | ✓ | | ✓ |
| CPC 31 | Non-current Assets Held for Sale and Discontinued Operations 07/17/09) | IFRS 5 | ✓ | ✓ | | ✓ |
| CPC 32 | Income Taxes (07/17/09) | IAS 12 | ✓ | ✓ | | ✓ |
| CPC 33 | Employee Benefits (09/04/09) | IAS 19 | ✓ | ✓ | | ✓ |
| CPC 34 | Exploration for and Evaluation of Mineral Assets | IFRS 6 | Adoption is postponed until completion of IFRS 6 revision | | | |
| CPC 35 | Separate Financial Statements (06/03/11) | - | ✓ | ✓ | | ✓ |
| CPC 36 | Consolidated Financial Statements (06/03/11) | IAS 27 | ✓ | ✓ | | ✓ |
| CPC 37 | First-time Adoption of International Financial Reporting Standards (11/05/10) | IFRS 1 | ✓ | ✓ | | ✓ |
| CPC 38 | Financial Instruments: Recognition and Measurement (10/02/09) | IAS 39 | ✓ | ✓ | | ✓ |
| CPC 39 | Financial Instruments: Presentation (10/02/09) | IAS 32 | ✓ | ✓ | | ✓ |
| CPC 40 | Financial Instruments: Disclosures (10/02/09) | IFRS 7 | ✓ | ✓ | | ✓ |
| CPC 41 | Earnings per Share (07/08/10) | IAS 33 | ✓ | ✓ | | ✓ |
| CPC 42 | Financial Reporting in Hyperinflationary Economies | IAS 29 | Adoption is postponed until completion of IAS 29 revision | | | |
| CPC 43 | First-time Adoption of Technical Pronouncements CPC 15 to CPC 41 (12/03/10) | IFRS 1 | ✓ | ✓ | | ✓ |
| CPC 45 | Disclosure of Interests in Other Entities | IFRS 12 | | ✓ | | |
| CPC 46 | Fair Value Measurement | IFRS 13 | | ✓ | | |
| CPC PME | Accounting for Small and Medium-sized Enterprises with Glossary (12/04/09) | IFRS for SMEs | ✓ | | | |

## Appendix B:
## Status of implementation of the recommendations of the 2005 ROSC

The table below summarizes the status of the implementation of the main policy recommendations of the 2005 ROSC A&A.

| Status of 2005 ROSC Accounting & Auditing Policy Recommendations | | |
|---|---|---|
| | Main Policy Recommendations | Status |
| 1 | Corporations Law should not include provisions on accounting standards; annual audited financial statements should be published by all *Sociedade por Ações* (S/A) and public-interest *Limitada.* | Partially implemented: some provisions on accounting standards are still in the law; and there is lack of clarity about the mandatory requirement on publication of the audited financial statements of large-sized *limitadas*, which has led to controversies. *Reference:Paragraphs 13 and 16* |
| 2 | Mandate the use of IFRS for consolidated financial statements of all public-interest entities. | Fully implemented: amended Corporations Law, CVM Instructions, and National Monetary Council Resolution provide legal backing for mandatory application of IFRS for consolidated financial reporting. *Reference: Paragraph 15* |
| 3 | Establish an independent accounting standard setter. | Fully implemented: amended CFC law provides legal backing for accounting standard setter—CPC. *Reference: Paragraph 40* |
| 4 | Adopt ISA and IFAC's Code of Ethics for Professional Accountants | Partially implemented: ISA--fully implemented; clarified ISAs were translated by IBRACON and endorsed by CFC. IFAC's Code of Ethics for Professional Accountants--translated but partially implemented. *Reference: Paragraphs 26 and 60* |
| 5 | Regulators and SRF should reach an agreement to ensure that tax rules do not interfere with preparing general purpose financial statements. | Temporarily fully implemented**:** The Transitional Tax Regime (*Regime Tributário de Transição* – RTT) was established by federal Law 11.941, from May 2009. Whereas general purpose financial statements would be prepared using new accounting standards, tax liabilities would continue to be calculated as previously done, ensuring the tax neutrality of these accounting standards. Although it appears that the RTT regime will continue in the foreseeable future, there is a need to put in place a permanent arrangement in this regard. *Reference: Paragraph 43* |
| 6 | A public oversight body should be established for the auditing profession to ensure that licensed auditors comply with their professional obligations. | Not implemented**:** An independent oversight body has not been established. However, the CVM with its limited resources carries out reviews of listed-company auditors following a risk-based approach. Also, BCB supervision department reviews audit files, following a risk-based approach, as a part of their regular inspection work. *Reference: Paragraph 70* |

| | | |
|---|---|---|
| 7 | Efforts should be made by universities, in cooperation with the accounting profession and the business community, to improve the quality of accounting curricula. | Partially implemented**:** Accounting curricula is being improved under a slow process—however, much more need to be done.<br>*Reference: Paragraph 32* |
| 8 | Strengthen existing professional examination to make the licensing process more selective. | Partially implemented**:** Although the CFC law amendment in 2010 provided legal backing for professional examination, there is a perception that introduction of practical training requirements in line with international good practices in this context, requires further amendment of the law. According to International Education Standard No.5, monitored practical training is an integral part of the learning process that IFAC member bodies should require their members to complete prior to qualifying as a professional accountant.<br>*Reference: Paragraphs 33 and 34* |
| 9 | Introduce mechanisms for monitoring compliance with continuing professional education and ensuring that the content of training is adequate. | Partially implemented: The CFC requires only the practicing auditors to comply with CPD requirements. However, according to International Education Standard No.7, all members of IFAC member bodies (practicing and non-practicing members) should comply with the continuing professional development requirements.<br>*Reference: Paragraph 38* |
| 10 | Increase financial regulatory agencies' enforcement capacity with respect to financial reporting, including by reassigning existing staff from current standard-setting function. | Substantially implemented: Since 2005, BCB and CVM have significantly improved their enforcement capacity with respect to financial reporting by the regulated entities. Both the regulators have put in place arrangements for increasing IFRS-trained human resources in monitoring and enforcement activities. The SUSEP and PREVIC need to strengthen capacity in this regard.<br>*Reference: Paragraphs 46 and 50* |