NEW REQUIREMENTS FOR INCREASING THE QUALITY OF FINANCIAL AUDIT MISSIONS

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Abstract:

The financial auditors' activity for investors, creditors, employees, shareholders regarding the financial-accounting activity and the correct financial reporting is based on the public's trust. As a result, the quality of the audit missions is very important. The control of the audit missions' quality enhances the credibility of the published financial information and contributes to the improvement of the book-keeping bringing added value to the audited entity. The quality control is the main means the auditor has to ensure the public that all the activity performed was conducted in accordance with the International Standards on Auditing, Code of Ethics, rules and decisions issued by the Chamber of Financial Auditors of Romania.

Keywords: *financial audit, quality, credibility, financial statements, control*

JEL Classification: M40, M42

1. Introduction

As a result of the important role they have in an economic entity, in the economy in general, the auditors' attitude and behaviour in providing audit services have a major impact on the welfare. Auditors can maintain this advantageous position only by continuing to provide the public professional services of a high quality. As a result, the quality control of the auditing activity is essential. The quality of the missions reinforces the credibility of the published financial reports and represents a guarantee of the reality and accuracy of the data for the shareholders, investors, creditors and other stakeholders.

The quality control contributes to improving and developing the missions carried out and at the same time they offer assurance to the audit reports consumer that the audit opinion, the procedures applied, the findings issued by the auditor, the worksheets drafted are based on the application and observance of the International Standards on Auditing.

2. The Need and the Role of Control in the Financial Audit

The audit missions are considered as qualitative when the auditor implements and complies with the international standards on auditing, including those referring to the quality control, ISQC1 and ISA 220, the requirements of the Code of Ethics, as well as the normative acts in force applied in auditing and the reports on the auditor's missions coincide with the circumstances.

The audit firms should have a quality control handbook which must be understood and respected by the auditors' team and which must include policies and procedures for the quality control (the statement on the audit firm's general policy, the general responsibilities of all partners and employees; the management's responsibility for the quality within the firm; the relevant provisions of ethics; the acceptance and continuance of the relationships with the clients; the human resources; achievement of the missions, monitoring, documentation).

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Synthesis of the quality controls elements

Analysis feature	Summary of requirements	Procedures used (examples)
Independence Integrity Objectivity	The component elements of an auditing mission must remain independent in facts and attitudes, exercise all the professional responsibilities with integrity and maintain objectivity in carrying out the professional responsibilities.	Each auditor and assistant must answer once a year an independence questionnaire addressing issues such as ownership of shares and participation in customer management as member of the Board of Directors.
Human Resources Management	Policies and procedures must be defined to provide the company a reasonable assurance in the following areas: the new employees of the company have enough qualifications to perform the duties competently; the assignment of the tasks must be done according to individual training and skills; the participation of all employees in the programme of lifelong professional training and in professional training activities to enable them to perform the responsibilities they have been assigned.	Each specialist should be assessed during each mission through an assessment report specific to the mission, prepared by the firm.
Acceptance and maintenance of missions and clients	Policies and procedures should be defined on the decision to accept a new client or to maintain the relationship with an existing client. These should minimise the risk of association with a client whose management shows a lack of integrity. The company should get involved in missions that can be performed competently and professionally.	A customer evaluation form addressing topics such as previous auditors' comments and client's management assessment must be filled out for each new client before approving the collaboration with him/her.
Enforcement of missions	There must be procedures and policies to ensure that the work carried out by the personnel involved in an audit mission complies with the professional standards applicable, with the legal provisions and with the company's quality standards.	The Company's directory must be available for consultancy and approve all the missions before concluding the contracts.
Supervision	There must be procedures and policies to ensure that the four elements of quality control mentioned above are really applied.	The person responsible for the quality control must test the control procedures at least once a year to ensure that the firm complies with them.

Source: Popa I. (eds.) - General Audit Standards, Publishing House Mirton, Timisoara, 2011

The review of the financial audit missions' quality should include checking the content and the preparation of the audit files, complying with the application of the audit procedures requested in the Handbook on the audit quality, as well as the compliance with the structure of the worksheets, achieving the audit report in accordance with the International Standards on Auditing (ISA 700, ISA 705, ISA 706) and the elaboration of the audit opinion.

The auditor's working files must provide at least the following:

- The existence of the financial statements at the auditor (balance sheet, profit and loss account, cash flow statement, equity situation, notes) of the audited entity with signature, seal and registered at the Trade Register;
- The letter of mission or the service contract made according to ISA 210;
- Making the letter of representation – according to ISA 580;
- Letter of communication of the deficiencies retained in the functioning of the accounting and internal control systems (ISA 265);

- Explaining the sampling methods used and determining the size of the sample used in checking the customers, the suppliers, etc.;
- Internal control worksheets *(review of the development and implementation of internal controls – testing by the auditor, who performs internal control activities? The decision to appoint the committee responsible for monitoring, coordinating and methodological guiding for the implementation of internal control, was the risk assessment performed? Have the internal control processes been established? Is there a programme of internal control? An internal control handbook? An action plan?);*
- internal audit worksheets *(checking the performance of the internal audit according to the law, the existence of rules and procedures of internal audit, of the internal audit charter, of the internal audit reports, worksheets, internal audit files, people carrying out internal audit missions – studies, respecting the principle of independence);*
- Availability for the audit files of the Declaration of Independence of the auditor;
- Compliance with the minimum number of hours for the audit missions (240 hours) – according to the CAFR Decision 44/2005, as well as for a mission based on an agreed procedure (95 hours) – CAFR Decision 52/2013;
- Review of the audit mission – each worksheet must be signed by the person who wrote it, and then reviewed by another auditor than the one who conducted the audit mission; the review of the documents by the person responsible for the quality control is performed both before and after expressing the opinion;
- Review of the public interest entities, taking into account the limitations set forth in Ordinance 90/2008 on statutory audit, such as: personnel rota for the audit firm performing audits for public interest entities, compliance with the independence including the provisions on the auditor's impossibility to work for the audited client for at least 2 years after completion of the audit mission;
- Documentation of the quality control through reports, worksheets, signatures of the person responsible for the quality control;
- Independence of the person in charge with the quality control within the audit firm;
- Worksheets, leasing – leasing situation, period of time, value, reviewing of leases, etc.;
- Checking how the reassessment of tangible assets was achieved: decrease, increase of value (auditor's worksheet and existence of *reassessment reports*). Are there rentals of land, buildings, and seizures on them?;
- Checking how the inventory was done and valuing the inventory results by recording in the book-keeping and reflected in the balance sheet including the ongoing production, the receivables and liabilities towards third parties, own equity, availability in domestic and foreign currency. (*documents: Decision of inventory, inventory protocol, inventory lists of property, general ledger of accounting notes made after the completion of the inventory, manager statement, trial balance, procedure for organising and conducting the inventory, inventory record*). If the auditor has not participated in the inventory – worksheet with the alternative procedures applied by the auditor;
- The list of stocks in whose inventory we participated and the sample of the stocks verified;
- Filling out questionnaires on the inventory, internal audit, internal control;
- Information and worksheets on the related parties, transactions between the parties;

- Worksheets – audit of the group's financial statements with details for the companies that have another auditor;
- Notes of the discussions with the management/CFO (preparation of the worksheets after each field visit);
- Accounting policies prepared according to the financial reporting framework;
- The assessment of the current production. The objectives of the testing should include: the proper record of the significant costs, the fair allocation of the overheads, the accurate reporting of the revenues and profits for the long-term production;
- Examination of cancellations of invoices/returns of income made after the sale or after the balance sheet date;
- documenting on the method of registration and payment of the VAT obligations, taxes and contributions to the public funds;
- checking the method of obligations registration and payment of income tax;
- checking and documenting the method of calculation and payment of the wages, salary income tax and security contributions;
- checking and documenting the adequacy of the provisions;
- documenting the audit evidence specific to the social capital taking into account: the reconciling of the equity with the provisions of the article of incorporation and the register of shareholders/partners, identifying the shares held by the management, identifying the equity issued during the financial year;
- documentation of the related parties;
- proper takeover of the opening balances;
- Checking the status of rents and rental income including whether the unearned amounts have been pursued, whether the late payments have been calculated, recorded and tracked according to the contract stipulations (*documents: contracts, invoices, account sheet*);
- Checking the method of recording the subsidies and donations (grants from the state budget, income from grants, checking the depreciation registration and calculation for modernisation works for which grants were received);
- Checking the inventories (*raw materials* under custody and the custody justification by minutes, *products available to third parties* – supporting documents and registration in accounting);
- Checking the recording method, revenue tracking and collection reflected in the "Clients" account balance – what measures have been taken, who are the clients within the group? Beyond the group? Whether penalties have been calculated and recorded in the accounts, if for the uncertain customers or in litigation, the company obtained favourable-unfavourable court rulings? Are there written procedures regarding the tracking and collection of revenue? Who is responsible according to the job description? Have these individuals fulfilled their tasks? Have permanent analyses been performed in order to collect them within the legal terms according to the OMPF no.946/2005 to avoid damage and recording adverse financial results (*documents: procedures, account statement*)
- Are there advances offered to the staff? Advances to the suppliers of materials? Were these advances followed? Have those materials been purchased? Was the reception performed? (*documents: procedures, account statement, minutes of the reception, invoices*);

- Checking the recording method of the penalties, costs and enforcement expenses from the economic agents in insolvency for which the company enrolled in the list of creditors but also from other economic agents bad payers;
- Filling out the A - V Section in the Quality Guide.

Subject to control by CAFR through inspectors, the audit firm must prove the transmission to CAFR of any addenda to the article of incorporation for updating the information according to the GEO 90/2008, the existence of the insurance policy for the year according to the CAFR Decision – 45/2005; to undergo verification of the fees declared by CAFR with those from the auditor's book-keeping – according to the CAFR Decision 237/2011; transmission of the Individual sheet of professional training to CAFR – according to CAFR Decision 6/2014; checking the auditor's participation in the annual compulsory training courses according to CAFR Decision 172/2010 and to additional training courses – CAFR Decision 49/2013; the existence of a quality assurance system which means preparing the Quality handbook – according to ISQC1 and ISA 220 and the implementation of policies and procedures in the audit firm; submission on the auditor's site of the Report on transparency – according to the GEO 90/2008.

Apart from their own internal control system on the quality of the missions, the financial auditors are checked to ensure the quality of the services performed and by the regulatory body, the competent authority – CAFR (Chamber of Financial Auditors of Romania) under the supervision of CSIPPC (Public Interest Oversight Board in the Profession accounting).

According to the CAFR rules and decisions, performing the audit missions may be achieved by the financial auditors who meet three conditions: they are CAFR members, they are active financial auditors and have visa for the current year (annual dues paid and have achieved the professional structured and unstructured training).

The inspection on the quality of the audit missions carried out by financial auditors CAFR members is performed every three years at maximum for the auditors who perform audits on public interest entities and every six years for the other auditors based on the quarterly inspection programme that also provides the teams that will carry it out.

Depending on the number of customers, the number of entities considered to be of public interest, the previous results of the quality assurance inspections, the violations of the ethical requirements, the deficiencies in the project or the compliance with the quality control system, or in the case of complaints substantiated with evidence, CAFR can have the quality control work carried out by the members of the House in periods of less than 3 years.

The inspection is performed wholly or at random in relation to the volume of activity of the Chamber members, as well as the frequency of the deviations previously detected and the findings are recorded in the Inspection letter signed bilaterally.

After the checking, the inspectors from the CAFR, depending on the objectives fulfilled/unfulfilled to which a percentage is assigned, establish the financial auditor who is reviewed with a qualifier: A, B, C or D, as follows:

- If he/she got up to 35% degree of fulfilment of objectives – D qualifier
- If h/she achieved between 36% -70% degree of fulfilment of objectives – C qualifier
- If he/she achieved between 71% -85% degree of fulfilment of objectives – B qualifier
- If he/she achieved between 86% -100% degree of fulfilment of objectives – A qualifier

The significance of the ratings is the following:

- For the "A" qualifier – no measures taken, it is considered that the auditor performs quality audit missions.
- For the "B" qualifier – the following measures are taken:
  - Participation in further professional training courses;
  - Sanctioning: written warning;

- For the “C” qualifier – measures:
  - Repeat the inspection after more than 1 year;
  - Participation in further professional training courses;
  - Disciplinary sanctions: written warning; reprimand.
- For the “D” qualifier – measures:
  - Participation in further professional training courses;
  - Repeat the inspection after more than 1 year;
  - Disciplinary sanctions: written warning; reprimand; suspension of the right to exercise financial audit activity over a period of 3-6 months; withdrawal of the CAFR membership.

Financial auditors participating in the audit missions as employees of an audit firm will not receive a qualifier.

Furthermore, the financial auditors who perform statutory audits will be ranked according to the risk of damage to the credibility of the financial reports by the inspectors of the Public Interest Oversight Board of the Accounting Profession. The criteria underlying the ranking of the statutory auditors and audit firms based on the risk of damage to the credibility of the financial reporting are the following: the degree to which the statutory audit reports are in accordance with the International Standards on Auditing (ISA), adopted by the Chamber of Financial Auditors form Romania (CFAR); the number of people (statutory auditors, statutory audit interns and experts) involved in the statutory audit mission; the results of the previous inspections; the existence of a system of quality control; the existence of a disciplinary sanction became final; the number of clients of the statutory auditors or of the audit firms that fall into the category of public interest entities; the fees set by contract by the statutory auditors or by the audit firms for the provision of statutory audit services to public-interest entities; the turnover of the statutory audit work related to the public interest entities; the amount of the non-audit contracts signed with the clients-public interest entities; the expiry of the collection of the fees stipulated in the contract; the existence of the report on transparency stipulated in the Government Emergency Ordinance no. 90/2008 on the statutory audit of the annual financial statements and of the annual consolidated financial statements.

3. References

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