

MAIN PRINCIPLES AS APPLICABLE TO DEVELOPMENT OF THE SYSTEM OF SUPERVISION OVER THE ACTIVITIES AND QUALITY OF AUDIT SERVICES

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Abstract: *The principles of the system of supervision over the activities and quality of audit services make up the foundation for its designing, allow avoiding problems of fair and impartial treatment of external quality control audit implementation and thus promote business development.*

During the scientific research on this topic, good European practices regarding the design of the system of supervision over the activities and quality of audit services were investigated, in view of the commitment assumed by the Republic of Moldova to transpose the provisions of the Community acquis into national law.

Based on the results of this research, the author finds several important conceptual issues with normative character, which should be addressed during the development of the system of supervision over the activities and quality of audit services through the principles of its organisation and functioning recognised at regional and international levels.

INTRODUCTION

The system of supervision over the activities and quality of audit services is defined as a set of principles, rules and elements ensuring the conduct of auditors and audit firms' activities in conformity with the professional standards, which are generally accepted by the international professional community.

From the perspective of compliance with the community acquis requirements, the EU Member States and those ones, which signed association agreements, have recognised the goods conceptual practices that relate to the system of supervision over the activities and quality of audit services and are based on certain principles, rules and standards ensuring the successful administration of the risks pertaining to the quality of audit.

Based on the Association Agreement, the Republic of Moldova undertook to make enormous efforts for prompt modernisation in conformity with the European standards, by assimilating about 70% of the community acquis and, respectively, by implementing the provisions thereof in the fields concerned, inclusively by complying with the requirements of Regulation (EU) No.537/2014 of the European Parliament and of the Council of 16 April 2014 on Specific Requirements regarding Statutory Audit of Public-Interest Entities.

First of all, aiming to realise this commitment, there was drafted the Table of transposing Directive 2013/34/EU of the European Parliament and of the Council of 26 June 2013 on the Annual Financial Statements, Consolidated Financial Statements and Related Reports of Certain Types of Undertakings, into national law [4].

According to Article 32 of Directive 2013/34/EU, 'Member States shall organise an effective system of public oversight for statutory auditors and audit firms based on the principles set out in paragraphs 2 to 7, and shall designate a competent authority that will be in charge of such oversight' [Article 32, Directive 2013/34/EU].

The principles of the system of supervision over the activities and quality of audit services refer to the system organisation and functioning requirements that settle the challenges pertaining to the equitable and unbiased treatment when carrying on the external control of audit quality, and that are simultaneously considered when setting the conditions for making the quality assurance information transparent and accessible to the entire society, thus contributing to business environment development. Further, the author shows in Table 1, the generally accepted principles at the level of EU community in parallel with domestic law requirements as correlated with the principles of oversight.

Table 1. Main Principles of Designing up a System of supervision over the activities and quality of audit services

Generally accepted principles at the EU community level	Requirements of domestic law as collaborated with the principles of oversight
P1. Any and all audit firms and statutory auditors are subject to public oversight	Any and all audit firms are subject to external quality control
P2. The competent authority is governed are governed by non-practitioners	The audit supervisory board is formed of 7 non-practicing members
P3. The ultimate responsibility for oversight is in charge of a competent authority	A public audit oversight body is the Council, approved by the Government
P4. The competent authority is vested with the competences required for exercise of its functions and competencies	The Council is an independent public establishment with the status of a legal entity, which is responsible for public audit oversight
P5. The competent authority is independent and transparent	The Council carries on its activities as based on self-management principles; the information about its activities is published on the official web page

Source: Developed by the author as based on the provisions of Directive 2013/34/EU and Act no.271/2017 [1; 2]

When analysing this table, one may see that since the Republic of Moldova is concerned about harmonisation of the domestic legal framework with the European standards, the author draws a conclusion that such principles are essential both for our State and for those ones, where democrats are less aware of the need for developing a concept of the system of supervision over the activities and quality of audit services.

The expectations of the business environment and, generally, of audit findings beneficiaries in respect of financial auditors are mainly related to realisation of certain commitments for quality audit. Hence, considering the good international practices as provided for in Directive 2006/43/EC of the European Parliament and of the Council of 17 May 2006 on Statutory Audits of Annual Accounts and Consolidated Accounts, the author thinks that there may be outlined the following main conditions for the concept of a system of supervision over the activities and quality of audit services:

- Area of applicability of external quality control,
- Independence of the public oversight system,
- Professional training and relevant experience of the supervisory authority's employees,
- Professional rationale and objectivity when conducting the quality assurance reviews.

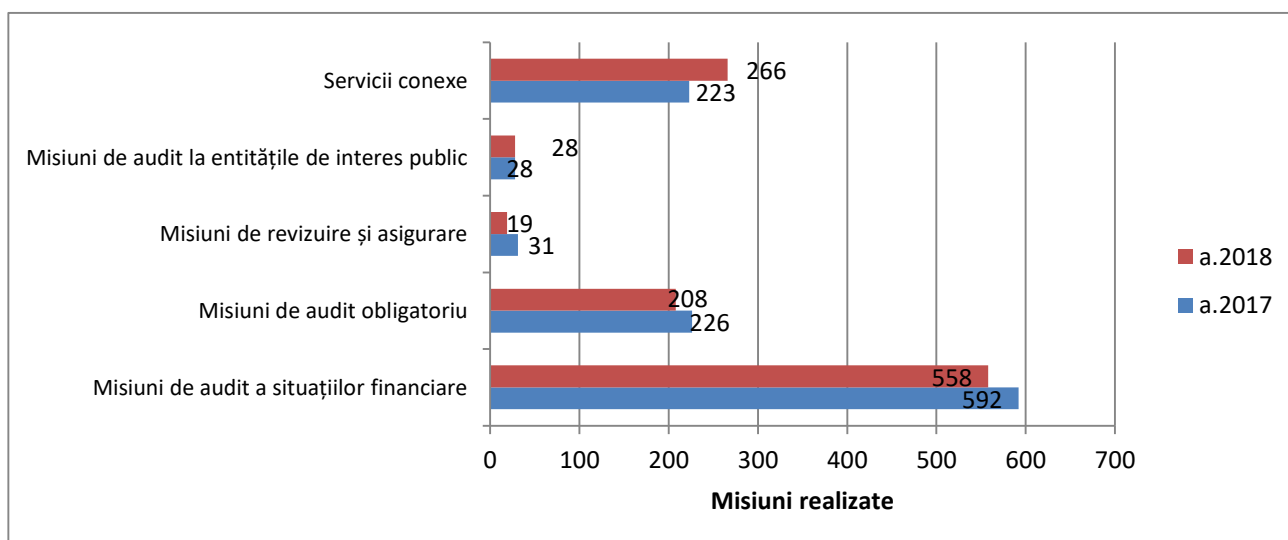
According to Directive 2006/43/EC, the State shall organise an effective system of public oversight for statutory auditors and audit firms, so that all of them should be subject to public oversight. [Article 32.1]. Thus, as a result of transposing the European requirements into national law, this provision is found in Chapter Eight of Act no.271/2017, stipulating that any and all auditors

and audit firms are subject to public oversight. Any and all audit firms are subject to external quality control at least every six years, while the entities that carry out audit of public-interest entities shall be subject to external quality review every three years. Any and all audit firms are subject to external quality reviews [Chapter VIII, 2].

However, we believe that since the functional aspect of the audit supervision system is determined by professional rationale thereof when setting the area of applicability of external quality reviews, then it is important that the conceived procedures for setting the area of such reviews conduct should be also supported by adequate testing of audit files, including the assessment of conformity with the standards of audit and the principle of independence, and there should be also considered the internal quality control system of an audit firm, audit fees recovered and other resources spent.

Moreover, it is proposed that there shall be also subject to external control other audit commitments, in addition to those ones realised at public-interest entities and at entities that are bound by different legislative and regulatory instruments to retain an audit firm for the audit of financial statements.

The chart below provides the types of audit commitments realised by auditors and audit firms from the Republic of Moldova.



Related services

Audit commitments at public-interest entities

Review and assurance commitments

Mandatory audit commitments

Financial statements audit commitments

Commitments realised

Chart 1. Audit commitments realised by audit firms from the Republic of Moldova over 2017-2018

Source: Developed by the author as based on the Information on audit services market [2.4]

If we analyse the chart of audit commitments realised over the last two years, we will notice that the subject of review of the majority of audit commitments are annual financial statements and/or consolidated annual financial statements. Only 28 audit commitments of those 592 ones concerning the financial statements were realised at public-interest entities in 2018.

Hence, we consider that it will be correct to extend the external controls realised in order to assure the quality, as well, of other audit commitments for financial statements, carried out by audit firms at their clients and relating to the period under quality review. Hence, the area of conduct of such controls may be also extended to other kinds of commitments, thus allowing to apply a more complex base for assessment of the quality control system at the level of an audit firm, as well as for examination of abidance by the professional ethics requirements to auditors.

The independence of the system of supervision over the activities and quality of audit services is a pre-condition for free and unbiased exercise of powers and functions by the relevant authority. The generally accepted principles at the level of the EU community stipulate that the competent authority shall be governed by non-practitioners. So, although a State may appoint one or more competent authorities to exercise the powers of supervision over the activities and quality of audit services, Directive 2006/43/CE provides that the ultimate responsibility shall be vested only on an authority. For instance, the authority charged with the ultimate responsibility for exercise of public oversight powers in Romania is the Statutory Audit Public Oversight Authority, which is subordinated to the Ministry of Public Finance [3].

In the Republic of Moldova, the ultimate responsibility for oversight is vested on the Council for Public Audit Supervision, which was approved as a body of public audit oversight by the Government of the Republic of Moldova [2].

The independence of the system of supervision over the activities and quality of audit services presupposes organisation thereof so that it would be independent from audit firms and statutory auditors under review. According to the generally accepted principles at the level of EU community, the competent oversight authority is governed by non-practitioners, who have knowledge in the fields that are relevant for statutory audit. They are selected as based on an independent and transparent appointment procedure.

Meanwhile, the abidance by the principle of independence presupposes that funding of the oversight system shall be secure and free from any potential undue influence by audit firms or auditors, i.e. this system must have the relevant resources not depending on the contributions of those ones subjected to public oversight. Presently, the Council for Public Audit Supervision has a varied range of financial sources, inclusively: payments for getting the professional qualification of auditor and for registration of the audit subjects, annual contributions of auditors and trainees, tariffs set for the services rendered under law, and allocations from the public budget.

However, according to the estimates, the main source of funding of the Council's activities are annual fees of audit firms and annual contributions of auditors. According to Article 39 of Act 271 of 15 December 2017, annual fees of audit firms are calculated as per auditor's report issued, i.e. as an average monthly salary in the national economy per auditor's report issued for the audit of individual financial statements at public-interest entities or at large entities. As for the audit of individual financial statements at non-public-interest entities or at large entities subjected to mandatory required audit, there is applied the annual fee amounting to 0.2 of the average monthly salary in the national economy, as forecasted and annually approved by the Government of the Republic of Moldova.

We think that it would be right if the activities of oversight authority were not funded directly by the subjects under control, otherwise, there is a risk of breaching the principle of independence of such an authority when it exercises its powers and functions. Directive 2006/43/EC provides that the

funding for the public oversight system shall be free from any undue influence by auditors or audit firms. [Article 32 (7), 1].

Thus, relying on the above principle, there may be allowed the funding from the subjects under oversight, provided that there is avoided their undue influence. Hence, the actual version of the Council funding model set by Act 271 of 15 December 2017 stipulates that the payments to be made by auditors and audit firms shall be in fixed amounts and shall depend only on the forecast of the average monthly salary in the national economy, but not on the amount of the fees received from realisation of audit commitments. All the more so, the annual contributions shall be paid both by auditors and by trainees in the field of audit. So, the annual contributions for auditors are set as amounting to 0.1 of the average monthly salary in the national economy, as forecasted and approved by the Government on a yearly basis, while the annual contributions for trainees are less and amount to 0.05 of the average monthly salary in the national economy.

The above principles are realisable if there are considered the goods practices shared by the EU Member States and manifested by compliance with a range of additional requirements as combined with the community *acquis*. Professional training and relevant experience are also a principle we regard as basic one for development of the oversight system, and directly ensuring the system quality. Not only successful configuration of such a system can settle the quality-related risks; but also professional skills of the oversight authority's employees, relating to statutory audit and financial reporting, can ensure the public's trust in realisation of commitments for supervision in the relevant sphere of activity.

We think that it is crucial that the concept of the system of supervision over the activities and quality of audit services shall avoid, in its basis, any and all conflicts of interests between those, who carry out external quality controls, and the audit firm or statutory auditor, who are subjected to such controls. Aiming to the abidance by this principle, we consider that it will be rational to emphasise the applicability of objective procedures for selecting audit firms or auditors included in reviews for specific quality control commitments.

CONCLUSIONS AND RECOMMENDATIONS

If we synthesise the foregoing, the following conclusions can be drawn:

1. The concept of the system of supervision over the activities and quality of audit services in the Republic of Moldova is being harmonised with the good European practices. This is the reason why it is essential to treat correspondingly the principles serving as a basis for creation of the system of supervision over the activities and quality of audit services, when setting and developing the domestic regulatory framework. In this regard, there is recommended to abide by the conditions of supervision over the activities and quality of audit services, such as area of applicability of the external quality control, independence of the public audit oversight system, professional training and relevant experience of the oversight authority's employees, professional rationale and objectivity when carrying out the quality reviews.

2. The number of commitments for audit of financial statements at public-interest entities is very small if compared to those ones at other entities. Aiming to ensure a relevant base for assessment of the quality control system at the level of an audit firm and to examine the abidance by the auditors by the professional ethics requirements, it is proposed to extend the external controls realised in order

to assure the quality, as well, of other audit commitments for financial statements, carried out by audit firms at their clients and relating to the period under quality review.

3. The good practices shared by the developed countries and relating to the public audit oversight do not allow undue influence by auditors and audit firms on the oversight system funding. We think that it would be correct if the activities of oversight bodies were not funded directly by the subjects under control. Otherwise, there is a risk of breaching the principle of independence of such a body when it exercises its powers and functions. Hence, there is welcomed the principle stipulating that concept of the system of supervision over the activities and quality of audit services shall avoid, in its basis, any and all conflicts of interests between those, who carry out external quality controls, and the audit firm or statutory auditor, who are subjected to such controls.

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