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OPPORTUNITIES FOR MODERNIZING THE FINANCIAL AUDIT QUALITY MANAGEMENT SYSTEM IN THE REPUBLIC OF MOLDOVA

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Abstract. *Replacing the concept of quality control with that of quality management will not be a formality in the modernization of the quality assessment process of audit missions, as long as the management of the audit entity will assume this responsibility. And the linear approach traditionally used until now can no longer cope with the tasks of a flexible internal control system within an audit firm.*
The research in question is an empirical investigation to establish whether the new reforms in the field of auditing determine the performance of the audit mission in the context of the current requirements of professional quality standards. At the same time, the aim of the study is to express the opinion regarding the advantages and disadvantages of these developments at the stage of harmonizing the auditor profession with international practices. As part of the research theme, the normative acts in the field were investigated, the international good practices in the exercise of the auditor profession, aiming to highlight the role of reforms in ensuring the quality of services in this field.
The research carried out on this subject aims to highlight the issue of the stability of the entire audit quality management system, consistently addressed in most of the approaches of the International Auditing and Assurance Standards Board (IAASB). The scientific investigations carried out on this research topic aim to identify and propose solutions regarding the improvement of the audit quality management system in the context of the review of international standards regarding quality assurance.

Key words: *audit monitoring, quality management system, policy monitoring, international auditing standards.*

JEL Classification: M42

Introduction

The current audit ecosystem faces increasing expectations of modern society in high-performance quality management systems that are proactive and adaptable to the needs of users of financial information. The new obscure elements of the realities determined the development of the concept for evaluating the quality of audit engagements completed by replacing the International Standard on Quality Control (ISQC) 1 "Quality Control for Firms that Perform Audits and Reviews of Financial Statements, and Other Assurance and Related Services Engagements" with the International Standard on Quality Management (ISQM) 1 "Quality Management for Firms that Perform Audits or Reviews of Financial Statements, or Other Assurance or Related Services Engagements". The modernization of the audit quality management system in the Republic of Moldova to international requirements will contribute to increasing the prestige and recognition of audit professionalism worldwide.

Replacing the concept of quality control with that of quality management will not be a formality in the modernization of the quality assessment process of audit missions, as long as the management of the audit entity will assume this responsibility. And the linear approach

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traditionally used until now can no longer cope with the tasks of a flexible internal control system within an audit firm. The research carried out on this subject aims to highlight the issue of the stability of the entire audit quality management system, consistently addressed in most of the approaches of the International Auditing and Assurance Standards Board (IAASB). The scientific investigations carried out on this topic aim to identify and propose solutions regarding the improvement of the audit quality management system in the context of the review of international standards regarding quality assurance.

I. Analysis of the normative framework regarding the internal audit quality control

The internal control of the audit quality is ensured by the development by the audit entity of its own internal control policies and procedures. Law 271/15.12.2017 on the audit of financial statements, as well as the audit standards, contains specific provisions regarding the assurance of audit quality, set out in table 1.

Table 1. The current reference framework for the exercise of internal audit quality control

Normative act	*Legal provision*	*News*
Law 271/ 15.12.2017	Article 24. Internal quality control within the audit entity	Application of audit quality control policies and procedures in accordance with auditing standards, quality control standards and the Code of Ethics
	Article 31(2), c). The audit entity is required to comply with the audit quality control requirements	The audit entity applies internal quality control procedures, effective risk assessment and audit procedures in accordance with auditing standards
ISQC 1/ IAASB Handbook	Quality control for firms performing audits and reviews of financial statements, as well as other assurance engagements and related services	The role of engagement quality control is to provide an objective assessment, on or before the date of the report, regarding the significant judgments made by the engagement team and the conclusions reached by it
ISA 220/ IAASB Handbook	Engagement teams are responsible for implementing quality control procedures that are applicable to the audit engagement	Quality control at the engagement level must provide the auditor with reasonable assurance regarding compliance with professional standards and applicable legal and regulatory provisions
Code of ethics / IAASB Handbook	Non-acceptance of threats to the independence of the auditor	Obtaining written confirmations from staff regarding compliance with independence policies and procedures

Source: developed by the author based on the provisions of the legislation of the Republic of Moldova [1, Law 271/15.12.2017; 2, IAASB Handbook]

All audit entities, in order to ensure audit quality, are obliged to develop, approve and apply audit quality control policies and procedures in accordance with Law 271/15.12.2017, audit standards, quality control standards and the code of ethics.

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Article 31(2) of Law 271/15.12.2017 on the audit of financial statements provides the audit entity to comply with the requirements regarding audit quality control. Under the conditions of the nominated law, the audit entity uses internal quality control procedures, effective risk assessment procedures, protection measures and control of information processing systems. At the same time, it is obliged to carry out the audit in accordance with the auditing standards and to be guided by rules that provide that the founders, board members and those of the executive or supervisory body of the audit entity do not influence the conduct of the audit and do not endanger the independence and the auditor's objectivity.

The International Standard on Quality Control (ISQC) 1 "Quality Control for Firms that Perform Audits and Reviews of Financial Statements, and Other Assurance and Related Services Engagements" is applied by the audit entities of the Republic of Moldova in accordance with the provisions of Law 271/15.12 .2017. According to article 2 of the nominated law, the notion of "quality control standards" means "international quality control standards, issued by the Council for International Auditing and Assurance Standards, which are intended for internal quality control, accepted for to be applied on the territory of the Republic of Moldova" [1, Law 271/15.12.2017].

Quality control standards, as well as audit standards, are accepted to be applied in the Republic of Moldova based on the Agreement on the right to reproduce Audit Standards and the Code of Ethics in the Republic of Moldova, signed by the Ministry of Finance on April 2, 2012 and the Council for Standards International Audit and Assurance Standards of the International Federation of Accountants on April 4, 2012. The standards are published and placed on the website of the Ministry of Finance.

The International Auditing Standards issued by IFAC in 2018 are placed on the official website of the Ministry of Finance [2, IAASB Manual]. Currently, internal quality control procedures are covered by the following quality control standards:

- International Standard on Quality Control (ISQC) 1 "Quality Control for Firms that Perform Audits and Reviews of Financial Statements, and Other Assurance and Related Services Engagements";
- International Standard on Auditing (ISA) 220 "Quality Control for an Audit of Financial Statements".

From December 15, 2022, ISQC 1 is expected to be replaced by the International Standard on Quality Management (ISQM) 1 "Quality Management for Firms that Perform Audits or Reviews of Financial Statements, or Other Assurance or Related Services Engagements" [3]. At the same time, a new International Standard on Quality Management (ISQM) 2 "Engagement Quality Reviews" will come into force, which will also be a standard for audit quality management [4]. Along with the development of the new quality standards, ISA 220 was revised, which is the only audit standard with direct tangents related to the modernization of the audit quality system. In the new version, this standard will be found under the name of ISA 220 (Revised) "Quality Management for an Audit of Financial Statements" [5].

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II. Current Status of Internal Quality Control for Entities Performing Audits and Reviews of Financial Statements

Currently domestic audit entities develop, comply with and apply internal quality control procedures in accordance with the provisions of ISQC 1, ISA 220 and the Code of Ethics. The legal framework prescribes a set of requirements, presented in figure 1, which must be respected in order to design and implement an internal audit quality control system.

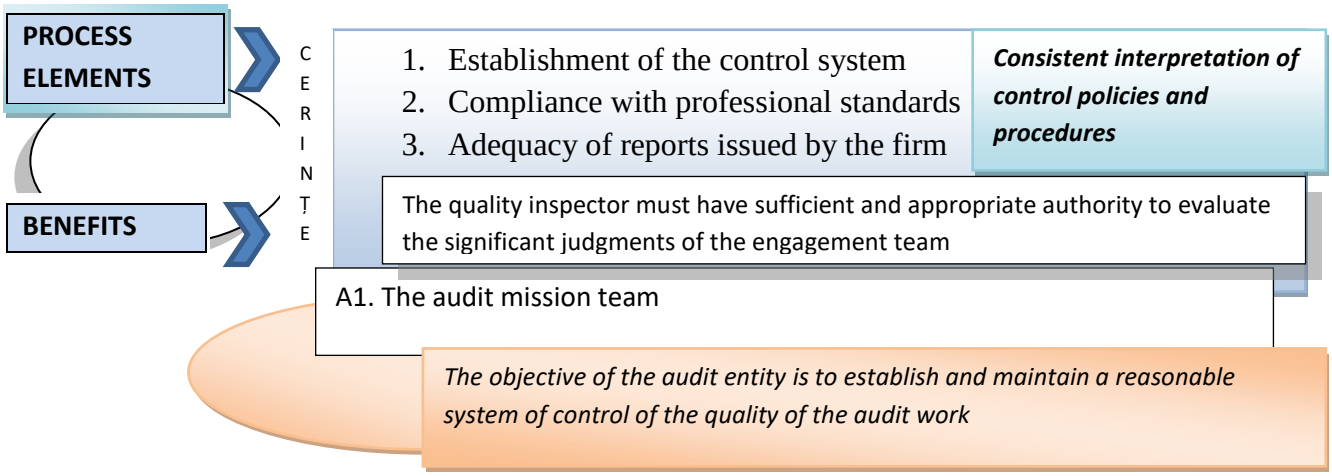


Fig. 1.Features of an internal quality control system in accordance with ISQC 1, ISA 220 and the Code of Ethics

Source: developed by the author based on the provisions of the Manual of International Auditing, Assurance and Ethics Regulations [2]

Taking into account the existing legal framework, we consider that any audit entity, authorized to practice audit activity, must independently develop a manual of audit quality control policies and procedures and issue an approval and notification provision his employees. There is already a practice in this regard within large audit entities, which consists of appointing an auditor who will be responsible for the internal audit quality control, as well as for the preparation of the report on compliance with the quality control procedures presented to the Public Supervisory Board of the audit within 4 months from the end of each management period.

According to article 24 (5) of Law 271/15.12.2017, the quality control of the audit mission is exercised at public interest entities and at large entities established according to the Accounting and Financial Reporting Law 287/2017. The control in question is carried out until the auditor's report or the additional report addressed to the audit committee is issued.

It is important to mention the condition of non-admission of quality control by an auditor who participated in the exercise of the audit. In the event of the existence of such a problem, the legal framework allows, on a contractual basis, the employment of an external auditor to carry out quality control while maintaining confidentiality and professional secrecy.

In the context of ISQC 1, the mission quality control process is permanently subject to monitoring, which involves not only the development of mission inspection guidelines and methodologies, but also their evaluation, including a periodic examination of a selection of

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completed missions, the purpose of which is to provide reasonable assurance that its quality control system is operating effectively.

The legal framework provides for the determination of the effectiveness of the audit quality control within the audit entity, which usually takes place through annual evaluations, but they can be performed even more frequently. In order to avoid subjectivism, it is recommended to evaluate the audit quality control policies and procedures from the point of view of their effectiveness, the best evidence in this sense is the record of the evaluations and the measures proposed for their efficiency.

At the same time, we consider it appropriate to take into account the provisions of Law no. 271/15.12.2017 regarding audit quality control, which must be started starting from the audit documentation archived in the mission file, including: audit contract; documents certifying the availability of the mission team to perform the audit; statements of the participants in the audit regarding compliance with the principles of independence and objectivity; documents and information that form the basis of the auditor's report; auditor's report; additional report addressed to the audit committee; auditor's opinion regarding the consistency between the management report and the financial statements; statements regarding material misstatements presented in the management report.

It is necessary to note that, objective assessment is the main purpose of the mission quality control process. This assessment must fulfill the role of providing an objective assessment of the significant judgments made by the engagement team and the conclusions reached in formulating the audit report. This process must cover not only the audits of the financial statements of the listed entities, but also the other missions for which the audit entity considers a quality control review of the mission necessary.

Currently, small audit entities face a shortage of qualified personnel. Therefore, it is important that these entities provide themselves with sufficient staff and resources when they intend to audit the financial statements of large companies. The audit entity must have as employee's no less than two auditors for the audit of public interest entities and large entities, established according to the Accounting and Financial Reporting Law 287/2017, or at other state-owned enterprises and joint-stock companies in which the state's share exceeds 50% of the share capital.

Often, the long-term relationships between the client and the audit entity, but also due to a narrower labor market in this field, can cause the emergence of circumstances that threaten the independence of the auditor. Professional ethics do not admit such threats, they must be eliminated or reduced to an acceptable level, and otherwise the issue of withdrawal from the mission arises. As the impact on independence provisions is central to the objectivity of an audit engagement, to control such issues it is recommended that:

- examination of information regarding the scope of customer services;
- encouraging the staff to promptly notify the audit entity of the circumstances and relationships that constitute a threat to independence;
- creating conditions that allow both the audit entity and its staff to promptly determine whether the independence provisions are met;
- maintaining, updating the records related to independence and undertaking the appropriate measures to eliminate the identified threats to independence that are not at an acceptable level.

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As a rule, compliance with the independence provisions requires the presentation of a written confirmation. The audit entity shall, at least once a year, obtain written confirmation from staff of compliance with independence policies and procedures. This requirement refers to the audit entity's staff who are required to be independent by the ethics provisions.

For convenience as well as from the point of view of the rational use of time and other resources, it may be practiced to draw up and present the confirmation not only on paper but also in electronic format. At the same time, in order to ensure the effectiveness of this procedure, the confirmations must be examined with caution and action taken regarding the information indicating non-conformities. Thus, by obtaining confirmation and adopting appropriate measures regarding information that indicates non-conformities, the audit entity demonstrates the importance of independence and brings this aspect to the attention of the staff.

III. The quality of the audit through the lens of professional management standards

The topics that have generated the most public interest attention in recent years include fraud, going concern, audit evidence and the desire to reduce audit risk to an acceptable level. In these circumstances, the IAASB at its meeting in December 2018, approved the draft ISQM 1 for public exposure together with the version of a new standard for audit quality management ISQM 2, as well as the revised version ISA 220.

The relevant international standards are considered to be relevant to public sector engagements. When appropriate, additional considerations specific to public sector entities are included, without exceeding the ethical standards that require the auditor to comply with the relevant ethical requirements, including those relating to independence, relating to financial statement audit engagements.

ISQM 1 deals with the responsibilities of an audit entity to design, implement and operate a quality management system for audits or reviews of financial statements or other assurance engagements or related services. ISQM 2 contains requirements intended to enable the audit entity and the engagement quality assessor to meet the stated objectives for the proper functioning of the quality management system.

These standards treat the quality management system in an interactive manner that is responsive to changes in the nature and circumstances of the audit entity and its engagements. However, in the context of the stated standards, a quality management system addresses the following eight elements:

Table 2.Key elements of a modern audit quality management system

System elements	*Concept*	*Approach*
Risk evaluation	The audit entity's risk assessment process	The audit entity must identify and assess quality risks to provide a basis for designing and implementing responses
Administration	Governance and leadership	The audit entity must demonstrate a commitment to quality through a culture that exists throughout the firm

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Ethics	Relevant ethical requirements	The audit entity must establish quality objectives that address the performance of responsibilities in accordance with relevant ethical requirements, including those related to independence
Engagement	Acceptance and continuation of customer relationships and specific engagements	The audit entity shall establish the following quality objectives that address the acceptance and continuation of customer relationships and specific engagements
Assessment	Engagement performance	Mission teams understand and fulfill their responsibilities in relation to the missions being exercised
Resources	Personnel resources	The audit entity must establish quality objectives that address the acquisition, development, use, maintenance, allocation and timely allocation of resources
Information	Information and communication	The information system identifies, captures, processes and maintains relevant and reliable information that supports the quality management system
Monitoring	Monitoring and remediation process	The audit entity must design and perform monitoring activities to provide a basis for identifying deficiencies

Source: developed by the author based on the provisions of ISQM 1, ISQM 2, ISA220 [3; 4; 5]

In order to proactively manage the quality of the assignments performed, according to the provisions of the audit quality management standards, an audit entity must apply a risk-based approach to the design, implementation and operation of the elements of the quality management system in an interconnected manner and coordinate. The risk-based approach involves:

- Establishing quality objectives;
- Identification and assessment of risks to the achievement of quality objectives;
- Designing and implementing responses to address quality risks.

In the sense of this concept, the audit entity must design, implement and operate a quality management system. It would appear to be a traditional approach, but nevertheless the standards for audit quality management draw attention to the exercise of professional judgment, taking into account the nature and circumstances and the engagements undertaken.

The key element supporting the design, implementation and operation of the quality management system is considered to be the governance and leadership of the quality management system. The current concept of audit quality management expressly states that the executive director of the audit entity has the final responsibility for the quality management system vis-à-vis the board of directors.

In the design of the new quality management system, the audit entity will appoint an engagement quality assessor qualified to perform an objective assessment of the significant judgments made by the engagement team and the conclusions reached. To achieve this objective, the audit entity shall develop policies and procedures regarding the assignment of responsibility

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for appointing engagement quality assessors to a person with the appropriate competence, capabilities and authority to fulfill their responsibility. Those policies or procedures shall provide for such persons to appoint the engagement quality assessor, as well as establish the eligibility criteria for appointment:

- ✓ Such policies or procedures shall require that the quality assessor is not a member of the engagement team and shall comply with the following eligibility criteria:
- ✓ Has the competence and capabilities, including sufficient time and appropriate authority, to perform the engagement quality review;
- ✓ Complies with relevant ethical requirements, including threats to objectivity and independence;
- ✓ Comply with the provisions of the existing law and regulations.

Conclusions:

The study found the existence of an adequate legal framework that encourages audit entities to design a quality management system that is adapted to the nature of the missions they carry out. It was found necessary to accelerate efforts in the near future to serve the public interest in implementing a modern audit quality management system. The present research focused on topics of interest in audit oversight and quality assurance. In this context, the modernization of the audit work management process and the development of new skills are key factors in addressing the complexity of audit quality.

At the same time, it is worth noting the current role of the audit quality management concept as a fundamental competitive lever for improving corporate governance within an audit entity. And the importance of this concept is proven by various procedural initiatives and activities to modernize the audit process. Audit quality management standards should contribute to the development of the market and increase the reputation of the auditing profession.

In today's conditions, an audit entity must demonstrate continuous progress in reforming the strategic objectives related to quality management, which need to be formally translated into manuals and inspection procedures of audit missions. In this sense, it is proposed:

- increasing the focus on emerging issues to ensure that the quality control system modernization process remains relevant;

- improving interactions with stakeholders, such as quality partners and audit entity management to keep system risks and issues under control;

The practical significance of the obtained results lies in the possibility of using theoretical and methodological developments to improve quality control for firms that perform audits and reviews of financial statements, as well as other assurance missions and related services.

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