

THE EFFECTIVENESS OF THE SYSTEM OF QUALITY CONTROL IN ACCOUNTING PRACTICES

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Abstract: Any accounting firm need to develop a system of quality control (SQC), which have the purpose to offer a reasonable assurance, that the accountants or the auditors, and their personnel, respect the professional standards and any legal or regulatory requirements, and the reports issued are appropriate, with the circumstances. The quality control system contains policies and their implementation is achieved through a system of procedures. A company can have a system of quality control, but only as a form, and as result, it is very important for everyone to be able to assess, how effective such a system works. An effective quality control means more than compliance with rules and provisions, and this is the reason why, for an accounting firm, it is very important, not just to have the system, but, also, to have some methods to evaluate how effective this system is. A lot of benefits can result from a robust SQC, regarding competitiveness on the market and the financial performance, and through monitoring controls, an accounting firm apply tests to ensure that controls are designed and works properly. The paper has the purpose to identify whether the accounting practices, small and medium, know how to evaluate the effectiveness of quality control system, and in connection with is, whether they have enough information to develop a set of indicators, which could measure the effectiveness of the firm's SQC. The research is based on descriptive statistics applied on the results of a survey addressed to small and medium practices in accounting and auditing. The results can make their contribution to disseminating how to design the system of indicators used to evaluate the effectiveness of the quality control system. The findings of the paper are not very optimistic, but if, at least it draws attention to the importance of building a set of indicators to measure the effectiveness of the quality control system, the objective has been achieved.

Keywords: Quality Control; policies; procedures; effectiveness; indicators; SQC.

JEL Classification: M41; M42.

1. Introduction

With the purpose to ensure that the professional accountants delivery high-quality services and meet the public interest, by regulation, accountancy profession organizations and their members must play an important role in the assessment of the quality control system (SQC) developed, also at the firms' level, and at any engagement performed.

All the professionals that are working in firms or as sole practitioners, and performs a wide range of professional services, in accounting and auditing practices, are required to develop and maintain a system of quality control (SQC). The International

Federation of Accountants, IFAC, achieves its objective to serve the public interest, and issues standards as guidance to establish the responsibilities of a firm to develop a system of quality controls and the responsibilities of a professional body to evaluate its application.

The most important guidance for an accounting or auditing firm, in establishing and maintaining a system of quality control (SQC), with the objective 'to provide it with reasonable assurance that a) the firm and its personnel comply with professional standards and applicable legal and regulatory requirements; and b) reports issued by the firm or engagement partners are appropriate in the circumstances' (IAASB, 2015), is given by ISQC 1 'Quality Control for Firms that Perform Audits and Reviews of Financial Statements, and Other Assurance and Related Services Engagements'. For the audits of financial statements, the provisions of the ISQC 1 should consider, the additional ISA 220 'Quality Control for an Audit of Financial Statements'.

The IFAC's member bodies of professional accountants, in each member's country, also, apply a complementary guidance through IPPS (International Professional Practice Statement) no. 1 'Assuring the Quality of Professional Services'. The purpose of this document is to assure an external review of the quality control's policies and procedures, through a quality assurance review programs, which evaluate whether the firm of practicing accountants comply with their SQC or not, or the system needs some improvements.

Also, the IFAC Board have issued the Statements of Membership Obligations (SMOs) and SMO 1 'Quality Assurance', that 'requires member bodies to establish and publish quality control standards and guidance requiring firms to implement a system of quality control in accordance with ISQC1' (IFAC, 2004).

As result of these provisions, accountants and auditors must have developed a SQC, policies and procedures at the firm and the engagement level, and the professional and statutory bodies, worldwide, perform periodic independent inspections of the accounting and auditing firms' systems of quality control.

The paper has the objective to establish whether the accounting and auditing practices are preoccupied to measure the effectiveness of the SQCs. The paper provides relevant provisions and literature in order to identify the regulation applied for a set of indicators with the purpose to measure the effectiveness of the SQCs. The hypothesis of the study is: *The professional accountants and auditors, in small and medium practices, have enough information for developing a set of indicators which evaluates the effectiveness of the firm's SQC?*

With the purpose to answer at this question the paper presents the data which are used, the descriptive statistics and the research design. Also, the study presents the results and the conclusion based on them that are reached.

2. Literature review

2.1. The System of Quality Control and the Public Interest

There have been a variety of other research projects and global initiatives on the topic of audit quality, and as result there has not been an universal agreement on a definition of audit quality, or the audit quality framework, or the most relevant indicators of audit quality and how and to whom they should be communicated.

The level of audit quality is linked to quality level of the information contained in financial statements, the reason for this is that the financial statement that have been audited by high quality auditors rarely contained substantial misstatements, which is reflected in minimization agency costs between shareholders and management. Thus, according to the literature, audit quality positively affects the quality of accounting information. (Soliman, 2014)

The accountancy profession and regulatory community act in a public/private arrangement of shared regulation that bears joint accountability for the actions of the profession, as well as their impact on society as a whole. (IFAC Policy Position Paper 5, 2012)

Accountants and auditors are responsible and have the aim to ensure the quality of their works. As result, all the professionals that are working in firms or as sole practitioners, and performs a wide range of professional services, in accounting and auditing practices, are required to develop and maintain a system of quality control (SQC). Policies and procedures, regarding the quality control of the professional accountancy services, are developed at the engagement level, at the level of the firm and at the national level, through the professional bodies.

An accountancy firm's system of quality control is intended to address certain key elements, such as: leadership responsibilities for quality within the firm, ethical requirements (independence, integrity, objectivity), client relationships, human resources/personnel management (which includes sufficiency of resources, technical knowledge and experience), engagement performance, communication and reporting, and monitoring.

Based on that key elements, a set of potential Audit Quality Indicators (AQIs) could provide additional perspective on the firm's system of quality control, and could be useful for understanding the matters that may contribute to the performance of a quality audit. A set of AQIs could help the firm's ability to support and perform quality audits, could help a better understanding the firm's policies, procedures, and processes related to its system of quality control, and could provide information about the engagement team's performance.

2.2. Quality Control according the Standard Setters

The Public Company Accounting Oversight Board's (PCAOB) and the International Auditing and Assurance Standards Board (IAASB) have developed two projects, analyzed further below, which have the purpose to identify characteristics and indicators of the audit quality, setting off by the two different perspectives and that responding to the issues arising in the previous main studies.

The Public Company Accounting Oversight Board (2013) released its Audit Quality Indicators Project in which they propose a set of qualitative/quantitative indicators discussed with the board's advisory groups, firms, other regulators, audit committees and academics in order to identify a good audit quality framework.

In the paper could be identifies the following indicators used to evaluate the quality of audit service:

- Operational inputs - indicators regarding the people that work in audit firm: ratio of partners to staff, partner and staff utilization percentages / workloads, chargeable hours per professional, percentage of work

outsourced to service center, industry expertise and proficiency, training hours per audit professional, and so on.

- Process - the firm leadership communications on audit quality and investors' interests: metrics related to independence, testing, and compliance; number and nature of internal quality review findings; compensation trends of prematurely rotated partners; leverage ratio of audit staff to partners, credentials of new hires and recruiting - academic achievement; best companies to work for rankings; compensation levels.
- Results - frequency and market impact of financial statement restatements for errors: number of material weaknesses cited in conjunction with material errors, number of audit reports lacking a going concern opinion which had a subsequent bankruptcy; number and nature of PCAOB inspection findings, and so on.

The Center for Audit Quality (CAQ), affiliated with the American Institute of Certified Public Accountants (AICPA) has closely followed the Public Company Accounting Oversight Board's (PCAOB) Audit Quality Indicators (AQI) initiative and developed a set of potential AQIs that could provide benefits relative to the oversight of the audit quality, CAQ (2014) - CAQ Approach to Audit Quality Indicators.

Similarly, the International Auditing and Assurance Standards Board (2014) released "Framework for Audit Quality: Key Elements that Create an Environment for Audit Quality", which describes the different elements that create the environment for audit quality at the engagement, firm, and national levels, as well as relevant interactions and contextual factors:

- Inputs – the audit firm's culture (values, ethics and attitudes), the time, knowledge and skill brought to the audit and the effectiveness of the audit's processes and quality control procedures
 - Engagement Level (for example the engagement team is independent, the engagement team exhibits professional competence and due care, the engagement team exhibits professional skepticism, partners and staff have the necessary competences, partners and staff understand the entity's business., partners and staff make reasonable judgments)
 - Firms level (Governance arrangements are in place that establish the appropriate "tone at the top", and which aim to safeguard the firm's independence, Necessary personal characteristics are promoted through appraisal and reward systems supporting audit quality Engagement teams are properly structured, Partners and more senior staff provide less experienced staff with timely appraisals and appropriate coaching or "on-the-job" training.)
 - National level (Regulators, national standards setters and professional accountancy organizations are active in ensuring that the ethics principles are understood and the requirements are consistently applied. Robust arrangements exist for licensing audit firms/individual auditors, Education requirements are clearly defined and training is adequately resourced and effective)

- Outputs – recognizing that some stakeholders (such as regulators) have the ability to influence outputs while for others (such as investors) outputs (in the form of the auditor's report) are relatively standardized. For these factors the IAASB distinguish:
 - Engagement Level (From the Auditor: Auditor's Reports to Users of Audited Financial Statements, Auditor's Reports to Those Charged with Governance Auditor's Reports to Management, Auditor's Reports to Financial and Prudential Regulators; From the Entity: The Audited Financial Statements, Reports from Those Charged with Governance, including Audit Committees).
 - Firm and national level
 - ✓ From the Audit Firm: Transparency Reports, Annual and Other Reports;
 - ✓ From Audit Regulators: Providing an Aggregate View on the Results of Audit Firm Inspections
- Interactions – the nature and quality of the various interactions between involved stakeholders e.g. auditors, management, those charged with governance and regulators during the audit process
- Context – the legislative and regulatory environment within which the audit operates. The impact of the financial reporting framework and corporate governance on financial reporting quality also give context to the audit.

However, the IAASB's framework does not present a definition of audit quality or or not provide AQIs.

3. Research Questions and Survey Design

Based on the indicators included in the papers presented above, that are relevant for evaluating the effectiveness of the system of the quality control developed in the accountancy firms, the research question of the study was: *The Romanian professional accountants and auditors, in small and medium practices, have information for developing a set of indicators which evaluates the effectiveness of the firm's SQC?*

With the purpose to test this hypothesis, the empirical data are collected based on a survey sent to the most important social media groups, where are registered more than 10.000 members, most of them certified as accountants or auditors, members of CECCAR or CAFR.

The survey instrument was prepared and send using www.docs.google.com and the responses was received in the same way. The professional accountants were asked to offer information regarding the quality control policies and procedures, the existence and the appliance of the SQC at the firm level, and also, to identify whether there exists information for the SQC assessment and could be developed indicators about the quality of the engagement.

The design of the questionnaire uses the multiple response for closed ended questions and the participants need to express the agreement ratings on a 5-point Likert scale ranging from 1 (strongly disagree/never), 2 (disagree/rarely), 3

(undecided/every once in a while), 4 (agree/sometimes), 5 (strongly agree/almost always).

The questionnaire consisted of 10 questions formulated in the Romania language to minimize misinterpretations from the respondents and to increase the reliability of the empirical study. In order to design the questionnaire, as well as increase reliability and ensure that the questions included in the questionnaire were in conformity with the study's purpose of investigation, the authors have led first a pilot test. The pilot test was completed by certified accountants and auditors during the professional courses conducted by the professional bodies. To test the questionnaire in practice, the questionnaire also was administered to different professionals, accountants and auditors, via electronic mails.

Based on the CAQ proposal for a set of AQIs, the questions were formulated in order to cover qualitative and quantitative information about the key elements of the SQC developed by the firm:

I. Firm Leadership and Tone at the Top - how the firm's tone at the top influences and reinforces audit quality at the engagement level.

Q1: The firm's Tone at the Top influences and reinforces audit quality at the engagement level.

II. Engagement Team Knowledge, Experience, and Workload – intend to determine that, collectively, the engagement team has the appropriate experience and competencies, and that specialists are engaged, as needed.

A. Knowledge and Experience of Key Engagement Team Members

Q2: The engagement team's members have the appropriate experience and competencies?

Q3: Are engaged specialist whether in the engagement there is needed?

Q4: Are measured, for all key members of the engagement team, the years of experience (on the engagement, in industry, in firm, in profession)?

B. Audit Firm Training Requirements

Q5: The firm considers the relevant training requirements for the key engagement team members?

Q6: For the highly specialized industry the firm has an approach regarding to determine the special knowledge and to obtain them by industry training courses or external industry professional conferences?

C. Allocation of Resources

Q7: The human resources are allocated by engagements based on the specialization and the prior experience?

D. Key Engagement Team Members' Workloads

Q8: The engagement team have appropriate time to perform any kind of work, and also, there is time enough for review and supervise the activity?

III. Monitoring

A. Internal Quality Review Findings

Q9: There are internal inspection for reviewing the control quality system, and as result of the findings are procedures modified?

B. Accountancy Organization Inspection Findings

Q10: The firm was the subject of the professional body inspection, and for the identified deficiencies were undertaken plans of remediation, including changes in the firm's system of quality control?

4. Results

The survey was administrated to a wide variety of accountants and auditors who works in small and medium practices. A total of 105 responses were obtained. The demographic profile is as follows: 56 percent of the sample are men, 63 percent were having bachelor degree education, 27 percent were having master degree education and 15 percent having a PhD, 67 percent have professional certification as chartered accountant, 25 percent have certification in auditing and 13 percent have certification as tax consultant.

Table 1 shows descriptive statistics of the responses, which describes professional accountants and auditor's perceptions regarding the variables used in the analyses. The results interpretation it is about the values of the mean, standard deviation, median and mode.

Table 1. Descriptive statistics—professional accountants and auditors' perceptions (N = 105)

| Descriptive statistics | Q1 | Q2 | Q3 | Q4 | Q5 | Q6 | Q7 | Q8 | Q9 | Q10 |
|------------------------|----------|----------|----------|----------|----------|----------|----------|----------|----------|----------|
| Mean | 4,12381 | 2,67619 | 2,190476 | 1,6 | 1,485714 | 2,857143 | 2,180952 | 3,571429 | 1,704762 | 3,847619 |
| Standard Error | 0,109691 | 0,093267 | 0,088842 | 0,062897 | 0,082447 | 0,087107 | 0,09832 | 0,110657 | 0,082235 | 0,108925 |
| Median | 4 | 3 | 2 | 2 | 1 | 3 | 2 | 4 | 2 | 4 |
| Mode | 5 | 3 | 2 | 2 | 1 | 3 | 2 | 4 | 1 | 4 |
| Standard Deviation | 1,123997 | 0,955704 | 0,91036 | 0,644503 | 0,844829 | 0,892582 | 1,007481 | 1,133893 | 0,842658 | 1,116149 |
| Sample Variance | 1,26337 | 0,91337 | 0,828755 | 0,415385 | 0,713736 | 0,796703 | 1,015018 | 1,285714 | 0,710073 | 1,245788 |
| Kurtosis | 1,831019 | -0,31938 | 1,025139 | 7,203738 | 5,840166 | -0,07386 | 0,363368 | -0,2003 | 3,117409 | 0,318577 |
| Skewness | -1,53242 | 0,222804 | 0,779821 | 1,704732 | 2,288943 | 0,70045 | 0,834623 | -0,6644 | 1,492554 | -1,00384 |
| Range | 4 | 4 | 4 | 4 | 4 | 4 | 4 | 4 | 4 | 4 |
| Minimum | 1 | 1 | 1 | 1 | 1 | 1 | 1 | 1 | 1 | 1 |
| Maximum | 5 | 5 | 5 | 5 | 5 | 5 | 5 | 5 | 5 | 5 |
| Sum | 433 | 281 | 230 | 168 | 156 | 300 | 229 | 375 | 179 | 404 |
| Count | 105 | 105 | 105 | 105 | 105 | 105 | 105 | 105 | 105 | 105 |

Source: For the statistical analysis of the collected data was used Microsoft Excel - Analysis Data package

In this study, we received 105 individual responses, and the mean's values for each of the question is presented in the Figure 1.

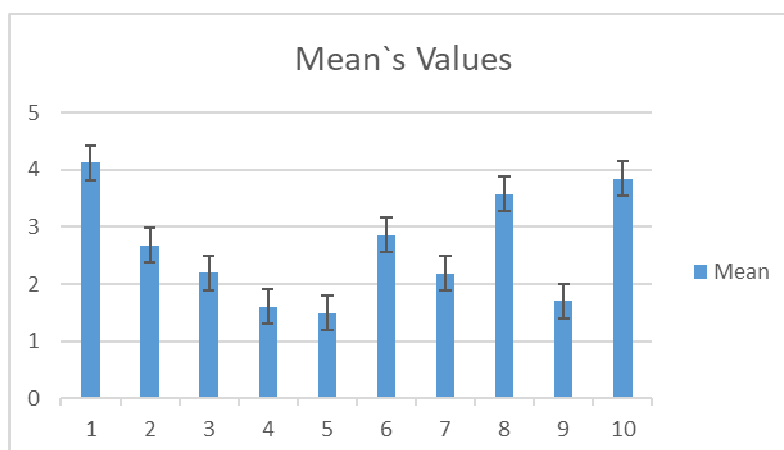


Figure 1. Mean's values for professional accountants responses

Source: For the statistical analysis of the collected data was used Microsoft Excel - Analysis Data package

Table 2. Indicators used to evaluate professional accountants and auditors' perceptions (N = 105)

| No. Q | Spec | Z | % | CV | Top Box | Top 2Box | Agree | Net Top B |
|-------|------|----------|-------|-------|---------|----------|-------|-----------|
| Q1 | 4 | 0,110151 | 54,4% | 27% | 46,7% | 81,9% | 81,9% | 40,0% |
| Q2 | 4 | -1,38517 | 8,3% | 36% | 2,9% | 19,0% | 19,0% | -6,7% |
| Q3 | 4 | -1,9877 | 2,3% | 41,6% | 2,9% | 5,7% | 5,7% | -19,0% |
| Q4 | 4 | -3,7238 | 0,0% | 40,3% | 1,0% | 1,9% | 1,9% | -43,8% |
| Q5 | 4 | -2,97609 | 0,1% | 56,9% | 1,9% | 4,8% | 4,8% | -63,8% |
| Q6 | 4 | -1,28039 | 10,0% | 31,2% | 5,7% | 21,0% | 21,0% | 4,8% |
| Q7 | 4 | -1,80554 | 3,5% | 46,2% | 2,9% | 11,4% | 11,4% | -22,9% |
| Q8 | 4 | -0,37796 | 35,3% | 31,7% | 21,0% | 60,0% | 60,0% | 14,3% |
| Q9 | 4 | -2,72381 | 0,3% | 49,4% | 1,9% | 2,9% | 2,9% | -45,7% |
| Q10 | 4 | -0,13652 | 44,6% | 29,0% | 30,5% | 74,3% | 74,3% | 25,7% |

Source: For the statistical analysis of the collected data was used Microsoft Excel - Analysis Data package

To find more meaning of the responses to the closed ended rating scale data and to make it more interpretable, after the descriptive statistics, and the calculation of the mean and the standard deviation, another 5 indicators could be calculated:

1. The percent of the agrees (the percent of respondents who choose 4 or 5);
2. Top Box (the percent of respondents who choose 5) and Top 2Box scoring (equal with the percent of the agrees);
3. Net Top Box (from number of respondents who choose 5 subtract number of respondents who choose 1);
4. Z-Score to Percentile Rank - converts the raw score into a normal score: $Z = (\text{Mean} - \text{Spec.}) / \text{Standard Deviation}$;

5. Coefficient of Variation (standard deviation is divided by the mean, higher values indicate higher variability, which indicates inconsistent attitudes).

The responses are interpreted through the agreement ratings, based on the 5-point Likert scale ranging (where 5 – almost always; 4 – sometimes; 3 - every once in a while; 2 – rarely and 1 – never), as follows:

R1: The firm's Tone at the Top influences and reinforces audit quality at the engagement level **sometimes/almost always**.

R2: The engagement team's members have the appropriate experience and competencies **every once in a while**.

R3: When in the engagement there are needed specialists, they are **rarely** engaged.

R4: The years of experience (on the engagement, in industry, in firm, in profession) are **rarely** measured for all key members of the engagement team.

R5: The firm **never** considers the relevant training requirements for the key engagement team members.

R6: For the highly specialized industry the firm has **rarely** an approach regarding to determine the special knowledge ant to obtain them by industry training courses or external industry professional conferences.

R7: The human resources are **rarely** allocated by engagements based on the specialization and the prior experience.

R8: The engagement team **sometimes** have appropriate time to perform any kind of work, and also, sometimes there is time enough for review and supervise the activity.

R9: There are **rarely or never** internal inspection for reviewing the control quality system, and as result of the findings are procedures modified.

R10: The firm was **sometimes** the subject of the professional body inspection, and for the identified deficiencies were undertaken plans of remediation, including changes in the firm's system of quality control.

5. In conclusion

The aim of this paper was to identify whether the professional accountants and auditors, who works in small and medium practices, are looking to get the information that can build a set of indicators, relevant for evaluating the effectiveness of the system of the quality control, developed in the accountancy firms.

The empirical analysis indicates that Romanian accountants and auditors, who works or as sole practitioners, or in small and medium firms, are not yet prepared to develop such a system of indicators for the SQC's assessment, because all the necessary information are or rarely or even never obtained, and just too few of them, are sometimes issued.

Throughout this paper we have shown that just the existence of a SQC, it is not enough to prove its efficiency.

The practical implications of this study aware the accountants and auditors to become more preoccupied by the SQC's effectiveness assessment, to have in intention to develop a set of indicators with this purpose.

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