

QUALITY ASSESSMENT OF AUDITS CARRIED OUT AT COMMERCIAL BANKS

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Abstract: This article is devoted to the significance of quality assessment of audits carried out at commercial banks and the essence of the quality standards. In addition, this article considers the views regarding carrying out external and internal audit and technique used for its assessment. Moreover, the article provides a comprehensive overview of the foreign experience regarding this issue.

Key words: Internal and external audit, audit quality, international auditing standards, quality assurance, assessment of the audit quality, financial reporting, verification of the quality of the financial statements' audit.

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Introduction. The peculiarities of carrying out audit at commercial banks in the Republic of Uzbekistan are determined by the Central Bank. According to the current legislation, audit activity at commercial banks is divided into internal audit and external audit. The difference between these two types can be classified as it follows:

1. If we analyze the factor of the audit object, external audit at banks implies the system of verifying consolidated financial statements, and internal audit is aimed at examining the banking performance and its management features;
2. The external audit is intended to provide an overview of financial statements for the needs of external users, as well as the auditor's conclusions, which include assessing the reliability of the financial statements and approving compliance of their indicators, and the internal audit enables to ensure that the commercial bank properly executes its functional responsibilities as well as to supervise bank's performance;
3. If we consider the factor of audit rules and procedures, when carrying out external audit, international financial reporting standards (IFRS) constitute the basis for compiling international auditing standards and auditor's reports. In case of internal audit, auditors examine internal subdivisions of the bank and the audit evidence revealed in the result of the internal audit and internal audit standards established by the internal audit department constitute that basis;
4. If we analyze the factor of the activity type, when carrying out external audit, the basis is represented by the financial and economic activities of the bank and financial statements reflecting these financial and economic activities. In case of the internal audit, it is the performance aimed at assessing the management of the Executive Board of the Bank and internal control services;
5. If we consider the factors of the work, in case of external audit the scope of activities is determined by auditors with the account of the rules and regulations of the international audit, and in case of the internal audit it is the implementation of the approved plan and specific tasks approved by the Council of the Bank;
6. If we analyze the factors of the auditor's fees, in case of the external audit auditors are paid for their activities accomplished according to the contract concluded with the bank, and in case of the internal audit specialists engaged in internal auditing process are paid according to the bank's staffing schedule approved by the Council of the Bank.

Therefore, the necessity to pay a particular attention to the risks which may occur when auditing performance of commercial banks as well as the quality assurance of their activities remains one of the an urgent current issues.

Literature review. An adequate determination of the quality assurance of audit activities implemented when carrying out audit at commercial banks, thus, this fact necessitates the research of foreign experience regarding this issue.

According to the opinion of Gutzeit (2004) on quality assurance: quality services provided by an auditor and the quality of an auditor's report are the direct result of the auditor's professional skills and experience. From the point of view of Bychkova (2005), the quality of the audit will be determined when it complies with the audit standards and the cost of the audit service which also emphasizes the cost of the audit services. Meanwhile, according to the opinion of Pakhomov (2001), the quality of the audit is a compliance with confidential customers' needs. In his scientific paper, Karagoda (2016) has expressed the view that the audit company should establish the principle of quality assurance in its internal documents and this principle should cover every element of the audit. In addition, this principle should be reflected in the audit documentation and each employee of the audit company should be informed about the content of these documents. Moreover, each employee must be informed about the quality assurance guideline and its compulsory character must be specified in the job descriptions. Furthermore, employees of audit companies must be always aware of all documents regarding quality assurance as well as about any amendments made in these documents.

From the point of view of Jariglasova and Suglobov (2008), auditors should perform constant oversight over the quality of audit activities to maintain and develop their professional abilities. Consequently, each audit company should focus on the quality assurance process and appropriate strategy and ensure its compliance with international audit standards.

The main aim of implementing the quality assurance policy is the following:

- professional requirements, skills and competencies;
- tasks assignment;
- consulting;

- attracting and retaining customers;
- monitoring.

Moreover, currently it is crucially important to improve the quality of the audit services. Therefore, a comprehensive study of the quality assurance of audit from the theoretical point of view is imperative of our time. In this regard, it is required to research advanced experience in this field and to apply developed conclusions in terms of Uzbekistan.

Based on the literature review on audit issues it is possible to develop a wider definition of the audit process: “Audit is a complicated process that collects, evaluates the information and provides its conclusions based on the information processed and with the account of regulatory rules of the country. Audit is carried out by a person with a certain competence who possesses relevant qualifications and can independently perform as an auditor”.

Audit can be divided into different types by the following criteria: by the users of its information, by the requirements of the legislation, by the object of the audit (according to the business type of the company), by the aim, by the period of its performance and by the character of its verification. Thus, rendering quality services by an auditor and ensuring the quality of the auditor’s report can be considered as a direct result of the professional competencies and experience of auditors.

According to the opinion of Pakhomov (2001), “Quality is compliance with the hidden requirements of customers”, thus an auditor should offer its services at such level that fits to meet hidden requirements (wants) of customers.

Tuychiyev (2018) in his article revealed the significance of the internal audit and emphasized the importance of the internal audit in management. Another domestic scientist - economist Avlokulov (2018) also emphasized the importance of the audit in his article saying that financial results of the properly conducted audit facilitate determination of problems and working out certain measures to improve financial performance of the enterprise.

Having studied above-mentioned statements, it is obvious that if the quality assurance of the audit is improved it would be possible to conduct a continuous monitoring over the efficient performance of the quality assurance of the audit. This, in turn, promotes efficient organization of the audit and internal control system at banks and as a result, performance of the banking system as a whole.

The next crucial issue is the issue of evaluating the quality of auditors' performance in international and national standards. Regarding this issue, national auditing standard 5 (NAS 5) "Supervision of the quality of the auditor's performance" was developed in Uzbekistan in compliance with the requirements of international audit standards and is being applied in practice since January 1, 2000. The aim of this national auditing standard is to identify and determine the standards for auditing the quality of auditors' performance.

The process of supervision of the quality of the auditor's performance can be implemented in various forms:

- *Supervision of the performance of the assistants by the chief auditor* (a chief auditor should regularly oversee and direct the performance carried out by the assistants during the auditing process. The assistants should be notified of the auditor's responsibilities on accountability issues that may affect the nature, timing and extent of the auditor's procedures, the objectives of the processes that they are required to carry out.
- The assistants must be notified about the aims which must be achieved during auditing processes, their functional responsibilities, performance of the economic entities, the essence of the probable auditing processes, timing and framework within which the audit must be carried out and other important factors;
- *Supervision of the performance of auditors by the auditing company* (supervision of the performance of auditors by the auditing company is implemented through the following means, in particular: through discussion and verification of feasibility of the audit plan and audit programme, strict observance over organizational and ethical norms as well as after obtaining official auditor's report to ask another auditor of this audit company to verify the results with the customer free-of-charge);
- *External supervision* (external supervision is exercised by the public authorities as stipulated by applicable laws and regulations).

According to international requirements, the International Standard on Quality Control (ISQC-1) covers the responsibility of the audit company to carry out audit of financial statements and the quality control system for their review, expressing confidence and related service agreements.

ISQC-1 is aimed at providing assistance to the audit companies in the following areas:

- perceiving the necessity of what is implemented; and
- decision-making resulted from the necessity of implementing more activities to achieve the aim set.

The aim of the audit company is to comply with quality control procedures that enable it to exercise reasonable assurance at the level of agreement:

- (a) Carried out audit should comply with professional standards and relevant requirements of the legislation and regulatory authorities; and
- (b) Should comply with the auditor's report or auditor's conclusion.

In general, considering the elements of the quality control system it should be noted, that audit company should establish a quality control system including such policies and procedures, which focus on the following elements, in particular:

- (a) The responsibility of the audit company management for the quality;
- (b) Appropriate ethical requirements;
- (c) Establishing relations with customers, as well as accepting and continuing these relations;
- (d) Human resources;
- (e) Executing agreements;
- (f) Monitoring.

Analysis and results. An audit company must formalize its policies and procedures and convey them to inform its employees. In addition, it is important to encourage auditors to express their views or concerns about the issues of quality control.

Moreover, it is crucial to encourage quality-based in-house culture, since it is essential for the audit company to establish strict requirements for achieving high quality in its business strategy in all its agreements and contracts. Encouraging such in-house culture includes the following aspects:

1. With the aim of demonstrating the particular responsibility regarding quality issues, it is necessary for the audit company to elaborate strategies and procedures directed to the evaluation of the company's employees, providing them with fringe benefits and opportunities for promotion (including incentive systems);
2. Sufficient resources should be provided to develop, formalize and maintain quality assurance policies and procedures.

There are also some ethical requirements determined for auditors. To achieve this aim, an audit company should develop policies and procedures in terms of ethics and moral behaviour that should strictly be observed by the audit company and its staff.

Herewith the company may use Specialized Code designed to determine ethical requirements for audit companies. In particular, this Code determines ethical and moral principals of the professional behaviour, such as:

- (a) Impartiality;
- (b) Fairness;
- (c) Professional competencies and skills;
- (d) Keeping privacy;
- (e) Professional integrity.

These principles can be strengthened through the following aspects:

- Leadership of the audit company;
- Education and training courses;
- Monitoring;
- Considering the cases of non-observance.

In addition, certain requirements have been determined for the fairness of the reviewer of the quality control. In particular, an auditor should determine in his agreement/contract the following requirements for reviewers of quality control:

- A reviewer is not selected by the contract partner;
- During the review period he (reviewer) does not participate in other contracts/agreements;
- Does not participate in decision-making by contracts or agreements.

Moreover, specific requirements have also been set up to the following aspects, in particular:

- Accomplishing consolidation of files of the last agreement;

- Keeping privacy of the agreement documents, maintaining their security, as well as observing impartiality, possibility to use and process these documents;
- Keeping the agreement documents;
- Monitoring.

In compliance with the Regulations “On the requirements set by the Central Bank to the internal audit of commercial banks” each bank must create the Internal audit unit as well as to develop and put into operation “Regulations on the internal audit service”, “Procedures and processes of carrying out internal audit” and “Guideline of the Chief auditor job position” approved by the Council of the Bank.

According to the Resolution of the President of the Republic of Uzbekistan № PR–4848 “Further activization of entrepreneurship activities, comprehensive protection of private property and improving the quality of business environment” there is a necessity of enhancing auditors’ responsibility regarding services offered and reliability of the auditors’ reports. In addition, the legal framework for audit activities has been complemented by the Resolution of the President of the Republic of Uzbekistan №PR–3946 “On measures for further development of audit activities in the Republic of Uzbekistan” which tackles the issues of particular importance of ensuring quality of audits performed.

With the aim of improving the quality of the quality assurance of audit companies and rating assessment technique, as well as applying and analyzing practical aspects of international auditing standards in practice it is recommended to hold workshops or training courses with participation of representatives of international audit agencies.

Table 1

Analysis of the shortcomings revealed in the accounting practice

№	Branch				
		Significant drawbacks in the reports	Number of auditors	Number of experiences auditors (with working experience)	Term of audit

				over 5 years)	
1.	Olmazar	304	4	0	18
2.	Okhangaran	164	6	1	24
3.	Tashkent region	146	4	0	18
4.	Fergana	117	5	1	23
5.	Kokand	164	4	0	18
6.	Jizzakh	489	6	2	26
7.	Chilonzar	1117	4	1	19
8.	Yunosabad	355	4	1	21
9.	Mirabad	540	4	0	17
10.	Yashnaabad	88	4	0	17
11.	Shaykhontaxur	116	7	2	26
12.	Nukus	366	7	2	28
13.	Chirchik	525	6	2	25
14.	Surhandarya	538	7	2	28
	Total	5039	72	14	308

We will carry out analysis on the basis of the data presented in this table. According to the table, shortcomings by accounting have been accepted as the basic factor. Number of auditors, number of experienced auditors and term of audit are accepted as depending factors.

If we carry out correlation analysis we can see the following data:

	Accounting	Number of auditors	Number of experienced auditors (with working experience over 5 years)	Term of audit
Accounting	1			
Number of auditors	0,687524	1		
Number of experienced auditors (with working experience over 5 years)	0,857454	0,882207	1	
Term of audit	0,756348	0,956418	0,946582114	1

As it is obvious from the table that there is solid relationship between factors so it is advisable to continue the analysis.

When performing regression analysis we can witness the following results:

Conclusion
of results

Regression statistics

Multinomial R	0,67822967				
R-square	0,459995485			0,459995485	
Standardized R-square	0,297994131				
Standard deviation	231,8230952				
Observations	14				
Variable analysis					3,708264819
	df	SS	MS	F	Value F
Regression	3	457793,4541	152597,818	2,839454565	0,091978132
Residual	10	537419,4745	52741,94745		
Total	13	995212,9286			

	Coefficient	Standard deviation	P-value	Lower 95%	Upper 95%	Lower 95%	Upper 95%
Y-intersection	2287,065688	949,9094294	2,409950436	0,03668647	172,5409077	172,5409077	4401,593469
Variable	-	175,7538456	-	0,615631686	-	-	300,5393316
X ₁	94,06464011		0,518137397		482,6686119	482,6686119	
Variable	622,2554158	234,5209102	8,653304625	0,024175536	99,71026413	99,71026413	1144,800567
X ₂							
Variable	-	79,54938669	-	0,26186235	-271,84072	-271,84072	82,65343833
X ₃	94,59364081		1,189118417				
			2,228138852				

According to the results of analysis, correlation coefficient R (or r_{xy}) is equal to 0,678.

According to the Chaddock's scale the relation is considered to be tight.

Thus, we can make a conclusion that change of the factors of impact can influence the shortcomings in the accounting to the great extent.

Correlation coefficient is equal to the significance value $t_r=2,839$. According to the regularity of Fisher distribution we are determining the table value (FRASPOBR (0,05;B12;B13)), and the

result equals to $t_f=3,708$. Significance of the determined regression parameters according to Student's distribution the table value looks like $t_{s(0,05;B13)} = 2,228$

We are comparing correlation coefficient with the table value:

$$t_r > t_f$$

Inequality is approved so correlation relationship is significant.

The next stage is devoted to compiling equation $(y = a_0 + a_1x_1 + a_2x_2 + a_3x_3)$ that is $y = a_0 + a_1x_1 + a_2x_2 + a_3x_3$. To compile the equation the following parameters (coefficients) a_0, a_1, a_2, a_3 are found.

We will carry out regression analysis via Excel software and we have found values of a_0, a_1, a_2, a_3, a_4 , they constitute: $a_0 = 2287,06$

$$a_1 = -91,06$$

$$a_2 = 622,25$$

$$a_3 = -94,59$$

General view of the regression equation looks like the following:

$$y = 2287,06 - 91,06x_1 + 622,25x_2 - 94,59x_3$$

So, it is possible to say that determined parameters a_0, a_1, a_2, a_3 are quite significant. In conclusion it should be noted that if at banks the number of auditors, the number of experienced auditors (with working experience over 5 years) as well as the term of the audit (x_1, x_2, x_3) increases by 1, we can witness average increase of 2287,06 of shortcomings by accounting. a_0 illustrates the impact of other factors on the bank profitability.

Adequacy of the regression equation can be checked with the help of determination coefficient R^2 .

Adequacy of the regression equation can be checked with the help of determination coefficient.

$$R^2 = 1 - \frac{\sum(y_i - y_x)^2}{\sum(y_i - \bar{y})^2} = 0.678$$

$$r^2 = 0,678^2 = 0,459$$

It is obvious that the determination coefficient equals to the square of the correlation coefficient. This factor justifies the accuracy of the compiled regression and straight linear correlation.

With the help of the elasticity coefficient we are determining the case if the impacting factor increases by 1 per cent, how much the effective factor will go up.

The elasticity coefficient is determined through the following formula:

$$E=a_1 \frac{\bar{x}}{\bar{y}} = -91,06 * 5,1 / 359,9 = -1,3 \quad (\text{case X1})$$

$$E=a_2 \frac{\bar{x}}{\bar{y}} = 622,25 * 1 / 359,9 = 1,7 \quad (\text{case X2})$$

$$E=a_3 \frac{\bar{x}}{\bar{y}} = -94,59 * 22 / 359,9 = -5,8 \quad (\text{case X3})$$

In case 1 if the impacting factor - the number of auditors - changes by 1 %, effective factor by the shortcomings revealed in the accounting, demonstrates 1,3% reduction.

In case 2 if the impacting factor - the number of experienced auditors (with working experience over 5 years) - changes by 1%, effective factor by the shortcomings revealed in the accounting, demonstrates 1,7% increase.

In case 3 if the impacting factor - the term of the audit - changes by 1%, effective factor by the shortcomings revealed in the accounting, demonstrates 5,8% reduction.

The analysis of the elasticity coefficient indicates that shortcomings revealed by accounting practice depend not on the number of auditors and the audit period, but rather on the number of qualified auditors. The main reason for this is the fact that account shortcomings happened mainly due to the input of information into computer programs. To solve this problem it is necessary to employ qualified auditors because auditors who do not have enough relevant experience may not find these shortcomings. As a result of the above-stated correlation and regression analysis, we can conclude that the general auditor should have an independent approach to the objects to be inspected by auditors.

According to the following model developed by the commercial banks in Uzbekistan as a result of a regression analysis based on the data of commercial bank Ipoteka Bank, it is possible to

make a conclusion that if the share of the loan portfolio in the branch is big, the number of auditors sent by the general auditor and the term of the audit should be reconsidered.

In particular:

$$y = -8\,411,96 + 157,59x_1 - 1\,140,59x_2 + 445,76x_3$$

Here:

y – number of shortcomings by lending;

x_1 – number of auditors;

x_2 – number of qualified auditors (with working experience over 5 years);

x_3 – term of the audit;

If the share of accounting practice at the bank branch is large, it should reconsider the number of auditors sent by the chief auditor and audit terms. In particular:

$$y = 2\,287,06 - 91,06x_1 + 622,25x_2 - 94,59x_3$$

Here:

y – number of shortcomings by accounting practice;

x_1 – number of auditors;

x_2 – number of qualified auditors (with working experience over 5 years);

x_3 – term of the audit;

In the research process, interpretive research method has also been used.

Conclusion. So, as a result of quality control of the audit, we can find the answer to the following questions:

- if it is any positive impact of introducing audit monitoring into quality control of the audit on the bank's performance?
- if interrelations between the Audit Department and the Audit Committee can be considered as satisfactory and meeting appropriate requirements? the aim of raising this question is that the Audit Department is directly supervised only by the Audit Committee and this fact will enable to determine the degree of how well is the Audit Department supervised.

There has been held an interview with the Chief auditor of the bank and all auditors on the issue of introducing a single assessment technique.

As a result, all auditors have confirmed the necessity of working out a clear guideline for the assessment system.

When having an interview with the Chief auditor of the bank he has confirmed the necessity of developing the unified guideline for all auditors which will reflect precise requirements for the documentation submitted, as well as the assessment technique which must be used in the audit process. In the opinion of the Chief auditor, availability of this guideline will positively impact overall operating process of the bank. This means that currently it is necessary to introduce based on a specific formula the assessment technique which will be single for all banks and which can be used simultaneously and timely to evaluate all aspects of auditors' activities.

In addition, during the interview it has been determined that other regulatory documents would not be an obstacle when applying a single assessment system for all banks in accordance with a specific standard document, since there is no requirement in any statutory act that prevents auditors' assessment. Moreover, it has been noted that the implementation of a particular program in practice would not cost much. This assessment system does not adversely affect other sections.

The factors influencing the efficiency of internal audit in banks have also been analyzed. It has been emphasized the accuracy of assessing the relationship between the audit department of the bank and the audit committee.

In doing so, interviewees and auditors of the audit department confirmed that these two key factors were the most important. In addition, the auditors in the internal audit department do not have the unified assessment principle in banks, whereas auditors have emphasized the need to include the single assessment principle for banks.

The current state of relations between corporate governance authorities, particularly the Audit Committee and the Audit Department, revealed that the relationship between them had no impact on the quality of the audit department.

In general, the audit committee is the authority which supervises the audit department in banks, but the relationship between them is limited to reporting and data exchange.

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