

# State control as an instrument for financial regulation of the market of audit services

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**Abstract**—This paper is dedicated to the regulation of activities in the audit market at the stage of forming the foundations of the digital economy, and a set of measures to control and improve the quality of audit activities in general. We review the issues of regulation of the market of audit services by a number of regulatory acts, and the performance of audit organizations to be checked and monitored by state bodies and public organizations, where the control functions are carried out by the Ministry of Finance of the Russian Federation, the Audit Council, the self-regulating organizations of auditors, and the Federal treasury.

**Key words**—*audit services market, audit activities, external assessment of improving the quality of audit services, results of planned external assessment of audit services, self-regulating organizations of auditors, impact measures based on audits of market quality of audit services, Audit Council, digital economy, anti-corruption.*

## I. INTRODUCTION

Audit as an activity over the past decade has undergone significant changes both in methodological and in practical aspects [5, 6]. The conditions for the functioning of the systems and the requirements for organizing an audit service are currently being modernized and changed [8, 14].

In the context of globalization of world processes and the pursuit of mass digitalization of the financial economy [4], auditing services as a whole more often act not as an independent business, but as a tool and an indicator of the state of economic processes in general.

The issues related to ensuring the quality of audit results are becoming increasingly important [11]. A preventive procedure in the complex of measures taken to improve the quality of audits to reduce risk can be, on the one hand, reforming legislation and adopting international auditing standards from a legislative point of view that is regulating auditing activities as a whole [10], and on the other hand increasing the responsibility for the result of audit services [12].

## II. METHODS

The methodological approach to research is determined by the current state of economic, institutional and applied management knowledge.

The research of the object and the analysis of the results of the measures taken are based on the use of general scientific methods and techniques, namely, empirical research methods, such as observation, comparison, and

measurement. Among the general logical research methods, we have used analysis, synthesis, and systematic approach.

State control over the activities of the audit market is carried out in accordance with the Federal Law “On Auditing” No. 307 [1], International Standards on Auditing [3] adopted by the International Federation of Accountants and recognized as applicable in the Russian Federation in the manner established by the Government of the Russian Federation, the Rules of Independence of Auditors and Auditing Organizations<sup>1</sup> and the Code of Professional Ethics of Auditors<sup>2</sup>.

The tasks of the Ministry of Finance of Russia are: to develop a state policy in the field of auditing, to adopt regulations governing auditing, to maintain the state register of self-regulating organizations of auditors and a control copy of the register of auditors and auditing organizations of self-regulating organizations of auditors, to analyze the state of the market of auditing services in the Russian Federation, to perform state control (supervision) of the activities of self-regulatory organizations of auditors, and other functions [15].

The Federal Treasury is in charge of carrying out external quality control (hereinafter - EQC), independent of the auditing profession, of audit organizations conducting a mandatory audit of the accounting (financial) reporting of socially significant clients [1]<sup>3</sup>.

Self-regulating organizations of auditors – non-profit organizations created on the terms of mandatory membership of auditors and auditing organizations in order to ensure the conditions for carrying out audit activities – act as public organizations controlling activities in the auditing services market. At present, there are two self-regulatory organizations of auditors in the Russian Federation: “Russian Union of Auditors” (the Association) and the Association “Commonwealth”.

Supervisory activities in the sector are carried out on the basis of the distribution of audit subjects according to the levels of possible risk (results of the analysis of the activities of subjects, the EQC of subjects, the assessment of their activities by the Federal Treasury and self-regulating organizations of auditors) [15]:

<sup>1</sup> Approved by the Audit Council on September 20, 2012, record number 6.

<sup>2</sup> Approved by the Audit Council on March 22, 2012, record number 4.

<sup>3</sup> “Socially significant” are organizations whose securities are admitted to organized trading, other credit and insurance organizations, non-state pension funds, organizations whose share in the authorized (share) capital is at least 25 percent, state corporations and companies, and public law companies.

- subjects of a significant risk level - audit organizations conducting a mandatory audit of the accounting (financial) statements of socially significant customers;
- subjects of a moderate risk level - audit organizations that do not conduct a mandatory audit of the accounting (financial) statements of socially significant customers;
- low-risk subjects - individual auditors.

This distribution allows us to pay increased attention to the supervised audit entities that have a significant level of risk of violation of the requirements of the law.

### III. RESULTS

The above-mentioned organizations carry out external control organization activities in order to improve the quality of the audit services market, however, we will focus on the activities carried out by the Federal Treasury responsible for the state control of the audit services market [15] (Table 1).

TABLE I. THE RESULTS OF EXTERNAL AUDITS OF THE QUALITY OF THE AUDIT SERVICES MARKET CONDUCTED BY THE FEDERAL TREASURY DEPARTMENT IN 2018.

Audit results	
<b>1. Violations of the requirements of the Federal Law "On Auditing," the Federal Law "On Banks and Banking," standards of auditing, the code of professional ethics of auditors</b>	
• Prescriptions on the elimination of violations identified as a result of an external quality audit	45
• Warnings on inadmissibility of violations of the requirements of the Federal Law "On Auditing", standards of auditing, rules of independence of auditors and auditing organizations, code of professional ethics of auditors	126
• Actions taken by the central office of the Federal Treasury	9
• Order on suspension of membership in a self-regulatory organization for a period of 90 calendar days	6
• Order on suspension of membership in a self-regulatory organization for a period of 60 calendar days	4
• Order on suspension of membership in a self-regulatory organization for a period of 30 calendar days	15
• Order on suspension of membership in a self-regulatory organization for a period of 180 calendar days	2
• The auditing organization is excluded from the Federal Treasury Plan on the grounds provided for by subparagraph "a" of clause 7 of the Rules for the preparation of annual plans for conducting scheduled inspections of legal entities and individual entrepreneurs by state control (supervision) and municipal control bodies, approved by the Government of the Russian Federation on July 30, 2010, No. 489	32
• Order to exclude information on an audit organization from the register of auditors and	8

audit organizations	
• Excluded from the self-regulatory organization of auditors and audit organizations	2
<b>2. The audit organization did not conduct a mandatory audit of the accounting (financial) statements of the organizations referred to in paragraph 3 of Article 5 of the Federal Law of December 30, 2008 No. 307-FZ "On Auditing Activity"</b>	
• The object of the audit was included in the Federal Treasury plan for the region of the Russian Federation on the basis of the data contained in the statistical reporting prepared by the audit organization	9
<b>3. No violations found</b>	2
<b>4. Minor violations found</b>	1
<b>5. Absence of a branch at the place of registration</b>	1
<b>TOTAL</b>	262

The Federal Treasury Department, assessing the external quality control of the audits, in addition to Federal Law No. 307 [1], is guided by the provisions and methodological recommendations for conducting audits, which set out the methods for conducting inspections, as well as possible risks and threats from unfair action (inaction) on the part of the auditing company. The results of the audit by this structural unit revealed a rather sad picture reflecting the quality of audit services in the market (Table 2).

After analyzing the data in the table, it is possible to notice an increase in the number of external scheduled inspections for the period from 2012 to 2018. At the same time, the range of audit organizations that fully comply with the requirements of federal legislation practically does not increase over time and varies in the range from 15.65 to 21.37 percent. Schematically, the dynamics are presented in Fig. 1.

The problem lies in the paradigm of now-changing legislation in the field of accounting and financial statements, transition to international auditing standards and their reform, as well as digitalization of the economy as a whole and the desire to improve the quality of auditing activities [10].

TABLE II. ANALYSIS OF THE DYNAMICS OF EXTERNAL AUDITS OF THE MARKET QUALITY OF AUDIT SERVICES CONDUCTED BY THE FEDERAL TREASURY DEPARTMENT IN THE PERIOD FROM 2012 TO 2018.

Year	Number of planned external audits	The number of audits after which actions were taken	Percentage of the audits with violations found	Percentage of audit organizations that carried out "quality" audits
2018	262	206	78.63	21.37
2017	272	224	82.35	17.65
2016	239	188	78.66	21.34
2015	237	191	80.59	19.41
2014	293	247	84.3	15.70
2013	293	240	81.91	18.09
2012	115	97	84.35	15.65

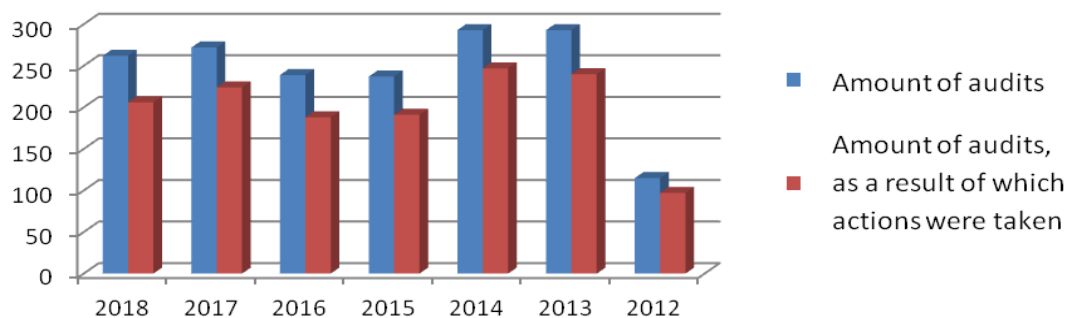


Fig. 1. Dynamics of external audits of the audit services market for the period from 2012 to 2018.

#### IV. CONCLUSION

The analysis of ways to influence audit organizations based on the results of scheduled inspections on external quality control of the services demonstrated a negative trend: 27 protocols were issued for suspension of membership in SROA in 2018 compared with previous periods; their share increased and amounted to 13.11%, which exceeds the figure for 2017 (8.93%) in absolute terms by 4.18%. Even such a serious measure as a revoke of membership in SROA does not help to change the situation, since its use remained at the same level in absolute terms and amounted to 3.57% in the total share of actions taken (Table 3).

In 2018, the Federal Treasury continued the practice of conducting control procedures, with respect to both audit organizations and their branches operating in the territories of several constituent entities of the Russian Federation (Table 4). Such complex audits allow us to give a comprehensive assessment of the activities of each branch of the controlled entities and to compile objective data on the presence (absence) of the quality differentiation of the services provided by the audit organization.

According to the results of the inspections conducted by the EQC, the total amount of actions taken against joint-stock companies in 2018 was 206 (among which 19 were issued based on the results of inspections during 2017) including:

- 126 warnings of audit organizations on the inadmissibility of violation of the requirements of the Federal Law "On Auditing", standards of auditing, rules of independence of auditors and auditing organizations, the code of professional ethics of auditors (61.17% of the total number of decisions made on the application of actions taken);

TABLE III. ACTIONS TAKEN BASED ON THE RESULTS OF PLANNED INSPECTIONS BY THE FEDERAL TREASURY FOR EXTERNAL QUALITY CONTROL OF AUDIT SERVICES FOR THE PERIOD FROM 2012 TO 2018.

Year	Orders binding to eliminate violations	Orders on inadmissibility of violations of requirements	Suspension of membership in SROA	Revoke of membership in SROA
2018	45	126	27	8
2017	46	150	20	8
2016	44	120	13	11
2015	34	149	5	3
2014	28	209	5	5
2013	27	181	22	10
2012	9	81	5	2

- 45 regulations requiring auditing organizations to eliminate violations of auditing rules identified as a result of external audits (21.84%);
- 27 orders addressed to self-regulating organizations of auditors (hereinafter referred to as SROA) on suspension of membership in an audit organization (13.11%);
- 8 orders to exclude information on an audit organization from the register of auditors and audit organizations, auditors in SROA (3.88%).

It should be noted that since 2015 the number of actions taken has been increasing in the form of orders addressed to SROA to suspend membership of an audit organization: if in 2015 these actions were taken against 5 audit organizations, then by 2018 the number of such actions has increased to 27.

Meanwhile, compared to 2017, in 2018, the number of actions taken in the form of warnings about the inadmissibility of violations of the requirements of the Federal Law "On Auditing", auditing standards, independence rules for auditors and audit organizations, the code of professional ethics of auditors has decreased (by 2.86% or 24 units). Despite the reduction in the number of warnings issued, this action still takes the largest share in the overall structure of the actions taken by the Federal Treasury (more than 60%) (Fig. 2).

TABLE IV. THE DYNAMICS OF THE SPECIFIC WEIGHTS OF THE ACTIONS TAKEN AS A RESULT OF PLANNED INSPECTIONS BY THE FEDERAL TREASURY FOR EXTERNAL QUALITY CONTROL OF AUDIT SERVICES FOR THE PERIOD FROM 2012 TO 2018.

Audit results	Specific weight, %						
	2018	2017	2016	2015	2014	2013	2012
Orders binding to eliminate violations	21.84	20.54	23.40	17.80	11.34	11.25	9.28
Orders on inadmissibility of violations of requirements	61.17	66.96	63.83	78.01	84.62	75.42	83.51
Suspension of membership in SROA	13.11	8.93	6.91	2.62	2.02	9.17	5.15
Revoke of membership in SROA	3.88	3.57	5.85	1.57	2.02	4.17	2.06
Actions taken, total	100.0	100.0	100.0	100.0	100.0	100.0	100.0

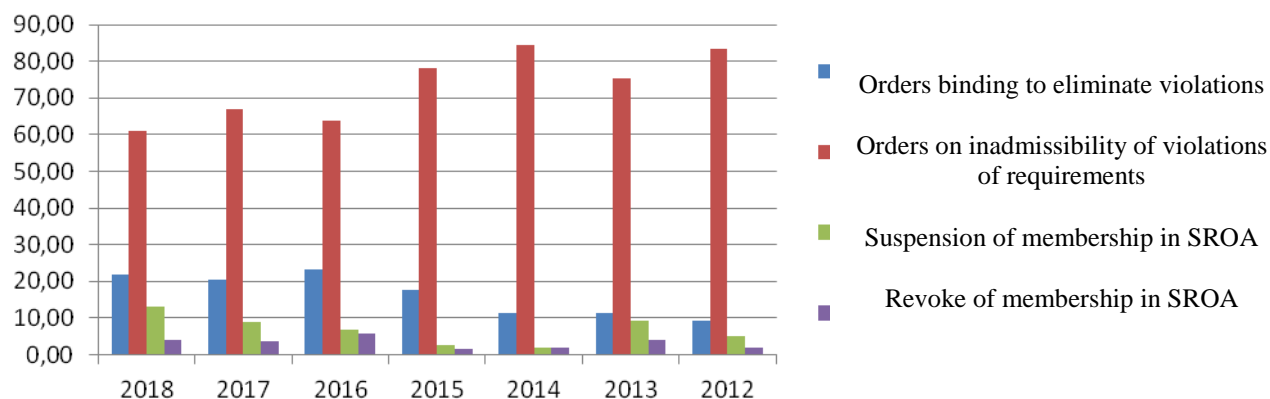


Fig. 2. Analysis of the structure of impact measures based on the results of audits of audit organizations

Thus, in a globalized economy, reforming and adopting international auditing standards, auditing has experienced a large number of key changes, but the professional community has managed to find the necessary balance and achieve a planned reforming of the audit market.

Currently, research results demonstrate an insufficient amount of measures taken to improve the quality of organization, conduct and results of audit services.

External audit quality control measures act as a sectoral assessment of the risks of legalization (laundering) of criminal proceeds and the financing of terrorism with the participation of auditors, which is the subject of further research.

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