

## **Inernal Control Of Quality Of Internal Audit**

PhD Abdieva Nargiza, *TFI, department of Audit and economic analysis*

Dr.oec Romena Sulce, *LLU, Head of department of internal audit*

PhD Murodova Dilnoza, *TFI, department of Banking*

### **Abstract**

*The article analyzes the provisions of international standards of internal audit in connection with the conceptual concepts of “internal evaluations” and “external evaluations”, assesses their similarity and difference, identifies areas for improving the quality of internal audit. The rules of internal audit in the Republic of Uzbekistan and the Republic of Latvia are compared.*

**Keywords:** *internal audit, internal control, risk based Internal Audit, quality of internal audit, Audit Committ*

### **INTRODUCTION**

In the context of the active development of economic relations, the role of internal audit is growing both in state institutions and in commercial enterprises. Internal audit as a key to successful enterprise management, the quality of this system increases the ability to increase the efficiency of the business entity. The requirements for the organization of this control are established by the International Professional Standards for Internal Auditing. The quality of the internal audit lies into the successful functioning and effectiveness of the internal audit service. But like in any system, in order to gain high quality of the internal audit, control of this system is required. The main objective of the quality control of internal audit is to ensure that the internal audit process meets specific requirements and is reliable, satisfactory and financially sound.

The aim of the study is to define the main criteria that determine the quality of the internal audit based on the study of the legislation of the European and Central Asian countries, such as Latvia and Uzbekistan.

The research problem is that, in many enterprises and institutions, methods are not defined and common requirements for monitoring and evaluating the quality of internal audit are not established.

The main purpose of evaluating the activities of the internal audit service (evaluating the quality of internal audit) is to determine the degree of effectiveness of both – the work of service and each auditor separately, as well as assessing how the activities of internal auditors comply with the requirements. Assessment of the work of the internal audit service is carried out to determine their strengths and weaknesses, and also forms the opportunity to improve the performance of internal audit services and, thus, allows:

- determine the effectiveness of the internal audit service and its employees;
- identify the need for advanced training of employees of the internal audit service.

As of January 1, 2020, more than 786 certified[16] internal auditors were operating in the Republic of Uzbekistan - 0.002% of the population (as of January 1, the population was 33905800 people[13]). In Latvia, this indicator is 190 people[12], about 0.01% of the country's population (as of January 1, the population is 1908100 people[11]). Determining the criteria for monitoring the quality of work of both - each internal auditor and the internal audit as whole, will ensure the quality of work and the responsibility of the auditor.

### **LITERATURE OVERVIEW**

Ioana Lupasc in its studies focused on the quality of internal control and audit in determining bank fraud: “The role of the internal auditor in detecting fraud depends on his training and practical skill and ability” [8].

Emilia VASILE in its studies considers the organization of the Audit Committee as the main criterion for the quality of internal control and audit by optimizing the quality of information provided to management based on the assessment, monitoring and control of internal control and audit

activities. One of the main conclusions is that internal auditors should have direct access to the audit committee for private negotiations with the audit committee, if necessary [6].

A study by Fedaa Abd Almajid Sabbar (2018) focuses on the relationship between corporate governance principles and the quality of internal audit. One of the main conclusions of the study is that the effective and proper implementation of the principles of corporate governance in companies will contribute to the improvement and development of the internal audit function and its effectiveness [10].

Oleg Kryshkin in his research focuses on organizing the “right” internal audit. “The right internal auditor should stimulate by his actions the management's choice of the optimal combination of risk and control, the optimal combination of two strategies”

Alina-Teodora CIUHUREAN argues that “One way to improve the internal control environment is to implement an effective integrity reporting mechanism.” In her studies, Alina-Teodora substantiates the need for an Audit Committee or the Audit Commission and studies the relationship with internal and external auditors [5].

## RESULT AND DISCUSSION

Speaking about the quality control of internal audit, attention should be paid to both - to quality control of each internal auditor and the internal audit service as a whole. In this article, we will consider the quality control of the work of these two components separately. Based on international standards of internal audit and regulatory acts of the Republic of Uzbekistan and Latvia.

The Republic of Uzbekistan is a rapidly developing Central Asian country. In 2019, Uzbekistan took 69th place in the Doing Business rating among 190 countries of the world, gaining 69.9 points out of 100[17]. Audit activities in the country are also rapidly developing. Based on the Decree of the President of the Republic of Uzbekistan “On Measures for the Further Development of Audit Activities in the Republic of Uzbekistan” dated September 19, 2018, the audit activity in the Republic from January 1, 2020 completely switches to the International Auditing Standards. The Decree also indicates measures to develop audit activities in the country. On internal audit, the provisions “Regulation on the Internal Audit Service at Organizations” and “Regulation on the Procedure for Certification of Internal Audit Service Staff” were adopted.

The Regulation of the Cabinet of Ministers of the Republic of Uzbekistan “On the internal audit service at enterprises” states that employees of the internal audit service must undergo annual certification. This is the only requirement that relates to the quality control of internal auditors.

Qualification requirements for internal auditors are also given:

The employees of the internal audit service must have at least two years out of the last ten years of practical work (including part-time) in accounting, auditing, financial or tax control, and must meet one of the following requirements:

- have a certificate of internal auditor;
- have a higher economic education obtained in higher educational institutions of the Republic of Uzbekistan or in educational institutions of a foreign state and in accordance with the legislation of the Republic of Uzbekistan recognized as equivalent to education in the Republic of Uzbekistan[2].

Latvia is one of the developing countries in Europe. It is in 19th place (data for 2019) out of 190 in the World Bank ranking on the ease of doing business in the country[15].

In 1999, Latvia joined the World Trade Organization, in 2004 - into the European Union. Latvia has a developed financial sector with a wide range of financial intermediaries serving most market segments. Commercial banks dominate the Latvian financial sector, and foreign credit institutions are actively present in it. Since Latvia is a member of the EU, it operates according to international standards.

The Law of the Republic of Latvia “On Internal Audit” provides the establishment of an Internal Audit Council, the tasks of which will be to promote the improvement of the quality of internal audit, as well as the introduction of audit policies and procedures and the development of audits in ministries and institutions. The Council of the State Audit Office approves regulations which govern the activities of the State Audit Office, takes decisions on approval of audit reports which are not approved by Audit Departments due to differences in opinion, as well as reviews other matters in accordance with its competency as stated in the State Audit Office Law. The Council is comprised of

the Auditor General and six members of the Council of the State Audit Office which act as directors of Audit Departments. The Auditor General recommends for approval by the Saeima the candidates for the office of member of the Council. Members of the Council are appointed for four years and may be approved to the office repeatedly, but no more than for two consecutive terms.

Audit departments perform audits in accordance with annual audit plan approved by the Council of the State Audit Office. Each department is comprised of the director of audit department and of audit sectors, heads of which are appointed by the Auditor General. Each audit department is comprised of heads of the sectors, senior state auditors, senior state auditors-lawyers, state auditors, state-auditors-lawyers and assistant state auditors. The director of the department and heads of sectors take decisions in respect of audit cases and allocation of audit work.

The aim of the Chancellery of the State Audit Office is to establish prerequisites to coordinated and optimal work of the institution, to provide performance of tasks of the State Audit Office as determined by the State Audit Office Law, by laws of the State Audit Office and other legal framework. The Chancellery consists of the Financial and Budget Planning Division, the Recordkeeping Division, the Information Technologies Division and the Maintenance Division.

The Quality Management and Planning Division, Policy Planning Project and Analysis Process Manager and Audit Result Analysis and Improvement Process Manager are directly subordinated to the Auditor General.

Head of the internal audit department:

1) is responsible for the organization of work of the structural unit and the implementation of the tasks assigned to it;

2) provides oversight of the quality of internal audit work.

As are the requirements for the internal auditor:

The internal auditor in his activities complies with the following ethical principles of a professional auditor:

1) ensures the use of knowledge, skills and experience in conducting internal audits;

2) carries out its work honestly, diligently and responsibly;

3) complies with the internal ethical principles of the ministry or institution;

4) they are not consciously involved in activities that discredit the profession of internal audit or internal audit;

5) respect the legal and ethical goals of the ministry or institution, contribute to their achievement;

6) do not use the information obtained during the audit in such a way that it can damage the legitimate goals of the ministry or institution;

7) during the audit, they evaluate all circumstances and evidence, without being affected by either their interests or the interests of others;

8) in the final audit report, all relevant facts about the audited system are disclosed[1].

The international standards of internal audit provide quality characteristics as:

1000 - Objectives, Powers and Responsibilities

1100 - Independence and Objectivity

1200 - Professionalism and professional attitude to work

1300 - Program for ensuring and improving the quality of internal audit

Consider all the above characteristics:

1. The goals, powers and responsibilities of the internal audit should be clearly defined in the regulations and also in the internal document of the enterprise. Of no less importance is the indication of the mandatory application of the Basic Principles of Professional Practice of Internal Audit, the Code of Ethics, Standards and the Definition of Internal Audit in the internal regulations.

2. Independence and objectivity is one of the main criteria for the quality of internal audit, since it is this characteristic that ensures the integrity and objectivity of the work of internal audit. Internal auditing is an independent, objective assurance and consulting activity designed to add value and improve an organization's operations. It helps an organization accomplish its objectives by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of risk management, control, and governance processes[14].

3. Professionalism and professional attitude to work - quality without which internal audit should not function.

Oleg Kryshkin in his studies gives clear examples of the difference between professionalism and non-professionalism of internal auditors as an example of a report and notes that the recommendations of the internal auditor should be clearly stated. “In the report, the internal auditor describes the shortcomings and suggests approaches to address them ... Depending on the level of professional training of the auditor, the recommendations can be both very detailed and practical (for example, a detailed description of the procedure) and very abstract (for example, masterpieces from the series “strengthen control” or “increase executive discipline”) The correct auditor should make every effort to minimize abstracts”[9]

Also, it should be noted that the professionalism of the internal auditor ensures the timely detection of errors and fraud. The role of the internal auditor in detecting fraud depends on his training and practical skills. [5]

4. The program to ensure and improve the quality of internal audit. In the regulations of both the first and second republics, the provision and improvement of the quality of internal audit is determined by qualification requirements and advanced training of 40 hours in 2 years (Table 1., The table is compiled by the authors)

### Regulation of internal audit in the Republic of Uzbekistan and the Republic of Latvia

№	Criteria	Republic of Uzbekistan	Republic of Latvia
1.	<b>Regulation of internal audit</b>	1. Regulation on the internal audit service at enterprises 2. Regulations on the procedure for certification of employees of the internal audit service	1. Law "On Internal Audit" 2. Procedures for the Certification of Internal Auditors
2.	<b>Certificate of internal audit issued</b>	1. Chamber of Auditors of Uzbekistan 2. National Association of Accountants and Auditors of Uzbekistan (NAAA) 3. Federation of Accountants, Auditors and Consultants of Uzbekistan (FAU).	The Latvian School of Public Administration (LSPA)
3.	<b>Qualification requirements for internal auditors</b>	At least 24 months out of the last ten years in accounting, auditing, financial or tax, and meet one of the following requirements: -have a certificate of internal auditor; -have a higher economic education -Certificate of special training courses (80 hours)	At least 24 months of professional experience conducting internal or external audits in a ministry or institution
4.	<b>Examination Procedure</b>	1) 60 test questions 2) at least 75% of the questions must be answered correctly 3) the exam is held for three astronomical hours.	1) 125 exam questions out of 500 2) at least 75% of the questions must be answered correctly 3) the duration of the exam is four astronomical hours
5.	<b>Exam questions</b>	-Internal Audit Management - Audit Management - Enterprise fraud risks and control procedures -Management system at the enterprise -Management principles and risk management -Organizational structure of the enterprise, business processes and risks	-The structure and operation of the State administration system of Latvia; -International standards -Types and systems of internal audit - Internal audit process; -Risks and risk management; -Internal control measures;

		<ul style="list-style-type: none"> <li>- Exchange of information at the enterprise</li> <li>-Information technology and business continuity enterprises</li> <li>-Financial accounting</li> <li>- Management</li> <li>- Accounting</li> <li>-Taxation</li> </ul>	<ul style="list-style-type: none"> <li>- Random methods;</li> <li>-Specific features of the audit environment in State administration;</li> <li>-Management of internal audit functions;</li> <li>-Financial planning and accounting of State administration</li> </ul>
6.	<b>Validity period of the certificate of internal auditor</b>	5 years	Dates not specified
7.	<b>Training requirements for internal auditors</b>	Take a continuing education course every year (20 hours)	Participate in continuing education events for at least 40 academic hours in two years.
8.	<b>Justifying reasons not to upgrade qualifications</b>	Not indicated in position	<ul style="list-style-type: none"> <li>-parental leave</li> <li>-work or study in foreign countries;</li> <li>-temporary incapacity to work (more than four continuous months within two years);</li> <li>-restrictions due to force majeure, unforeseen event or other exceptional circumstances (more than four continuous months within two years).</li> </ul>

Speaking about the quality of work of the internal audit service, it must be said that it is influenced by the presence of such factors as:

- qualification and experience of auditors;
- effective planning of internal audit;
- compliance by auditors with ethical professional standards;
- transparent internal audit report;
- stimulation of internal auditors, etc.

The foregoing factors can be attributed to factors that depend on the auditors themselves, but also factors that are independent of the auditors differ [6]:

- a strict corporate governance structure operating in the audited entity, including existing audit committees and supporting shareholders;
- a regulatory environment conducive to achieving audit quality.

Based on this, we offer a program to ensure and improve the quality of internal audit work. Based on international standards of internal audit, the quality assurance and improvement program should include both internal and external evaluations. In our opinion, internal and external evaluations should contain a number of criteria given in Fig. 1 (Figure compiled by the authors based on ISA.)

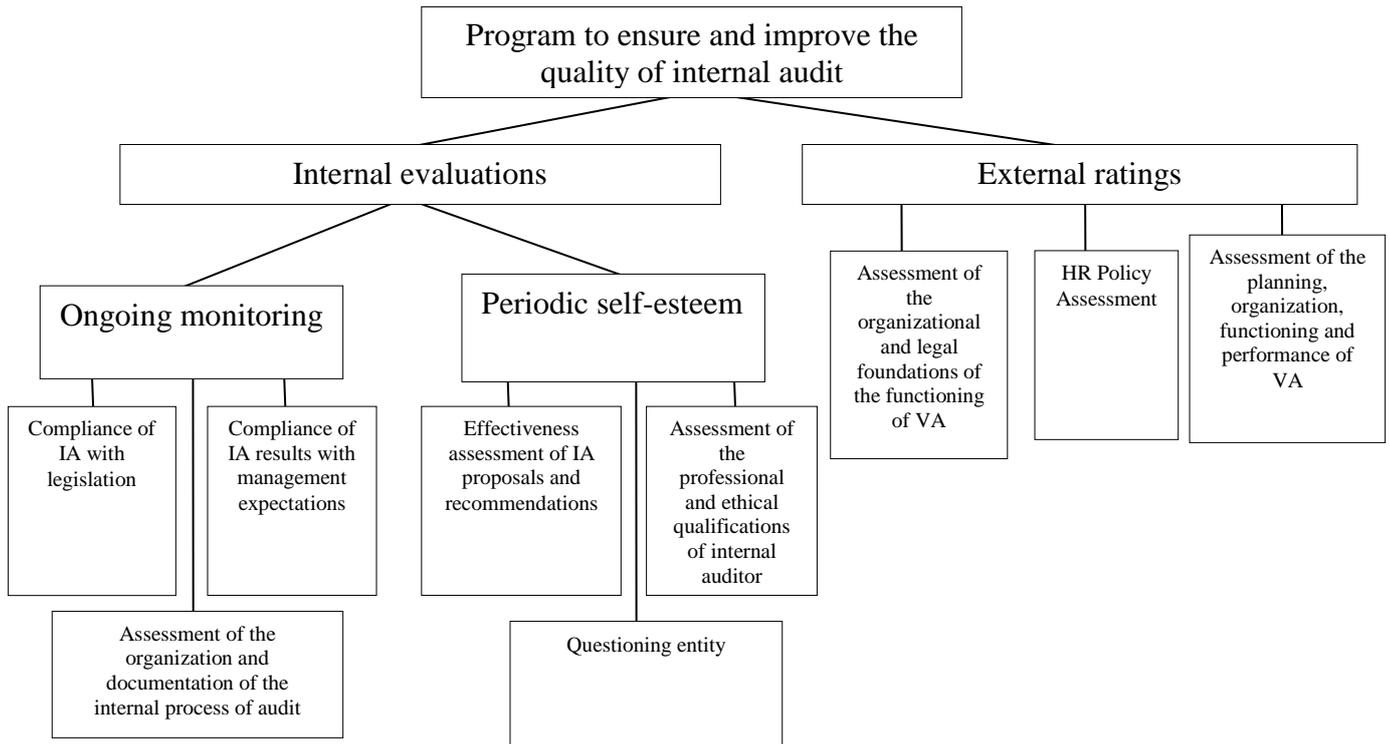
Internal quality assessment is a process of analysis of the activities of the internal audit unit, which is carried out by the head of such a unit in order to ensure and increase the efficiency of the internal auditors in fulfilling their functions.

The internal quality assessment of the internal audit function is carried out by two main methods: current monitoring and periodic self-evaluations of the internal audit activity. Internal evaluations should be included into the policies and procedures for managing internal audit, using processes, tools and information that are considered necessary to assess compliance with the Code of Ethics and Standards.

The purpose of internal quality assessments is to increase the effectiveness of the implementation of the internal audit function within each specific institution and to ensure compliance with the requirements of domestic regulatory legal acts on internal audit, IA Standards, the Code of Ethics of the Internal Auditor, as well as the internal regulatory framework of each specific institution in procession of the implementation of internal audit functions.

Responsible (and accountable) for organizing and conducting internal quality assessments is the head of the internal audit department.

Conducting periodic internal quality assessments in accordance with the requirements of domestic IA Standards is part of the Program for ensuring and improving the quality of internal audit, which should be compiled annually by the head of the internal audit unit and approved by the head of the relevant institution.



**Figure 1. The program to ensure and improve the quality of internal audit.**

The periodic self-assessment process includes the following:

- Oversight of assignments or internal audit missions;
- Filling out prescribed checklists;
  - Summarizing opinions received as feedback from audit entities or other interested parties through surveys and reviews;
- Selective expert reviews of working documentation by employees who did not participate in the relevant audit activities;
  - Verification of the implementation of the audit plan;
    - Analysis of additional performance indicators (for example, the duration of the audit and the timeliness of the implementation of recommendations);
  - Comparison of the current practice of the IA unit with the best practices of internal audit.

External quality assessment is a process of research and analysis of the activities of the internal audit unit, carried out by the Commission or by an independent appraiser in order to ensure that the internal audit activities comply with international and national standards, codes, rules and other requirements of normative legal acts in the field of internal audit, as well as providing recommendations to improve the efficiency and effectiveness of this function. External evaluations should be carried out at least once every five years by a qualified and independent evaluator or a

group of evaluators who are not employees of the organization. The head of internal audit should discuss with the Board:

- format and frequency of external evaluations;
- the qualifications and independence of an external appraiser or group of appraisers, including any possible conflict of interest.

The independence of the appraiser or group of appraisers implies the absence of an actual or apparent alleged conflict of interest. Independent appraisers cannot be employees or are under the control of the organization in which the internal audit is evaluated. The head of internal audit should facilitate the involvement of the Board in conducting external evaluations to prevent potential conflicts of interest.

Requirements and forms of organization and implementation of continuous monitoring of the Program to ensure and improve the quality of internal audit should be prescribed by each institution individually in internal documents.

Fedaa Abd Almajid SABBAR, in its research, states that periodic auditors are evaluated to improve the performance of the internal auditor and achieve the highest administrative efficiency[10].

The chief audit executive must inform senior management and the Board of the results of the quality assurance and quality improvement program. Informational reports should include the following:

- volume and frequency of both internal and external evaluations;
- the qualifications and independence of an external appraiser or group of appraisers, including any possible conflict of interest;
- conclusions of appraisers;
- corrective action plan.

In ensuring the quality of the internal audit work, control plays an important role. In the international standards of internal audit, it is indicated that the head of internal audit has overall responsibility for the control over the implementation of the task, which is done by the internal audit itself or for internal audit, but may entrust the control to employees with appropriate work experience in internal audit. Appropriate evidence of control should be documented and kept[14].

Based on the foregoing, the quality of the internal audit work is provided by the criteria given in table 2(The table is compiled by the authors)

**Table 2**

**Performance criteria for internal audit**

<b>№</b>	<b>Performance criteria for internal audit</b>	<b>Practice</b>	<b>Recommendations</b>
1	<b>Effective organization of work of IA</b>	Unified requirements for the organization of the IA service (at least 2 internal auditors) are established	Determine the requirements for the number of internal auditors based on the activities and volume of work of the organization
2	<b>Optimal internal audit planning</b>	Requirement for the general annual plan of the IA is established	Preparation of an optimal plan and internal audit program for each object
3	<b>Requirements for the qualification professionalism of internal auditors</b>	The requirements for certification and annual advanced training of internal auditors are established (higher education and at least 2 years of work experience from the last 10)	In the requirements for the qualifications and professionalism of internal auditors, specify that higher education should be economic or legal, at least 4 years of experience in accounting
4	<b>Ethics Compliance by Auditors</b>	The legislation of the Republic of Uzbekistan does not establish compliance with ethical standards by internal auditors	Compliance by internal auditors with the International Code of Ethics for Internal Auditing
5	<b>Audit quality control</b>	Certification is carried out by the	Develop a program to monitor

		Supervisory Board once a year	and improve the quality of VA
6	<b>Single IA working documentation</b>	Unified requirements for documenting the internal audit process are not established	Develop unified requirements for documentation of the internal audit process from the planning stage to the synthesis of results

Iain Gray, Stuart Manson and Louise Crawford determine the following qualities that contribute to improving the quality of the audit and ensure the effectiveness of the audit process [7]:

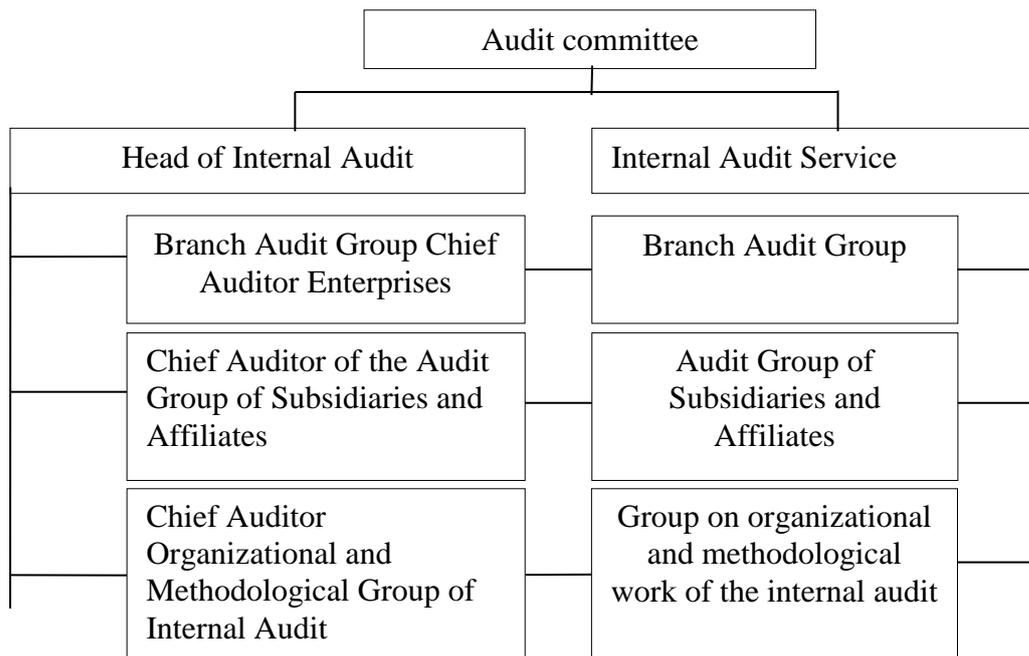
- audit planning in accordance with ethical and audit standards, collecting sufficient relevant audit evidence

- audit work is documented and reviewed, and technical support is provided as needed.

- the reliability and usefulness of audit reports. This quality can contribute to improving the quality of the audit and depends on the audit report as a means of expressing satisfaction of the auditors or dissatisfaction with the financial statements, that the audit report is clearly indicated, and that the auditor has collected sufficient relevant information, and reliable evidence to conclude that the financial statements give a true and fair look;

- a strong, clear and thorough discussion with the Audit Committee of issues arising in connection with the audit, the main conclusions arising from the audit and judgments related to it, issues related to the independence of the auditor, significant areas of risk and ways to achieve improved financial statements within customer.

In order to implement a program to ensure and improve the quality of internal audit, as well as effective quality control of internal audit, we offer the following structure for monitoring the quality of internal audit (Fig. 2)



**Figure 2. Organizational structure of the internal quality control of the internal audit.**

The organization of the Audit Committee as well as its monitoring and evaluation of the work of the internal audit service will contribute to the effective work of the internal audit service and improve the quality of work.

The activities of the Audit Committee should provide 2 tasks [6]:

- 1) that the audit function is effective and efficient, whether internal or external;
- 2) what policies and procedures are in place to ensure strict corporate governance.

## CONCLUSIONS

In conclusion, we present the following proposals for improving the quality control of internal audit

**Table 3 Proposals to improve the quality control of internal audit**

<b>№</b>	<b>Suggestions</b>	<b>By regulation</b>	<b>By quality</b>
1.	Organization of the internal audit service. When organizing the service, it is advisable to divide it into the responsible groups and determine their tasks and functions.	The tasks and functions of individual groups should be indicated in the internal situation of the enterprise “On the Internal Audit Service”	The performance of certain functions will lead to an increase of the quality of work of the internal audit service
2.	Making an optimal internal audit plan that requires a minimum of costs and maximum efficiency	It is advisable to indicate the unified requirements for the preparation of an internal audit plan based on international standards of internal audit in the internal regulations of the enterprise	An effective plan is a guarantee of the effective work of the internal audit.
3.	Attraction of highly qualified individuals in the field of accounting, audit and finance with an experience of at least 4 years to internal audit	The requirements for the length of service of individuals to approve an internal audit position or to obtain a qualified certificate of an internal auditor should be specified in the legislation governing internal audit	Experience is one of the essential components of the quality work of the internal auditor
5	To develop criteria for the quality of work of internal audit and methods for their assessment	The criteria for assessing the quality of work of the internal audit service as whole, must be developed on the basis of international standards of internal audit and indicate in the legislation governing activities	Monitoring and evaluating the quality of internal audit work will increase the sense of responsibility and improve the quality of work
6	Define common requirements for certification or assessment of the quality of work of internal auditors	Criteria for assessing the quality of work of the internal auditor as whole, should be developed on the basis of international standards of internal audit and indicate in the legislation governing activities	Unified standards for certification and assessment of the quality of work will contribute to the unification of quality assessment
7	Define a single internal audit report form	It is advisable to approve the unified requirements for the preparation of an internal audit report.	Since there are no unified requirements for compiling an internal audit report.
8	To establish in regulatory enactments a single requirement for internal audit in the form of the obligatory presence of a certificate of internal or external audit or international certificates in accounting, auditing and finance	In the regulations of this area, we propose to indicate: “The internal auditor is an individual who has a qualified certificate of an internal auditor”	A clear definition of the internal audit position will contribute to the observance of qualified and ethical requirements in auditing

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