

Audit Inspections and Findings in Slovakia

Denisa Domaracká

University of Economics in Bratislava
Faculty of Economic Informatics, Department of Accounting and Auditing
Dolnozemska cesta 1, 852 35 Bratislava, Slovakia
E-mail: denisa.domaracka@euba.sk

Abstract: *Statutory audits contribute to the credibility of the financial statements, the quality of which must be constantly improved. Regular inspections are suitable for achieving long-term high quality of statutory audits. Controls of statutory auditors and audit companies carried out in an organized manner and at the same time independently from the audited entities are referred to statutory audit quality checks which are the main topic of this paper. The topic of the paper was chosen due to the contribution to the improvement of the statutory audit quality.*

Keywords: *Audit Quality, Audit Inspections*

JEL codes: M42

1 Introduction

Statutory audit quality assurance reviews (hereinafter referred to as "audit inspections") are currently regulated within the framework of European legislation by the Directive 2006/43/EC of the European Parliament and of the Council of 17 May 2006 on statutory audits of annual accounts and consolidated accounts, as amended (hereinafter referred to as "Directive 2006/43/EC") and the Regulation (EU) No. 537/2014 of the European Parliament and of the Council of 16 April 2014 on specific requirements regarding statutory audit of public-interest entities (hereinafter referred to as "Regulation 537/2014").

The national regulations of the individual member states of the European Union are subsequently based on the European regulations. In the European Union and its member states the EU legislation is implemented (Juhászová, Markovič, and Mokošová, 2014).

Research of authors Maijoor and Vanstraelen (2012) demonstrate the public oversight, audit market concentration, audit quality, audit firm ownership structures, audit firm operating structures, audit firm governance, and auditor liability on the EU market as it provides unique natural experimental settings. The author Raffegaue (1996) states that in the world, the methods of carrying out the audit inspections of statutory auditors or auditing companies differ from the conditions set by specific national legislation.

The audit inspections resulting from the Directive 2006/43/EC do not apply to all statutory audits. An exception is the statutory audit of annual and consolidated financial statements of public-interest entities. In achieving a common regulatory framework for the statutory audit of public-interest entities, the Regulation 537/2014 was adopted which began to be applied in the Slovak Republic and other EU member states from June 17, 2016.

2 Methodology and Data

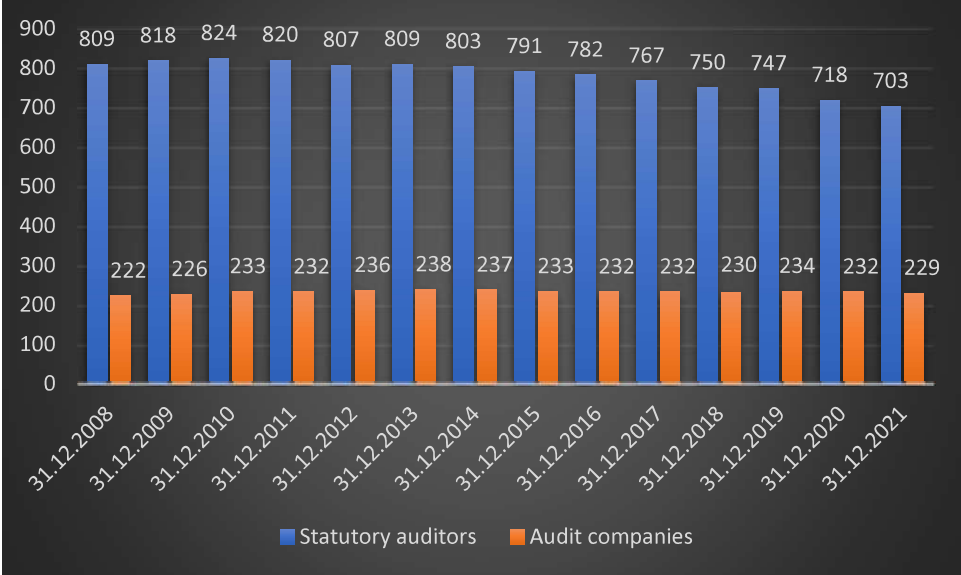
One of the main requirements of the Directive 2006/43/EC was that all statutory auditors and audit firms are subject to a system of quality assurance which is subject to public oversight (Directive 2006/43/EC, Art. 29(1)).

Regarding the number of all statutory auditors and audit companies in Slovakia, as of December 31, 2021, there were operating:

- 703 statutory auditors with an active license; and
- 229 audit companies with an active license (see Fig. 1.).

Regarding the establishment of public oversight over statutory auditors and audit companies, it was already accomplished in Slovakia in 2008, when the Auditing Oversight Authority (hereinafter referred to as "the Authority") was established.

Figure 1 Statutory auditors and audit companies in Slovakia in individual years



Source: Register of Auditing Oversight Authority

The performance of the audit inspections in Slovakia is carried out through the bodies defined in par. 35(1) of the Act No. 423/2015 Coll. on Statutory Audit, as amended, by the Auditing Oversight Authority and the Slovak Chamber of Auditors (hereinafter referred to as "the Chamber"). Carson et al. (2013) draw attention to the fact that over the years, more and more independent national regulatory bodies have decided to unite within a single organization, focused primarily on the support of audit quality.

The authors Baker, Mikol and Quick (2010) examined several key functions of audit regulation and how these functions were deployed in countries as United Kingdom, France, and Germany. The authors Francis, Michas, and Seavey (2013) in their research pointed out the audit regulators around the world that have expressed concern over the market dominance by Big 4 which may adversely effect on the quality of audited financial statements. In connection with the abovementioned the authors Mao, Qi, and Xu (2017) state that regulators suggest that small audit firms join international accounting networks to reduce their resource constraints in serving large clients and providing high-quality service.

In Act No. 423/2015 Coll., the competences of the Authority were extended to include the area of ensuring and performing audit inspections of statutory auditors and audit companies that carry out statutory audits of public-interest entities (and of companies according to par. 2(15f) of Act No. 423/2015 Coll.).

The main activity of the Chamber in connection with the performance of audit inspections is to implement a system of ensuring the quality of statutory audits, to which statutory auditors and audit companies will be subject, except those that carry out statutory audits of public-interest entities or companies according to par. 2(15f). The mentioned system of inspections performed by the Chamber is subject to the oversight carried out by the Authority according to par. 36 of Act No. 423/2015 Coll.

Regarding performance of audit inspections in the case of the Authority, we speak approx. 10 statutory auditors of public-interest entities and approx. 30 audit companies of public-interest entities. The remaining statutory auditors and audit companies are under the audit inspections carried out by the Chamber.

It should also be noted that the Authority can perform audit inspections also of statutory auditors and audit companies that carry out statutory audits in entities that are not public-interest entities or companies according to par. 2(15f).

The activities of the Authority and the Chamber in the field of audit inspections are not mutually comparable, since, as we have already mentioned, the system of audit inspections performed by the Chamber is subject to the oversight of the Authority. Nevertheless, it is possible to find several key differences regarding the audit inspections.

3 Results and Discussion

As already mentioned, audit inspections are performed within the Slovak Republic in accordance with valid legislation through the Authority and the Chamber. Both bodies publish the results of the audit inspections carried out, while these publications served to display the individual findings from the inspections carried out within the comparable period. The comparable period was the years 2017 - 2020, as it was an intersection of periods during which audit inspections were carried out by both bodies at the same time.

The authors Carson et al. (2017), Florou and Shuai (2017), and García Osma et al. (2017) agree that there are significant differences in audit inspection rules in countries (and within the EU, too), including whether there are results of audit inspections published. In a similar context, the author Jošt (2015) analyzes the quality of audit services in V4 countries, focusing on the quality control system in individual V4 countries. It also evaluates the level of services provided by statutory auditors and the criteria used by oversight authorities to measure the quality.

Table 1 contains 10 main findings of the Authority identified in the inspected subjects - statutory auditors and audit companies within the audit inspections carried out between 2017 and 2020.

Table 1 Main findings of audit inspections identified by the Authority in years 2017 - 2020

	Main Finding of the Authority	2017	2018	2019	2020
1	Insufficiently developed methodology for verification of general and application IT controls	x	x	x	x
2	Inadequate fulfillment of notification obligations towards the Authority	x	x	x	x
3	Weaknesses in the Transparency reports	x	x	x	x
4	Insufficiently developed audit methodology	x	x	x	x
5	Insufficient communication with audit committee, no audit committee report submitted	x	x	x	-
6	Insufficiently developed/observed rules and procedures according to ISQC 1	x	x	x	-
7	Non-developed adequate internal procedures for withdrawing from an audit engagement or withdrawing from a relationship with a client	x	x	-	-
8	Non-observed procedures during the audit engagement acceptance	x	x	-	-
9	Non-observed period of archiving audit documentation	x	x	-	-
10	Non-observance of set procedures in the field of engagement quality control	x	x	-	-

Source: own processing according to Prehľad o celkových výsledkoch previerok zabezpečenia kvality štatutárneho auditu Úradu pre dohľad nad výkonom auditu za rok 2017, 2018, 2019, 2020

Based on the main findings from the audit inspections carried out by the Authority (listed in Table 1), it can be concluded that the Authority's audit inspections are in a large extension aimed at assessing the adequacy of the system setup of the inspected subject, which primarily consists of the quality of the activities of statutory auditors and audit companies, the quality and quantity of resources spent for the performance of the statutory audit, as well as the system of internal quality control of audit activities.

The reason may be the so-called the first 3-year cycle of the Authority's audit inspections, which may be a prerequisite for the future focus of repeated audit inspections.

Table 2 contains 10 main findings of the Chamber identified in the inspected subjects - statutory auditors and audit companies within the audit inspections carried out between 2017 and 2020.

Table 2 Main findings of audit inspections identified by the Chamber in years 2017 - 2020

	Main Finding of the Chamber	2017	2018	2019	2020
1	Non-determined / incorrectly determined level of significance in planning and performing the audit	x	x	x	x
2	Insufficient documented assessment of the internal control system, knowledge of the audited entity, legal regulations relating to the activity of the audited entity	x	x	x	x
3	Absent method of the auditor's reaction to the evaluated risks	x	x	x	x
4	Absent documentation of sample selection methods, sample scope and linkage to the determined risk	x	x	x	x
5	Absent documentation to assess audit risk, fraud risk, communication with the client	x	x	x	x
6	Absent / insufficient documentation of audit evidence evaluation for conclusions of statutory audit	x	x	x	x
7	Weaknesses in audit planning, inconsistent monitoring of the audit duration and subsequent determination of the fees	x	x	x	x
8	Unverified / undocumented fact, whether the audited entity is not in crisis or bankruptcy or is not at risk of bankruptcy	x	x	x	x
9	Absent written statements of management	x	x	x	x
10	Unclear course on the performance of the audit, the applied procedures, the impact of detected irregularities and the justification of the conclusions based on the audit documentation	x	x	-	x

Source: own processing according to Prehľad o celkových výsledkoch previerok zabezpečenia kvality štatutárneho auditu Slovenskej komory audítorov za rok 2017, 2018, 2019, 2020

Based on the data from Table 2 on the main findings of the audit inspections carried out by the Chamber, it follows that the Chamber's audit inspections are methodologically focused on the performance of statutory audits and related audit documentation. It is therefore an assessment of the compliance of the statutory audit performance and the organization of the audit activities with the ISA international auditing standards, ethical

standards, internal quality control standards and with the requirements for continuous education of statutory auditors.

Conclusions

Statutory auditors and auditing companies in Slovakia are subject to a quality assurance system which the competent bodies are responsible for, primarily to ensure objectivity and independence from the audit profession. The main contribution of the submitted paper is to increase awareness of the issue of quality assurance inspections of statutory audits, to explain the related legislation, but also to provide information of actual audit inspections carried out by the Authority and the Chamber.

We found that the range of findings is relatively high in all analyzed years, and therefore statutory auditors and audit companies need to continue to make efforts to eliminate identified findings and irregularities during the audit inspections. The recurrence of the same findings in individual years indicates the need of further improvement of the statutory audit performance. Available sources show that the Authority as well as the Chamber use the findings from the performed audit inspections with the aim of more efficiently setting up the performance of audit inspections for future periods.

Acknowledgments

This article is an output of the project of the Scientific Grant Agency of the Ministry of Culture of the Slovak Republic and Slovak Academy of Sciences (VEGA) no. 1/0517/20 (2020-2022) "Virtual Cryptochains as a Relevant Tool to Eliminate Economic Crime".

References

- Act No. 423/2015 Coll. on Statutory Audit and on Amendments and Supplements to Act No. 431/2002 Coll. on Accounting, as amended.
- Auditing Oversight Authority. Prehľad o celkových výsledkoch previerok zabezpečenia kvality štatutárneho auditu vykonaných Úradom pre dohľad nad výkonom auditu za rok 2017, 2018, 2019, 2020. Retrieved from: <https://www.udva.sk/sk/dohlady-a-previerky/previerky>.
- Baker, C. R., Mikol, A., Quick, R. (2001). Regulation of the statutory auditor in the European Union: A comparative survey of the United Kingdom, France and Germany. *European Accounting Review*, vol. 10(4), pp. 763–786.
- Carson, E., Simnett, R., Vanstraelen, A. (2013). Auditing the Auditors: An International Analysis of the Effectiveness of National Inspection Regimes on Audit Quality. Retrieved from: <http://www.hec.unil.ch/documents/seminars/dcc/1237.pdf>.
- Carson, E., Lamoreaux, P. T., Simnett, R., Thürheimer, U., Vanstraelen, A. (2017). Establishment of National Public Audit Oversight Boards and Audit Quality. Retrieved from: <https://ssrn.com/abstract=3049828>.
- Directive 2006/43/EC of the European Parliament and of the Council of 17 May 2006 on statutory audits of annual accounts and consolidated accounts, as amended.
- Florou, A., Shuai, Y. (2017). The costs and benefits of public oversight design: Evidence from the EU. Retrieved from: [doi:10.2139/ssrn.3595454](https://doi.org/10.2139/ssrn.3595454).
- Francis, J. R., Michas, P., Seavey, S. 2013. Does audit market concentration harm the quality of audited earnings? Evidence from audit markets in 42 countries. *Contemporary Accounting Research*, vol. 30(1), pp. 325-355.
- García Osma, B., Gisbert, A., de las Heras Cristóbal, V. G. (2017). Public oversight systems for statutory auditors in the European Union. *European Journal of Law and Economics*, vol. 44(3), pp. 517–552. Retrieved from: <https://doi.org/10.1007/s10657-014-9460-1>.
- Jošć, M. (2015). Kvalita auditorských služieb v zemích Visegrádu. Retrieved from: [doi:10.18267/j.cfuc.453](https://doi.org/10.18267/j.cfuc.453).
- Juhászová, Z., Markovič, P., Mokošová, D. (2014). Fair value and its importance for financial decision-making. IFRS: global rules & local use: proceeding of the 2nd International scientific conference, pp. 64-69.

Mao, J., Qi, B., Xu, Q. (2017). Does International Accounting Network Membership Affect Audit Fees and Audit Quality? Evidence From China. *The International Journal of Accounting*, vol. 52(3), pp. 262-278.

Maijor, S., Vanstraelen, A. (2012). Research Opportunities in Auditing in the EU. *Auditing: A Journal of Practice & Theory*, vol. 31(1), pp. 115–126. Retrieved from: <https://doi.org/10.2308/ajpt-10209>.

Raffegau, J. et al. (1996). *Finanční audit*. Praha: HZ Praha.

The Slovak Chamber of Auditors. *Prehľad o celkových výsledkoch previerok zabezpečenia kvality štatutárneho auditu za rok 2017, 2018, 2019, 2020*. Retrieved from: <https://www.udva.sk/sk/dohlady-a-previerky/previerky>.