

**Methodology Article**

# Audit Activity in Modern Conditions: The Nature of the Relationship Between the Categories "Quality", "Efficiency", "Competitiveness"

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**Abstract:** Audit activity has a multi-subject field, uses interdisciplinary methodology, which complicates the scientific interpretation and application of such categories as – "competitiveness", "quality", "efficiency" and this circumstance predetermined the purpose of the study, in which the author, using the existing theoretical and methodological base, develops definitions of these categories and informal methodological approaches to their assessment (calculation and measurement), considered in the relationship and dependence. Understanding the essence of the basic categories and qualitative and quantitative assessment are of scientific and applied interest from the audit community around the world.

**Keywords:** Audit Activity, Competitiveness, Quality, Efficiency, Methodological Approaches to Evaluation

## 1. Introduction

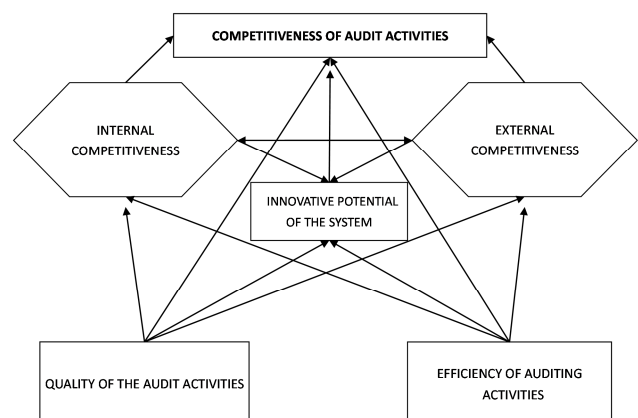
Audit activity (audit services) has a multi-disciplinary field and is in matter a process of independent financial control, that is conducted as an entrepreneurial activity, with a wide variety of possible goals (with the main goal of making profit), as a management activity in terms of audit-related services and other audit-related activities.

Multi-subject nature of the field imperatively predetermined audit as a form of scientific knowledge, the result of scientific research based on interdisciplinary methodology.

For the current stage of development of audit activities, research of the essence of the categories of competitiveness, quality and efficiency, that are significant for the field, continues to remain relevant.

In understanding the essence of these categories, the author adheres to the following position: competitiveness is the objective and the condition of presence in the subject field, quality is the postulate (principles) of the process activity

technology, efficiency is the result of the functioning or development of the system, which are interrelated and interdependent (figure 1)



**Figure 1.** The cognitive model of the relationship between competitiveness, quality and efficiency of audit activities.

## 2. Competitiveness of the Audit (Audit Activities): the Nature of the Determining Factors

Russian audit community has been assigned the most

difficult mid-term target: increasing the competitiveness of the Russian audit in the international audit markets. To achieve the stated goal, it is necessary to handle a number of problems, first of those being identification of the factors that determine (shape) the competitiveness of an audit market, considered as a system, subject and object of control (figure 2).

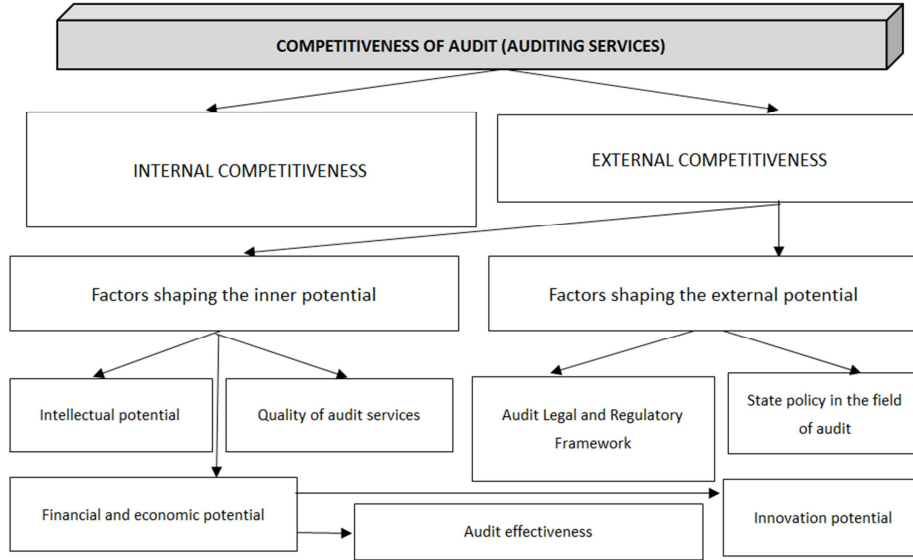


Figure 2. Factors determining the competitiveness of audit (audit services).

It is proposed to represent the competitiveness potential of audit (audit services) in the form of the following function:

$$SPRA = f(PRA_v, PRA_w) \quad (1)$$

Where:

SPRA is the total potential of competitiveness of audit (audit services);

PRA<sub>v</sub> is the internal potential of competitiveness of audit (audit services);

PRA<sub>w</sub> is the external potential of competitiveness of audit (audit services).

Following indicators for assessment of competitiveness level of audit (audit services) are proposed:

at the macro level – the share of national auditors (both firms and individual auditors-entrepreneurs) in the total amount of the audit market income as calculated in the framework of GDP estimation;

at the meso level – the proportion of regional auditors (firms and individual auditors-entrepreneurs) in the total amount of the audit market income as calculated in the framework of GDP estimation;

at the micro level – the share of segmentation of the regional and national audit market (audit services) in the formation of GRP and GDP.

## 3. The Quality of the Audit (Audit Activities): Interpretation, Measurement

The International Auditing and Assurance Standards Board

(IAASB) developed the Audit Quality Concept, which describes the initial parameters, process parameters and results, the impact on the quality of audit of financial statements at the level of an individual audit engagement, an audit organization, and at the country level as a whole. According to this Concept, quality in audit is achieved through:

the commitment of auditors to appropriate values, ethics and attitudes;

availability of sufficient knowledge, skills, experience and time for auditors to perform auditing work [1].

International Standard ISO 9004-2-91 "Administrative Quality Management and Quality System Elements" defines quality as understanding and satisfying customer requirements, achieved through a systematic approach to its management, strict adherence to the principles and continuous work to improve it [2].

ISO 8402-94, "Quality Management and Quality Assurance", interprets quality as a combination of properties and characteristics of a product or service, which give them the ability to satisfy conditional or perceived needs [3].

The International Standard of Audit 220 "Quality Control during the Audit of Financial Statements" obliges auditors to implement quality control procedures at the level of the audit engagement that ensures with reasonable confidence that:

the audit conducted is in accordance with professional standards and applicable legal and regulatory requirements;

the issued audit report is appropriate in the circumstances [4].

Scientific research examines various approaches to defining audit quality. Sirotenko E.A. notes that the quality of audit is

defined by the properties and materials, compliance with which is the essence of the audit [5]. Skobara V.V. believes that the opinion of an auditor is useful only if the users trust its authenticity [6].

J.S. Robertson and T.J. Louwers note that audit is necessary for studying business operations in order to develop recommendations for a more economical and efficient use of

resources, and effectiveness in achieving business goals [7]. This nature of services is possible only with the high quality of services provided.

The development of audit quality management systems is in constant development and can be represented by a set of elements, tools, taking into account the specifics of their implementation (table 1).

**Table 1.** Elements, tools and features of their application in the management of audit quality (audit activities).

Elements	Application features	Tools
Authorization	The audit is conducted in accordance with the qualification certificate and the requirements of regulatory legal acts	Legislative support. Standardization, unification. Development of internal standards
Independence and objectivity	Process participants are not related to each other, auditors are impartial and objective	Laws. International Standards on Auditing. Code of Professional Ethics. Independence rules
Organizational and methodological support	Development, substantiation and approbation of the methodology, methods of auditing examinations, non-traditional approaches, adapted to the features of the audited entity	Auditors, experts Software and methodological materials. Training specialists in the field of performance audit
Consulting support	Scaling up the participation of experts, specialists and other professionals	Leading scientists and practitioners in the field of audit, accounting and tax accounting, financial management Safety standards
Safety and security of information	Creating a security system. Limited access to audit products	Admission procedures Security policy Standardization
Performance Management	Monitoring, evaluation and analysis	Development of instrumental and methodological apparatus

The level of quality of audit activities can be assessed only within the framework of the interaction of the entity being audited with the external business environment, provided that the dimension and method of assessment is justified.

The dimension requires the justification of the quality indicator as a vector of indicators of essential properties (table 2).

**Table 2.** The dimension of the quality of the audit (auditing).

Essential properties	Indicators
1. Performance indicator (as a result for which the system operates)	1. The degree of reliability of the information presented in the financial statements, according to which an audit opinion was issued with an unqualified or qualified opinion
2. Indicators of sustainability	1. Homeostasis (or equilibrium of the system) 2. Financial sustainability
3. Performance Indicators	1. Profitability 2. The share of segmentation of the sectoral regional market
4. Indicators of sustainable development	The system of non-formalized approaches to the assessment of the audited entity, considered as a socio-ecological-economic system

#### 4. The Effectiveness of the Audit (Audit Activities): the Nature, Methodological Approaches to the Assessment

The degree of achievement of (compliance to) the expected (hypothetical) result by the actual result is efficiency.

Efficiency – compliance of the achieved results of the development of an auditor (a company, an individual auditor-entrepreneur, a regional or national market of audit services) to the results required by to the objectives set.

The author believes that the goals are subject to differentiation by the levels of economic systems, an integral element (subsystem) in relation to which is the market of audit (audit activities).

**Table 3.** Target objectives of development of audit (audit services) by levels of economic systems.

System elements	Macro Level - National Economy	Meso level - Regional Economy	Micro level - Auditing Firm
Ecological	Efficiency of the state environmental policy and environmental audit system	Efficiency of implementation of environmental and economic policies	Optimization of environmental expenditures
Social	Growth of social activity and social security	Unemployment reduction	Social satisfaction from professional experience
Economic	Growth share of GDP segmentation	Growth share of GRP segmentation	Profitability growth
Synergy of elements	Sustainable development or growth	Sustainable development or growth	Sustainable development or growth based

When developing a system of balanced indicators for evaluating the effectiveness of audit (audit activities) at the meso and micro level, the author sought simple, model and compromise between financial and non-financial components.

The author proposes to evaluate (calculate and measure) the effectiveness of an audit (audit activity) at the micro level by the indicator - the profitability of the audit activity and using

the following algorithm:

$$R_{ad} = K_1 * K_2 * K_3 * K_4 * K_5 * K_6 * K_7 * K_8 \quad (2)$$

$K_1, \dots, K_8$  – local indicators aggregated in a multiplicative model (Table 4)

**Table 4.** Local indicators for evaluating audit performance (auditing) at the micro level.

Indicators	Calculation algorithm	Comment
$K_1$ – net profit per ruble cash flow from audit activities	$\frac{NP}{CF_{audit}}$	The amount of net profit received from each cash flow ruble from the core activities
$K_2$ – the share of cash flow from audit activities in the total amount of cash flow	$\frac{CF_{audit}}{CF_{total}}$	The share of cash flow from the core activities in the total amount of cash flow of the auditor
$K_3$ – the total amount of cash flow from all activities for one ruble of income received by the auditor	$\frac{CF_{total}}{Inc_{total}}$	The amount of cash flow from each ruble of the income of the auditor
$K_4$ – the ratio of total income to total expenditures of the auditor	$\frac{Inc_{total}}{Exp_{total}}$	The amount of income received from each ruble of the expenses of the auditor
$K_5$ – the amount of expenses for one ruble of asset investments of the auditor	$\frac{Exp_{total}}{A}$	The amount of expenses for each ruble of investments in the auditor's assets
$K_6$ – capital multiplier	$\frac{A}{CE}$	The degree of financial independence (autonomy) of the auditor
$K_7$ – equity for one ruble of the cost of audit services	$\frac{CE}{C_{audit}}$	The value of the average cost of equity for 1 ruble cost of audit services
$K_8$ - the cost of one ruble of audit services delivered	$\frac{C_{audit}}{R}$	The cost of 1 ruble of sold audit services

Legend:

NP - net profit;

$CF_{audit}$  – cash flow from audit activities;

$CF_{total}$  – total cash flow;

$Inc_{total}$  – the amount of income from all activities;

$Exp_{total}$  R total - the amount of expenses from all activities;

A – the average value of assets;

CE – the average cost of equity;

$C_{audit}$  – the full cost of the implemented audit services;

R – revenue from the audit services.

For the calculation and subsequent measurement of the effectiveness of audit (auditing) at the meso level, the author suggests a system of local indicators in the context of innovative, environmental, organizational, financial, economic and resource saving components (Table 5).

**Table 5.** Local indicators for evaluating audit (audit activities) performance at the meso level.

Indicators	Calculation algorithm
Innovative efficiency	
$K_1$ – the share of innovative developments with the participation of auditors	The number of innovative inventions created with participation of auditors divided by the total number of innovative inventions
$K_2$ – the share of the implemented innovations developed with the participation of auditors in the total number of implemented innovations	Number of innovations developed with participation of auditors introduced divided by the total number of innovations introduced
$K_3$ – the growth rate of the amounts of investments per capita in the region fostered by the introduction of innovations with the participation of auditors	Inventions with the participation of auditors divided by the total number of innovations
Organizational effectiveness	
$K_4$ – the share of the potential capacity of the regional audit market covered by audit services	The total number of economic entities covered by the audit in the reporting period divided by the potential capacity of the regional audit market in the reporting period
$K_5$ – the share of auditors registered in the region in the total number of auditors operating in Russia	Number of auditors registered in the region (working as individual entrepreneurs or for audit firms) divided by the total number of auditors registered in Russia at the end of the reporting period
Environmental performance	
$K_6$ – the share of segmentation of the environmental audit in the total number of audit services rendered in the region	Number of environmental audit services rendered in the region during the reporting period divided by the total number of audit services rendered in the region in the reporting period
$K_7$ – the share of innovations of an environmental nature implemented in the total number of innovations introduced with the participation of auditors	Number of environmental innovations implemented in the region during the reporting period divided by the total number of innovations introduced in the region during the reporting period with the participation of auditors
Resource Efficiency	

Indicators	Calculation algorithm
K <sub>8</sub> – growth rates of labor productivity in the priority sectors of the regional economy audited in the reporting period	Production per worker for the reporting period divided by the corresponding indicator of the base period
K <sub>9</sub> – growth rates of material performance in the priority sectors of the regional economy that were audited in the reporting period	Material performance for the reporting period divided by the corresponding indicator of the base period
K <sub>10</sub> – growth rate of capital productivity in the priority sectors of the regional economy audited in the reporting period	Capital productivity of fixed assets for the reporting period divided by the corresponding figure of the base period
K <sub>11</sub> – growth rate of turnover ratio of working capital in the priority sectors of the regional economy audited in the reporting period	The turnover ratio of working capital in the reporting period divided by the corresponding indicator of the base period
Financial and economic efficiency	
K <sub>12</sub> – segmentation share of the industry audit market	Audit services revenue in the region in the reporting period divided by the audit services revenue in the country in the reporting period
K <sub>13</sub> – the share of the regional audit market participation in the formation of GRP in the reporting period	Audit services revenue from the sale of provided in the region during the reporting period divided by GRP
K <sub>14</sub> – the growth rate of tax revenues in budgets of all levels from auditors for the reporting period	The amount of tax revenues from regional auditors to the budgets of all levels for the reporting period divided by the corresponding indicator in the base period
K <sub>15</sub> – the growth rate of profits earned by regional auditors in the reporting period	Profit before tax according to the reporting for the reporting period by audit firms registered in the region divided by the corresponding indicator in the base period

Source: developed by the author.

The integral indicator of audit performance at both the micro and meso levels can be defined as follows:

$$K_n = \sqrt{K_1 \times K_2 \times \dots \times K_{15}} \quad (3)$$

Where: K<sub>1</sub>-K<sub>15</sub> are the local indicators of efficiency.

The effectiveness of the audit (audit activities) is determined not only by the economic effect, but also by the quality, whereby the efficiency is proposed to be calculated using the formula:

$$E_{audit} = \sum_{i=1}^n E_i \times K_{quality} \quad (4)$$

Where:

$E_{audit}$  is the economic effect;

$E_i$  is the effect of the i-th commercial or non-commercial project;

$K_{quality}$  is the service quality ratio.

The International Standard of Audit 570 “Going Concern” obliges the auditor to analyze the presence of events and conditions, as a result of which significant doubts may arise in the organization’s ability to continue as a going concern [8].

For these purposes, the auditor examines events or conditions of financial nature, events or conditions related to operating activities, and other events and conditions. The quality of this assessment is one of the components of the quality of an audit, which is required by the professional approach.

Depending on the realistic forecast of the auditor regarding the organization’s ability to continue as a going concern, it is proposed to establish a quality factor (Table 6).

**Table 6.** The value of the quality ratio of the audit of financial statements, depending on the results of the prediction of the continuous activity of the entity.

Indicators	Feasibility of the forecast – absolute	Feasibility of the forecast – high	Feasibility of the forecast – moderate	Feasibility of the forecast – low	Feasibility of the forecast – very low
The quality ratio of the audit of financial statements ( $K_{quality}$ )	1,00	0,75	0,50	0,25	0,10

The basis for assessing the quality of audit in terms of feasibility of the forecast about the stability of the system being audited is a comparative analysis of the actual state of the system after 12 months following the audit, with a forecast made by the auditor in the audit process (Table 7).

**Table 7.** Differentiation of the degree of feasibility of the forecast of the continuous activity of the entity being audited.

Stability type	Feasibility of the forecast – absolute	Feasibility of the forecast – high	Feasibility of the forecast – moderate	Feasibility of the forecast – low	Feasibility of the forecast – very low
Economic sustainability (system homeostasis)	There is no deviation from the forecast	There is no deviation from the forecast	There is no deviation from the forecast	Deviation from the forecast by one level of the state of the system	Deviation from the forecast for two levels of the state of the system
Financial stability	There is no deviation from the forecast	Deviation by one type of state	Deviation by two types of state	Deviation by three types of state	The condition is fully different from the forecast

The degree of detailing of non-formalized methodological approaches to assessing (calculating and measuring) the

quality of audit (audit activities) can be significantly expanded with the introduction of second, third, etc. degree factors into

the calculations.

## 5. Conclusion

Audit (auditing) has a multi-disciplinary field of activity, which complicates not only the methodology and interpretation of the essence of the basic categories of "competitiveness" and "quality". "Efficiency", but their practical support. Audit is not only a public institution of financial control, but also entrepreneurial activity and this circumstance encourages research into the search for compromises between the protection of public interests and entrepreneurial advantage. Without satisfying certain information needs of the society (or its individual members), auditing (auditing) is impossible, and without self-financing at the expense of entrepreneurial income, it will lose its status as public and independent. At the same time, there are cognitive interrelations between the studied categories, in relation to which the author considers not only their theoretical interpretation, but also offers the developed assessment tools from the position of qualitative components.

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