

Research on Audit Quality Management System of Accounting Firms: The case of the Yabaite Audit Failure

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Abstract: In recent years, the frequent financial fraud and audit failures in the capital market show that the audit work in China has not been as expected by the public, which not only brings serious consequences to the social and economic development, but also reduces the public's trust in the CPA industry. The audit quality directly affects the professional service effect of the certified public accountants, and is the foundation of their survival. In view of the comprehensiveness and systematicness of audit quality management, this paper takes Zhonghua Accounting Firm as the research object, combining with the case of audit failure of Yabaite company, analyzes the current situation and problems of audit quality management of the firm, and puts forward corresponding optimization suggestions and safeguard measures, in order to provide improvement ideas for the construction of audit quality management system, and also bring some reference for audit quality management in the same industry.

Keywords: Accounting firm, Audit failed, Audit quality, Quality management.

1. Introduction

In recent years, with the rapid development of China's economy, accounting firms have become an indispensable part of the social supervision system. But at the same time, the competitive pressure of the industry is also gradually increasing. In order to win the competitive advantage, accounting firms gradually neglect the quality of audit business, and cases of being punished by institutions such as the CSRC are also common. In the public's attention to the audit quality problem, whether accounting firms can truly play the role of audit supervision is also challenged unprecedentedly. At present, Zhonghua Accounting Firm as the industry leader, its brand reputation is improving year by year. With the continuous injection of the industry, its scale is also expanding, but the road of development is not smooth. In the process of expanding its scale, the management of audit quality is ignored. It is precisely for this reason that Zhonghua Company has been successively sanctioned by the China Securities Regulatory Commission and other regulatory authorities, which not only adversely affected the firm's brand image, but also caused the public to lose their trust in the firm.

Under this background, Zhonghua Accounting Firm must take the initiative to change, recognize its own defects, and discuss its own direction and specific countermeasures in combination with past work, in order to get rid of the current predicament as soon as possible. Only in this way, Zhonghua Accounting Firm can maintain the brand image of the company and win the trust of the public again on the basis of improving the audit quality and enhancing the competitiveness of the industry. Therefore, this paper starts with the Zhonghua Accounting Firm's audit failure of Yabaite Company as the breakthrough point, analyzes the eight elements of the quality management system in detail, and puts forward the corresponding countermeasures and measures for these problems, in order to provide some reference for Zhonghua Accounting Firm and similar or similar firms to improve the audit quality management level.

2. Brief Introduction of Audit Failure Cases of Yabaite Company

In 2017, in the "Decision of Administrative Punishment" issued by China Securities Regulatory Commission, Yabaite was ordered to correct, warn and impose a fine of 600,000 yuan; At the same time, the relevant responsible person of the company will be punished within the legal scope. Behind the relevant decision, Yabaite Company fabricated a large number of false financial information in 2015-2016 by fictitious overseas engineering projects, fictitious international trade and internal trade, resulting in the inflated business income of 580 million yuan and profit of 260 million yuan.

2.1. Yabaite Fictionalizes Overseas Engineering Projects

According to the annual report of Yabaite in 2015, the company undertook the overseas urban bus rapid transit line project, which had been completed by the end of the reporting period of that year. But actually, Yabaite is not involved in this project. In order to create the illusion of engineering construction, Yabaite arranged the false export of goods through the logistics company during this period. However, most of the goods were not transported to the destination, but were finally sent back to China after a series of twists and turns by the transportation company. The fund return of this project is also an illusion created by the company through 16 third-party companies at home and abroad.

2.2. Yabaite Fictionalizes Domestic and Foreign Trade

Between 2015 and 2016, Yabaite didn't make any actual transactions with customers, but falsely purchased materials from a number of enterprises by signing false purchase and sale contracts and forging warehousing documents. Then, they colluded with other customers to sell these materials under false pretence, but in fact, no goods were transferred. At the same time, Yabaite sends money to "sales customers" through "suppliers" and enterprises controlled by the

chairman of Yabaite, and then transfers the money back in the name of sales money, forming a "real" capital circulation.

In the audit of Yabaite, Zhonghua Accounting Firm appointed Sun Mou and Gu Mou as project partners. After completing all the work, Zhonghua Accounting Firm easily recognized that its audit work was correct and had collected enough evidence to support the audit results, so it issued a standard unqualified opinion to Yabaite. Later, it was proved that the opinions expressed by Zhonghua were completely contrary to the actual situation.

After the event, Zhonghua Accounting Firm said that due to the problems of fraud and falsification of financial information in the management of Yabaite, it was difficult to find out the general audit procedures, so it failed to find out the major errors. However, a large amount of evidence indicates that Zhonghua did not strictly follow the relevant standards in the whole audit process. The root cause is the defect of audit quality management of the firm, which leads

to the failure to find the significant misstatement of Yabaite Company.

3. Problems Existing in Audit Quality Management System of Zhonghua Accounting Firm

Next, taking Yabaite Company's audit failure as an example, this paper will analyze the problems of Zhonghua Accounting Firm's quality management system from the aspects of governance and leadership, resources, accounting firm's risk assessment procedures, relevant professional ethics requirements, customer relationship and specific business undertaking and maintenance, business execution, information and communication, monitoring and rectification procedures, according to the structure of quality management system, see Figure 1.

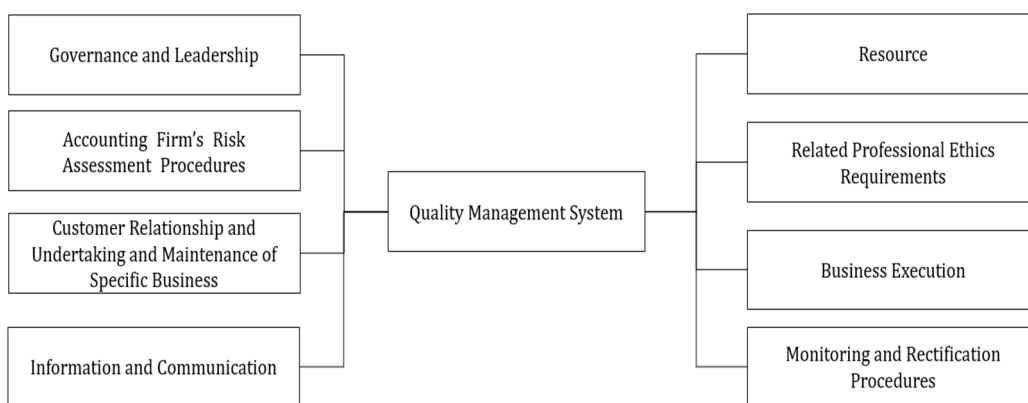


Figure 1. Quality Management System

3.1. Governance and Leadership

The poor quality management effect and ineffective implementation of audit procedures are mainly due to not only the lack of audit ability, but also the lack of ideological understanding of auditors. Therefore, under the situation of heavy annual audit work, Zhonghua Accounting Firm often shortens the audit process to ensure the timely completion of the work.

In the process of auditing, there are always some problems when programs are cut in order to speed up the work progress, but in the final analysis, this is due to the ideological and cognitive problems of auditors. On the one hand, auditors may misjudge the importance of some audit matters in the audit process, and easily think that they only need to obtain a small amount of audit evidence to prove it, so they do not operate according to the requirements of Auditing Professional Ethics, thus neglecting some important audit processes. On the other hand, Zhonghua implements a strict three-level review system, so some auditors are very dependent on this system. They believe that even if something goes wrong in their work, they can make up for it through review, and they only need to finish their tasks on time and record all their work. Therefore, some auditors' working attitude in the audit process is loose, and they only perform tasks mechanically, which leads to inaccurate judgment of the importance level of some businesses, and even ignores key issues. However, audit quality management itself is a process involving all employees, and some auditors do not pay enough attention to it, thus laying a hidden danger for future

work.

3.2. Resource

Before the Zhonghua officially started the audit, it didn't appoint the project leader and team members according to the nature, risk and difficulty of the project. In addition, due to the shortage of time and manpower, Zhonghua often temporarily assigns a group of new employees who have just joined the company and are inexperienced to audit. For this, it is necessary to have a senior auditor to do a good job of supervision.

During the year-end audit in 2015, Zhonghua Accounting Firm did not have much time to train and supervise the novice due to the numerous audit projects and tight task time. In addition, due to the high mobility of the assigned employees and their lack of sufficient work experience, the authenticity and accuracy of information such as operating costs and sales expenses of Yabaite have not been tested. If the Zhonghua can reasonably allocate employees and ensure the coordination of the appointment of employees, it can avoid the audit failure to some extent.

It can be seen that Zhonghua has no discipline in talent allocation planning, no comprehensive staff evaluation, and no selection of suitable staff according to the staff's ability and the actual situation of the project. In such an environment, the lack of coordination and complementarity among team members requires a lot of time and energy to communicate and guide, which greatly affects the implementation and management of audit work.

3.3. Accounting Firm's Risk Assessment Procedures

When confirming and evaluating the quality risk, Zhonghua Accounting Firm didn't fully understand the factors or situations that might cause negative impact on the quality objectives, but only thought that the quality risk of the project was not big according to past knowledge or arbitrarily.

In 2015, Yabaite signed a gambling agreement with its backdoor company on performance commitment. According to the agreement, Yabaite had to ensure that the actual net profit of the company remained above the relevant requirements, which put some pressure on Yabaite. Faced with fierce competition in the industry and huge cash compensation pressure, it can be predicted that Yabaite is difficult to meet the requirements of its performance commitment, and at the same time, it is also faced with high operational risks. All this shows that the management of Yabaite has a strong motivation for financial fraud. However, when Zhonghua Accounting Firm evaluated the quality risk, it failed to consider the impact of this incident on the quality risk, so that Yabaite Company could not be evaluated as an important risk.

3.4. Related Professional Ethics Requirements

When Zhonghua audited Yabaite Company in 2015 and 2016, the agreed audit fees were 660,000 yuan and 630,000 yuan respectively. In that year, the average audit cost of Zhonghua to other listed companies was more than 700,000 yuan. Not only that, in 2016, compared with 2015, the operating income and total assets of Yabaite both increased significantly, but its audit expenses decreased. In the actual audit business, the audit cost depends on the size of the company, the total assets and the amount of audit work. The higher the total assets, the more complicated the actual audit workload and the higher the audit cost. However, the audit fee charged by Zhonghua to Yabaite Company is not only lower than that of other companies in the same period, but even decreases reversely when it should have been increased, which can not help but arouse people's doubts about the independence of this firm. In addition, the low audit cost will also reduce the enthusiasm of auditors for audit work, thus simplifying the relevant audit procedures, leading to neglect of some major misstatement risks that are questionable.

3.5. Customer Relationship and Undertaking and Maintenance of Specific Business

Before starting the audit of the audited entity, we must first know the basic situation of the audited entity, and check whether there are any abnormal changes in its operating conditions and business scope, as well as the credit status of the management. However, Zhonghua obviously didn't fully understand and evaluate Yabaite before auditing, including the following aspect:

3.5.1. Not fully understanding the business environment and scope

As Yabaite was listed on the backdoor in 2015, and signed a gambling agreement with its backdoor company to guarantee its performance, compared with previous years, the risk of fraud of Yabaite under the heavy performance burden is greater. Therefore, Zhonghua not only needs to publicly disclose this matter in the relevant annual audit report, but also needs to re-examine its audit risk. In addition, the company changed its main business type in the same year, and

the businesses before and after the change were not directly related. Therefore, before auditing, Zhonghua must investigate whether there are other changes in technology and human resources behind the changes in its business types[1].

Based on the analysis of the audit results, it can be seen that Zhonghua should actively identify the motivation and pressure of fraud in Yabaite during its initial business activities, focus on whether the company's business type changes and whether the changes have reasonable business reasons, and make a substantial assessment of its existing audit risks. However, in the actual audit work, Zhonghua ignored this important process, which eventually led to audit failure.

3.5.2. Failure to fully understand the integrity of the management

Whether the management is honest or not is the important information that the firm needs to know before auditing. The firm should design and implement the corresponding audit procedures based on the understanding of the management's honesty, and evaluate the authenticity and reliability of the audit evidence. When Zhonghua undertakes audit business, it should pay attention to the integrity of the management of the audited entity, especially deeply understand and evaluate whether the executives are honest or not, and link it with possible fraud motives. However, judging from the series of investigation and evidence collection activities of the CSRC after the audit, it is obvious that the executives of Yabaite have the problem of lack of integrity, while Zhonghua has neither paid corresponding attention to this problem nor taken corresponding measures, which is one of the important causes of audit failure.

3.6. Business Execution

The completed audit work must be checked and supplemented, which is also an important role of the review system. The review mechanism of Zhonghua Accounting Firm includes: firstly, the project leader will review the completed audit work in detail; Secondly, the project implementing partner is responsible for the comprehensive review of the work related to major issues; Finally, at the overall level, the chief partner will supervise and control it comprehensively. However, the review system of Zhonghua Accounting Firm has not been well implemented. During the audit review of Yabaite, the reviewers concentrated on finishing the work on time, and urged the relevant departments to file the work documents in accordance with the prescribed time, but forgot the review tasks specified in the company. In addition, when the relevant supervisor conducts the review, the focus of attention is whether the audit work has been successfully completed, not whether the so-called audit procedures implemented or the audit evidence obtained have eliminated doubts[2]. If the review system can be strictly observed, the review process can be effectively implemented, and the reviewers are conscientious, they can find the negligence and loopholes in the previous work and correct them through the review process. From this point, it can be seen that the three-level review system established by Zhonghua Company has not been well implemented, and can't play the role of leak detection and monitoring.

3.7. Information and Communication

In any failed audit project, it is often a common problem that information transmission and communication are not effective or timely enough. In the process of auditing Yabaite,

Zhonghua Accounting Firm also has some problems, such as poor communication with the general manager and financial supervisor of Yabaite, asymmetric internal information, etc. In addition, when auditing the major misstatement risk of Yabaite, the auditor only conducted a simple audit procedure, but did not conduct a comprehensive internal discussion on the income and expense accounts of Yabaite, thus failing to find the phenomenon that Yabaite fictionalized its sales revenue in 2015 and 2016, and then inflated its profits.

3.8. Monitoring and Rectification Procedures

According to the auditing standards, Zhonghua Accounting Firm should conduct self-examination every three years. However, in practice, it is usually conducted by the leaders of the quality control department and the heads of the supervision departments, which may lead to repeated audits, resulting in a mere formality in the audit process, which reduces the audit quality, which is seriously inconsistent with the principle of separation of incompatible posts required by China's quality control standards. Zhonghua Accounting Firm's record of supervision and evaluation procedure is too simple, and it fails to make a detailed record of the problems and treatment procedures in the process of supervision, and lacks supervision over the implementation of practice standards, professional ethics codes and quality management policies. Under normal circumstances, accounting firms should take timely measures to reduce audit risks and give corresponding penalties when finding problems in audit work, and constantly improve the company's quality management system and process. However, there are some problems in Zhonghua, such as the lag of information transmission, neglect of problem handling, failure to investigate relevant responsible persons, failure to inform internal staff of the firm, etc., which increase the probability of repeated incidents, thus affecting the quality of supervision and failing to ensure audit quality and control audit risks.

4. Countermeasures for Zhonghua Accounting Firm to Improve Audit Quality Management

The purpose of the audit is to provide appropriate audit opinions and ensure the audit quality. How to improve the audit quality is an urgent problem for accounting firms. Therefore, we must learn and summarize the shortcomings of previous audit work, find out the corresponding improvement measures, and ensure the quality of audit work.

4.1. Perfecting Audit Quality Awareness Control from Management

To ensure high-quality audit services, we should first build a corporate culture with quality as the core[3]. Therefore, it is necessary to form a unified working concept within the firm, so that everyone can realize the important role of audit quality management.

Usually, the internal cultural concept of an enterprise is passed from the management to all levels. The management concept and value concept of the staff will directly affect the overall working concept of the firm. Therefore, the development concept of the firm should first be constructed from the management. If they regard profit as more important than business quality, it will affect the long-term development of accounting firms. Therefore, they must change their ideas, not focus on short-term interests, but gain more and longer-

term development benefits from high-quality audit services.

4.2. Rational Use of Audit Human Resources

The previous analysis shows that the audit work arrangement of Yabaite, especially the personnel assignment, presents a random assignment mode, which lacks certain coordination and planning. Therefore, in the audit planning stage, how to allocate human resources reasonably and efficiently is an important link in the personnel entrustment plan. Zhonghua Accounting Firm should change the working mode of random assignment before, so as to ensure the efficient use of human resources and realize the self-worth of each auditor in the audit. On the premise of fully understanding the nature, risk level and difficulty of the project, Zhonghua can assign and distribute personnel according to factors such as qualifications, expertise, independence, rotation years, and the principle of cost-benefit, so as to ensure the establishment of a project team with auditors matching the audit business[4].

4.3. Make Full Use of Risk-oriented Audit

At present, with the increasing complexity of the audit market and the development and integration of different industries, financial fraud by listed companies in order to win the competitive advantage also happens from time to time, which leads to a severe test for accounting firms in the process of maintaining high-quality audit services. Therefore, accounting firms must strengthen their awareness of risks and increase their investment in high-risk projects, so as to enhance their pertinence and purpose, prevent the inefficiency of audit work, and then improve the audit quality. In the audit of Yabaite Company by Zhonghua, because Yabaite Company is a traditional manufacturing industry, cost accounting is the focus of its accounting treatment. Therefore, auditors can reasonably assume that the management has the motivation of financial fraud, and should pay attention to key indicators such as cost carry-over and profit as highly vigilant risk points. In addition, the risk assessment is not only carried out in the understanding stage of the project, but its essence should run through the whole process. Therefore, with the continuous advancement of audit work, auditors should always assess whether there are new risks, timely adjust the audit plan and carry out other audit procedures.

4.4. Integrating Professional Ethics Construction into Internal Management

Zhonghua Accounting Firm failed to observe its due professional ethics when auditing Yabaite. Therefore, Zhonghua Accounting Firm should carry out the construction of auditing professional ethics throughout the whole process of internal management, and urge it to abide by its own professional ethics in the auditing process by means of supervision and education. At the same time, Zhonghua can also build its own internal management rules and regulations, so that every auditor can audit under the rules and regulations. In addition, it is necessary to strengthen the supervision of professional ethics and establish a sound reward and punishment mechanism to promote and restrict auditors' attention to professional ethics. Finally, professional ethics education should be strengthened in continuing education, professional title examination and other aspects, so that auditors can establish professional beliefs and strictly abide by professional ethics.

4.5. Strictly Undertake Business

In recent years, apart from the audit failure of Yabaite Company, Zhonghua Accounting Firm has been punished by CSRC for many times, and its reputation in the industry has gradually declined. The reason is that Zhonghua Accounting Firm has failed to achieve effective business undertaking control. Therefore, Zhonghua Accounting Firm should establish a sound business undertaking audit system, fully consider various factors before undertaking business, set up a completely independent team to audit the business undertaking, avoid neglecting the evaluation of the client and the company itself due to the close relationship between partners and clients, pay attention to the abnormal indicators and phenomena, properly put forward possible risks in relevant audit papers, and obtain sufficient audit evidence to eliminate doubts[5]. In addition, Zhonghua Accounting Firm should actively implement the brand strategy of enterprises, strengthen the brand concept of enterprises, enhance brand building, and stand out in the auditing industry with high-quality service and good image, so as to improve the reputation of enterprises.

4.6. Strengthen the Business Execution Review Mechanism

In recent years, the characteristics and financial situation of the audited units have become increasingly complicated, and the implementation of audit business has become more and more difficult. Everyone who participates in the audit project will directly affect the audit quality. Therefore, the firm should clearly divide the responsibilities of all levels to ensure the effective implementation of the review mechanism[6]. First of all, Zhonghua Accounting Firm should improve its internal control, establish a sound quality monitoring system, make the division of responsibilities clear and reasonable, so as to achieve the purpose of improving audit efficiency. Secondly, it is necessary to implement the audit accountability system in the whole process, and put the specific responsibilities of each link into everyone's body, so as to truly track the whole process of audit work and monitor the audit quality in all directions[7]. Finally, Zhonghua Accounting Firm should strengthen the independence of auditors to ensure that the audit work will not become a mere formality because of its close relationship with the audited party; At the same time, we should further refine the business review, so as to find key errors and risks in a targeted manner, and then strengthen the control of audit quality.

4.7. Establish and Improve the Communication Mechanism of Major Issues

Zhonghua Accounting Firm should emphasize that auditors can communicate with each other in time on questions with doubts or matters worthy of attention during the audit, including within the project team or between the project team members, the accounting firm and the audited entity, so as to ensure that sufficient and appropriate audit evidence can be obtained; At the same time, it is also possible to improve the internal informatization construction, build a shared database platform[8], and ensure that the project team members can transfer information in time and effectively, so as to avoid providing inappropriate audit opinions due to information asymmetry.

4.8. Strengthen the Monitoring of Audit Business

Zhonghua Accounting Firm shall appoint experienced and experienced auditors who are responsible for guiding and supervising all aspects of the audit project. In view of the situation that the audit process is inconsistent with the specific audit scheme, the on-site supervisor should point it out in time and check its applicability, so as to avoid auditors from auditing according to subjective judgment. Guide and monitor the difficult problems in the audit work, conduct a comprehensive review of the implemented audit procedures to ensure that the required audit procedures have not been simplified, and make corresponding records of the supervision, so as to provide a basis for the effectiveness of the supervision. In addition, a special person should be appointed to supervise the quality management at all levels, and the person in charge of supervision should report to the auditors and correct them, and record them at the same time to ensure the effectiveness of quality management.

To sum up, strictly following the quality management system is the key measure for accounting firms to implement the audit quality optimization effect. Firms should constantly improve the quality management system and achieve full coverage among the audit process, audit procedures and auditors, so as to comprehensively improve their audit quality and better serve the rapid development of modern economy and society.

5. Conclusion

As the main body of social audit, accounting firms play an important role in the market. However, in recent years, there have been many problems in China's audit quality, which seriously questioned the effectiveness of audit quality management. Therefore, based on the audit case of Yabaite Company by Zhonghua Accounting Firm, this paper makes an all-round and multi-angle analysis from the perspective of quality management system framework, and summarizes its existing problems. At the same time, in order to improve the audit quality management of Zhonghua Accounting Firm, some improvement suggestions are put forward, in order to be helpful to the audit quality management of this accounting firm, and play a certain reference role for the development of accounting firms in China.

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