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2. A Study on the Role of Stakeholders and Auditors in Global Financial Crisis

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Abstract:

This article aims to qualitatively examine the ways in which the financial crisis affected auditors and how auditing practices may be changed to avert such crises in the future. Although audit quality has been extensively studied, it is still a challenging notion to assess, which is why a number of proxy metrics have been created. Since it allows for the analysis of a relatively small sample size, the earnings quality measurement discretionary accruals have been selected as the proxy measurement for this study. This is because it catches tiny variations in audit quality. With an emphasis on risk assessment, internal control review, and handling complexity in financial instruments, this study explores the critical role that auditors play in reducing the risks connected with financial crises. Data were acquired through thematic analysis and a thorough examination of the literature using a qualitative research approach. The results highlight the importance of auditors in maintaining financial integrity by spotting fraud and mistakes in financial statements and boosting openness and investor confidence. Additionally, the evaluation of internal controls by auditors supports compliance risk management and fraud prevention, both of which are essential for organizational resilience. We will talk about in this essay. research on the part auditors and stakeholders played in the global financial crisis.

Keywords:

Stakeholders, Auditors, Global Financial Crisis, Sales Strategies, Customer Demands, Global Economy, Corporate Governance, Stock Market Crashes, Emerging Trends, Cybersecurity Audits, AI Integration.

2.1 Introduction:

Demand, supply, logistics, resources, and talents are all interconnected in today's global economy. A business's processes, goals, objectives, related risks, policies, procedures, sales tactics, client expectations, and many other aspects are all altered when a crisis arises. Change, however, is not only visible or physical; it is also habit- and emotion-oriented. Uncertainties and risk dimensions may increase if the business does not operate as usual.

Given the abrupt nature of the effect and the subsequent cascade of changes, monitoring these ups and downs requires close attention to detail about procedures and readiness.

In contrast to previous decades, stakeholders in 21st-century firms, including customers, employees, rivals, creditors, the government, and the general public, are more concerned with the organizations and their performance than they were in the past. Depending on the stakeholder and their level of interest as well as expectations from the organization, there are differences in the reasons behind their interest in the organization and its performance. [1]

The majority of well-known, prosperous businesses in today's commercial environment are either private or public limited firms. In those businesses, the owners or shareholders and the management are two distinct parties. As a result, an agency relationship arises between the owners and the management of the company, with the managers functioning as the agents of the principles and managing the owners' funds to increase the wealth of the shareholders. Because of this agency arrangement, managers answer to the shareholders. As a result, the duty to compile the financial statements for each fiscal year and inform the shareholders of the performance of each year remains with the managers and the Board of Directors.

Financial crises have a significant impact on financial markets, institutions, and the larger socioeconomic fabric. They have long been a common occurrence in the global economy. Therefore, it is critical to comprehend how different stakeholders—including auditors—play a part in reducing the risks and consequences associated with these crises. In order to better understand the complex role that auditors play in averting financial crises, this qualitative analysis will look at the roles, difficulties, and efficiency of auditors in preserving financial stability. As an independent source of assurance regarding the dependability and correctness of financial statements, auditors are essential to the financial system. Their main duty is to determine if financial statements accurately depict an organization's financial situation and performance in compliance with applicable legal and accounting standards. Auditors provide insightful analysis to stakeholders, including as creditors, investors, and regulatory bodies, by methodically examining financial records, internal controls, and risk management procedures. This promotes openness and confidence in financial reporting. [2]

Auditors were essential to financial reporting and supervision during the global financial crisis. Going Concern Opinions, which had important ramifications for stakeholders, were issued by them after they evaluated the Going Concern Assumption. In order to help regulatory agencies stabilize the world economy and harmonize banks' risk reporting with accounting systems, auditors were also invited. The crisis raised the danger of an audit engagement, especially for money market funds, which prompted auditors to raise their rates for the riskiest fund class.

Those who have the power to affect or are influenced by others' actions are known as stakeholders. Stakeholders often represent not only their own interests but also those of other individuals, families, groups, organizations, collectives, and even inanimate objects like plants, animals, and future generations. Organizations and individuals that initiate, respond to, and are impacted by an enterprise crisis are considered stakeholders in the matter.

Authorized staff members who examine and confirm the accuracy of financial documents and guarantee that businesses adhere to tax regulations are known as auditors. Their main goals are to safeguard companies against fraud, draw attention to any inconsistencies in accounting procedures, and, among other things, provide a judgment on the accuracy and fairness of financial accounts. In this instance, an auditor's job is to examine a company's financial data and make sure that it is accurate and compliant with regulations.

The set of procedures, relationships, and controls that different stakeholders utilize to manage and run a corporation is known as corporate governance.

In order to ensure that all departments are adhering to a specified system of documenting transactions, an auditor will physically check inventories after examining or inspecting various books of accounts. The purpose of this is to verify if the organization's financial accounts are accurate. [3]

The time between mid-2007 and early-2009, when global financial markets and banking systems were under tremendous strain, is known as the global financial crisis (GFC). A US housing market collapse during the Great Financial Crisis (GFC) served as a trigger for a worldwide financial crisis that extended from the US to every country in the globe due to connections in the global financial system. Around the world, a lot of banks suffered substantial losses and had to rely on government assistance to stay afloat. The major industrialized economies went through their biggest recessions since the 1930s Great Depression, which resulted in millions of job losses. In comparison to previous recessions that were not accompanied by a financial crisis, the crisis' recovery was also considerably slower. [4]

2.2 Review of Literature:

The definition of financial crises is constantly altering to reflect the ever-shifting dynamics of the global financial landscape. These occurrences include stock market crashes, currency crises, banking crises, and sovereign debt defaults. New trends, contributory variables, and the changing role of auditors in reducing the risks connected to such disasters have all been clarified by recent study. The comprehension of financial crises has been transformed by a number of recent advancements that have been recognized by academics. One noteworthy trend is the financial markets' growing complexity and connection, which is being fueled by financial innovation, globalization, and technology improvements. Due to increased interconnectedness, there is a greater chance of systemic risk and cross-border contagion when financial shocks spread through more channels (Reinhart, 2009). [5]

Internal audit and controls have grown in importance over the last ten years. The goal of this research is to present survey data regarding the value of internal controls, their ability to deter fraud, and their ability to raise the caliber of financial reporting. Financial reporting fulfills the following functions, according to the IFRS 2011 guide: general intention The goal of financial reporting is to give financial data about the reporting organization so that it can be evaluated for resource provision and to see how well its governing board and management have managed those resources (Bruce, 2011). Numerous academics and standard-setters have stressed the importance of accurate financial reporting. In order to stop fraud and errors, the audit intern is crucial. As was already indicated, in order to utilize the resources at hand effectively and efficiently, trustworthy financial reports are required. If companies produce trustworthy financial reporting, they ought to consider the role of auditors. [6]

2.3 Objectives:

- To identify the suitability of such changes to international standards on Auditing issued to address the global financial crisis.
- A study on the role of stakeholders and auditors in global financial crisis
- Financial Crises and Stakeholders

2.4 Research Methodology:

Research methodology guides researchers in the gathering, processing, and interpretation of data and forms the basis for carrying out thorough and systematic investigations. An orderly and systematic approach has been taken in our analysis of the complex relationships between auditors, stakeholders, and the Global Financial Crisis (GFC). The research paper is an endeavor that is founded on secondary data that was obtained from reliable online resources, newspapers, textbooks, journals, and publications.

2.5 Result and Discussion:

After that, the specialist examined the lessons discovered and contributed to the creation of suggestions for resolving the major problems that surfaced during the crisis. Governance of corporations following the global financial crisis Anger shot up. It displays connections between reviews. The financial crisis led to a broad wave of reforms, and more recent reforms have prioritized disclosure and corporate governance. Corporate Sphere Insolvency In the global financial market, operational management is evaluated at every level of regulation. Not only are financial institutions changing, but so are other publicly traded companies. Large A number of governments have started updating their corporate governance regulations. rules other than the evaluation of the system of financial supervision. The management of key markets has brought about significant changes, including in executive compensation and risk management, shareholder rights, the caliber of board control, and corporate governance disclosure. This is due to the regulator's appetite for stronger governance standards and a stronger voice for corporate shareholders. [7]

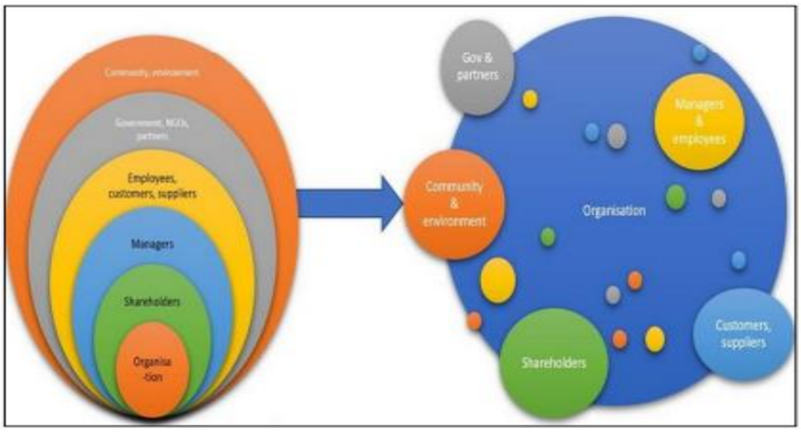

Figure 2.1: Financial Crises and Stakeholders

The market for auditing services has expanded significantly in the last several years. At a cumulative annual growth rate (CAGR) of 5.5%, it will increase from $226.82 billion in 2023 to $239.29 billion in 2024. The expansion noted during the historical period can be ascribed to the following: business globalization; regulatory compliance; increased complexity of financial transactions; emphasis on investor confidence and public accountability; and growing necessity for risk management and corporate governance practices.

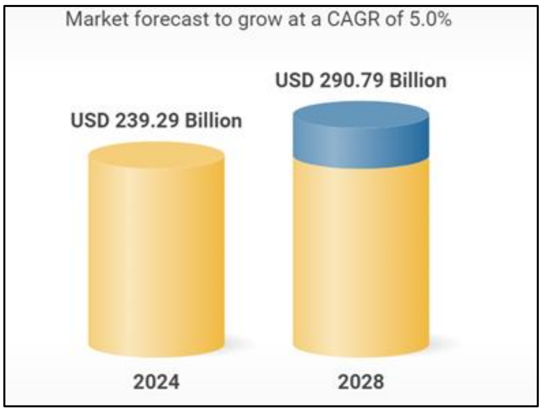

Figure 2.2: Global Auditing Services Market (Source: www.researchandmarkets.com)

Over the coming years, a steady expansion in the size of the auditing services industry is anticipated. It will increase at a compound annual growth rate (CAGR) of 5.0% to $290.79 billion in 2028. The focus on ESG auditing, cybersecurity audits, remote auditing solutions, internal team communication, advanced data analytics, and AI integration are the main drivers of projected growth.

Adoption of regulatory technology (Reg Tech), blockchain integration, technology breakthroughs, digital transformation in auditing, and increased attention to data protection are some of the major themes. The auditing services industry is expected to grow in the near future due to the predicted increase in corporate spending on financial audits and recording. Driven by a heightened focus on financial transparency, regulatory compliance, and strong corporate governance procedures, this trend is defined by an increase in the financial resources that firms devote on auditing and recording activities. In order to help businesses detect fraud and mistakes in financial statements, comply with legal requirements, improve internal controls, and reduce risks, auditing services are essential.

For instance, the US-based private research institution Harvard Law School stated in November 2022 that the total auditing fees for businesses that report in a fiscal year reached $18.9 billion in 2021, indicating a 3.3% increase from 2020. Interestingly, average costs for audit services and average amounts paid by Securities and Exchange Commission (SEC) registrants increased to $2.17 million and $0.23 million, respectively. In addition, the average audit cost increased, hitting $1.9 million for US corporations and $2.9 million for international companies by 2021. [8]

2.6 Financial Crisis and Auditors:

The financialization of Western economies, particularly the US economy, is a prominent aspect of the current financial crisis. This process generated a lot of credit and encouraged excessive risk-taking through the use of sophisticated financial instruments (such as credit default swaps and derivatives), corporate structures, and inefficient regulatory frameworks (Ferguson, 2008; Morris, 2008; Soros, 2008). Insurance firms, banks, and hedge funds all played significant roles in the financialization of the economy and are thought to have lost around US$2.8 trillion.

Historically, investors and regulators have depended on company financial statements to understand bank exposure, risks, and liabilities, but this has proven to be a very problematic approach. According to a preliminary estimate (Financial Times, June 3, 2008), banks held approximately US$5000 billion in assets and obligations off their balance sheets despite a plethora of accounting regulations. However, this amount is subject to regular revision. A mere $1.23 trillion in assets are held by Citigroup alone in organizations that are not included on its balance sheet (Wall Street Journal, November 24, 2008).

Derivatives have historically been a "powerful tool for inflating company profits by hiding losses and hence the risks of company operations," and some banks have shown assets, particularly subprime mortgages, at significantly inflated valuations (Hildyard, 2008, p. 30). According to the the chief executive officer of a well-known financial advising company, "a large portion of the issue is that accounting rules have allowed banks to inflate the value of their assets." Because accounting has evolved into a new genre of creative writing, banks are now carrying a large amount of "sludge" assets that are cluttering the balance sheet.

Because it is believed that "a green light from an auditor means that a company's accounting practices have passed muster," auditors have come under scrutiny (New York Times, April 13, 2008).5. Table 1 demonstrates that unqualified audit opinions were given to distressed financial firms in the UK, USA, Germany, Iceland, The Netherlands, France, and Switzerland about their financial statements that were released just before they were publicly declared to be in financial difficulties. A Big Four accounting firm, PricewaterhouseCoopers (PwC), Deloitte & Touche (D&T), Ernst & Young (E&Y), and KPMG, supplied these opinions. [9]

Table 2.1: Auditors and distressed Banks

Company	Country	Year end	Auditor	Date of audit report	Audit opinion	Fee (millions)	
						Audit	Non-audit
Abbey National	UK	31 December 2007	D and T	4 March 2008	Unqualified	£2.8	£2.1
Alliance and Leicester	UK	31 December 2007	D and T	19 February 2008	Unqualified	£0.8	£0.8
Barclays	UK	31 December 2007	PwC	7 March 2008	Unqualified	£29	£15
Bear Stearns	USA	30 November 2007	D and T	28 January 2008	Unqualified	$23.4	$4.9
Bradford and Bingley	UK	31 December 2007	KPMG	12 February 2008	Unqualified	£0.6	£0.8
Carlyle Capital Corporation	Guernsey	31 December 2007	PwC	27 February 2008	Unqualified	N/A	N/A
Citigroup	USA	31 December 2007	KPMG	22 February 2008	Unqualified*	$81.7	$6.4
Dexia	France/ Belgium	31 December 2007	PwC + Mazars and Guérard	28 March 2008	Unqualified	€10.12	€1.48
Fannie Mae	USA	31 December 2007	D and T	26 February 2008	Unqualified	$49.3	–
Fortis	Holland	31 December 2007	KPMG + PwC	6 March 2008	Unqualified	€20	€17
Freddie Mac	USA	31 December 2007	PwC	27 February 2008	Unqualified*	$73.4	–
Glitnir	Iceland	31 December 2007	PwC	31 January 2008	Unqualified	ISK146	ISK218
HBOS	UK	31 December 2007	KPMG	26 February 2008	Unqualified	£9.0	£2.4
Hypo Real Estate	Germany	31 December 2007	KPMG	25 March 2008	Unqualified	€5.4	€5.7
Indymac	USA	31 December 2007	E and Y	28 February 2008	Unqualified*	$5.7	$0.5
ING	Holland	31 December 2007	E and Y	17 March 2008	Unqualified	€68	€7
Kaupthing Bank	Iceland	31 December 2007	KPMG	30 January 2008	Unqualified	ISK421	ISK74
Landsbanki	Iceland	31 December 2007	PwC	28 January 2008	Unqualified	ISK259	ISK46
Lehman Brothers	USA	30 November 2007	E and Y	28 January 2008	Unqualified	$27.8	$3.5
Lloyds TSB	UK	31 December 2007	PwC	21 February 2008	Unqualified	£13.1	£1.5
Northern Rock	UK	31 December 2006	PwC	27 February 2007	Unqualified	£1.3	£0.7
Royal Bank of Scotland	UK	31 December 2007	D and T	27 February 2008	Unqualified	£17	£14.4
TCF Financial Corp	USA	31 December 2007	KPMG	14 February 2008	Unqualified	$0.97	$0.05
Thornburg Mortgage	USA	31 December 2007	KPMG	27 February 2008	Unqualified	$2.1	$0.4
UBS	Switzerland	31 December 2007	E andY	6 March 2008	Unqualified	CHF61.7	CHF13.4
US Bancorp	USA	31 December 2007	E and Y	20 February 2008	Unqualified	$7.5	$9.6
Wachovia	USA	31 December 2007	KPMG	25 February 2008	Unqualified	$29.2	$4.1
Washington Mutual	USA	31 December 2007	D and T	28 February 2008	Unqualified	$10.7	$4.3

Notes: Information derived from statutory filings and financial statements that are accessible on the website of the relevant business. [10]

2.7 Conclusion:

The confidence that a company's financial statements are accurate, dependable, and compliant with relevant accounting and regulatory requirements is something that audits are essential in delivering to stakeholders. Auditors were essential to financial reporting and supervision during the global financial crisis. Going Concern Opinions, which had important ramifications for stakeholders, were issued by them after they evaluated the Going Concern Assumption.

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