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A Study on the Role of Auditing to Prevent Financial Crisis

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Abstract: *The monetary disaster that we encountered in the latest decade didn't get going abruptly. The root reasons of the monetary emergency should be concentrated by scholastics. We'll attempt to zero in on inward control and interior review concerning corporate administration. A monetary disaster might be not too far off, as per research, yet the primary drivers are an absence of monetary identification and an absence of information about the significance of the inner review capability in the inner control framework. Inner review is a significant principle of business administration. To upgrade the review cycle and comprehend how monetary evaluators see their insight into inside controls as a figure the formation of excellent monetary detailing, our review will investigate this viewpoint. In this review, we additionally assess the significance of interior review in the interior control framework utilizing information from 70 of the 1178 individuals from the Romanian Monetary Examiners Chamber who are evaluators from everywhere the nation of Romania. To feature the exploration, we have zeroed in on the exact examination in Romania*

Keywords: Internal audit, internal control, fraud, financial crisis, and ACFE (Association of Certified Fraud Examiners).

I. INTRODUCTION

Over the past ten years, internal audit and controls have become far more important. This study intends to provide survey evidence on the necessity of internal controls, their effectiveness in preventing fraud, and their capacity to improve the standard of financial reports. The IFRS 2011 guide states that financial reporting serves the following purposes: general intent The purpose of financial reporting is to provide financial information about the reporting institution that can be used to assess whether or not to provide it with resources as well as how effectively and efficiently its management and governing board have used those resources (Bruce, Danie, Tapiwa, & Raymond, 2011). The need of accurate financial reporting has been emphasised by several academics and standard-setters. The audit intern is essential in preventing fraud and mistakes. As previously mentioned, reliable financial reports are necessary to make efficient and effective use of the resources available. Companies should think about the role of auditors if they deliver reliable financial reporting.

Accounting scandals like those involving Enron in 2001, WorldCom in 2002, Qwest Communications, Adelphia, Global Crossing, Nortel, and Parmalat at the beginning of the twenty-first century complicated the financial world and highlighted its complex character. External auditors have faced criticism following this type of financial catastrophe, but academics have understood the importance of internal audit and that it cannot be ignored.

The Institute of Internal Auditors (IIA, 2011) defines internal auditing as an unbiased, objective assurance and consulting activity intended to provide value and improve an organization's operations. It helps a firm achieve its objectives by using a methodical, disciplined approach to assess and improve the effectiveness of risk management, control, and governance systems. Studies show that after the accounting crises, internal audit staffing and resources have increased by 10%. The audit committee and internal audit department now communicate and share information 25% more frequently than they did prior to crises. Year 2009 (Atanasiu& A).

The internal audit function plays a specific role in corporate governance by monitoring organisational risks and making sure thatorganisational procedures are effective and regulated (IIA, 2003). For the financial system to operate correctly, internal audit and internal control, which are elements of corporate governance, serve as its pillars. It goes without saying that it makes sense if the senior management confirms and evaluates the internal audit reports. If top management doesn't have time to evaluate reports and ignores them, the organisation starts to deteriorate. Based on this assertion, the study aims to show how crucial internal audit is to the system of internal controls for the financial markets. The creation of the financial reports will be aided and irregularities will be prevented if the internal control function is efficient.

II. REVIEW OF LITERATURE

Numerous sources (e.g., AICPA 2007; Beck 1986; Bierstaker et al. 2006; Heier et al. 2005; Hooks et al. 1994; Mautz and Mini 1966; PCAOB 2008; Rae and Subramaniam 2008; Wales 1965; Wells 2008) claim that an effective internal control system (ICS) is the key to preventing, spotting, and fixing fraud and mistakes. However, ex post forensics, a type of induction, performed by practitioners, mostly assumes what precisely an effective ICS is. (Barra, 2010)

Recent academic studies have shown that a strong internal audit system could thwart financial statement fraud. Management may try to use falsified accounting techniques to make the business appear financially successful by indulging in financial statement fraud. Auditors should approach the examination of financial accounts with considerable scepticism. Taxonomies of financial statement fraud are also established to distinguish common fraud strategies (Rezaee, 2009).

The Association of Certified Fraud Examiners (ACFE) has studied the effects of internal control gaps in depth. This study pinpoints the crucial component that enabled fraud. In 38% of the instances, a deficiency in internal controls, such as a lack of task division, was cited as the primary failing. In more than 19% of the cases, internal controls were there, yet the fraudster or fraudsters got around them to commit and cover up the crime. Given that hotlines are consistently the most effective detective control mechanism and that less than half of the victim organisations had one in place at the time of the fraud, it is interesting that the lack of a reporting mechanism was the control deficiency that was least frequently cited by the CFEs who participated in our study. (ACFE, 2010)

Prawitt et al. (2009) claim that by minimising potential errors in incentive system design, the Internal Audit Function (IAF) can improve reporting quality.DumitruMatis and Cristina Bota (2010) carried out a further nationwide investigation in Romania. The goal of this study's authors was to determine how crucial it is to create an internal audit report in order to ensure effective corporate governance. In order to ensure openness for healthy corporate governance, one of the questions posed to respondents inquired if they recognised an opportunity or necessity for the internal audit report. Yes, creating the internal audit report can aid in increasing transparency, according to 58,70% of respondents. 39.13% of respondents, however, disagreed.

In 2006, one of the significant internal audit studies by Holt and DeZoort was released. (Holt &DeZoort, the Perceived Reliability of Financial Reporting and the Effects of Internal Audit Report Disclosure, 2006). The objective of this empirical study was to show how the internal audit report affects investors' confidence in the veracity and correctness of financial reporting. Investors claim that they have greater faith in organisations that create internal audit reports than in those that do not when it comes to the accuracy of their financial reporting.

The same writers later developed this work. Their research focuses on ways to increase the governance transparency of internal audit reports for external stakeholders. To evaluate the potential costs and benefits of IAR disclosure, including increased transparency and accountability as well as increased information load, legal exposure, and reporting costs, they analyse the literature and the findings of 18 semi-structured interviews with analysts, audit committee members, internal auditors, and policymakers. They reach the conclusion that an IAR has the ability to improve the governance disclosures that are currently made, increase stakeholder confidence in the efficiency of governance, and promote internal audit vigilance. Improved Governance Transparency Requires an Internal Auditor Report to External Stakeholders (2008) Holt, DeZoort, and Deborah descriptive analysis of internal control device opinions from financial auditors.

The second research issue, which is represented by an accurate understanding and appreciation of the internal control mechanism, is covered in the section "Knowledge and Assessing of Internal Control" in particular. Respondents are asked to rank the importance of various risks that can be reduced by utilising internal control mechanisms in the first question in this section.

The independent audit committee's role is to oversee the financial reporting process, which must produce reliable, accurate financial data. Of course, as a result of this monitoring method, the audit committee shouldn't spend the entire day in the organisation overseeing the accounting records. Deficits in internal control systems are seen to be a primary factor in financial data falsification. Inadequate internal controls over financial reporting and accounting procedures could have a detrimental impact on the ability to guarantee timely and accurate financial reporting. On the other hand, every publicly traded company must have an internal control department that is appropriate for its size and that employs knowledgeable people who can confirm whether the financial reports were produced consistently and accurately.

III. CONCLUSION

The AFCE has identified three main occupational frauds:
1. Misappropriation of assets
2. Corruptness
3. A false financial statement.

These professional frauds, according to the ACFE (Association of Certified Fraud Examiners), include: Asset misappropriations are frauds in which the perpetrator takes or improperly uses an organization's resources. An employee participating in a corruption scheme uses their power in business negotiations in a way that violates their obligation to the employer in order to benefit either themselves or a third party. Financial statement fraud refers to plans that intentionally falsify or omit important information from an organization's financial reporting. Common fraudulent financial statement manipulation strategies include falsely recording income, concealing commitments or expenses, and fraudulently inflating reported assets (ACFE, 2010).

The aforementioned definitions of fraud serve to emphasise the importance of internal control in the financial markets. We conclude that internal control is important in the financial markets. The internal control reports must be prioritised by executive management and the business administration for them to be effective. Internal control applicants run the risk of having their efforts overlooked, which could result in insolvency, especially for firms.

Particularly in the previous ten years following the 1929 USA financial crisis, there have been enormous financial losses. We live in a global community where every financial activity has the potential to affect other financial markets globally. The first step in avoiding any financial concerns is to produce reliable and accurate financial reports. Financial crises in the financial markets will unavoidably occur in the absence of such action, and this could unleash a destructive wind that has an impact on the global financial system. Numerous practitioners and auditors have examined the effects of internal control while developing mathematical models since financial markets serve their functions globally. An internal control must have all of its parts working together in order to be successful. Otherwise, it would be difficult for senior managers to make prudent decisions, and this kind of bad decision could cause the company's financial structure to quiver.

As a result of the research and in accordance with the research, internal audit may improve the transparency and quality of the financial position. Users of financial information should understand the financial reports correctly to prevent adversely affecting the decision-making process. Additionally, research shows that the internal audit report is significant and a chance for the senior management of the companies. Results from the studies mentioned above could vary from nation to nation. Here, an opinion regarding the new European country that transitioned from communism to democracy in 1989 is being attempted. Compared to other Balkan countries, Romania was the most successful at attracting foreign investment. Romania may be the region's former communist country that has adapted to eastern countries the best.

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