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GLOBAL FINANCIAL CRISIS: ACRITICAL STUDY OF THE ROLE OF AUDITORS AND STAKEHOLDERS

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Abstract- The purpose of this paper is to investigate qualitatively how the financial crisis ducted auditors and how the auditing practice can be modified in order to prevent future financial crisis. Audit quality is a widely researched topic but remains a complex concept that is difficult to quantify, which is why several different proxy measurements have been developed. The earnings quality measurement discretionary accruals has been chosen as the proxy measurement for this study as it captures small variations in audit quality which is important since it allows for analysis of a relatively small sample size. Lastly, concluded that the global financial crisis came as a result of excessive risk taking on the one hand and high irresponsibility on the other hand. It is true that auditing might have gone a long way to reduce the gravity of this crisis. But to mitigate future occurrences, it is going to take more than just auditing to prevent it since much research points to the fact that auditing alone was not enough to stop the crisis.

Keywords: Financial Crisis, Audit Quality, Mitigate Future Occurrences, Quality Measurement

I. INTRODUCTION

The global economic crunch or melt down that stroke the world starting from 2008 is one of the greatest financial crises that planet earth has experienced since the great depression. This crisis left many people in a state of doubt concerning what the actual cause of the crisis was. Many blamed the crisis on the free market and its excessive risks taking. After the fall of Enron, it came to notice that the auditors of Enron could go a long way to indicate to investors and make public the accounting procedures used by Enron to show escalating profits on an accrual basis (using their so called mark to market accounting), as a result some international accounting standards and international auditing standards were introduced and others were modified in a bit to see how future occurrences of this nature could be mitigated. Just a few years later, the world was hit not just by a corporate failure but by a global financial meltdown. In these trying times, accountants and auditors, to use the words of one observer, "have come to it." While not without flaws in a highly complex environment, professional accountants have been proactive in working with regulators when market crises have occurred. The expert then analyzed the lessons learned and helped formulate recommendations to help address key issues that arose during the crisis. Corporate governance after the global financial crisis Anger suddenly rose. It shows links between reviews Broad wave of reforms following the financial crisis and recent reforms focus on corporate governance and disclosure. Corporate Governance Bankruptcy Operational management is assessed at every level of regulation in the global financial market. There are changes not only in financial institutions but also in other public corporations. Big Several jurisdictions have begun revising their corporate governance codes. Regulations other than the assessment of the financial supervision system. Appetite regulator for stronger governance standards and a stronger voice for corporate shareholders the management of key markets has brought significant changes, including in executive compensation and risk management, shareholder rights the quality of board control and corporate governance disclosure.

ISSN- 2394-5125 VOL 6, ISSUE 01, 2019

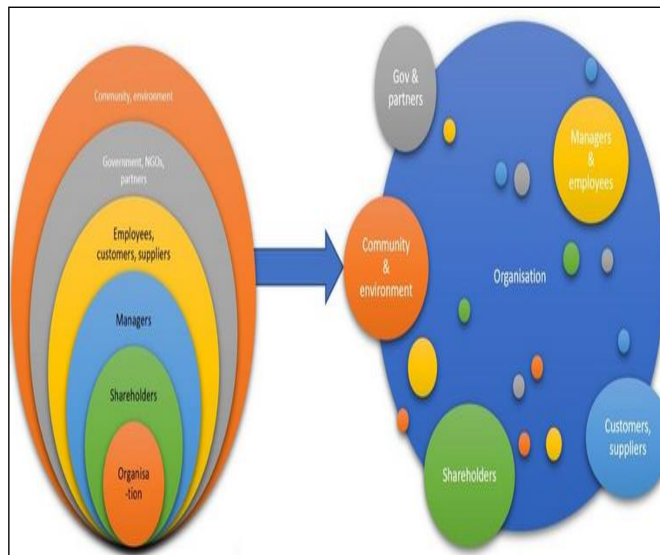

Figure 1.1 Financial Crises and Stakeholders

1.1 The Economic and Market Drivers of the Crisis

To understand accountants and the financial crisis of 2007-2009, it is useful to first examine the causes of the recession. Historians continue to study and debate the underlying factors, but examination of the chronology of the crisis shows that the main driving force is economic and market factors - accounting scandals (such as the failure of Enron or Worldcom) or employee reporting, as seen in this United . states. . Securities and Exchange Commission (SEC), Fair Value Accounting Practices. Simply put, easy access to seemingly cheap credit to finance the growing supply of housing, the proliferation of innovative financial products, and the ease of credit standards and documentation, burst the asset bubble.

This economic shift is marked by a failure to manage risk at multiple levels. Consumers owe too much. Lenders issued subprime mortgages that were packaged and resold. Lenders had large amounts of risky leveraged products. Investors bought complex securities they did not understand. All these factors, in turn, triggered a crisis in the global financial system due to an unprecedented level of interconnectedness.

1.2 Understanding the Role of the Auditor

Could the accountant have prevented this crisis? Was it their duty? In short, no. Public Company Accounting Oversight Board (PCAOB) Chairman James Doty said in his 2011 address to the accounting profession in times of crisis that accountants have no responsibility to "implement good risk management practices in financial institutions." Or, in 2011, James L. Crocker, the SEC's chief accountant at the time. "Auditors need to understand how these risks affect financial reporting risks," he said. Strategies". Kroeker adds that audits "are not and should not be designed to eliminate all investment risk".

Croker's testimony echoes observations made in 2010 by the Financial Reporting Council (FRC), a UK financial regulator. In its commentary on the European Union (EU), the FRC noted that "there is a gap in expectations between the actual scope of the audit and the public's perception of the information that the audit should reveal". "The main purpose of the audit is to provide shareholders with independent assurance that the directors have prepared their financial statements correctly," the FRC said. "There is no audit to give general views or opinions on the business model of the company," he added.

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II. RESEARCH OBJECTIVE

The purpose of this article is to qualitatively examine how financial crises prepare accountants and how auditing practices can be applied to prevent future financial crises. But before we get into it, let's first try to show what caused the financial crisis. And later in this section, we will try to answer the following questions:

• Is the bank's management taking excessive risks to harm investors?

• The internal auditor of the audit report 25. Show the essence

This is true? • What role did accountants play in the emergence of this crisis?

• Can the auditor reduce or eliminate the severity of the crisis?

III. LITERATURE REVIEW

Following the global economic turmoil of recent years, researchers have conducted extensive research to identify the root causes of financial crises and to determine what can be done to reduce the risk of similar crises in the future. Although none of them believed that auditing was a major cause of financial crises, auditors, like all capital market participants, should consider the lessons learned from the crisis and their role in improving auditing standards. Others that may contribute to market integrity and investor protection. But some researchers have painted a picture of the causes of the recent financial crisis: The explosion of innovative financial products, easy access to cheap home loans and loan underwriting and documentation standards that ultimately created an asset bubble. It bursts like an asset bubble (Carmassi et al., 2009). It was an economic shift resulting from the disruption of risk management at many levels. Consumers borrowed too much. Lenders issued and resold subprime mortgages, and these lenders held large amounts of risky, leveraged products. Investors bought complex securities they did not understand. The interconnectedness of the financial system made the impact of adverse changes even greater. The root of the crisis is about leveraged financial institutions (banks) that make money by taking risks.

Banks are just one category of financial institutions. According to Hull (2007), a financial institution is an institution that performs many functions, but its main function is to act as an intermediary between buyers and sellers of financial services such as lending funds and insuring risks. Financial services are broadly divided into custodians, insurance companies, finance companies, investment and securities banks, companies, pension funds and mutual funds. A bank, like any other company, is a limited liability company with separate management and control. 26 are limited liability companies, owned by banks Managed and controlled by shareholders and board of directors move. This separation of ownership and management often leads to conflicts of interest between the owners of the bank and those who lead and manage the banking operations, resulting in the bank being run with each stakeholder always looking out for their own interests. at the expense of other stakeholders. This requires good corporate governance measures from banks that can eliminate conflicts between those who own and manage the company and those who are in any way connected to the bank (creditors, governments, employees, taxpayers - other stakeholders). minimum) balance interests and conflicts, especially when it comes to risk management in banks. Now comes the problem. Can the board manage the bank's risk? While we cannot answer this question with an immediate yes or no, the Board will look at the factors or issues that make it difficult for banks to manage their risk. Lucien & Spamann (2010) argued that the reward structure of bank executives provided incentives for excessive risk-taking. Preferred shareholders, depositors and taxpayers. They explain that this has encouraged managers to underweight the downsides of risky strategies. According to Lucien & Spamann's (2010) analysis of bank financing structures and fees, bank executive fees are generally associated with high leverage of bank asset values. This is because bank CEOs often own the bank's common stock, and because of their limited liability, they often take risky actions that are

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optimal for personal benefit but highly disproportionately socially disproportionate. Excessive risk here means risk. It may increase or decrease the value of the bank's assets, but the expected effect on the value of the bank is negative (Lucien & Spamann). Some banks have tried in the past to limit the undue risk of bank executives by citing the connection between the design of compensation plans and the interests of shareholders. However, this alone does not eliminate excess risk, as common shareholders may benefit from taking on excessive social risk. As a result, bank executives are often pressured by shareholders to take these excessive risks in order to make more profit. Therefore, the remuneration structure of bank executives makes them take excessive risks or vice versa, which makes objective risk management difficult because they usually protect their own interests. Empirical studies have shown that CEOs who are insulated from shareholder pressure and who are underpaid are less likely to take risks

It encourages banks to rely less on uninsured lenders with supervisory incentives and more on insured depositors with no incentives to exercise corporate governance. 3. Deposit insurance also strengthens the role of lenders as the central bank's last resort. It helped a bank with a very low asset-to-equity ratio compared to other companies. And as that capital declines, so does the dominant owners' desire to increase the bank's risk.

IV. BANK AND AUDITOR

If there is any positive legacy of the financial crisis, it must be in the lessons that market participants learned in their most difficult moments. Like all stakeholders in a banking crisis, bank auditors need to learn a lesson. Accountants play an important role in financial markets, building trust in the financial information of banks and other financial institutions and overseeing directors and management. This report attempts to identify further improvements future operation of the system. Judge Regulatory frameworks supporting audits have worked well during the crisis. The necessary reforms to the audit regulatory framework introduced after the Enron collapse appear to have passed their first major test. However, the UK House of Commons Treasury Committee has questioned the value of bank audits, as audits do not provide an early warning of a banking crisis. European Commission Green Paper of June 2010 on Corporate Governance and Remuneration Policy in Financial Institutions, which covers similar areas to some of the recommendations in this White Paper. It raises questions about the scope of the auditor's responsibility. This report is based on the UK experience, but we believe the analysis and recommendations will be more relevant.

The purpose of the audit is to increase confidence in the information provided by directors through an independent assessment of truth and impartiality. This is true for both banks and other organizations that provide audited financial statements. For banks, regulators and supervisors have different objectives and key stakeholders, but provide additional protection.

One way auditors respond to crises is by proposing changes to regulatory, financial reporting or auditing standards. In practice, we suggest several areas in these areas that could change in the long term. However, such changes take time, and auditors can take direct action to drive positive improvements through marketing solutions and better communication.

Politicians may, above all, question professional judgment when discussing the role of accountants. The auditor's work is conducted within the framework of professional standards, including auditing, ethical and financial reporting, as well as laws and regulations. It is not displayed according to the procedures provided by the internal control body. This helps the auditor explain why questions about the use of professional judgment may arise. If there is one big lesson for auditors from the crisis, it may be that they need to do more to explain the value of gratitude to people outside the audit process. Providing more information about discussions

ISSN- 2394-5125 VOL 6, ISSUE 01, 2019

between accountants and banks increases the value of the audit and thus increases market confidence. It reflects the views of the bank's stakeholders. Our goal has always been to solve their problems. The financial crisis has made it clear that excessive risk-taking can be very damaging to the health of the global financial economy, and it is time for accountants to rethink how they assess risk. The recent financial crisis, comparable to the Great Depression of the 1930s, demonstrates the failure of banks to monitor and assess risk. Excessive lending to defaulting bank customers drained banks of liquidity and exacerbated the financial crisis. The question is whether good internal controls could have prevented the recent financial crisis or mitigated similar economic downturns in the future.

According to a report published by Global Audit Information Network (GAIN) The impact of the global financial crisis on many organizations around the world in 2009 required some research to assess the extent to which the crisis affected internal audit functions. With the above in mind, the Institute of Internal Auditors (IIA) and the IIA Research Foundation (IIARF) conducted a survey in early March 2009 with participants, primarily CAEs, asking specific questions about the overall impact of the recession on organizations there were performed. After that, their general internal control activities. Analysis of the study revealed five key findings:

1. The recession affected not only the organization but also internal audit activities.
2. The internal audit function has received a great deal of attention in recent years, paying more attention to the risks posed by changes in economic conditions.
3. Although most respondents did not agree that improving risk management could play a significant role in preventing the current crisis, most respondents believe that internal controls are more useful in helping companies identify key risks.
4. Changing stakeholder expectations affect the focus of internal audit efforts.
5. Coverage of new risks associated with receiving internal audit oversight and government stimulus funds is not sufficient.

The authors of this report describe how Enterprise Risk Management (ERM) alerted some organizations to the risk of over-lending, while others, such as financial services, did not. As the authors describe, there are some common characteristics of organizations for which ERM does not predict lasting financial impact.

1. Barriers to full ERM implementation due to lack of top management support for risk management.
2. Inefficiency of risk identification and assessment channels.
3. Lack of a clearly documented and communicated risk appetite that defines the amount of risk an organization is willing to take to achieve its goals.
4. Fragmented ERM reporting.
5. Lack of regular risk monitoring. With the above in mind, the authors recommend in the report that internal auditors learn from the mistakes of current risk management failures to ensure that their risk management efforts are effective and to accurately identify key risks.

"Internal auditors have a historic opportunity to use lessons learned from the current crisis to facilitate the emergence of new integrated enterprise risk management (ERM) processes or to improve an organization's existing ERM processes." State George Aldhiser, Ph.D., CIA Associate Professor, Wake Forest University, and Mark Stone are the authors of the report. "The global crisis has forced many auditors and CFOs to rethink the effectiveness and efficiency of company processes for managing business risk."

V. DISCUSSION AND CRITICAL EVALUATION

In the general literature review above, we clearly see that the global financial crisis was primarily caused by risky ventures in many companies and financial institutions. The fact that banks provide financial leverage to

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institutions that make money by taking risks further complicates the extent to which they should be considered appropriate risks. Since this crisis, many corporate governance reforms, especially those related to internal risk management, have been implemented, the responsibilities of internal auditors have been expanded and emphasis has been placed on internal risk management and governance.

Auditors are required to advise clients on inappropriate risk issues and report deviations from the company's maximum risk indicators to independent board members. As we saw above, many bank CEOs take excessive risk because they are often insulated from these risk reversals, but this is because these risky companies hopefully receive very large bonuses at the expense of common stock Shareholder.

Could audits have avoided the recent financial crisis? A straight "yes" to the question still requires some qualifications, and it is also very problematic to say that good auditing and internal risk management do not reduce the magnitude of a crisis, as many studies show different results. What is true and certain is that the accounting profession must grow with the business world and those banks and corporations must develop 21st century internal control and risk management systems to address the business challenges of the 21st century.

VI. CONCLUSION

From the above we have come to the conclusion that the global financial crisis is the result of excessive risk on the one hand and a high level of irresponsibility on the other. It is true that the audit has helped a lot in reducing the severity of this crisis. However, there is no need to prevent this from happening in the future, as many studies show that auditing alone cannot prevent crises. That's why the various stakeholders involved in the business (CEOs, auditors, employees, governments, etc.) need to sit down and do their homework. Accountants should also try to do the right thing, not just do the right thing. This requires the introduction of a Code of Ethics and Professional Conduct in all aspects and requires each stakeholder to recognize that others influence us regardless of themselves.

VII. FUTURE SCOPE

Initiate and encourage reflection for developing a vision for the future scope and scale of audit and assurance; Engage with outside stakeholders to discuss our services and how they should evolve in the future.

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