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Challenges of the Audit Profession in the Globalization Era

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Abstract *Massive unprecedented changes, that best describe this era, are affecting the accountant and auditor profession, as well as the global business environment. The traditional role of the financial auditor will change, but if it will adapt and provide new services, may become a trusted councillor for its clients. The way financial auditors approach future tendencies will shape the destiny of the accountant and auditor profession. Financial auditors must understand innovation, to be open towards globalization, to be prepared as human resources that are competing not only nationally but also globally.*

Key words Change, financial auditor, challenges, globalization, change management, E.C. regulation

JEL Codes: M42

1. Introduction

We live and act in an era described by unprecedented massive *changes* that affect, mostly, the global business environment and especially the accountant and auditor profession.

Thus, new business models, globalized markets, new types of assets and new risk factors exist, all of them representing permanent challenges for professional accountants. Innovation, technology and a work environment always changing will define future. In this context, financial auditors must be prepared for the future. They must be up to date, to show agility in business, to keep and develop relevance and credibility in front of their clients, to predict and adapt to new evolutions, standards, practices, market conditions, in order to recognize their value and to help their clients to succeed in business.

It is expected an evolution of the financial auditor's role in terms of a change, which, despite numerous efforts and challenges will become the key factor of professional development; even more so, when financial auditors and professional accountants, in general, are key actors in national economic development, and currently, in international and cross border economic development.

2. Literature review

The audit is among the oldest profession in the world, even if not formally recognized as such. With the development of society in general, and trade and technology in particular, the auditor is currently a professional in every sense of the word. Until the emergence of the European directives, governing financial statements and the statutory audit, the main research used were: Strain M.M. (1946) "Questions on audit from professional examinations, and reviews on cases and selected topics"; Kamp W.H. and Cashin J.A. (1947) "Standards of internal control and audit procedures"; Cashin J.A., Owens G.C. and Byrnes W.T. (1963) "Audit", Brasseaux J.H. and Miles F.L. (1972) "Auditor's Report: cases and illustrations"; Marwick P. and Mitchell & Co.(1976) "Research opportunities in audit"; Moonitz M. and Stamp E. (1979) "International Standards on Auditing (ISA)".

At European level, the eighth Council Directive No. 84/253/EEC and Commission Recommendation 2001/256/EEC is governing the audit of the annual financial statements or annual consolidated financial statements, as required by Community legislation, transposed in national regulations.

Dewing and Russell (2002) analyses the trends in the way of thinking and new developments in the regulatory framework for statutory audit in the European Union. Tabone and Baldacchion (2003) discuss *the need for statutory audit in the owner-led companies; the results indicate that the statutory audit has two main roles: it is important for stakeholders outside the company, and has a positive effect on the owner and staff.* Loebbecke and Arens (2003) *integrate the most important concepts of audit and practical aspects in a logical way, to understand the decision-making process applied in audits and the collection of audit evidence.*

Karmel (2005) states that "A proposal for a Directive on statutory audit would clarify the duties of statutory auditors and independent and ethical standards by providing public oversight of the audit profession and improve cooperation within the EU". A clear contribution to process of reorganization of principles governing the profession of financial auditor comes from Sarbanes and Oxley Law (SOX) Act, which currently marks a significant impact on the external perception about the planning and execution of audit missions. Although this law, of American inspiration, did not change the responsibility of the external auditor in an audit of financial statements, the effect on how the external auditor leads an audit of financial statements entails a significant scale (Marchetti, 2005). An introduction to international audit standards is also achieved by authors Hayes *et al.* (2005), describing the development and practical application of all relevant national standards and ISA in various countries.

The authors Kumar and Virendra (2006) and Millichamp and Taylor (2008), also talk about audit principles and practice, highlighting the importance and necessity of the

audit report, the auditor's responsibility in the reporting process and, not least the relevance of the audit opinion.

In 2006, the European Federation of Accountants (FEE) subscribes to Article 26 of the eighth Directive on Statutory Audit, which provides legal audits at all companies, in accordance with international auditing standards. FEE believes that this approach to statutory auditing is in the public interest. It aims to ensure coherent and of high quality statutory audit in Europe.

The actuality of audit of financial statements on an international level, appears, on one hand, from the existence of Project Clarity II, resulted in the publication, in 2009, of the new International Auditing Standards with International Standard on Quality Control, and on the other hand from the Green Card Project on audit Policy: lessons from the crisis, implemented in October 2010 on how the audit function could be improved, even though in the past there was no evidence to show that the audit was not conducted in accordance with the relevant rules and requirements. To this document there were a lot of reactions (the most recent ones the European Parliament Report from 13th September 2011 which asks the Commission to insure more transparency and competition on the audit services market, the European Economic and Social Committee Report from 16th of June 2011 on the same topic), and more recently the existence of the proposal Regulation of the European Parliament and Council *on specific requirements regarding statutory audit of public interest entities, on the European Commission Agenda*. Also, the number of projects initiated by the IAASB, regarding the evaluation of effective and consistent application of ISAs worldwide, respectively drafts revision of ISAs on using the results of the work of internal auditors and the auditor's responsibilities relating to other information in documents containing audited financial statements.

The presentation and analysis of the International Audit Standards was achieved by Pigé (2009) as well as Obert and Mairesse (2010). If Pigé stopped only on ISA240, ISA500-501 and ISA505, Obert and Mairesse show all international standards issued by the IAASB, and finally conduct a financial audit based on these standards. Arens *et al.* (2011) present the process of auditing using illustrative examples in this regard, key audit decisions, with an emphasis on audit planning, on processes of risk assessment on collecting and evaluating evidence in response to identified risks. Selwood (2011), Collings (2011) and Chidgey and Nendick (2011) included in their books International Auditing Standards. Selwood talks about International Auditing Standards (including ethical standard) used in UK and Ireland. Chidgey and Nendick made available to practitioners and those interested a practical guide on the implementation of generally accepted auditing standards (2011-2012), in UK. Collings provides interpretations and applications to international auditing standards presented.

3. Methodology of research

The objective of the research is to bring into discussion the role of the financial auditor, in the context of challenge and change specific to a business environment that is in a continuing transformation. This happens because new business models, globalized markets, new types of accounts and risk factors exist and manifest it and the future will be defined by innovation, technology and a changing work environment. The research highlights, on one hand, challenges provided by globalization and new technologies, and on the other hand, challenges provided by changes in regulations set by authorities, as well as the need for financial auditors to recognize the value of civic responsibility and sustainable development. The study is based on achieving a synthesis and antithesis of the ideas found in literature, European and international regulations of the accounting and auditing professions, as well as professional expertise and practice.

The conclusion of the study is that future must be seen by auditors as an opportunity. They must be prepared to overcome future changes and challenges. The way they approach future tendencies will establish the destiny of auditor profession.

4. Challenges for financial auditors

Browsing the findings of studies on the evolution of the financial auditor profession highlights several challenges for the future, including:

4.1. Financial auditors must “embrace” globalization and cross -border transactions. Relationships and business transactions will constitute a significant part of everyday activities, given the expansion of several entities and organizations globally, across national boundaries. Also, there are new emerging markets (a considerable growth in Asia and Africa) and new emerging economies (India and China). Thus, a great competitiveness will be the foundation of a dynamic environment.

4.2. Financial auditors must understand and adapt to new technologies (intelligent equipment, computers and 3D printing etc.), in order to be competitive, to communicate with business partners and clients, and to work in a global economy. Business models will be undermined by new digital interaction models.

4.3. Financial auditors must better understand innovation (cloud computing, predictive analysis, automated controls, Big Data technologies, mobile connectivity, e-Commerce etc.), to successfully develop future business operations for them and their clients. Innovation is value and must be included in the activity and business sector.

4.4. Financial auditors must keep up with change and quickly adapt, because the human resources market is changing continuously. Changes must be included and perceived more as challenges, than obstacles that cannot be overcome. Financial auditors may ask for assistance from national professional authorities, international accounting organizations (in Europe, European Federation of Accountants or at international level, IFAC-International Federation of Accountants), national regulatory authorities or public supervision organisms.

4.5. Financial auditors must expect changes in regulations (and be prepared to answer accordingly), set by authorities and decision factors. Practitioners have stated, numerous times that, the frequent legislature changes can affect the evolution or the development of the business environment regarding small and medium enterprises. The truth is, that in an environment based on rapid changes, updates and alterations in legislation are unstoppable. Therefore, financial auditors must be up to date with the changes, to understand and apply them accordingly, in order to offer high standard services, client counselling, and viable solutions.

4.6. Financial auditors must adapt to the need of recognizing the value of civic responsibility and sustainable development. Climate change, social responsibility, sustainable development and environmental protection can attract customers in an era of business transparency and social communication. These trends can be seen and perceived as risks or opportunities. Clients tend to be followers of a sustainable future, so they will be more attracted to an industry that promotes and demonstrates awareness practices for sustainable development and environmental protection. Auditors must convince the entity's decision makers that auditing is more than a necessity expressed in terms of three theories depicted in figure no.1.

Figure 1. Theories expressing the need for audit

The motivational theory	Agency theory	The insurance theory
<ul style="list-style-type: none"> explains the need for financial audit in the light of higher professional behavior of those who respond to financial statements 	<ul style="list-style-type: none"> justifies the need for audit in that the investors can have full confidence in managers that will use the funds allocated appropriately, without them being diverted into the personal fund managers 	<ul style="list-style-type: none"> explains the need for financial audit through two principles: a) the principle of ensuring (audit provides those who rely on the information obtained, the insured); b) the principle of information (audited information is more reliable for decision making by managers, owners, etc.).

Source: own interpretation

5. Financial auditors' role evolution

In a continuously changing environment, the accounting and auditing profession will also change. As a consequence, the role of the financial auditor will change, asking him to provide services like:

- Assistance in developing entities;
- Risk management;
- Counselling.

Professional accountants need to be closer to customers, to guide them, to help them develop and manage their various risks. They will use the new data and technologies to deliver an overview and to offer new services. Audit and related services on insurance provided by audit are presented in Figure no. 2.

Figure 2. Audit and related services on insurance provided by audit

The nature of service	Insurance commitments				Related commitments	
	Audit of Financial Statements ISA 100-720 and 810	Special purpose audit ISA 800-805	Commitment Review ISRE 2400 - 2410	Examination of prospective financial information ISAE 3400	Commitment on the procedures agreed-upon ISRS 4400	Commitments compilation ISRS 4410
Insurance level provided by auditor	High but not absolute insurance		Moderate insurance		No insurance	
Conclusion drawn	Positive assurance on assertions		Negative assurance on assertions		Findings of procedures	Identifying information compiled
The finality of the report	Opinion		Negative insurance	Negative insurance (hypothesis) Opinion (fin.statem.)		

Source: Available on-line: www.C.A.F.R.ro

Therefore, the *role* of the financial auditor, as well as the value of the services provided by them will increase. As the auditors come to be seen as trusted advisors of their clients, they will have to incorporate a new skill into the skill set - the ability to help customers cross a fast and complex future. Currently the situation regarding the progress of audit is as follows (figure no.3).

Financial auditors must understand innovation, to be open towards globalization, to be prepared as human resources that are competing not only nationally but also globally.

Figure 3. Synthetic presentation on the development of audit

Period	Authorizing Officers of Audit	Auditors	Audit objectives
Until 1700	Kings, emperors, churches and State	Churchmen or scribes	Thieves' punishment for misuse of funds. Protection of the patrimony.
1700-1850	States, commercial courts and shareholders	Accountants	Repression and punishment of perpetrators of fraud. Protection of the patrimony.
1850-1900	State and shareholders	Professional accountants or lawyers	Avoiding fraud and error and testing the reliability of historical financial statements.
1900-1940	State and shareholders	Audit and Accounting Professionals	Avoiding fraud and certification of the reliability of the balance sheet.
1940-1970	States, banks and shareholders	Audit and Accounting Professionals	Attesting the sincerity and accuracy of historical financial statements.
1970-1990	State, third parties and shareholders	Professionals in audit, accounting and counseling	Assess the quality of internal control and compliance with accounting and auditing rules.
After 1990	State, shareholders, banks and others	Professionals in audit, accounting and counseling	Attesting true and fair view of the accounts and the quality of internal control compliance. Protection against international fraud.

Source: Collins Lionel et Valin Gerard, 1992, "Audit et control interne", Ed. Dalloz, Paris

In addition to education and training they need to understand that talent will be an advantage in getting and keeping a job, in an environment where competition comes not only from within (co nationals) but also from abroad (immigrants). Today anyone can travel and find a job abroad; language barrier is no longer an obstacle, key factors being the set of skills and talent of the candidate. The way in which auditors will *manage change* will define future success and competence. Managing change is needed and is a valuable tool that will influence business performance and financial systems.

6. New regulations of European Commission (E.C.) that impact on statutory audits

Browsing the two regulations of the European Commission: the 2014/56/UE Directive regarding the legal auditing of annual and consolidated financial statements, and the 537/2014 Regulation regarding specific requirements of

statutory auditing of public entities of interest, we notice that the two highlight key elements that must be considered in the work of financial auditors, namely:

A. The social role of auditors is enhanced by:

a) a higher quality of audit: auditors should issue detailed audit reports, providing relevant information to investors (to reduce "expectations"). Audit approach and its recommendations must lead to identifying the risks that expose the entity to unexpected threats. Auditors must contribute fully to supplementing benefits due to the incorporation of risk management into the organizational culture of the entity. These benefits are shown schematically as follows:

Figure 4. The benefits of incorporating risk management into the entity culture

Benefits of incorporating risk management into the entity culture
▪ decreasing the time spent by management in controversies;
▪ less surprises, support for development;
▪ more happy customers, less complains;
▪ Protecting its reputation reduced insurance costs.
▪ More attention in doing the right things in a right way;
▪ Greater possibility to achieve the objectives of the firm;

Source: Own interpretation

b) a greater responsibility: audit committees closely follow work of financial auditors; 5% of the shareholders of the entity may initiate action to dismissal of auditors; competent authorities may apply administrative sanctions in case of infringements.

B. Reinforcing the independence regime by:

a) mandatory rotation: profile audit institutions are subject to rotation after an audit mission 10 years. This period may be extended up to 10 years for public auctions and up to 14 years for joint audits.

b) prohibition of non-audit services: to limit conflicts of interest, audit entities are forbidden to provide certain non-audit services (tax services, financial and investment);

c) Limitation on the provision of non-audit services: when a statutory auditor/audit entity has provided non-audit services for a public interest entity audited for 3 years in a row or more, the total fees for those services in the 4th year will be up to 70% from the average fees paid in the past consecutive years.

C. Audit market in the EU is becoming more dynamic and competitive, as follows:

- a) a single market for statutory audit:** according to European Commission, new regulations will strengthen cross-border mobility and harmony of International Standards of Audit (I.S.A) - these are adopted by EU, but are to be applied proportionately in statutory audits of small entities, and EU members may enforce “additions” to improve quality and credibility of national jurisdiction;
- b) more options:** promoting competition by removing restrictive clauses enforced on entities, promoting joint auditing and public auctions, decreasing taxes for small and medium enterprises.
- c) increasing supervision in auditing:** by strengthening cooperation inside European Union, between national surveillance authorities and competent organisms (those that supervise public interest), that have great responsibility in regards to inspection for insuring quality of audits.

7. Conclusions

Auditors should see the future as an opportunity. They will have the perfect opportunity to prove that they are virtual professionals adding value to customers and the economy as a whole. Being prepared for the future becomes a requirement for auditors. In the European Union, the new legislative package of European Commission may cause some challenges for auditors, but they must acquire knowledge and expertise that allows them to overcome these challenges. The way in which auditors will address future trends will shape the destiny of the audit profession.

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