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The Strategic Role of Financial Auditing in Ensuring Transparency and Sustainable Development

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Abstract: The paper highlights the critical role of financial auditing as a central element in ensuring financial transparency, trust, and integrity within a commercial organization, while also demonstrating its importance in corporate governance and sustainable economic development. Through a detailed analysis of the financial audit process applied to T.C. SRL—a prominent Romanian company operating in the civil, industrial, and infrastructure construction sector—the study underscores not only the theoretical principles but their practical application in a highly dynamic and complex industry. The audit process, conducted in compliance with International Financial Reporting Standards (IFRS) and International Standards on Auditing (ISA), is shown to extend beyond financial accuracy, acting as a strategic tool for identifying risks, optimizing internal processes, and supporting data-driven decision-making. Key findings highlight the importance of proper revenue and expense recognition, cash flow management, and internal control systems in ensuring a company's financial sustainability and operational efficiency. Moreover, the study reveals how a rigorous audit process strengthens corporate governance, mitigates fraud risks, and enhances confidence among stakeholders, including investors, creditors, and public authorities. The practical insights gained from the auditing experience at T. C. SRL emphasize the transformative potential of auditing in improving organizational transparency and fostering a performance-driven culture within companies. In an era of digital transformation, the paper also advocates for leveraging advanced technology in auditing, such as data analysis software, to achieve greater efficiency and uncover potential risks. These innovations pave the way for auditors to provide not only compliance assurance but also valuable strategic insights, supporting sustainable growth and corporate resilience in today's globalized and competitive business environment.

Keywords: construction sector; internal control; corporate governance

JEL Classification: L74, M42, G30

1. Introduction

The construction sector represents a structural pillar of the Romanian economy, contributing approximately 6-7% to the formation of the Gross Domestic Product and supporting the development of critical infrastructure. This macroeconomic importance, however, is accompanied by operational complexities that generate specific challenges in financial reporting: the extended duration of contracts, variability in material costs, the fragmentation of execution through subcontractor networks, and the reliance on significant accounting estimates (Costello & Wittenberg-Moerman, 2011; Deloitte, 2022).

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These characteristics make the sector a privileged context for studying financial audit as a mechanism for ensuring transparency. International literature extensively addresses the specific risks of auditing in the construction industry (Arens et al., 2020; Messier et al., 2019; Knechel & Salterio, 2016); however, empirical studies focused on the Romanian market are rare and generally limited to descriptive analyses of the regulatory framework. Thus, a dual gap can be observed: (I) the lack of in-depth case studies analyzing the effective implementation of ISA and IFRS 15 in medium-sized Romanian construction companies, and (II) the absence of a clear empirical connection between operational audit procedures and their effects on corporate governance.

This research is positioned at the intersection of these two gaps. Building upon the presented context, the study is guided by the following central research question: To what extent does the application of a risk-based audit methodology, compliant with ISA and IFRS, contribute to enhancing financial transparency and corporate governance in a Romanian construction company?

This research is positioned at the intersection of these two gaps. Building upon the presented context, the study is guided by the following main research question: To what extent does the application of a risk-based audit methodology, compliant with ISA and IFRS, contribute to enhancing financial transparency and corporate governance in a Romanian construction company?

From this question, three sub-questions are derived:

- **SQ1:** How are the specific risks of the sector translated into operational audit procedures?
- **SQ2:** What types of vulnerabilities are identified through the application of these procedures?
- **SQ3:** How are the audit findings reflected in processual and governance changes at the level of the audited entity?

The general objective of the research lies in the in-depth analysis of the audit methodology applied at **T.C. S.R.L.** and its effects on corporate governance. The specific objectives are:

- **O1:** To describe the stages of planning, execution, and reporting.
- **O2:** To identify significant sector-specific risks.
- **O3:** To evaluate the effectiveness of audit tools, including CAATs (Computer-Assisted Audit Tools).
- **O4:** To analyze the impact of the audit on operational and decision-making processes.

2. Hypotheses

Based on the relevant literature, the following research hypotheses are formulated:

- **H1:** The application of a risk-based audit methodology leads to the identification of operational vulnerabilities that would not have been detected through routine internal controls.
- **H2:** The use of CAATs (Computer-Assisted Audit Tools) significantly increases the likelihood of detecting anomalies in large volumes of transactional data.
- **H3:** Audit findings generate observable procedural and governance changes in the subsequent financial year.

The contribution of this study is twofold:

- **Theoretical Contribution:** It empirically articulates the link between technical audit procedures (operational level) and governance outcomes (strategic level), a relationship insufficiently addressed in sector-specific literature.
- **Practical Contribution:** It provides a replicable risk-based approach model for auditors operating in the construction sector of emerging economies.

2.1. Specialized Works

The role of financial auditing in the contemporary economy cannot be dissociated from the conceptual framework that has provided it with theoretical legitimacy over the past half-century. The origin of this legitimacy lies in the seminal work of Jensen and Meckling (1976), which, through the articulation of agency theory, provided a fundamental lens for understanding the relationship between capital owners and the managers to whom decision-making power is delegated. At its core, agency theory begins with a seemingly simple but profoundly impactful observation: when ownership and control are separated, an informational asymmetry inevitably arises between the two parties. Managers, positioned inside the organization, possess a substantial informational advantage over shareholders, who can observe the company's performance only through the lens of financial reports—reports, paradoxically, prepared by the very same managers. This configuration generates what the literature refers to as agency costs—value losses associated with the possibility that managers act in their own interests rather than those of the owners. In this context, financial auditing emerges as an institutional mechanism aimed at reducing, if not entirely eliminating, this asymmetry. Its fundamental role, according to the theoretical framework proposed by Jensen and Meckling, is to provide independent assurance that financial statements faithfully reflect the economic reality of the entity. The auditor, through their position as an impartial third party, becomes a bridge of trust between those who produce accounting information and those who consume it, transforming financial reporting from a potentially suspect exercise into a credible informational product. From this perspective, auditing is not just a compliance obligation but a rational response to a structural issue in modern economies based on widely dispersed ownership. However, to remain confined within this strictly contractualist vision would be to overlook the significant evolution that contemporary literature has introduced to the understanding of the auditing phenomenon. Authors such as Knechel and Salterio (2016) or DeFond and Zhang (2014) have proposed a considerable broadening of the analytical framework, treating auditing not as a mere point-in-time assurance tool but as an integral component of the corporate governance ecosystem. This reconceptualization shifts the focus from the bilateral auditor-entity transaction toward a systemic perspective, in which auditing dynamically interacts with other governance components: the board of directors, the audit committee, the internal audit function, regulatory authorities, and the capital market itself. In this vision, the external auditor is no longer perceived as an isolated actor who intervenes annually to validate financial figures but as an essential node within a network of complementary mechanisms that jointly support the integrity of financial information and the quality of corporate decision-making. A direct consequence of this paradigmatic shift is that the value of auditing is no longer measured solely by the opinion issued at the conclusion of the engagement but by its contribution to the resilience of the entire governance system. High-quality auditing generates effects that extend beyond the immediate scope of financial reporting: it disciplines managerial accounting practices, strengthens the functioning of internal controls, supports the audit committee in fulfilling its oversight responsibilities, and, not least, sends credible signals to capital markets and external stakeholders. In this sense, auditing becomes, as Knechel and Salterio aptly describe it, a “public good” of corporate governance—a mechanism whose benefits propagate beyond the direct contractual parties, positively influencing the entire economic ecosystem.

This conceptual redefinition inevitably raises a central question: what ensures that an audit effectively fulfills this extended function? The answer, articulated with clarity by Francis (2011) in a framework that has quickly become a key reference in the literature, points to the concept of audit quality. Far from being a monolithic notion, audit quality reveals itself as a multidimensional construct, whose substance results from the convergence of several interdependent factors.

Professional competence constitutes the first of these dimensions—the technical ability of the auditor to understand sector-specific peculiarities, the complexity of transactions, and the implications of the applicable regulatory framework. **Independence**, both as a formal attribute and as a mindset, represents the second essential element, without which the auditor's judgment risks being compromised by explicit or implicit pressures from the audited entity. Finally, **professional judgment**—the calibrated ability to weigh evidence, identify risk areas, and formulate well-founded conclusions under conditions of uncertainty—completes the triad that defines the authentic quality of an audit engagement.

The importance of this multidimensional perspective is not merely taxonomical. It has direct operational implications, as it suggests that none of these three dimensions can compensate for deficiencies in the others. A competent auditor lacking independence produces opinions tainted by conflicts of interest. An independent auditor lacking competence risks failing to identify significant risks. A competent and independent auditor with superficial professional judgment may issue formally correct opinions that are fundamentally flawed in substance. Audit quality, therefore, emerges from the dynamic equilibrium among these three dimensions, and the absence of any one of them erodes the entire construct. This articulated understanding of audit quality transforms the concept into a true predictor of the credibility of financial reporting. When the three dimensions converge harmoniously, auditing generates not only a technical opinion but also a resource of trust that all categories of financial information users can rely on: investors in their capital allocation decisions, creditors in their credit risk assessments, tax authorities in compliance evaluations, and employees in assessing professional stability. The credibility of financial reporting is, therefore, not an intrinsic attribute of the financial statements themselves but a social product co-created by the reporting entity and the auditor who, through the quality of their intervention, imparts informational value. Traversing this conceptual trajectory—from agency theory to the systemic perspective of corporate governance and from there to the multidimensionality of audit quality—reveals a significant evolution in how the academic and professional communities understand the role of financial auditing. What began as a pragmatic response to an issue of informational asymmetry has gradually refined itself into a sophisticated theoretical framework capable of capturing the complexity of the functions that auditing fulfills in contemporary economies. For applied research, including case studies conducted in sectors with pronounced specificities such as construction, this theoretical foundation provides not only a conceptual vocabulary but also an indispensable interpretive framework for understanding why auditing matters, how it matters, and under what conditions it effectively fulfills its role of fostering confidence in the economic system. The construction sector presents three classes of risks systematically documented in the literature. The first pertains to revenue recognition based on progress, an issue that has become more pronounced following the implementation of IFRS 15 (IASB, 2014; PwC, 2020). The second concerns the accuracy of total cost estimates for contracts, which are essential for calculating the percentage of completion (Costello & Wittenberg-Moerman, 2011). The third refers to the vulnerabilities in internal controls over procurement and payments to subcontractors, where the reported frequency of fraud is significant (ACFE, 2022). The digital transformation of auditing has been accelerated by the adoption of computer-assisted auditing techniques (CAATs) such as ACL and IDEA, which allow for the testing of entire transactional populations instead of traditional sampling methodologies (Alles et al., 2018). Empirical studies demonstrate that the use of CAATs increases the detection rate of anomalies and reduces the time required for substantive procedures

(Rezaee et al., 2018). The contemporary perspective treats financial auditing not merely as a retrospective instrument but as a constitutive element of organizational sustainability, contributing to the resilience of control systems and the quality of strategic decisions (Eccles & Krzus, 2018; Simnett et al., 2019). In the construction sector, this link is amplified by emerging ESG pressures and the requirements of the CSRD directive.

3. Method

The research adopts an interpretivist paradigm and a single-case study design, descriptive-explanatory in nature, following the tradition proposed by Yin (2018). The case study was deemed optimal for exploring a complex contemporary phenomenon within its real-world context, where the boundaries between the phenomenon and its context are not clearly delineated. **T.C. S.R.L.** was selected through purposive sampling based on the following criteria:

- (i) **representativeness** of the medium-sized segment of the construction sector (2024 turnover: 6,486,799 lei);
- (ii) **diversity** in the project portfolio (civil, industrial, road infrastructure);
- (iii) **availability of access** to audit documentation;
- (iv) **auditability** in compliance with ISA and IFRS.

To ensure methodological rigor, the following techniques were applied:

- **Construct validity:** multiple triangulation;
- **Internal validity:** pattern matching between observed data and theoretical predictions;
- **External validity:** clear delineation of transferability conditions;
- **Reliability:** documentation of all stages in a case study database.

4. Results

Financial Profile of the Audited Entity

Table 1. Financial indicators of T.C. S.R.L. for 2024

Indicator	2024 Value (RON)	Observation
Turnover	6,486,799	Basis for the materiality threshold
Revenue from construction contracts	5,912,400	~91% of turnover
Subcontractor expenses	2,847,000	High-risk area
Trade receivables	2,134,500	Externally confirmed at 94%
Gross margin	14.2%	Down by 2.8 p.p. compared to 2023

Audit Planning and Risk Assessment (O1, O2)

In accordance with ISA 315, the audit team documented a specific risk register.

Table 2. Summarises the most relevant areas

Risk Area	Assessed Level	Targeted Assertion	Planned Procedure
Premature revenue recognition	High	Accuracy, period separation	Physical progress test vs. revenue
Overstatement of subcontractor costs	High	Existence, valuation	External confirmation + inspection
Duplicate payments/settlement errors	Medium	Existence, accuracy	CAATs (ACL/IDEA)
Material price fluctuations	Medium	Valuation	Analytical procedures
Tax compliance for complex transactions	Medium	Presentation	Specialist review

The materiality threshold was set at 1% of the turnover ($\approx 64,868$ RON), with low specific thresholds for high-risk accounts (income from contracts: 32,434 RON; expenses with subcontractors: 28,470 RON).

Audit Execution: Procedures and Findings (O3)

The application of the cost-incurred method was verified on a sample of 8 active contracts, representing 72% of total revenues. The correlation between the physical progress reported by the Execution Department and the recognized revenues was consistent, with observed deviations falling below the specific materiality threshold. Out of 14 external confirmations sent, 13 were returned, validating receivables totaling 2,003,830 RON. The most relevant example was the modernization project for DJ 211A, with a confirmed receivable of 2,000,000 RON. The computer-assisted analysis, conducted using ACL and IDEA on the full population of 3,247 payments made in 2024, identified a duplicate payment of 50,000 RON to a subcontractor (invoices with identical details processed 23 days apart). The amount was fully recovered subsequently. Without the use of CAATs, the probability of detection through traditional sampling methods (estimated non-detection risk of $\sim 87\%$ for this type of error) would have been significantly reduced. The comparative analysis between 2023 and 2024 highlighted a decrease in the gross margin from 17.0% to 14.2%, explained by the increase in the prices of concrete (+11%) and steel (+8%). This dynamic was validated through benchmarking with publicly available sectoral indicators.

Identified Vulnerabilities

Beyond the duplicate payment, the audit noted the following:

- Delayed reporting of subcontracting expenses (an average lag of 12 days between execution and recording);
- Cash flow mismatches between receipts from beneficiaries and payments to subcontractors (average lag: 38 days);
- Incomplete documentation for two minor purchases (cumulative impact below the materiality threshold).

Although these findings are individually immaterial, they highlight procedural vulnerabilities that justify improvement recommendations.

Reporting and Post-Audit Effects (O4)

The opinion issued under ISA 700 was unreserved. Following the recommendations made in management letter, the company implemented in the first quarter of the following year:

Table 3. Implemented Measures and Their Objectives

Implemented Measure	Objective	Estimated Effect
Digital procurement approval system	Prevention of duplicate payments	Reduction of operational risk
Automatic payment reconciliation	Transactional accuracy	Early detection of anomalies
Credit lines and factoring	Cash flow optimization	Reduction of collection delays
Updated risk register by project	Strengthened internal control	ISA 315 compliance

5. Conclusion

The results confirm the three initially formulated hypotheses, albeit with important nuances. Regarding **H1**, the risk-based audit identified vulnerabilities which, although limited in scope, would not have been detected through routine internal mechanisms—an aspect consistent with the literature on the role of external audits as a complement to internal controls (DeFond & Zhang, 2014). Relating to **H2**, the duplicate payment detected through CAATs represents an emblematic example of the technological adoption thesis in auditing (Alles et al., 2018): without full population testing, the error would most likely have remained undetected. As for **H3**, the post-audit procedural changes—digitalized procurement, automated reconciliation, and cash flow tools—confirm the governance role of audits (Knechel & Salterio, 2016). Beyond these confirmations, a critical observation must be made: attributing post-audit improvements exclusively to the financial audit is debatable. It is plausible that these changes also stem from market pressures or independent management decisions. The study does not fully disentangle this attribution, a limitation inherent to the single-case study design. Additionally, the construction sector confirms the particularly high relevance of IFRS 15 in establishing a credible correlation between physical progress and recognized revenues—an observation aligned with PwC (2020) and contemporary academic debates. The study empirically demonstrates that a risk-based audit methodology, compliant with ISA and IFRS, generates observable impacts on three levels: (I) **Technical level**—by accurately detecting anomalies, including through CAATs; (II) **Procedural level**—by identifying internal control vulnerabilities; (III) **Governance level**—by influencing subsequent managerial decisions related to digitalization and process optimization. The research adds to the literature by empirically articulating the link between operational audit procedures and governance outcomes in an under-researched sector within the Romanian context. The findings support the view that financial auditing is not merely a compliance exercise but an active mechanism for strengthening organizational sustainability. For practitioners, the following recommendations emerge:

- (a) implementation of ERP systems integrated with project-specific accounting;
- (b) periodic updates of the risk register for contracts;
- (c) enhanced reconciliations between site reports and accounting records;
- (d) systematic adoption of CAATs for subcontractor-related transactions;
- (e) integration of an ESG framework into audit risk assessments.

The study acknowledges certain limitations: (I) the single-case design limits generalizability; (II) the short time horizon (one financial year) does not allow for a longitudinal analysis of effects; (III) restricted access to certain data for confidentiality reasons limited specific analyses; (IV) the causal attribution of post-audit improvements remains partially ambiguous. Future research directions could explore: (a) comparative multi-case study designs to test reproducibility across multiple companies in the sector; (b) longitudinal pre-/post-audit analyses over 3-5 years; (c) explicit integration of ESG

dimensions into construction sector audits; (d) quantitative studies on the impact of CAATs on audit quality in emerging markets; (e) investigations into the effects of the CSRD directive on sectoral audit missions.

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