Audit research from the perspective of corporate governance: role and development

Mengnan Hao

Northwest University of Political Science and Law, Xi’an, Shaanxi, 710000, China

Abstract: The separation of ownership and management rights is the cause of corporate governance, as well as the cause of internal audit and external audit. Based on the core keyword search results of many domestic mainstream academic websites, this paper selects relevant topic articles based on core journals to reveal the research status of auditing from the perspective of corporate governance, explore the coordinated development path of auditing and modern corporate governance systems, and the challenges and suggestions faced by audit work in the governance process in order to provide reference for relevant researchers and practitioners.

Keywords: Literature review; corporate governance; Audit

1. Introduction

With the continuous spread and development of economic globalization, the competitive pressure and survival challenges faced by enterprises are becoming more and more fierce. To survive and develop of enterprises, good and effective corporate governance is the key. As the two cornerstones of corporate governance, internal audit and external audit play an irreplaceable role in corporate governance. Since the role of audit will directly affect the effect of corporate governance, so if the internal audit and external audit can play a coordinated role together, it will inevitably strengthen the effect of corporate governance. As the bridge of communication between internal audit and external audit, the role of the audit committee is the key factor that determines the role of internal audit and external audit together. Therefore, the discussion of the relationship between corporate governance, external audit and internal audit has an important practical significance.

2. The discrimination of relevant concepts and theories

2.1. The concept of corporate governance

At present, there are two main theories about the concept of corporate governance. In a narrow sense, it mainly refers to a mechanism derived for the adjustment of its interests and contradictions after the separation of ownership and management rights, and through this mechanism to supervise and make checks and balances. In a broad sense, it mainly includes law and culture to safeguard the rights of shareholders, ensure the legitimate rights and interests of all shareholders and stakeholders, and ensure the scientifity and effectiveness of the company's decision-making, so as to safeguard the interests of all aspects of the company. In general, the nature of corporate governance is still an institutional arrangement.[1]

2.2. The concept of internal audit

China's internal audit standards of internal audit definition is: internal audit is an independent and objective confirmation and consulting activities, it through the use of system, standard method, review and evaluate the organization's business activities, internal control and risk management of appropriateness and effectiveness, in order to promote the organization to improve governance, increase value and achieve goals. [2] The International Association of Internal Auditors defines internal audit as "a systematic and standardized approach to evaluate risk management, control and governance procedures to increase organizational value and improve operational efficiency, and improve their efficiency, so as to help the organization achieve its goals".
2.3. Theoretical discrimination

A sound corporate governance system inevitably needs the support of an effective internal audit system. The ultimate goal of both enterprises is to effectively manage the enterprise and maximize its interests.In a word, for the relationship between internal audit and corporate governance, the academic mainstream academic views mainly include: the essence of the homology, the same goal and the close mechanism of the two.[3-5] The difference between the two is mainly reflected in the composition structure and the key two aspects.[6]

3. The action mechanism of audit and corporate governance

3.1. Internal audit: the supervision system of corporate governance

In modern enterprises, the importance of internal audit is self-evident. The Guidelines on the Articles of Association of Listed Companies (2022 Revision) revised in 2022 clearly stipulates that the company implements an internal audit system with full-time auditors to conduct internal audit supervision over the company's financial revenues and expenditures and economic activities. Internal audit plays an irreplaceable role in helping management and audit committees to evaluate and report internal control.[4] The international research on the role of internal audit on corporate governance has been fruitful. Due to the special system in China, the research of internal audit is relatively late, and the object are mainly specialized cases. With the rapid development of economy, the team of domestic listed companies is becoming more and more large, and the empirical research on the governance and internal audit of listed companies is also gradually increasing, especially popular in the topic selection of dissertation.

3.1.1. Internal audit is conducive to ensuring the integrity of the corporate governance structure and the autonomy of enterprises

As a kind of the corporate governance system arrangement, the internal audit not only evaluates and supervises the corporate governance status, but also the corporate governance is an important factor in the internal audit system environment. In addition, because internal audit can weigh the power of owners and operators to a certain extent, it is an important means to improve the effectiveness of corporate governance. Zhang Pei (2012) believes that effective internal audit can not only improve the quality of financial reporting, alleviate surplus management, but also even have a close linkage relationship.[5] Chen Ying et al. (2016) tested the value-added role of internal audit from the perspective of the interaction between internal audit and other governance subjects, and showed that internal audit has an important value-added role, and proposed that the benign interaction with other governance mechanisms helps to give full play to the role of internal audit in promoting the value of the company.[6]

3.1.2. Internal audit is conducive to improving the effect of corporate governance

The main goal of internal audit is to play a role in strengthening the units and departments' management, improving efficiency and establishing a good order. Therefore, internal audit can not only put forward opinions on the flaws of enterprise operation, so as to improve the corporate governance system and ensure the quality of corporate governance. For example, Wang Guangyuan et al. (2006) discussed the relationship between corporate governance and internal audit based on the theory of fiduciary responsibility, and concluded that internal audit is an internal governance mechanism to ensure the performance of fiduciary responsibility.[7] Zhang Qingya (2014) conducted an empirical study on the internal audit of commercial banks, and concluded that the internal audit ultimately serves the corporate governance, and provides a sufficient basis for the stable operation and efficient management of banks.[8] Therefore, the relationship between the two is inseparable. While corporate governance promotes the effective operation of internal audit, internal audit has also become an important part of corporate governance.

3.1.3. Internal audit is conducive to the company's risk prevention and management

With the popularity of risk-oriented audits[9], internal audit is also considered as a line of defense for corporate risk. Because the uncertainty of risk poses a significant threat to corporate governance, risk prevention and management is an important part to modern corporate governance. As a third party within the organization, internal audit has a high degree of independence. It can effectively promote the management to control risks by evaluating whether the company has risk management procedures and whether the risk management procedures are reasonable and effective. If the company does not establish
risk management procedures, the internal audit can actively assist in the establishment of a risk management system through investigation and analysis. If established, the internal audit can timely assist the management to develop risk prevention and control strategies when a major risk occurs; when the management and shareholders risk preference inconsistency, the internal audit can determine whether the management risk prevention measures are reasonable and whether the risk can be controlled within the shareholders accept real-time monitoring, can ensure that the management measures to deal with risks meet the shareholders’ expectations. In addition, some scholars also mentioned "value-added internal audit" when exploring the relationship between corporate governance and corporate performance and audit[10]. The concept of "introverted management audit", and the improvement of corporate governance environment has a positive impact on improving the business performance of enterprises. And when the quality of the enterprise's internal audit is the higher, the better the enterprise performance will be. It explains the three elements of value-added internal audit, corporate governance and enterprise performance.[11-12] And “inward-management audit” is a multi-faceted supervision and evaluation activity carried out with internal audit as the main body. Its implementation can help to reduce the asymmetry of information, and can effectively make up for the defects of corporate governance structure.

3.2. External audit: Validity test of corporate governance

Compared with internal audit, the current research results on corporate governance and external audit are not rich, but more literature involving external audit or internal and external audit merger research. However, for the external audit, the effective internal audit can reduce the external audit workload and assist in the external audit work.[13] In order to make external auditors trust and use the results of internal audit, the premise is to make internal audit meet the external audit expectations[14]. At the same time, internal and external audit jointly undertakes the functions of ensuring the sound and effective internal control of enterprises, strengthening the enterprise risk management, and ensuring the true and reliable company information disclosure. They both serve to ensure the effective performance of the entrusted economic responsibilities. High-quality internal audit work can bring many benefits to external audit. External audit also has a crucial impact on internal audit. The premise of external audit using internal audit work is that internal audit has objectivity and independence, otherwise the role of internal audit for external audit will be out of the question. External audit can improve the comprehensive quality of internal audit personnel by strengthening the effective evaluation of internal audit and giving support in the work.

As early as 2007, Jiang Rong and other scholars conducted an empirical study on the governance effectiveness of the external audit of listed companies in China, and found that the CEO change was significantly and positively related to the "non-standard" opinions, which is the initial verification of the effectiveness of the external audit governance mechanism.[15] Since then, the research results in this field have been remarkable. Chen Bo (2014)[16] Through the relevant empirical study of accounting firms and listed companies, the research is found that the internal governance of accounting firms is an important factor affecting the quality of capital market audit. Du Xingqiang (2014) Chen Lirong et al. (2016)[17] In the empirical research based on voluntary audit, corporate governance and agency costs, it is concluded that the conclusion of semi-annual report voluntary audit can significantly reduce the agency costs between the management authorities of listed companies and shareholders, thus revealing the information value and corporate governance role of audit. However, because the article mainly studies the utility of mandatory and non-compulsory audit, it is not specifically divided based on the concept of audit subject.[18] In addition, some literature studies the positive effect of government audit intervention on state-owned enterprise governance. For example, Cui Yuchen (2018)[19]. Su Huishui (2019) believes that the intervention of government audit governance is of help to improve the governance level of state-owned enterprises and urge the maintenance and appreciation of state-owned assets, so as to produce complementary effects and improve business performance.[20] However, due to the limitations of the scope of Chinese government audit, this effect can only cover the enterprises with the main equity in some countries. With the influence of China's political system, this effect will be greater than the external audit effect hired by ordinary companies, but it is not universal. Yang Hanming, Tang Miaoning (2019) from the perspective of enterprise stakeholders, respectively analyzed the external audit to the main agent problem solution path, concluded that independent external auditors, on the one hand, minority shareholders can provide objective and real audit results, on the other hand also can serve the company creditors, and its independence, technical can help the company internal audit improve audit quality.[21] Lin Chunlei et al (2019) It points out that external audit and internal control are important components of corporate governance. With the extensive promotion and development of external audit strengthening and internal control construction, the management has realized the positive role of both in
improving company efficiency and company value.[22]

3.3. Audit Committee: the long-term development mechanism of corporate governance

According to the Sarbanes Oxley Act, the audit committee is a committee (or equivalent group) initiated by the members of the board of directors of the issuing securities company. Its purpose is to supervise the audit of the accounting, financial reports and the accounting statements of the company. However, the current development of audit committees in the domestic capital market is still in the initial stage. Li Xia (2009) tried to find out the factors affecting the audit scale from the perspective of corporate governance, and concluded that there was a positive relationship between the internal audit scale and the proportion of independent directors, the independence of the chairman of the board and the utility of the company's audit committee.[23] The eight major changes in the Governance Guidelines for Listed Companies, revised in 2018, include new requirements for "strengthening the role of the audit committee of the Board of Directors".[24] The working relationship between the internal auditors and the audit committee is a subject that has been studied for many years. Only the frequent communication with the internal auditors and the open conversation can make the internal audit more effective. In addition, the study of the evaluation of internal control.

For example, Shi Qingmei (2020)[25] By exploring the enterprises listed on the main board of Shenzhen-Shanghai A-shares, the infectious effect of the major defects of internal control within the group is empirically tested, so as to provide empirical evidence of the importance of internal control. Zhu Caijie (2021)[26] By exploring the internal mechanism of the influence of board of directors governance on bond credit rating, and using the corporate bond data of listed companies from 2016 to 2018, it is concluded that the effectiveness of internal control shows some intermediary effect in the professional impact of the audit committee on bond credit rating. Ni ZiTing (2022) selected part of the data of listed companies nearly ten years of theoretical analysis, research assumptions and model setting, finally concluded in other conditions, the perfection of the audit committee of the relationship between the internal control and audit quality, and emphasizes the high requirements of the audit committee for independence.[27] Zhang Zhihong et al. (2022)[28] Through the research on the disclosure information of some listed companies, it is found that the financial expertise of the audit committee can govern the management's strategic disclosure behavior, and the governance role of the management tone manipulation behavior is more significant in the enterprises disclosing "good news", which also provides new evidence for the performance utility of the audit committee.

4. In other: How to make audit and corporate governance synerg-together

Although the current enterprises have generally set up internal audit institutions, but there are still some problems. For example, the management attention, the enterprise management system is not perfect and other aspects will inevitably affect the independence of the internal audit department.[29] In addition, some enterprises still have internal audit supervision responsibility is not enough.[30] The lack of professional competence of audit personnel can lead to the inevitable limitations of internal audit, and it is difficult to play a full role in corporate governance.[31]

4.1. To guide enterprises to voluntarily set up internal audits

Ma Mengchao (2016) studied the governance effect of internal audit from the perspective of national institutional change and concluded that the internal audit voluntarily selected by enterprises has a better governance effect than the internal audit under government regulatory intervention, and proposed to further improve the internal audit construction under government regulatory intervention.[32] For example, standardize the internal audit system to ensure the performance of the internal audit function; enhance its independence by setting up a reasonable internal audit organization form; and strengthen the internal audit needs by strengthening the cooperation between the internal audit and other governance subjects. In addition, enterprises should be encouraged to voluntarily promote the development of internal audit.[33] To correctly understand the role of internal audit and actively try to establish internal audit, and strengthen the construction of internal audit team.[34]

4.2. Strengthen the application of inward-looking management audit

Management audit replaces financial audit is the development trend of audit, and the exploration of management audit theory and practice will be a hot issue in the audit industry now and later.[35] At the
same time, the future development of the current management audit is limited by many restrictions, the company’s internal audit independence is poor. Therefore, strengthening the development of introverted management audit and corporate governance is an inseparable and close relationship. The improvement of corporate governance structure is the necessary environment for carrying out audit work, is the institutional scale for the implementation of management audit norms, and is the basis for ensuring the function and role of management audit. In a good corporate governance environment, the establishment of management audit committee is conducive to the effective development of introverted management audit. Therefore, the leadership of the enterprise should, for the needs of the reasonable operation of the introverted management audit, establish a management audit committee within the enterprise, provide high independence and authority for the introverted management audit work, and cooperate with the committee to recruit senior audit talents. Implement necessary measurement examination and cooperate with the reward policy, so as to improve the enthusiasm of audit staff and ensure the quality of introverted management audit work.[36]

4.3. Develop the innovation of internal audit in the governance system

To sum up, the important role of internal audit in the corporate governance system has been widely recognized. In the face of the development of science and technology and high and new technology, and the continuous challenge of the epidemic, how to survive steadily in the environment of internal and foreign troubles is the motif that every enterprise should think about. For example, Shi Henggui(2010)[37], Ying Zhang(2017)[38], Tang Hualin (2021) For energy enterprise internal audit standard governance, further combed the internal audit innovation path in corporate governance, including improving governance mechanism, increase organizational value, achieve organizational goals, such as three aspects, and emphasize the internal audit role, ensure the importance of internal audit independence, advocate to strengthen the construction of internal audit system, build internal audit company culture, and if necessary can outsource internal audit business measures.[39]

5. Conclusion

In summary, the current research on corporate governance in our country mainly for listed companies, and the integration of audit and corporate governance research mainly for the functions of internal audit and corporate governance of positioning and the relationship, for the literature of external audit and corporate governance research is less, involving the "audit committee" and corporate governance system is more rare. As the role of the "immune system", audit plays an indispensable responsibility in the process of the construction and improvement of the corporate governance system. Based on the brief analysis of the action mechanism of corporate governance and audit, the current internal audit research and development of the corporate governance system has gradually become a system, and the future development is mainly based on the improvement of independence and the optimization of the system. The function of external audit can be considered to expand, and with the advantage of the strong independence of external audit, it gives the more objective evaluation result of corporate governance. In addition, shared audit for upstream and downstream enterprises in the supply chain in the future [40], The establishment of the audit committee, the application of management audit and other aspects of exploration and research, give full play to the effectiveness of audit. At the same time, based on the starting point of the new journey of national planning, Chinese enterprises should also actively absorb the world's advanced corporate governance model, deepen the comparison, preserve the competitive strength in the economic downward pressure, and realize the improvement and innovation of the corporate governance system.

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