



Value-added Internal Audit from the Perspective of Corporate Governance

Yushen Ma

Department of Accounting, Business School, Shandong University of Technology, Zibo, China

Email address:

sdutmys@163.com

To cite this article:

Yushen Ma. Value-added Internal Audit from the Perspective of Corporate Governance. *International Journal of Accounting, Finance and Risk Management*. Vol. 6, No. 4, 2021, pp. 121-127. doi: 10.11648/j.ijafirm.20210604.14

Received: November 19, 2021; **Accepted:** December 6, 2021; **Published:** December 11, 2021

Abstract: In an increasingly competitive market, internal audit, an integral part of corporate governance, has become increasingly important. Traditional internal auditing no longer fully responds to the current complex scope of internal auditing and the governance objectives of adding value to companies. With the continuous strengthening of corporate governance by modern enterprises, the goal of internal audit is gradually consistent with that of corporate governance: to increase the overall value of the company. This makes internal audit function, audit content and audit scope change accordingly, and value-added internal audit emerges as the times require. With the continuous development of international economic globalization, value-added internal audit is the inevitable trend of internal audit transformation from the perspective of corporate governance. Modern internal audit plays a very important role in improving the governance structure and internal control, and can bring value added to enterprises. The functions and responsibilities of internal audit are positioned to promote the achievement of corporate governance objectives, with increasing emphasis on improving governance and adding value. This means that the functional scope of internal audit has changed from simple financial audit at the beginning to a series of activities such as review and evaluation, control and risk management that run through all aspects of corporate governance. Internal audit is not only a part of corporate governance, but also evaluates and improves the effectiveness of corporate governance procedures. The benign interaction of the two contributes to the improvement of the management procedure and the increase of the overall value of the company. Internal audit can make use of its unique independence to control the risk of the company, improve the efficiency of corporate governance and improve the process of corporate governance by performing a comprehensive evaluation function, so as to enhance the comprehensive quality and economic benefits of the company and realize the overall value of the company.

Keywords: Corporate Governance, Value Added, Internal Audit

1. Introduction

Internal audit develops with the rapid development of economy. The traditional internal audit is generally positioned to serve the management, which determines the audit function, audit content and audit scope are greatly limited. With the continuous strengthening of corporate governance by modern enterprises, the goal of internal audit is gradually consistent with that of corporate governance: to increase the value of the organization. This makes internal audit function, audit content and audit scope change accordingly, and value-added internal audit emerges as the times require. Internal audit plays a very important role in improving the governance structure and internal control, and can bring value added to enterprises [1].

The international operation of enterprises makes more and

more enterprises, especially many listed companies, begin to participate in international economic cooperation and competition on a larger scale and in a deeper degree. Risk management has gradually become the focus of corporate governance and corporate governance has changed from a static control mode to a dynamic mode of constantly preventing various risks. According to the experience and lessons of developed countries, internal audit plays a very important role in internal control, risk management and corporate governance [2].

The effective operation of modern enterprise system needs standardized corporate governance as the premise and effective internal audit system is conducive to improving corporate governance. With the continuous development of corporate governance theory and practice, internal audit

theory and practice have also undergone significant changes, showing a trend of value added [3]. How to improve the value manufacturing ability of internal audit and serve for enterprise value increment is worth studying. A growing number of scholars have gradually begun to explore the value-added internal audit system at both the theoretical and practical levels. In order for companies to develop steadily and healthily in the long term, company managers should give full play to the value-adding function of internal audit in the areas of corporate governance, corporate risk management and corporate internal control from the perspective of achieving corporate governance objectives.

Therefore, to strengthen the study of internal audit theory, promote the development of internal audit, strengthen the internal audit of the company, fully and effectively perform the role of internal audit, prevent risks, improve governance, and then add value to the organization is an important subject in front of us, but also has important practical significance. Based on this background and significance, this paper conducts a more in-depth study on value-added internal audit under corporate governance.

2. The Relationship Between Internal Audit and Corporate Governance

Corporate governance is generally defined as a mechanism of supervision and checks and balances between the former and the latter under the separation of ownership and management. The core is to deal with the distribution of rights and interests among various stakeholders, such as large and small shareholders, creditors and the general manager, so as to form an effective multi-party check and balance relationship, thereby creating a harmonious and stable internal environment for the company to achieve smooth operation and overall value appreciation.

From the perspective of organizational structure, the internal audit department is a department existing in the organizational structure of the company but its own independence is relatively obvious. The functions of internal audit include assisting company managers to find out a series of potential problems that may exist in the setting of internal control processes; Identify and control all kinds of risks that may be faced in the internal and external environment of the company based on the whole market level, so as to help the organization minimize losses as much as possible. The functions and responsibilities of internal audit are positioned to promote the achievement of organizational goals, with increasing emphasis on increasing organizational value [4] and improving organizational governance. This means that the functional scope of internal audit has changed from simple financial audit at the beginning to a series of activities such as review and evaluation, control and risk management that run through all aspects of corporate governance, further reveals the new positioning of the value-added functions mentioned therein [5].

The function of internal audit can help the governance layer

identify the possible problems in the internal control system, and identify and evaluate various risks faced by the internal and external enterprises from a macro perspective. Company managers often make plans and make decisions at the level of overall strategic layout. In these management activities, the internal audit department plays the function of lubricant and adhesive between relevant departments, which can avoid or reduce information asymmetry in the process of departmental collaboration to the maximum extent. Comparatively objective and fair opinions and suggestions are given when enterprise managers make goal decisions, so as to reduce the probability of decision-making errors in work. In addition, internal audit can also help employees form a good professional ethics and quality and promote the company to create a high spirited organizational culture and harmonious working atmosphere, so as to stimulate employees' enthusiasm for work and create more benefits for the company.

Internal audit procedure is an indispensable part of corporate governance. Internal audit is not only a part of corporate governance, but also evaluates and improves the effectiveness of corporate governance procedures. The benign interaction between the two is conducive to the improvement of governance procedures and the increase of organizational value [6]. The existence of the internal audit department to supplement the organization internal control functions. The internal audit department is able to check the soundness of internal control mechanisms and the efficiency of procedures, identify gaps and risks in internal control systems and mechanisms, and make sound recommendations to the governance on corporate governance, which is very effective in improving the internal control mechanisms of the audited entity and promoting prior control and process control.

Internal audit can make use of its unique independence to control the risk of the company, improve the efficiency of corporate governance and improve the process of corporate governance by performing a comprehensive evaluation function, so as to enhance the comprehensive quality and economic benefits of the company and realize the overall value of the company [7].

3. The Significance of Establishing Value-added Internal Audit in Corporate Governance

Internal audit is usually regarded as an important part of internal control, belonging to the supervision and evaluation of internal control. Traditional internal audit is mainly supervisor-oriented post-audit, with emphasis on compliance audit [8, 9]. This audit method can help enterprises reduce operational risks, but it does not help to improve the overall operational efficiency and avoid huge risks caused by major decision mistakes. The concept of value-added internal audit is a new concept that builds on the traditional concept of internal audit, while accompanying the improvement of corporate governance. It is the overall direction of the future development and transformation of internal audit, and is a

further enrichment and expansion of the original functions possessed by traditional internal audit.

Value-added internal audit is not a new type of audit. It is a new stage in the development of internal audit, a succession and expansion of the previous financial audit and management audit operations. Value-added internal audit represents a new audit concept and is a new direction of the development of internal audit. By closely combining strategic objectives, value-added internal audit provides consulting services and constructive audit suggestions for corporate governance and helps corporate governance to clarify strategic direction, further improve operational efficiency and prevent and control operational risks.

Value-added internal audit can directly add value to enterprises through value-added activities [10]. By improving work efficiency, reducing resource consumption, expanding business areas with high value-added and minimizing or eliminating non-value-added business activities, enterprises can add value.

Because the organization still only focuses on the functions of internal audit in accounting and internal control and lacks deep understanding and cognition of value-added internal audit in daily corporate governance and other links so it also lacks the support and action power to establish value-added internal audit system within the organization. This makes it impossible for corporate governance to fully perform its value-adding function. The consulting function of internal audit to improve the quality and efficiency of the organization is established on the basis of the inspection and evaluation function. Inspection and evaluation activities are aimed at advisory services, i.e. the inspection, evaluation and advisory functions are discursively aligned to add value to the organization and achieve the goals that serve the organization [11, 12].

In order to achieve stable and healthy long-term development of enterprises, corporate managers should give full play to the value-added functions of internal audit in the field of corporate governance, risk management and internal control from the perspective of realizing corporate governance goals [13, 14].

Under the mode of value-added internal audit, the internal audit department can find and control the company's potential risks, improve and perfect the company's plans and organizational goals so that the internal audit is appropriately integrated into the corporate governance structure and constitutes an integral part of it.

To perfect and improve the internal control mechanism is an effective way for an organization to enhance its overall market competitiveness. Therefore, value-added internal audits can be seen as an essential catalyst for the improvement of internal controls by evaluating the quality and efficiency of internal testing procedures, testing the soundness and accuracy of internal control mechanisms, identifying gaps and failures in the organization's business decisions, and then identifying targeted improvement initiatives to enable the company to finalize a series of long-term and effective internal control systems as soon as possible.

If a mathematical relationship is used to represent the relationship between risk and reward for an organisation, it can be seen as proportional, i.e. the more reward an organisation attempts to capture, the greater the risk it faces. Risk management is also a part of corporate governance, which is highly valued by the organizational governance layer. In daily work, value-added internal audit can, through various audit tools and methods, comprehensively monitor and explore the potential risks in the organisation's operations and work scope, establish a sound risk control system, promote the company to improve the corresponding risk management mechanism and organisational structure, and strive to establish long-term effective risk control within the organisation, so as to further use the audit results of financial data to enhance the organisation's professional level of risk anticipation, risk avoidance and efficiency. This will further enhance the organisation's professionalism in risk identification, risk avoidance and efficiency, thereby achieving the overall objective of corporate governance to add value to the business.

If the internal audit department wants to get the attention of the corporate governance layer, allocate internal resources preferentially and improve its own status, it should give full play to its functions and roles in promoting the operation of the company and enhancing the value of the organization to assist the organization to achieve decision-making goals. Value-added internal audits can also enumerate countermeasures to improve business processes and internal organisational structure from different perspectives, so as to further stimulate the innovation of internal staff and enhance the market competitiveness of the company, ensure the rational allocation of resources, control costs and losses, and achieve the governance objective of adding value to the organisation [15].

4. The Difference Between Value-added Internal Audit and Traditional Audit

Value-added internal audit is a new type of internal audit that aims to improve the efficiency of the organisation's operations and add value to the organisation, using the special position, resources and methods of internal audit to improve its own efficiency while providing clients with continuous value-added in a new and changing environment. The difference between value-added internal audit and traditional internal audit is mainly in the area of value-added.

First of all, traditional internal audit does not pay attention to adding value to the organization. Many of the activities it undertakes are not value-added in relation to value-added internal audit, or are not value-added overall because the resources and costs expended are greater than the value added. The value-added internal audit comprehensively changes the concept of audit and tries to do less non-value-added audit business, while the traditional audit business that can add value tries to improve work efficiency, reduce resource consumption and cost, and focuses on vigorously expanding

the audit business with high value-added.

Second, the traditional internal audit department is a resource consumer and a cost center that does not directly add value to the organization. However, value-added internal audit is committed to value-added. While consuming resources, it directly adds value to the organization by providing meaningful audit results or valuable suggestions.

Finally, the fact that traditional internal audit indirectly adds value to an organization is often overlooked. Because it is positioned as a cost center and does not measure income, people only measure the consumption of internal audit expenses. However, value-added internal audit is different. It is positioned as a profit center. The cost is recorded and the value added to the organization is measured and recorded.

5. Obstacles to Establishing a Value-added Internal Audit in Corporate Governance

5.1. Lack of Advanced Corporate Governance Internal Audit Concept

At present, the management of many companies still adhere to the traditional concept of audit, and do not realize that internal audit, as a functional department of the company, can assist the company to optimize the business process, improve the management system, prevent internal and external risks, reduce the loss that the company may face, and realize the value increment of the company.

Because internal audit plays its value-added function in an indirect and auxiliary way, it is often regarded unilaterally as a cost center that generates a lot of expenses. Internal audit is often hastily defined as the resource consumption department of the company, which may lead to the management of the company to restrict the allocation of resources of the internal audit department in order to reduce the overall cost of the organization, and thus severely restrict the play and development of the value-added function of internal audit.

To gradually build the structure of value-added internal audit department and give full play to its value-added function, we must first learn new concept knowledge from top to bottom in the concept of corporate governance and internal audit. However, at this stage, the awareness and understanding of the functions of the internal audit department is still only superficial, from the management level down to the junior staff. They are not yet aware of the value-added functions of the internal audit department, i.e. to promote the improvement of the organisation's work processes and management mechanisms, to prevent potential risks within the company and the external environment, and to reduce the company's exposure to losses, so as to achieve the ultimate goal of corporate governance, i.e. to add value. This will lead to the deviation of the function positioning of the internal audit department in the enterprise. Managers are often shackled to the financial audit in the traditional sense, and usually do not pay attention to the opinions and suggestions of corporate

governance, risk control and other aspects proposed by the internal audit department.

5.2. Lack of Corporate Governance Organization Model to Implement

It is generally believed that the mode of internal audit department directly under the leadership of the board of directors or the board of supervisors can guarantee its highest authority and independence in organizational structure. However, at present, most companies adopt the model under the leadership of the general manager. Although it is convenient for managers to directly audit the company's business processes, the scope and extent of audit implementation are greatly limited, and the audit results are easily affected by the will of the management layer. In this mode, the internal audit department is restricted too much by the governance layer, and its independence is difficult to be guaranteed, thus hindering the organization to achieve efficient corporate governance.

5.3. Lack of High-quality Human Environment

With the gradual extension of the scope of work of the internal audit department, value-added internal audit involves much more extensive professional knowledge than traditional internal audit, and the comprehensive characteristics of disciplines are more obvious. Both in theory and in practice, internal audit personnel of enterprises are put forward stricter requirements. In the past, the staff of single accounting and audit specialty cannot adapt to the new requirements of value-added internal audit work. Internal audit personnel had not received due to internal audit comprehensive unified training, professional knowledge of the company's business process audit and corporate governance decisions lack basic field experience. A and for the use of high-tech means to unfamiliar, no accurate professional judgment to carry out the audit business and identify potential risks in corporate governance. This will greatly hinder the expansion and extension of internal audit's value-added functions in corporate governance.

6. The Path of Establishing Value-added Internal Audit System in Corporate Governance

6.1. Update the Audit Philosophy of the Enterprise from the Governance Level to the Grassroots

The management of the company should consider the function orientation of internal audit in corporate governance, update their personal concepts, actively explore the expansion direction of audit function, increase the importance of internal audit and change the function orientation of internal audit from a simple error correction organization to a decision-making assistant department to achieve corporate governance goals.

First of all, the management layer should guide the

grass-roots staff to define the new goals of internal audit in the new era from top to bottom. It should not only pay attention to the theoretical study but also promote the practical exploration of internal audit, so as to further improve the internal audit mechanism of the organization. Secondly, the governance layer should gradually pay attention to the decisions and suggestions listed by the internal audit department and realize the corporate governance goals with the help of the internal audit report. For internal auditors, in the future, they should not only perform their own functions of finding problems within the company but also form the ideology of realizing value increment for the organization and give full play to their subjective initiative to realize value increment for the company. If internal audit wants to find its niche, it must start to change its mindset and make a difference in order to get its rightful place, a layer of philosophy that is far from being present in the traditional oversight-based internal audit mindset.

6.2. Optimize the Setting of Internal Organizational Structure

If the value-added internal audit mode is to be successfully carried out in an organization, a perfect organizational structure is indispensable. Meanwhile, the relative independence of the internal audit department is the premise to ensure the objectivity and accuracy of audit reports. This means that a sound and complete way of setting up the internal audit organization structure should exist within the enterprise, with clear separation of powers and responsibilities and accurate and comprehensive positioning of the audit function, which requires the governance staff to actively improve the internal audit group institutional management tools, improve resource allocation and promote the optimization of the internal audit department.

First of all, the managers of the company should actively change their attitude, improve the status of the internal audit department in the company, mobilize the enthusiasm of departments at all levels of the company and make them actively cooperate and obey the development of the work process of the internal audit department. At the same time, the establishment of a special audit committee allows the internal audit department to operate relatively independently and not be influenced by other departments or personnel. In addition, the Board of Directors exercises direct jurisdiction, so that the internal audit department is supervised by the Supervisory Board and is not subject to the control of the management, which allows the internal audit staff to maintain the authority and objectivity of the audit reports at all times, while at the same time enabling the internal audit department to perform its value-added functions while being under the supervision of the Supervisory Board. A sound organizational structure is of great benefit to internal auditors to produce objective and true audit results so that value-added internal audit can be carried out and applied.

Secondly, if value-added internal audit wants to give full play to its departmental functions, it cannot be divorced from the effective cooperation of other departments within the

organization. The corporate governance layer should take the initiative and actively guide the organizational personnel at all levels of the company to deeply learn the importance and necessity of implementing value-added internal audit, so as to promote departments at all levels of the company to efficiently respond to and cooperate with the work of the internal audit department, and give full play to their value-added functions.

6.3. Set up and Cultivate Professional Audit Team

Whether value-added internal audit can be successfully carried out and fully perform its functions in an enterprise depends largely on the professional quality and overall ability of employees. High levels of internal audit personnel should have a combination of auditing, accounting, law, theory of computer information and other aspects of professional skills to ensure that the value-added internal audit mode can give full play to the functions in the internal audit work. In addition, the company should improve the comprehensive quality of staff training to form a high quality of internal audit team.

First, the company should establish and improve a series of employment criteria. When recruiting auditors, enterprises should pay attention to select comprehensive talents with various professional theoretical knowledge as far as possible, enhance the diversity of internal audit team's skill level and enrich the theoretical system and practice category of the team. It can also transfer a group of employees with accounting, auditing, computer and other professional skills from other departments of the company to assist in promoting the implementation of internal audit business processes, which can greatly reduce recruitment and training costs for the company.

Secondly, for the organisation's original internal audit staff, the company cannot slacken the professional knowledge and skills training for internal audit staff. Improve their overall professionalism as well as their logical thinking and interpersonal communication skills as soon as possible in a short period of time so that they can be qualified for their positions under the requirements of the new era. Establish a high-level internal audit team capable of discovering loopholes and risks in corporate governance, and put forward reasonable countermeasures, so as to expand the all-round skills of the internal audit department of the company.

Finally, establish and improve the internal reward and punishment system of the enterprise, give multiple rewards to the employees with a number of professional skills certificates and excellent performance appraisal results. Transfer or dismiss employees with improper work attitude and perfunctory work in a timely manner so as to gradually improve the overall standard of internal audit staff.

6.4. Enrich Internal Audit Technology and Means

With the increasing size of organizations and the increasingly complex scope of audit work, more and more loopholes and risks in corporate governance have emerged that are difficult to detect. Traditional internal audit is no longer able to cope with the standards and requirements of the

new era, and how to use computer information technology and means to promote the transformation of internal audit information has become the focus of the governance of domestic enterprises. At present, the computer application level of existing internal auditors in domestic enterprises is low, and the auxiliary internal audit software that has been introduced is very selective, so the internal audit department of enterprises should vigorously carry out systematic training in computer technology, and gradually buy auxiliary internal audit software and technical means to carry out the internal audit workflow, which can significantly improve the accuracy and objectivity of the audit work report while conducting an overall analysis of the audit unit.

First of all, enterprises can establish an internal audit data information management system, similar to the yonyou accounting information system software used by financial departments, which can completely record and store the data and information of the entire audit cycle by classification. Various internal audit reports are then automatically generated with the help of the system's computerised big data function. In this way, we can directly grasp and monitor any data and information in the entire business process through the computer system, and then make risk indications on the vulnerability of corporate governance based on the abnormal data reflected in the system.

Secondly, this new model of internal audit with the help of computer information technology allows internal auditors to obtain effective and real audit data and information through the software system at any time, and also to use the algorithmic analysis tools in the computer system to carry out professional and accurate systematic analysis of the selected data. This "human-machine" internal audit model opens up a new way of internal audit and is a new internal audit tool that helps companies strengthen their internal control management while bringing into play the value-added function of internal audit, so that value-added internal audit can achieve long-term sustainable development.

7. Conclusion

With the continuous development of international economic globalization, internal audit, as an organic part of organizational management control, is becoming more and more important in the increasingly fierce market competition. Value-added internal audit is the inevitable trend of internal audit transformation from the perspective of corporate governance. As the development and extension of traditional internal audit, value-added internal audit will play a positive role in promoting the achievement of corporate governance goals and the improvement of corporate operations. The gradual improvement of internal audit system and means will also help value-added internal audit to play an increasingly indispensable role in the future corporate governance process. With the gradual increase in the importance attached to value-added internal audit by internal audit theoreticians and practitioners, internal audit has gradually risen to the level of corporate governance. To develop value-added internal audit,

it is important to focus on the positive interaction between internal audit and corporate governance, and to actively expand the functions of internal audit by sorting out the organisational structure of the company, improving the internal audit management mechanism, and forming new ideas on internal audit work, so that internal audit can play a positive role in adding value to corporate governance.

References

- [1] Giselle Bou-Raad. (2000). Internal Auditors and a Value-added Approach: the New Business Regime [J]. *Managerial Auditing Journal*, 15 (4): 182-187.
- [2] Dan Wang and Yajun Guo. (2009). Study on the Internal Audit for Listed Companies Based on Value-added View [J]. *International Journal of Business and Management*, 4 (7): 52-55.
- [3] Lise Muriel Botha and Naomi Wilkinson. (2019). A Framework for the Evaluation of the Perceived Value Added by Internal Auditing [J]. *Meditari Accountancy Research*, 28 (3): 413-434.
- [4] Audrey A. Gramling and Nur Irem Nuhoglu and David A. Wood. A (2013). Descriptive Study of Factors Associated with the Internal Audit Function Policies Having an Impact: Comparisons Between Organizations in a Developed and an Emerging Economy [J]. *Turkish Studies*, 14 (3): 581-606.
- [5] Xiaolong Qu and Bin Liang and Hsing Hung Chen. (2020). Research on the Value-added Role of Internal Audit [J]. *International Journal of Higher Education Teaching Theory*, 1 (4): 211-213.
- [6] Lourens Erasmus and Philna Coetzee. (2018). Drivers of Stakeholders' View of Internal Audit Effectiveness: Management Versus Audit Committee [J]. *Managerial Auditing Journal*, 33 (1): 90-114.
- [7] Cecily Raiborn, Janet B. Butler, Kasey Martin, Mina Pizzini. (2017). The Internal Audit Function: A Prerequisite for Good Governance [J]. *Journal of Corporate Accounting & Finance*, 28 (2): 10-21.
- [8] Dessalegn Getie Mihret and Getachew Zemenu Woldeyohannis. (2008). Value-added Role of Internal Audit: an Ethiopian Case Study [J]. *Managerial Auditing Journal*, 23 (6): 567-595.
- [9] Zhao Baozhu. (2019). Audit Model Study of Professional Research Institutions in Power Grid Enterprise [J]. *Journal of Finance and Accounting*, 7 (5): 161-167.
- [10] Dale L. Flesher and Jeffrey S. Zanzig. (2000). Management Accountants Express a Desire for Change in the Functioning of Internal Auditing [J]. *Managerial Auditing Journal*, 15 (7): 331-337.
- [11] Wadesango Newman and Makerevi Comfort. (2018). Investigating the Value Creation of Internal Audit and Its Impact on Company Performance [J]. *Academy of Entrepreneurship Journal*, 24 (3): 1-21.
- [12] Sun Lihui. (2019). Research on the Economic Value-Added Effect of Internal Audit Joint Internal Control [J]. *Frontiers of International Accounting*, 8 (3): 100-106.

- [13] Kenneth D' Silva and Jeffrey Ridley. (2007). Internal Auditing's International Contribution to Governance [J]. *Int. J. of Business Governance and Ethics*, 3 (2): 113-126.
- [14] Kennedy Sakaya Barasa. (2015). Statistical Analysis of the Role of Internal Audit in Promoting Good Governance in Public Institutions in Kenya [J]. *Journal of Investment and Management*, 4 (1): 38-46.
- [15] Imbrescu Carmen Mihaela and Peța Crina. (2017). Internal Audit: 'A Necessary Evil' or A Creator of Added Value? [J]. *Ovidius University Annals: Economic Sciences Series*, 2017, 17 (2): 571-575.