

A Comparative Study of the Theoretical Framework for Evaluating the Effectiveness of Internal Control between China and the United States

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Abstract: Although our internal control system has been initially built, the ideas, connotations and elements of internal control have not been well developed in practice. Many enterprises do not realize the importance of internal control, which directly affects the implementation effect and process of the internal control system. Therefore, the author makes a comparative study on the theoretical framework of internal control effectiveness evaluation between China and the United States. In order to provide a theoretical basis for the quantitative evaluation of the effectiveness of internal control. After reviewing the development history of internal control between China and the United States, and conducting comparative research, it is believed that the primary task of strengthening the implementation of internal control is to strengthen the construction of "software" such as the control environment.

1. Introduction

The capital market is increasingly important to the country's economic development, and investor protection is one of the most important factors affecting the development of the capital market [1]. In October 1939, the Auditing Procedures Committee of the American Institute of Certified Public Accountants published the Audit Procedures No. 1 and added the content of internal control review for the first time in the revised standardized audit report [2]. In the future, the audit procedures based on internal control were repeatedly identified in several documents and decrees [3]. After the industrial revolution, the emergence of internal control in the United States, but only at the time of internal containment, that is, through account reconciliation and job separation to avoid financial accounting fraud, after hundreds of years of development, this containment is gradually refined [4]. The basic norms promulgated this time combine some advanced international concepts and methods with the actual situation of Chinese enterprises. It establishes the basic framework for the establishment and implementation of internal control in Chinese enterprises, and opens the prelude to the comprehensive and systematic improvement of the internal control management system of Listed Companies in China [5]. It can be seen that strengthening the construction of internal control of government departments is the general trend, and is becoming an important part of national governance. Since the 21st century, with the outbreak of malignant fraud cases at home and abroad, such as Enron, WorldCom and Yinguangxia, it has aroused unprecedented attention from all walks of life on how to protect the interests of investors as much as possible.

Since the mid-20th century, the internal control responsibility of government departments around the world has gradually become rigid [6]. Investigate its reason, information asymmetry is the biggest obstacle to investor protection. On the whole, the new basic norms of internal control of enterprises have been in line with international standards in system [7]. Since the beginning of this period, the accounting-oriented audit has gradually been replaced by the system-based audit, and the evaluation of internal control has also become an integral part and an important feature of audit [8]. By the 1940s, in order to meet the needs of management and protect the economic interests of investors and creditors, the connotation of internal control began to break through the restrictions in the field of financial accounting, and extended to various fields of enterprises [9]. Before the formal implementation of the internal control basic norms, enterprises must actively respond to the establishment of specialized agencies or specialized personnel to formulate the internal control

system of the enterprise. In recent years, Chinese government departments have paid more and more attention to internal control and have issued a series of related policies [10]. Therefore, the country's legal provisions may not be fully reflected in the company's institutional arrangements. Analysis of the differences and linkages between China and the United States in the theory of internal control frameworks will facilitate the smooth implementation of new internal control norms. Therefore, companies need to reduce the impact of information asymmetry through internal mechanisms or other measures to strengthen investor protection, thereby reducing agency costs and financing costs.

2. Internal Control Effectiveness: Analysis of the Transmission Mechanism of Investor Protection

2.1. Direct conduction mechanism

Internal control reduces agency costs and increases corporate value by constraining the behavior of management and controlling shareholders. In addition, the protection of investors is directly realized, that is, according to the idea of “internal control effectiveness—reducing agency costs—improving corporate value—investor protection”, the internal control governance function plays a role in protecting investors. Among them, investor protection focuses on protecting investors' income rights. From the specific guidelines for independent auditing in 1996 to the recent new internal control regulations, it can be seen from the latter that the concept of internal control has gradually improved and is consistent with the concept of the international internal control framework. For example, it is gradually clear that internal control needs to guard against various risks of operation and management. In 1979 and 1998, the Securities and Exchange Commission (SEC) proposed mandatory reporting of internal controls. In 1989, the United States Government Audit Office (GAO) also proposed that the internal control of management and auditors should be reported in the Emergency Assistance Bill for Deposit and Credit Institutions, but no final bill was formed. Prior to this, the guiding principles, guidelines and norms of internal control in China were mainly designated by the regulators of various industries for their own industries, which lacked uniformity and coordination. The promulgation of the framework marks that the theory of internal control has entered a new stage centered on enterprise risk management, representing the latest and most perfect theory of internal control.

2.2. Indirect conduction mechanism

Internal control can protect investors indirectly by guaranteeing the true reliability of accounting information and reducing information asymmetry. It mainly focuses on the protection of investors' right to know and decision-making. There are many factors influencing the control environment: the board of directors, the quality of managers, managers' conduct and management philosophy, ethics and codes of conduct, organizational structure and power and responsibility allocation system, information system, human resources policy and practice. Generally speaking, legal operation is the most basic quality for an enterprise to participate in market activities, and it is a relatively easy goal to achieve. With the change of economic environment, enterprises are facing more risks. Especially after the scandals of Enron and WorldCom, a comprehensive risk management framework is needed to help and guide enterprises to identify, assess and control risks. The above-mentioned related policies have put forward new norms and higher requirements for the relevant government departments to strengthen internal control. Therefore, in order to seize limited capital. Companies with effective internal control highlight their competitive advantage by voluntary disclosure or mandatory disclosure of relevant information, and financial reporting is an effective vehicle for disclosure. In order to improve the quality of financial reports, reduce the uncertainty of external investors on the relevant information of enterprises, and play a role in protecting investors.

3. Enlightenment from the Comparison of Internal Control between the Two Countries

Whether the internal control system is effective depends on many factors, but the key is the internal environment of the enterprise which is in the basic position. According to the evaluation criteria, the evaluation subjects adopt appropriate evaluation methods to evaluate the evaluation objects, so as to achieve the goal of the effectiveness evaluation of internal control. In an effective internal control system, power checks and balances help to restrain the management of the company, maintain the independence of CPAs, and then improve the audit quality. In fact, the improvement of business information system plays an important role in company risk management and management objectives. For example, insurance companies' aggregation of insurance policy information, claims information and the establishment of statistical databases are essential for correctly calculating the solvency and liquidity risks of various reserves and reserves. Therefore, China should also pass laws and regulations to require listed companies to implement mandatory internal control information disclosure. No matter how complete the accounting system of the enterprise, how detailed the internal control procedures are, once the enterprise has loopholes in some aspects such as integrity and morality, organizational structure, governance structure, management philosophy, power distribution and authorization, and human resource management. Nothing can fundamentally avoid problems. Considering that the financial sector has no departmental interests, it can play the best coordination role of the neutral institutions, thus forming a mechanism jointly led by the financial department and jointly formulated by other departments.

It can be seen from the comparison of the formation mechanism that the political environment determines the object of accounting services. In order to ensure the authenticity of internal control information disclosure, the certified public accountant responsible for the annual accounting statement audit shall issue a verification opinion on the internal control report and disclose it together with the audit opinion of the accounting statement. The internal control office or the internal control team mainly exercises both supervisory and evaluation functions, and can participate in the formulation of reform measures as well as the implementation of reform measures. The role of governance function is mainly to constrain the opportunism of insiders, reduce agency costs, ease the degree of information asymmetry afterwards, and protect the legitimate rights and interests of investors. Therefore, in order to ensure that the internal control system is effectively implemented and the implementation effect is good, and that the internal control can adapt to the new situation at any time, the internal control must be supervised. The Internal Control Committee consists of an office or working group whose members are selected from the heads of relevant departments and business backbones. The head of the internal control committee may act as the convenor of the internal control committee. Supervision is a process of evaluating the quality of system implementation over time. With the preliminary establishment of internal control system in China, a good control environment has become the key to restrict the effectiveness of internal control. This means that internal control has changed from the past process-oriented control to the future process uncertainty control.

4. Conclusions

Scientific and reasonable evaluation of internal control of government departments is conducive to improving the internal management level of government departments. Therefore, it is particularly important to evaluate the effectiveness of internal control. Based on the analysis of the transmission mechanism of internal control to investor protection, this paper studies the elements and their relationships in the theoretical framework of internal control evaluation based on investor protection. Its evaluation needs theoretical guidance. We should base on the historical evolution of internal control and its latest research results and future development trend. Therefore, the staff of the theoretical and practical circles in our country attach great importance to the study of the construction of internal control norms, and have made a lot of efforts in introducing theory and improving practice. When constructing the internal control standard system, China must consider

China's specific environment, relevant national laws and regulations, and business management practices, and closely follow the international trend in advanced concepts and technical methods. In China's internal control system, the functions of monitoring are basically consistent with the COSO internal control integration framework. If a reasonable and effective internal control evaluation index system is not established, the evaluation method cannot be used to determine the scientific indicator weights. The seven elements of demand side, subject, object, goal, idea, standard and method of enterprise internal control effectiveness evaluation constitute the theoretical framework of enterprise internal control effectiveness.

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