

Analysis on the Reasons for Imperfect Promotion of Risk-Oriented Internal Audit in China

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Abstract

At present, risk-oriented internal audit has entered into a relative perfect stage in developed countries, the implementation and promotion of which have become relatively comprehensive. The countries in U.S. and Europe have carried out many mandatory stipulations and policy about the risk-oriented internal audit. The risk-oriented internal audit in the developed countries has been widely applied to the enterprises. However, there are still some problems in the promotion of the risk-oriented internal audit in our country. This paper analyzes the reasons for the imperfect promotion of the risk-oriented internal audit in Chinese enterprises and proposes some policies and prospects about it.

Key words: Risk-oriented internal audit; Promotion; Insufficient realization

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INTRODUCTION

After a decade of development, the worldwide corporate governance emerging in the 1990s enters into a relative mature stage. The laws about the corporate governance made by the countries are more and more elaborate and perfect. The development of the corporate governance creates good conditions for the production of risk-

oriented internal audit. From the 1950s, the corporate managers of the developed countries have paid more and more attention to the importance of risk management. In the 1980s, China also brought the risk management into the corporate practice. Since then, the internal audit fields of our countries began to pay attention to the risk management. In the 1990s, many scholars began to focus on the field of the risk-oriented internal audit. The Standards for the Professional Practice of Internal Auditing IIA-The Institute of Internal Auditors IIA-The Institute of Internal Auditors carried out by IIA (the Institute of Internal Auditors) in 2002 proposed that the internal audit work of the organization should be guided by the risk to meet the needs of organization's operating management. IIA believes that the internal audit should focus on the risk management. Therefore, the internal audit formally enters the risk-oriented stage.

The risk of risk-oriented internal audit not only means the audit risk, but also means the corporate risk to a greater extent. The risk-oriented internal audit is to combine the ideas such as risk management, corporate management and internal control to engage in the auditing work. The risk-oriented internal audit takes the risk as the core of internal audit. However, at present, the academics hold different ideas about the risk, so there is no unanimous definition of the risk up to now. The opinions of the academics mainly include: (1) believing the risk is the uncertainty of the possible result of events; (2) believing the risk is the uncertainty of the future loss; (3) believing the risk is the uncertainty of possible loss and the degree of damages. Although there is no unified definition about the risk, we can also infer from the above three opinions that the basic core of the risk "the uncertainty or loss of the future results". In 2001, IIA held that the risk is the uncertainty of the events affecting the realization of goals and also put forward that the measure of risk is the consequences and the possibilities.

In 2001, IIA amended The Standards for the

Professional Practice of Internal Auditing, defined it in this way: The internal audit is a kind of independent and objective consultation activity, aiming at increasing value and improving the organization's operation. It comments and improves the effects of risk management, controls and governances and helps the organization to realize its goals in a systematical and prescriptive method. This definition pushes forward the development of the risk-oriented internal audit.

1. THE CURRENT DEVELOPMENT OF RISK-ORIENTED INTERNAL AUDIT

1.1 The Current Development of Foreign Risk-Oriented Internal Audit

Currently, the risk-oriented internal audit has stepped into a more perfect stage in developed countries, the implementation and promotion of which have become relatively comprehensive. The countries in the U.S. and Europe carried out many mandatory stipulations and policy about the risk-oriented internal audit. The risk-oriented internal audit in the developed countries has been widely applied to the enterprises. Most of the listed companies of developed countries establish the internal audit committee to supervise the company's accounting, the financial report and to audit the financial statements. The internal audit departments of the company led by the internal audit committee and reporting to the internal audit committee are responsible for the internal audit committee directly. The responsibilities of internal audit department in the process of risk management mainly include: Checking the existing and potential risks during the operation of the company and proposing effective suggestions and measures to the management of the companies. Helping the companies reach the operation goals and increase value by risk checking and control. Compared with the foreign developed enterprises, the internal audit department of our country's enterprises has been able to supervise the enterprises' risk management comprehensively. The foreign developed countries have stipulated the relatively clear, elaborate and specific regulations in the field of the risk-oriented internal audit, making the risk-oriented internal audit have rules to follow. In addition, compared with the management structure of domestic companies, the foreign counterparts are more perfect, the management structure of the companies of which can improve the operational efficiency of the company.

1.2 The Current Development of China's Risk-Oriented Internal Audit

In China, most of enterprises still remain at the stage of finance-oriented internal audit; however, there are few enterprises implementing the risk-oriented internal audit. The company's internal audit process, there are different

audit models like the financing orientation, management orientation and risk orientation. The differences of these orientations are that they have different audit scopes, goals and the audit ways. In the finance-oriented internal orientation, the internal orientation institutions check the credibility and the stability of the information of accounting and finance so as to report to the higher level department. Therefore, the objects of the finance-oriented internal audit are accounting and financial affairs.

Although compared with the risk-oriented internal audit, the finance-oriented internal audit has low efficiency, and most of China's enterprises still adopt the traditional finance-oriented model to enforce the internal audit for the companies. There are different focuses and audit scopes in the orientation of finance and risk. The finance-oriented internal audit mainly are aimed at the accounting data and information, and the financial statement audit and it also focuses on the objectiveness, credibility and the authenticity of the accounting data and information, and the financial statement audit. Most of the finance-oriented audits which audit the past data and the financial statement of the company and propose some advice about the audit are ex post audit, a check of the historical business records, accounting and financial matters while the risk-oriented audit pays more attention to the pre-audit and the concurrent audit. The latter one requires the internal audit institutions to analyze the risks existing in the company's operation in advance, control the risks during the matters and regulate and provide the audit advice after the matter so as to achieve the audit goals. It also puts the risk consciousness through the work of internal audit.

2. THE ANALYSIS ON THE INSUFFICIENT REALIZATION OF CHINA'S RISK-ORIENTED INTERNAL AUDIT

This paper will analyze the insufficient realization of Chinese enterprises from the internal and external factors.

2.1 The Internal Factors

The risk-oriented internal audit only begins to develop in China. In the 1990s, the developed countries in Europe and the U.S. have made comprehensive research on the theory of the risk-oriented internal audit and have been widely applied to the company nowadays. However, our country brought in this audit model theory after 2000. At present, the risk-oriented internal audit has gained attention from China for just ten years, and the implementation time of it is even short. Therefore, if our country wants to promote the risk-oriented internal audit, it will take a certain period of time to research and explore.

2.1.1 The Weak Risk Management Consciousness

Although China has brought in the idea of risk management in the 1980s, the risk management has not been fully

applied to our companies. In addition, most of Chinese enterprises have not fully realized the importance of the risk management and that the risk management can effectively help the enterprises reach goals and increase their profits instead of focusing on the enterprise's short term profits, and neglecting the long term development of the company. The ignorance of the risk management directly causes the company to fail to forecast the risks existing in the company's long term development process and even be unable to cope with the risks. Although some companies have a certain risk management consciousness, they are not aware that the risk-oriented internal audit plays an important role in the process of company's development.

2.1.2 Imperfect Risk Evaluation System

Currently the risk management system undertaken by most of Chinese companies is stipulated in accordance with the following two standards: The first is to stipulate the system according to the laws and regulations conducted by the state and its relevant department. The second is that the leaders of company stipulate the system according to their own perception to the risks. Nevertheless, the risk management still remains at the preliminary stage, and the current risk evaluation system cannot meet the state's requirement and meet the companies' actual needs at the same time. The risk evaluation system of the internal audit in country is still imperfect, which will restrict the promotion and application of risk-oriented internal audit in our country.

2.1.3 The Independence of Chinese Companies' Internal Audit is Very Poor

Firstly, Chinese companies' internal audit lacks independence. In Chinese companies, the internal audit is a supplement to the external audit and is usually not a dependent department of the company, but belongs to the finance and other departments. Doing some audit work or activities always consider the interests of its department or the control by its department, leading to the poor independence and make it difficult to guarantee its justice, equity and objectiveness. Besides, the internal auditors lack independence. In our country's subconsciousness, the auditors amount to the accounts or the finance personnel. Therefore, the internal auditors of most of companies are the finance personnel or accounting personnel, causing the poor specialty of the internal auditors and difficulties in auditing independently.

In addition, the prejudice and the hostility to the internal audit by the leaders of company leads the internal auditors not to have enough freedom to audit according to the professional quality, even affecting their exploitation of independence. What's more, economically, the internal audit lacks independence. The company's internal audit of our country is a kind of independent activity of its internal development, the financial source of which is determined by the management of the enterprise. Therefore, the internal audit's every move will involve with their own

interests. In order to gain a foothold in the company, the internal auditors are easily to serve the management layer and meet their requirement in every aspect. Otherwise, the audit expenses of the internal audit will be restricted by the management layer, causing that the internal audit are unable to go smoothly and damaging the independence of the internal audit seriously.

2.1.4 The Internal Auditors Lack the Corresponding Professional Ability

The auditors implementing the risk-oriented internal audit should have more strong comprehensive ability and more profound knowledge. Besides being familiar with the finance and laws, the internal auditors should have the abilities for forecasting, evaluating and coping with the risks. For now, though, the internal audit personnel of our country are composed of the finance and audit personnel and they do not have the abilities such as laws, computers and the risk management required by the risk-oriented internal audit. Therefore, the personnel of the internal department of the company is very single, which can not meet the needs of implementing the risk-oriented internal audit in the company.

2.1.5 The Risk Management Technology is out of Date

Most of foreign enterprises have adopted the approaches like the financial engineering and mathematical statistics to confirm the risky projects in the working field of risk-oriented internal audit. However, the technology of Chinese companies in the fields of risk management and risk-oriented internal audit lag far behind the advanced enterprises of the developed countries. Currently, the analysis of the risks made by the Chinese enterprises still remains at the stage of analyzing the financial data and analyzing the risks qualitatively. The lack of the technology of analyzing the risks quantitatively and the outdated risk management model cause that the forecast, analysis and handling of risk by the relevant departments cannot meet the requirement of the enterprises and the risk-oriented internal audit is hard to conduct in the enterprise.

2.2 The External Factors

2.2.1 The Constant Improvement of the External Audit's Service

The constant improvement of the external audit's service providing makes company outsource the business of the internal audit, leading to cuts in the internal audit personnel and even the cancelation of the internal audit institutions. In recent years, the internal audit of Chinese is still at the finance-orientated stage. The poor independence of the internal audit causes the internal audit can't meet the company's requirement, fail to help the company realize their operation goals, and cannot increase value effectively for the company. The value of the internal audit cannot be realized fully, making the company ignore the function of auditing and causing a vicious cycle. Most of companies'

internal audits are unable to meet the requirement of the company, and the leaders of which did not look for the reasons and improve the technology of the company's internal audit to find an auditing method adapting to the company. Instead, the leaders give all of the work to the external audit units to reduce the auditing cost and expenses. Nowadays, the working field of external audit is expanded constantly and provides more and more perfect auditing service to meet the company's varieties of auditing requirements. The external audit can not only conduct traditional financial audit, but also includes the current risk-oriented audit in the scope of work. In fact, although the service provided by the external audit is more and more diversified, it cannot replace the internal audit completely. Compared with the external audit, the internal audit is clearer about the corporate position, goals and the actual situation, and is more familiar with the company's operation procedure. So, the importance of the internal audit cannot be ignored. Cutting the internal audit institutions and the internal auditors makes risk-oriented internal audit difficult to progress.

2.2.2 The Lack of Laws and Regulations

The lack of laws and regulations makes the enterprises lack the pressure of risk-oriented internal audit. There are few laws and regulations about the risk-oriented internal audit in our country. China Institute of Internal Audit carried out a newly revised China Internal Auditing Standards in 2013, which mentions that the company should integrate the internal audit work with the risk management in the process of company's internal management. But this revision only gives a general description about the risk-oriented internal audit without elaborating the specific contents of the risk-oriented internal audit. Nowadays, the norms of China's risk management audit are still too principle, the relevant departments do not stipulate mandatorily the development of the risk-oriented internal audit in the company and not pay real attention to the importance of the risk-oriented internal audit for the company. The lack of corresponding normal instruction and the company's ignorance to the risk-oriented internal audit makes it more difficult for this audit model to roll out in Chinese companies.

CONCLUSION

There are few laws about the risk-oriented internal audit, resulting in the lack of application basis of the

risk-oriented internal audit in our country. In addition, the outdated risk management method and weak consciousness of risk management cause that many of Chinese enterprises are based on the finance-oriented internal audit. Therefore, rolling out the risk-oriented internal audit model is not practical. Firstly, it needs the relevant departments of China to set up the rules, which are elaborate, complete and consistent with the real situation of our country to put the risk-oriented internal audit on a legal footing. Besides, the company needs to gradually transform their auditing ideas from the traditional finance-oriented internal audit to the risk-oriented internal audit. Thirdly, our companies need to bring in the advance management technology suitable for the companies and gradually update the risk management according to the national condition of China and the condition of the enterprises. Fourthly, it needs to improve the corporate governance of China and enhance the independence of the internal audit. This process cannot happen overnight, for example, the sound laws and regulations the transformation of the internal ideas is a long term process. Imitating blindly the advanced internal audit model of the developed countries is not line with China's national condition and the company's operation model, which will be counterproductive. Therefore, our companied should be combined with the previous internal audit model to gradually realize the risk-oriented internal audit and form the risk-oriented internal audit with Chinese characteristics, according to the real situation of our country.

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