The Influence of Board Characteristics on the Effectiveness of Internal Control

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Abstract: Under the background of rapid economic development, companies must establish a modern enterprise internal control system to adapt to the changing times. The essence of internal control is to make sure the true integrity of financial reports disclosed to the outside world and the legal operation of the company, sustainable development, asset security, etc.. It can play a supervisory role for managers and can evaluate the implementation of the system. For the establishment of modern enterprise system, how to guard against risk is very important. Internal control can produce a marked effect to prevent and control risks in keeping the company running, financial reporting, etc.. The perfection of internal control directly affects the enterprise's risk response. The current market competition is fierce, only a set of effective internal control system can make enterprises stand out in the market competition, sustainable development.

Introduction

In terms of the current listed companies, although most companies have to be suitabled internal control regulations that is thought to be suitable for the company's development has been introduced, the considerable climacteric domestic companies still occur one after another. Overall, there are three major risks: First, the risk caused by the poor validities of internal control. The second is speculation in financial instruments, and the third is production safety accidents. In addition to the production safety accidents, the first two types of risks have two obvious characteristics: First, the losses caused by the occurrence of risks to enterprises are huge, and the frequency of action will make the enterprises "hurt"; Second, similar accidents occur in large enterprises. Therefore, the effective implementation of enterprise internal control is worth paying attention to. Many companies have loopholes such as the lack of supervision system, the lack of penalties, and the lack of implementation. The ineffective internal control will make the management process of the company make mistakes, which will reduce the operating effect of enterprises. From this point of view, analyzing the effective performance of internal control activities in turn guides internal control, and scientifically and effectively evaluating the effective performance of internal control is conducive to managers choosing decisions that meet strategic goals and improving organizational strength and operational efficiency.

Corporate governance act on important function in the supervision, making strategic decision, restraint, and management of establishments. As an important part, it constitutes a modern enterprise management system. Board of directors is the basic level of internal control. As a key center mechanism of the board of directors, corporate governance functs the key factor of the strategic development and management of enterprises. From the point of view of agency relationship, board of directors in the relevance with shareholders as agency relations, and with the management level, but also act as entrusted supervision role. Therefore, the efficient operation of the board of directors can obviously help increase the efficiency of corporate governance, create more development and strategic decisions for enterprises, and thus enhance the internal control ability of enterprises. The board of directors has a decisive role in the organization, coordination and development of the company's development strategy, formulating development strategies for the company, and having control over the business operations of the company. Owing to the detachment of management rights and ownership, the board of directors may make decisions that
are more likely inclined to harm shareholders' interests in order to seek to maximize its own interests. However, from the current research results, most of them are based on the perspective of the company's main body, and less on the impact of the board of directors on the impact of internal control.

**Effectiveness of Internal Controls**

The effectiveness of internal control is a measure of the extent of perfection and implementation of built-in control in an enterprise. As a measure of the effectiveness of inner controls, whether or not inner control defects are disclosed. Therefore, the effectiveness measurement method is mainly measured by the identification of internal regulation defects, the disclosure of internal regulation information, and the establishment of internal evaluation models.

Internal control defects: The company that discloses a major defect is related to its age, profitability, and the complexity of the incorporation's organizational framework. The company has a long life, and the higher its emphasis on internal control, it is willing to take high-quality internal control system to better the business ability of the establishment. Inner control of the company's feasibility weak-point is inversely proportional to that of enterprises with longer establishment time. That is, enterprises with longer establishment time will be more aware of the importance of improving the internal control's effectiveness on account of political and economic factors. Similarly, the greater the likelihood of inner control flaws in companies with small, chaotic governance and poor cash flow, the study indicated that the scale was big or small of the board of directors of directors is inversely proportional to the performance of the company. Gaoliang Tian(2010) constructed a conceptual model of internal control defect disclosure by collecting sample data of the defect announce part of the inner control self-evaluation report in the yearly report of 494 public companies in Shenzhen. The method of Logit regression analysis is used to obtain that change the company's auditor and financial restatements are more inclined to disclose defects. In addition, the improvement of inner control construction has relationship with the complex level of the company's vocational work operations. The more complex the business, the more likely there is a greater financial insecurity. Concurrently, the number of branches of the company and the company's scale can effect the defects of internal control. Wanfu Li, Bin Lin, and Dongjie Lin(2012) explored internal control deficiencies disclosure by collecting information on defects in internal control of public corporations and company rectification reports. The study used 15 indicators to judge the main defects of internal control. In conclusion, the more the internal control defect is proportional to the abnormal accrual; The greater the auditor's competence, the possibility of disclosing defects in internal control.

Measurement of availabilities of internal control: The enterprise risk-management framework is an active inner control evaluation organization, which describes and evaluates the internal control objectives, procedures, and related to inner control elements indicated in the COSO report. The inner control evaluation mainly includes interest collection, information recording in the audit working paper and internal control evaluation. A number of academicians have evaluated a model of evaluating the internal control system of small companies from this point of view effectiveness of the costs. This evaluation model is also designed based on the five factors of inner control to help such companies effectively respond to risks. Strengthening internal controls. It can be seen that the measurement of internal control's efficacious continues to develop with the development of internal control theory, and the understanding and research on internal control evaluation is also continuously developing, gradually from the internal control defect identification of inner control evaluation model transition.

The theoretical study on the measurement control's efficacious is an attempt to construct a quantitative index model for assessing the inner control's effectiveness. In terms of research, it is mainly divided into two types: objective view and element view.

Evaluating model of internal control based on the element view is to build the internal control assessment index system founded the five factors of inner control, and then based on the observation value of the index, the weight of each indicator value is weighted to obtain a
comprehensive index evaluation result. To estimate the built-in control's effectiveness. The internal control is evaluated by whether the inner control system, process, etc. are comprehensive and appropriate, and whether they are effectively implemented. The specific indicators in each element are assigned to reduce the effectiveness of internal control. The internal control quota of public enterprises studied by the Xiamen University's discussion group which study on internal control uses the five elements about internal control as the first-level evaluation index. Each evaluation indicator has a series of subdivided evaluation indicators, and then utilize the AHP analysis technique to weighted mean of the indicators. Finally, based on the observed values of each index, after consistency and dimensionality, the inner control evaluation index is on the basis of weight weighted average. By establishing the mathematical analysis model of internal control assessment, using reliability theory and mathematical statistics, the internal control's effectiveness is evaluated by using the reliability of computable programs and system reliability in the model.

Evaluating model of internal control in accordance with the objective view is a comprehensive quantitative evaluation in line with the realization degree of inner control goals. From the goal of internal control as the starting point, the internal control evaluation system is based on selecting specific indicators that are representative and measurable. The evaluation weights and evaluation criteria are determined, and the score weights of the evaluation indicators are averaged to obtain the comprehensive evaluation index of internal control effectiveness. The inner control target is determined by analyzing the subject of internal control evaluation and positioning the target, including: defensive control evaluation index; Constructive control evaluation indicators: general control evaluation indicators. Through empirical analysis, this paper mainly discusses the relationship between company management formation and the validity of internal control. The objective of is to measure the degree of implementation of policies by listed companies. Xianzhi Zhang and Wentao Dai(2011) are divided into three parts: the internal control's assessment of the enterprise, the writer report of the external CPA(Certified Public Accountant), and the comprehensive evaluation of the company by the government regulatory authorities through the announce about internal information of the company. As an evaluation indicator, Determining the weight of index by AHP are used to construct multi-layer fuzzy comprehensive evaluation method for effectiveness evaluation of internal control. Dibo of Shenzhen issued the "Dibo's Internal Control Index for Listed Companies in China". Wang Hong and others used the fundamental framework of internal control as the institutional fundament, and designed the underlying internal control index on the basis of the five major standards of inner control policy, operation, reporter, compliance, and asset safety. The main inner control defects are taken as the correction index, and the basic internal control quota is supplemented and corrected.

**Influence of Board Characteristics on the Effectiveness of Internal Control**

Board size and inner control effectiveness: Board of directors scale is adverse to the worth of listed companies concave curve relationship, listed companies which has the smaller board of directors scale can gain a bigger value on the market, and the company value as the board of directors from small to midsize changes its loss to maximum. Some researchers think that the larger the board size, the more professional knowledge and work experience of board members, will strengthen the degree of supervision of the company, facilitate the improvement of company outstanding achievement, and the scale of the board of directors is affecting internal control. However, some people hold different opinions. They believe that the larger the board, the more prone to financial fraud. Therefore, the larger the board of directors, the more prone the company is to financial fraud and financial risks. The relatively low productiveness of the large-scale board further reduces the ability to monitor the company's legal compliance operations. Guizhen Meng(2013) believes that the scale of the board should be controlled within a reasonable range. Larger scale is prone to inefficiency, higher costs, and smaller scale is prone to lack of professionalism, which affects the act on the board. However, the smaller measurement of the control activities can easily influence the of internal control's effectiveness due to the professionalism and lack of experience of board members.
Board independence and internal control effectiveness: Independent directors are conducive to strengthening the supervision of the management level, and can effectively solve the problem of "internal control" of the company, thus promoting the effective operation of inner control. Independent directors also can make a significant effect in corporate governance. Compared with internal directors, external directors tend to make a fair and objective assess about company decisions and decrease company risks. At the same time, the greater the independence of companies with a high ratio of external board members, the more they can prevent management from controlling the board, the easier it is to terminate work contracts when senior managers have problems, and the better the performance level of the company. Harris & Raviv(2008): Model tests determine the distribution of board rights between internal and external directors, and their advice is that when oversight costs are low and management private interests have reached a threshold that may jeopardize shareholder rights, The board members should raise the proportion of external members in time to prevent the manager from harming the interests of shareholders and satisfying his desires. When researching the relevance between the ratio of board members and the return on net profit, Dongzhi Yu (2003) selected 91 public establishments in 1999-2000 cite a research instance and found that the two were simply linear related relationships. Instead, it presents a significant "U" relationship, while pointing out that the composition of the board members does not influence the level of of the company's performance, whether it is an external director or an internal director. Board independence has a definite relationship with the performance of company, but it must have certain conditions, that is, when the fairness concentration and the scale of independent board members react, there is a positive connection between the ratio of external board members and the performance of company, and when the ratio of liabilities and the ratio of independent directors react. There is a negative correlation between board independence and company performance.

The effectiveness of the chairman and general manager's two positions and inner control: The separation of the chairman and the two positions can effectively reduce agency costs, form a good restriction within the company, and reduce the one-sidedness of information. The combination of the chairman and general manager will affect the independence of the board of directors. General manager will determine the personnel of the independent director and may harm the company's interests. In the study of Chinese companies, it was found that chairman hold a concurrent post with general manager can effectively increase the sales volume of the company and study the relationship between the chairman hold a concurrent post with general manager and the performance of company. The results of empirical data indicate that there is no correlation between the combination of the two positions and the changes in the return on equity and the stock price, but it is negatively related to the return on investment. For corporate performance, Only the chairman hold a concurrent post with general manager in a particular industry will be significant positive correlated to company achievement. Statistical analysis of the equity structure, board size, supervisory board size, capital composition, and company achievement of public companies in China shows that the major reasons for the different positions of chairman and general manager are the different ownership structure. Among public companies controlled by state-run shares, chairman hold a concurrent post with general manager is preferred, which can significantly increase the achievement of the company. Rizhi Yang(2017) believes that although the chairman of the board of directors has reduced the internal transaction costs of the board of directors and managers, but at the same time, the level of oversight functions of the board members has declined, and the contradiction between shareholders and management's different value orientations still exists. When the number of part-time directors in the two positions is greater, the board of directors is more easily manipulated by major shareholders. The more serious that major shareholders infringe the interests of small shareholders, the more likely internal control is to be a problem.

The frequency of board meetings and the effectiveness of internal control: If the board meetings are formal and less involve substantive issues of the firm, the grow in the number of meetings will increase the cost of the firm; The reason why the frequency of board meetings is "negatively related" to the company's current achievement is not that the high number of board meetings has led
to low performance, but that the board meeting that exists as a "fire extinguisher" is a passive behavior. The biggest limitation on the frequency of board meetings is the time. External directors and internal directors have different needs for the number of board meetings based on different starting points. In their study, they found that for the sake of guarantee the quality of the meeting, external directors generally want to have enough time for meeting preparation and on-site discussions. Therefore, they expect to hold meetings every year for two days each time and at least once every two months. Yifeng Chen (2009) found that the high number of board meetings for the study sample of state-owned listed companies does not mean that the company's performance has improved, because the listed companies in China will only hold frequent board meetings when the company's performance has declined. This is a passive behavior, not an active one. Therefore, he believes that there is an important negative relationship between the number of board meetings and the value of the company.

Board shareholdings and compensation and internal control effectiveness: Equity incentives can bring the attraction of management and shareholders into line to a certain extent, and promote management to actively put forward good decision-making suggestions for the development of the company. Higher management shareholdings have improved the robustness of the company's surplus. Bin Liu (2012) used the listed companies in Shenzhen as an empirical sample to explore the influences of ownership structure and board remuneration and internal control efficiency. It is research finding that the degree of equity concentration and the degree of equity balance have a positive influence on the effectiveness of internal control within a certain reasonable range. According to the difference between state-run enterprises and non-state-run enterprises, the positive correlation between ownership concentration and equity balance control in non-state-run establishment is more significant; Compensation and equity incentives in state-owned enterprises will have a positive influence on the effectiveness of inner control. The improvement of board ownership will also help enhance the effectiveness of inner control.

Board members' personal characteristics and inner control effectiveness: Research from the perspective of the age of the manager shows that older and experienced managers always put financial security and the stability of their own work first. They pursue stability and do not like adventure. Is a typical risk evader; Younger managers are more willing to accept challenges, including major changes to the company's strategy. When the internal and external environment changes, they will generally take the initiative to meet opportunities and challenges, and they will be able to seize strategic advantages and seize strategic opportunities. Although it sometimes ends in failure, young managers are generally risk buffs. Li Liang (2016), an empirical study of 722 public companies in Shenzhen and Shanghai, found that the trend of younger board members and the role of younger members in the board is becoming more and more obvious. The age characteristics of board members have a certain influence on the performance of the board. They believe that despite the older board of directors have rich work experience, due to their age, their enthusiasm for work is declining and their energy is clearly insufficient, while young board of directors are more prone to perform supervisory and management functions. Actively invest in the operation of the enterprise to find out the problem in time to solve the problem. The findings of Bei Wang (2016) are different. In an empirical study of the relevance between the personal peculiarity of board members and company achievement of 121 listed companies in the Northeast, they found that the older the board members are, the higher the average age of the board or the proportion of experienced directors over the age of 50, the better the performance indicator.

Summary

On the basis of the research of "the impact of board of directors on the effectiveness of internal control", the influence of different characteristics of board members on the effectiveness of inner control is further discussed through the use of existing research methods and results. The board of directors has a very important role in the internal control of the company. On the one hand, the board of directors is the representative of shareholders' interests. The board of directors protects the legitimate shareholders' equity and embodies the will of shareholders. On the other hand, the board
of directors decides on the company's major policies, monitors the company's strategy, and shoulders the responsibility of selecting, evaluating, evaluating, and motivating managers. This is an important guarantee for deepening reform, strengthening management, and improving efficiency within the company. Whether or not the board of directors has been fully utilized plays a decisive role in the effectiveness of corporate governance. It is also an important criterion to test the success of modern corporate system construction.

References


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