

Research on Self-evaluation of Internal Control of Listed Companies on GEM

Renzao Lin

Fuzhou University of International Studies and Trade
Fuzhou, China 350202

Abstract—Internal control system is the essential determinant of the sustainable and healthy development of enterprises. With the unceasing speeding up of economic development in China, the market competition pressure of enterprises gradually increases and listed companies are facing with many challenges in the both domestic and foreign markets. For listed company, it is necessary to establish and perfect an internal control system in the enterprise in order to improve its core competitiveness and market share. Taking the internal control self-evaluation system of listed companies on GEM as the research object, this paper analyzes the current status of self-evaluation, summarizes the existing problems and further puts forward countermeasures for listed companies on GEM to perfect their self-evaluation system so as to improve their core competitiveness.

Keywords—listed companies on GEM; internal control; self-evaluation; countermeasure

I. INTRODUCTION

Since the issue of the SOX legal provisions in the United States and up to the issue of the "Guidelines for Self-evaluation of Internal Control of Enterprises" in China in 2010, the self-evaluation system for internal control of Chinese enterprises has become a hot spot for corporate research [1]. The academic and economic circles have never interrupted the researches on the internal control self-evaluation system of enterprise. Wherein, Dai Yan (2010) once pointed out that the enterprise internal control self-evaluation system provides a "comprehensive" and "all-round" evaluation function for enterprise evaluation. Therefore, it is available to make an overall assessment and comparison between different enterprises and further continuously extend the practicality of internal control self-evaluation. Taking the internal control self-evaluation system of listed companies on GEM as the object of research; this paper analyzes the current status of self-evaluation from the perspective of self-evaluation system and puts forward countermeasures.

II. CURRENT STATUS OF SELF-EVALUATION OF INTERNAL CONTROL OF LISTED COMPANIES ON GEM

In 2006, Shanghai Stock Exchange and Shenzhen Stock Exchange respectively issued the "Guidelines for Internal Control of Listed Companies in Shanghai Stock Exchange" and the "Guidelines for Internal Control of Listed

Companies in Shenzhen Stock Exchange" which was executed from Jul.1, 2006 and Jul.1, 2007 [2]. Those Guidelines specify that listed company must put forward recommendations on the internal control self-evaluation system and disclose it together with the annual report of the enterprise to show their responsibility to the public. However, it is not compulsory for Chinese listed companies on GEM to disclose internal control self-evaluation system information to the public. The specific data is as shown in "Table I":

TABLE I. STATISTICS OF INTERNAL CONTROL SELF-EVALUATION DISCLOSURE OF CHINESE LISTED COMPANIES ON GEM

Year	Companies disclosed Internal control self-evaluation information to the public		Companies failing to disclose Internal control self-evaluation information to the public		Total
	Qty	Proportion	Qty	Proportion	
2013	192	54%	163	46%	355
2014	284	67.4%	137	32.6%	421
2015	301	62.2%	183	37.8%	484
2016	376	70.14%	160	29.86%	536
2017	503	72.89%	187	27.11%	690

^a. Data source: Collected and sorted out by the author.

As can be seen from "Table I", the quantity of such companies listed on GEM as disclosing their internal control self-evaluation information to the public only accounts for 54% in 2013, but in 2014 and 2015 the proportion shows an upward trend and in 2016 that proportion reaches 70.14%. This indicates that more and more Chinese enterprises are aware of the truthfulness of the self-evaluation content disclosed to the public and more and more Chinese enterprises are willing to get their internal control self-evaluation information disclosed to the public. In 2017, the quantity of such companies listed on GEM as disclosing their internal control self-evaluation information to the public accounts for 72.89%, showing a good upward trend.

III. COMPANIES LISTED ON GEM HAVE PROBLEMS IN INTERNAL CONTROL SELF-EVALUATION

Although the enthusiasm of Chinese companies listed on GEM for disclosing their self-evaluation information to the public has increased, the authenticity and reliability of information disclosure by them need to be improved [3] and there are some problems in the process of disclosing such information to the public. For example, the management of company ignores self evaluation; the disclosure of self-

evaluation information is not under that effective supervision and control; self-evaluation information disclosure format is not standardized; the confidence level of self-evaluation information is not that high; and there is not a perfect regulation and rules for self-evaluation information.

A. The Management of the Company Ignores Self-evaluation

First, some management of listed companies ignores the internal control self-evaluation work, some believe that their self-evaluation mechanism is very perfect; some think that their self-evaluation has very tiny effect on internal control work and it is not useful to conduct self-evaluation on internal control [4]. Secondly, the auditing departments and auditors of some listed companies are less independent. Although the company has set up an audit department, there are fewer relevant auditors and the professional quality of auditors needs to be improved. Most of the evaluation on internal control is often a formality and lack of practical supervision.

Second, auditors in Chinese enterprises lack a certain spirit of innovation. In the process of audit, what internal auditors generally do after finding out problems is to deal with it in accordance with corresponding regulations and rules of the enterprise and few of them may analyze and summarize the cause of the problem. They lack certain spirit of innovation. What they often do is only to summarize their experiences and few of them may try to find out the regularity in the problems.

B. The Disclosure of Self-evaluation Information Is Not Under That Effective Supervision and Control

First, companies listed on GEM have limited supervision extent over the self-evaluation information of the internal control system and lack an effective internal accountability mechanism. According to the "Basic Management Regulation for Internal Control of Enterprises", "With respect to accidents that have been verified and cause major defects, enterprise shall promptly take remedial measures, minimize the risk and investigate the responsibility of the responsible person." [5]. However, this Regulation is not aimed at the accountability for the listed company's internal control system and the internal evaluation system of the enterprise is lack of accountability for the results of performance evaluation and the accountability for the result and quality of corresponding work completed. Therefore, it can be seen that companies listed on GEM are lack of a mechanism for investigating the responsibility for internal control evaluation.

Second, for the time being, the departments responsible for supervising the information externally disclosed by Chinese enterprises mainly include China Securities Regulatory Commission, China Banking Regulatory Commission and self-regulatory organization of the industry and so on. These institutions have also introduced a number of policies to put into practice the supervision on listed companies. Although the regulatory authorities have executed an all-round regulatory system on listed companies,

their supervision contents are the same to a large extent. Moreover due to the restricted communication channel among various regulatory authorities, their supervision responsibilities are not clearly divided so that it is easy to cause supervision blind area and further reduce their supervision efficiencies.

C. Self-evaluation Information Disclosure Format Is Not Standardized

Although at present Shenzhen Stock Exchange and Shanghai Stock Exchange encourage enterprises to make self-evaluation reports, they don't have a specified format for external disclosure of self-evaluation information but only explain the disclosure content. Shenzhen Stock Exchange and Shanghai Stock Exchange stipulate that enterprise shall determine the method, time, content and scope of external disclosure according to its own business object and the specific industry. Due to lacking a unified format for external disclosure of information, the content of self-evaluation information disclosed by Chinese companies varies. Over research, it is found that the self-evaluation reports disclosed by listed companies in China mainly have the following two types: the first type is an overview of the internal control activities, namely a brief introduction of the mode of internal control activities conducted in the company, further explaining the internal control activities and pointing out the problems existing in internal control activities conducted in listed companies and finally making an overall comment on the internal control activities of the company. The second type is similar to the first one, but its internal control activities are not described on the basis of the conduction status of key businesses but are described in five elements of internal control activities. That is, if there is internal control problem in the listed company, the report will make explanation on it; otherwise, the report will directly summarize. All in all, it is lacking a standard for the entire format.

D. The Confidence Level of Self-evaluation Information Is Not That High

This problem is mainly reflected in the insufficient disclosure of accounting information, namely the omission of key indices or key financial data in accounting information. This problem mainly includes the fact that the disclosed financial information or the shown event or financial data is incomplete. According to incomplete statistics and the appointment time of annual report of listed companies in China from 2015 to 2016, it is indicated that a total of 1,050 listed companies announced the appointment time of annual report in the year, but only more than more than 100 companies (only accounting for 10%) published annual reports in the first quarter. However according to later statistical data, it is indicated that 40%~50% enterprises in China choose to publish their enterprise annual reports in May of the next year and more prefer to disclosing annual report of the last year in latter time. With respect to the self-evaluation information disclosed by listed companies in China, there is much information about internal control of the enterprise, there are dozens of notes on the disclosed information statement, but explanation on accounting policy

is still the key point on major accounting information disclosure. The information disclosed in aspect of profit statement is to be perfected. At the same time, the information disclosed by listed companies in terms of risk management and social responsibility also needs to be improved.

E. There Is Not a Perfect Regulation and Rules for Self-evaluation Information

With respect to internal control self-evaluation information of enterprise, there is no perfect laws and regulations related. Firstly, although Chinese law specifies the disclosure of internal control self-evaluation information of listed companies, it does not stipulate the key points of external disclosure information. The contents of information disclosed by Chinese listed companies mainly focus on more than ten items of content such as internal environment, corporate governance, risk analysis, fund management, financial analysis and so on. But there are many items of content on self-evaluation and many enterprises' internal control evaluation haven't been specified to specific analysis content so that the self-evaluation on internal control of Chinese enterprise is cumbersome and complex [6]. At the same time, the internal control system of Chinese listed companies actively matches with the business object, business environment and risk structure and so on of listed companies and changes with the change of market environment. However from view of the current execution status, the internal control self-evaluation system in China can hardly adapt to the development demand of listed companies due to the imperfect relevant laws and regulations.

IV. PERFECTING THE SELF-EVALUATION ON INTERNAL CONTROL OF LISTED COMPANIES ON GEM

A. Strengthening the Attention of Listed Company Managers to Self-evaluation Work

1) *The management needs to establish a management concept of internal control:* Creating a good internal supervision environment: first, it is necessary to establish a value concept jointly recognized by listed companies, vigorously promote the corporate culture and promote the employees of listed companies to constrain their behaviors, so as to better implement the internal control system. In addition, it is also necessary to clarify the responsibilities of each department of listed companies, refine it to each staff member, implement the post responsibility system and clearly define the control responsibility of each person. In the increasingly fierce market competition environment, customers are the most important, and customers are the cornerstone for surviving and development of an enterprise. Therefore, listed companies must adhere to the customer-centered principle, actively provide service and gradually make strategic goals suitable for the development in the market environment.

2) *Increasing the cost input in internal control self-evaluation:* Increasing investment in internal control

construction: The premise of internal control is that there is sufficient investment, especially in human resources, financial resources and material resources. In terms of human resources, it is not only necessary to have a high-level leading group but also needs talents with strong professional knowledge to guide the auditing work; in terms of financial resources, it is necessary to ensure providing sufficient funds for the internal control self-evaluation team; in terms of material resources, it is necessary to get various assets under good management and improve the use efficiency of assets.

B. Enhancing the Ability of Legal Restriction and Strengthening the Authenticity of Self-evaluation Information Disclosed

In order to enhance the self-evaluation information disclosure behavior of listed companies, China should enhance supervising and restricting the internal control self-evaluation by virtue of legislation. Especially for the behavior of partial listed companies deliberately reporting false accounting information, it is necessary to enlarge criminal punishment extent on them. At the same time, it is also necessary to constantly improve the supervision and litigation mechanism for listed companies, establish and perfect an accountability system for noncompliance of self-evaluation information disclosure of listed companies, enhance leaders' consciousness of responsibility and investigate the civil responsibility of relevant responsible person involved in deliberately reporting false self-evaluation information. Therefore, relevant laws and regulations can be amended to give the CSRC certain enforcement powers such as the right to inquire and freeze related accounts, so as to reduce the information lag caused by cumbersome formalities. Meanwhile, China's financial department can issue corresponding standards to require listed companies to disclose self-evaluation information, strengthen the law enforcement extent, and enhance the authenticity of self-evaluation information disclosed.

C. Specifying and Unifying the Standard for Disclosure of Self-evaluation Information

The China Securities Regulatory Commission and the financial department of China should specify the content and manner of information disclosure of listed companies, gradually standardize and unify the standard for disclosure of self-evaluation information, constantly improve the existing internal control self-evaluation system of listed companies, and improve the authenticity and transparency of their information disclosed [7]. Listed companies should strengthen self-supervision on external disclosure of internal rating methods, risk asset measurement methods, internal asset composition, and risk management systems and so on. Chinese listed companies on GEM should unify their self-evaluation information disclosure standards as soon as possible and integrate it with the international standard to build a listed company self-evaluation information disclosure system with Chinese characteristics.

D. Improving the Confidence Level of Self-evaluation Information of an Enterprise

1) *Increasing the transparency of self-evaluation information of listed companies:* At present, the self-evaluation system of listed companies in China has deficiencies in rating method and database construction, which needs to be further perfected. The main points to be concerned include: first, learn from foreign mature experience and introduce its self-evaluation content and technology; second, establish and perfect basic database for self-evaluation; third, focus on the combination of quantitative analysis and qualitative evaluation; fourth, improve the organizational structure that matches the internal self-evaluation system; fifth, listed companies should perfect the audit department's responsibilities, broaden the audit team, and set up committee of experts to supervises various aspects such as engineering, contracts, materials, etc., and discloses self-evaluation reports on this basis.

2) *Timely disclosing self-evaluation result:* After finishing the self-evaluation report, listed company needs to timely disclose the evaluation results so as to warn other projects. The important issues found in the audit can be sorted out and form case and then organize all employees to learn from it so as to improve the risk prevention awareness of all employees and further enhance the internal control system of an enterprise.

E. Improving the Legal System of Internal Control Self-evaluation System of a Company

First, The Securities Law was revised in 2013. It is suggested to create a special seal for information disclosure of listed companies so as to improve the legal role of internal control information disclosure.

Second, the "Basic Standard for Internal Control of Enterprises" and supporting guidelines can require all listed companies to engage CPAs to audit the internal control and issue audit comment and specify the disclosure content and format of internal control self-evaluation information. At the same time, it is also necessary to further follow up the relevant regulatory mechanism, investor protection mechanism and strict violation responsibility mechanism and gradually expand the scope of implementation of the "Basic Standard for Internal Control of Enterprises".

V. CONCLUSION

In this paper, by analyzing the internal control self-evaluation activities of companies listed on GEM, it is found that there are many problems in the self-evaluation section and such problems are mainly reflected in the ignored self-evaluation work of the management of enterprise, non-compliance disclosure, weak supervision on such information disclosure and lacking of feasibility and relevant laws and regulations. After that analysis, this paper further puts forward countermeasures to solve the problem, expecting to provide reference for relevant enterprises through the researches in this paper.

REFERENCES

- [1] Wang Panfeng. Research on Self-evaluation Report of Internal Control of Agricultural Listed Companies [D]. Shandong Agricultural University. 2013. (in Chinese)
- [2] Song Weiwei. Internal Control Theory and Practice [M]. Beijing Jiaotong University Press. 2013. (in Chinese)
- [3] Wang Kun. Research on Social Responsibility Information Disclosure System of Companies Listed on GEM [D]. Yunnan University of Finance and Economics. 2014. (in Chinese)
- [4] Wang Zhiyuan. A Brief Discussion on Self-evaluation of Internal Control of Enterprises [J]. Modern Business. 2011 (29): 123. (in Chinese)
- [5] Wang Xiuguo, Zhao Qingtao. On the Defects in Internal Control of Enterprise [J]. Contemporary Economics. 2012(13): 50-51. (in Chinese)
- [6] Zhang Kun. Problems Existing in Internal Control Self-evaluation of Enterprises and Analysis on the Causes [J]. Industrial Science Tribune. 2012(08): 228-229. (in Chinese)
- [7] Wei Wei. Overview of Internal Control Information Disclosure of Listed Companies and Exploration of Countermeasures for Improvement [J]. China Chief Financial Officer. 2016(9): 115-117. (in Chinese)