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THE INFLUENCE OF INTERNAL CONTROL AND RISK MANAGEMENT SYSTEMS ON INFORMATION TRANSPARENCY AND BUSINESS SUSTAINABILITY

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Abstract:
Corporate governance continues to be an issue of great interest to both researchers and practitioners, as a result of the ongoing challenges to which companies have to answer for. The economic context and the current pandemic, but also the need for development bring new requirements to governance, imposing a rethinking of the strategy, as well as of the business processes. The internal audit function to which the necessary resources have been allocated can and must provide reasonable assurance as to the achievement of the objectives and provide a range of solutions to the problems identified. The motivation that determined the authors to approach this internal audit function was the topicality and importance given to the internal audit in the current period. Because of the analysis, it appears that, although a number of changes have been made to the internal audit function essential pylon in corporate governance recently, the role and importance of this function within the entities will change as a result of the digitalization of the profession.

Keywords: corporate governance, internal audit, internal control, risk management

JEL classification: G38, G41

INTRODUCTION

The realities of recent years have made risk management (CRM) very important in companies due to various factors such as technological development, globalization, rapid change, increasing competition, information technology, deregulation, global scandals, supranational companies, corporate governance. The literature abounds in scientific materials that address the role of internal control systems, risk management, internal audit, and their role for effective corporate governance and also focuses on many factors that influence it.

According to Arthur Hald (1944), "no big deal can avoid internal audit. If so far, the big organizations have not adopted the internal audit, they will do so sooner or later, but if the events are going to take place as they did until now, they will certainly do so sooner. Under such circumstances, a flexible approach towards risk management in the decision-making processes is indicated, providing solutions even for situations that are unlikely to happen.

All the tools we use today in risk management and decision analysis, from the strict reasoning of game theory to the challenges of chaos theory, have their origin in the discoveries that took place between 1654 and 1760, except for two cases:

- in 1875, Francis Galton, amateur mathematician and primary cousin of Charles Darwin, discovered linear regression, thus explaining why pride foretells and why there is no evil without good. When we make a decision based on the idea that things will return to normal, we apply the notion of linear regression. Regression, he wrote, is "the tendency of the average ideal filial type to move away from the parental type, returning to what we might call in general terms, but also objective, the average ancestral type."
- in 1952, Nobel Laureate in Economics Harry Markowitz, then a young doctoral student at the University of Chicago, demonstrated mathematically why choosing to bet everything on one book is a particularly risky strategy and why diversification is one of the tools more convenient for an investor.

There are often tense discussions between those who believe that the best decisions are made based on numerical calculations, based on patterns of past events and those who base their decisions on more subjective degrees of confidence about the uncertain future. This is a controversy that has never been resolved. The issue boils down to everyone's vision of the extent to which the past conditions the future (Boghean F., 2014)

Internal audit helps an organization to meet its objectives by imposing a systematic, disciplined approach to the process of evaluating and increasing efficiency in the processes of risk management, control and corporate governance"(IIA, 2021). The role of internal audit is (a) to provide estimates that provide assurance on the correct design and efficient functioning of governance structures and processes; and (b) to provide advice on potential improvements in governance structures and processes (Țurlea, E. si Mocanu, M., 2016). For a long time, internal audit was seen as a support activity for external audit.

DEFINING OBJECTIVES AND RESEARCH METHODOLOGY

The research approach was based primarily on a qualitative analysis of the legislative and economic environment in EU countries. This research is theoretical, but also empirical, addressing aspects of risk management, internal control systems and their role for effective corporate governance. The paper reviews the literature on the current state of knowledge regarding governance principles, which addresses issues related to transparency, financial reporting, internal control and risk management.

We aim to emphasize the importance of the connection between corporate governance and audit. In order to benefit from opportune results and conclusions in the research activity specific to the economic field, we must analyze most unnecessarily facts, economic events, figures and statistical data.

RISK MANAGEMENT SYSTEMS ASSESSMENT

Adopting risk management in companies is a strategy to thrive, a way to avoid spectacular bankruptcies, financial crises and considerable differences between compensation for directors and company performance, benefiting companies by attracting new investors, increasing economic performance, competitiveness in the long run, through a better management of the company's risks and last but not least through the company's advertising. (Boghean F., 2019)

Audit professionals provide reasonable assurance about the reliability and relevance of information in an organization as well as internal control. In an environment full of change, fierce competition, new forms of organization, improved information technology, measures taken by regulators on the current situation and the recent past are relatively less important, while information and measures that can be implemented in the future In general, there is a shift in focus from the internal audit function to threats to strategies. In the current environmental conditions, some questions arise for the management team (Boghean F., 2014):

- Digitization may lead to increased operational risks• Can the entity's assets be stolen?
- Does the current internal control system provide appropriate measures and information on threats to assets, processes and objectives?
- Is the information in the reports to stakeholders in accordance with applicable standards, applicable laws and regulations?

This process refers to possible scenarios that could seriously threaten an organization and are part of the risk management process.

Another specific aspect is related to the factors that generate the risks that can change quickly and these changes must be identified before they materialize. Third, threats cannot be fully assessed even after the passage of time, as some do not materialize and others occur but are prevented or mitigated by the mechanisms of the internal control system.

THE ROLE OF CORPORATE GOVERNANCE IN ENSURING INFORMATION TRANSPARENCY

Shleifer & Vishny (1996) highlight the financial aspects of corporate governance in their work and define "corporate governance as how a company's fund providers ensure that they receive the benefits due to their investment." Hofstetter (2002) defines "corporate governance as the totality of organizational, structural issues of the entity that directly or indirectly protect shareholders. Simultaneously corporate governance is concerned with organizational and control issues of the management" (Shleifer A., Vishny R. W.,1996).

Corporate governance* is a concept that includes the following elements:

- the responsibility of the managers regarding the quality of the information from the financial reports, the way of organizing the financial accounting activity;
- the existence of very tight deadlines for financial reporting;
- full communication and transparency regarding financial results;
- transparency of internal audit, processes and external audit.

Such approaches to risk management as a component of corporate governance have not always been well implemented, or well received. The Long-Term Capital Management Hedge Fund included two Nobel laureates, who, after accumulating a large amount of capital, continued to lose more than $ 4 billion over several months following the 1998 financial crisis in Russia (Lowenstein, R., 2000). In this example, it was necessary for the Federal Reserve to intervene in order to get out of its investments. Excessive and abusive use of such complex financial instruments has been at the root of the 2008 global financial crisis and financial crises in general (Patterson, S., 2011). In fact, some hedge fund managers have benefited greatly from exploiting such situations (Lewis, M., 2008). In a series of scientific papers on the 2008 financial crisis, Lewis explains that the nationwide unrelated housing price assumption has allowed diversified low-quality individual mortgage combinations to be sold at a higher quality due to orders, payment priority and diversification. between several mortgages. By investing, many managers have managed to take advantage of the crisis (Zuckerman, G., 2009).

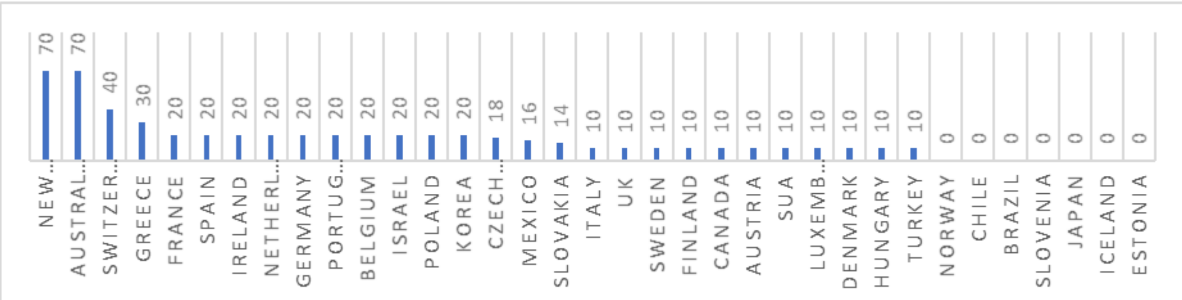

Figure 1. The share of companies that have implemented an efficient risk management, 2017

Source: author own processing according to OECD datas

The results of the study presented above provide a clear picture for stakeholders seeking to reward risk management practices in their investments. a problem has already occurred. Because it usually appeals to risk management when perceiving problem solving through little effort, an investigation of the deeper analysis of how much time and effort involves solving problems that can be justified, as we can see in Figure 2 and Figure 3. How to do this could be a fair cost-benefit ratio for efforts to identify solutions to problems in the typical scenarios the company faces.

* In practice, the concept of corporate governance needs to be seen as a process in which the organization is involved as a whole and refers to all the internal components that work together and which will eventually be integrated into a single recognized management structure.

Figure 2. Poor governance has led to reducing or giving up holding shares in a company.

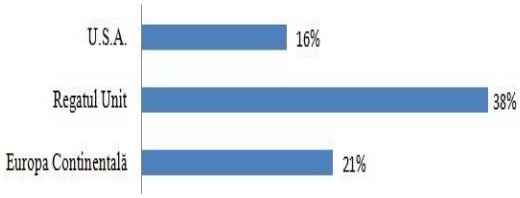

Figure 3. Existence of measures to evaluate the governance practice in companies

Source: author own processing

Actors involved in corporate governance should try to encourage the implementation of risk management policies in their companies. These policies should be geared towards external and internal risk-generating factors, towards the creation of scenarios that may affect the likelihood of achieving the objectives set by the owners. Therefore, policies need to focus on the process rather than the results. Managers should not be remunerated for their short-term profit, but should be rewarded for their sustainable performance as a result of rigorous risk management.

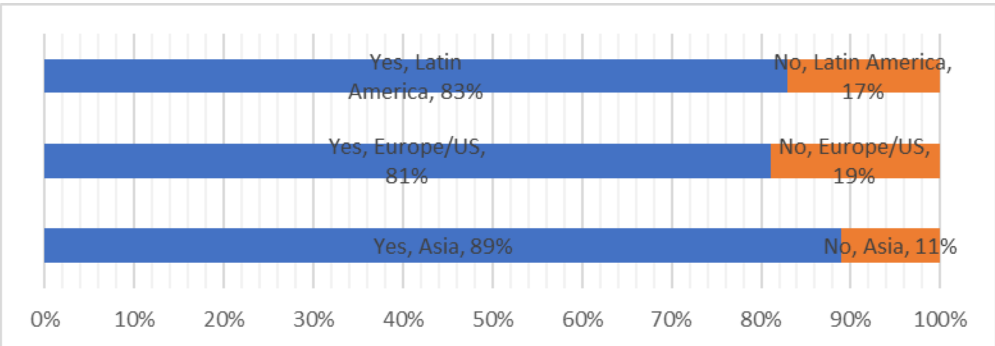

Figure 4. Share of investors willing to pay more for an entity with effective co-operative governance

Source: author own processing

In the presence of too strong an information asymmetry between banks and investors, financial markets cannot develop. In fact, the question may be asked how a minimum of security will be provided to investors without guaranteeing them that the information is sufficiently reliable. In the US, the regulatory environment has fostered the development of markets, forcing companies to disclose more information compared to Japanese or German companies as we can notice in Figure 4. In fact, in the United States, investors are accustomed to treating the most diverse information, especially those from small and medium-sized enterprises or developing companies, which can be seen in the chart above.

Issuers of corporate governance codes are different from country to country. Among them we meet: stock exchanges, real estate commissions, government entities, institutional investors, business associations, shareholders' rights protection associations, etc.

The way companies are run and the efficiency influence a country's economy. Due to the process of globalization, corporate governance is a factor in this phenomenon of generalization of good practices. The debates on corporate governance intensified especially during the 1990s, first in the Anglo-Saxon countries and then in continental Europe, eventually expanding worldwide. The interest shown in the study of governance at the corporate level was focused on the analysis of the power of managers and on the limits of its exercise. The creation of corporate governance codes emerged as a reaction to the economic crisis, at a time when shareholder confidence was suffering (Boghean F., 2016)

CONCLUSIONS AND PROPOSALS

Corporate governance or corporate governance is an area of economics that investigates how to motivate and ensure the efficient management of enterprises. This complex system involves:

- *a set of formal or informal rules that establish certain relationships between the executive management of a company, the board of directors and the shareholders of that company, as well as with other persons or interest groups that have links with the company;*
- *the mechanisms by which the company's objectives are set and the means to achieve these objectives and to monitor performance are established;*
- *the incentive system used to make the directors and executive management of a company pursue those objectives that are in the interest of shareholders and to facilitate their monitoring, encouraging a more efficient use of resources.*

Management is responsible for the preparation and integrity of the financial and operational statements of the organization, all related information and publications that appear or should appear in public reports or sent to regulators.

To ensure the credibility of financial and operational reports and the effectiveness of risk management, management is responsible for establishing and maintaining an effective system of internal controls designed to provide reasonable assurance about the achievement of the following objectives:

- credibility of financial and operational reporting;
- asset security;
- compliance with laws and regulations;
- effectiveness and efficiency of operations;
- achieving business objectives.

The current economic environment is constantly changing. We could say that change is the only certainty in the life of companies. All organizations are interested in increasing their performance. This is not possible if the internal audit department within them does not keep pace with the rapid development of economic entities. What does it mean to keep up? It means identifying potential risks, evolving processes and outcomes, changes in the external environment. There is a direct relationship between the sustainable performance of companies and the internal audit function, performance being the effect, and the internal audit function being one of the causes.

A good governance process requires more than a focus on compliance with laws and regulations. Good governance, which would stand the test of time, requires:

- establishing a culture based on appropriate business practices and ethics;
- strong emphasis on results management;
- ensuring that civil servants / management have adequate knowledge of how to manage risks;
- implementing an appropriate risk management and monitoring process.

Priority in the work of internal auditors remains risk assessment and internal control. Last but not least, the internal auditor must work with the audit committees and the external audit to identify the risks. Moreover, in recent times there has been an increasing emphasis on IT knowledge which involves a rigorous approach to IT risks by integrating them with business risks.

A company without corporate governance is like a state without democracy. You can't expect those who manage other people's money to be as careful and caring as they are, according to Adam Smith.

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