

Governance and Internal Control of the Small and Micro Enterprise

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Abstract. Whether the internal control system of small and micro enterprise is sound depends on the governance structure of enterprise. Small and micro enterprises are very active in the development of China's national economy, but the internal bottleneck that restricts the development of small and micro enterprises, which is corporate governance is not clear. This has caused many small and micro enterprises lack lasting vitality. This paper takes strengthening small and micro enterprise corporate governance and building internal control system as the theme to explore the issue of small and micro enterprise corporate governance and internal control system construction.

Corporate Governance and Its Internal Control Relationship

The Sarbanes-Oxley Act of the United States has made strict regulations on corporate governance and internal control. The general principle of the bill is to implement the reliability of financial reporting and the responsibility of internal control to the key figures who actually hold the power of the company, which breaks through the mechanical division of corporate governance and internal control, and strengthens the responsibility of the board of directors and executives. Corporate governance and internal control have the relationship as below:

Corporate Governance Structure is the Basis to Implement Internal Control in Enterprises. COSO is the most authoritative organization in the field of enterprise

risk management and research of internal control theory. The *Basic Rules for Internal Control of Enterprises* issued by the Ministry of Finance of China in 2008 adopted the elements and contents of the internal control framework issued by COSO. The COSO report, that is *Internal Control-Integrated Framework* proposes that Internal control is a process in which the board of directors, management and other personnel of the company provide reasonable assurance for achieving the reliability of financial reporting, the efficiency and effectiveness of business activities, and the compliance of relevant laws and regulations. This explanation is widely recognized by the board of directors, executives, investors, creditors, auditors, and other sectors of society, as well as experts and scholars. According to the COSO report, we can understand the internal control of the company as a kind of supervision and balance mechanism of the owner to the operators. That is, reasonably configuring the rights and responsibilities between the owner and the operator through an institutional arrangement. It is realized through the corporate governance structure and related mechanisms formed by the shareholders' meeting, the board of directors, the board of supervisors and the executives. From this level, it can be said that the internal control of enterprise is the corporate governance process, and a good corporate governance structure is the basis for effective internal control[1].

Effective Internal Control is Conducive to The Improvement of Corporate Governance Structure. Enterprise corporate governance is carried out on the premise of perfect corporate governance structure of legal entity, which forms a governance model characterized by common governance, and keep the balance between balance and efficiency. Internal control is a dynamic behavior that will be influenced by subjective factors and external environment during the operation of the enterprise. Building up a sound internal control system is an important part of improving the company's own construction. Establishing and improving the internal control system of enterprises requires the attention of enterprise owners first. The operating sense and financial management sense of the enterprise owners are the keys to the internal control of the enterprise. Enterprise owners should continuously improve their cultural quality and management level to ensure that the efficiency and effectiveness of business operations, the reliability of economic information and financial report, implement scientific management, and improve the overall management level of enterprises. The goal of corporate internal control is to comply with applicable laws and regulations. The object of internal control is the power manipulator of the enterprise. It's the power constraint on the power manipulator, and is the power

balance between the power manipulators as well[2]. It can be seen that an effective internal control system of an enterprise not only needs a good corporate governance environment, but also helps to improve the corporate governance structure of the enterprise.

Problems in the Governance Structure of Small and Micro Enterprises and the Internal Control

From the current situation of small and micro enterprises, the understanding of enterprise owners on corporate governance and the construction of internal control system is insufficient. In the eyes of enterprise owners, running an enterprise is for profit, as long as it can make money, corporate governance, internal control of the enterprise is dispensable. Therefore, the company has been ran with virus since the day it was opened. There are three prominent problems in the governance of small enterprises:

The Equity is Unclear, and Insider Control Replaces The Balance Relationship.

There are three cases in the distribution of equity in lots of small and micro enterprises. One is a registered shareholding, which is the public and legal. The second is the agency equity, the actual controller holds the equity in the name of agent. The third is that the hidden surname is not publicly held for some kind of forms. Due to the unclear equity, the embarrassing situation of the enterprise of the executives is that the management is quite difficult. Because of the unclear property rights of the enterprise, it is impossible to establish a corporate governance system that conforms to the actual situation of the enterprise in the specific operation process, so that the board of directors cannot make better decisions. Insider control takes the place of the board of directors, and top members of executives cannot effectively manage the company, and the internal control cannot get to the balance relationship[3].

Ignore Institutional Management and Replace it t with Personal Reasons.

Enterprise system construction has always been the weak link in small and micro enterprises. Due to the lack of a series of institutional norms, the internal control of enterprises is very weak, and the phenomenon of human factors replacing institutional norms is quite serious. For example, accounting staff's division of work is not clear, the accounting and financial systems are imperfect, the internal control is often out of control, and there is no effective supervision mechanism. The quality of financial

statements of most companies are very poor, and accounting statements have never been audited. For a long time, due to the imperfect internal control system, small enterprises have many irregular business operations and management in their business activities, which have resulted in a large amount of false accounting information.

The Interests of Small and Medium Shareholders Have Been Violated.

Shareholders are distinguished based on the amount of money they offered, that is, the number of shares they hold. In a company, the interests of small and medium shareholders are violated in two cases. One is from the executives. Since the substantial shareholder has the highest decision-making power of the company, he may deliberately violate the company's articles of association and refuse to pay dividends; Pay high compensation to the director or the high-ranking executives who are controlling shareholders unreasonably; Provide preferential loans to the controlling shareholder for guarantee with company's property; Hold back related information of enterprises to the small and medium shareholders and so on. On the other hand is the violation from the substantial shareholder. Since the substantial shareholder has the final decision-making power, they usually will abuse their voting rights; Substantial shareholders set unreasonable terms for small and medium shareholders to avoid them attend shareholders' meeting; Substantial shareholders will arbitrarily remove or obstruct small and medium shareholders as executives; Substantial shareholders will make arbitrary decisions and implement major issues of the company; Substantial shareholders will also increase their income and reduce their risks through connected transactions.

Optimize the Management of Small And Micro Enterprises and Countermeasures of Internal Control

The operating mechanism of an enterprise can be divided into two levels which are corporate governance and enterprise management. Corporate governance is the mechanism of enterprise operation. If the current corporate governance does not meet the requirements of the modern enterprise system, it will not achieve the governance model characterized by common governance, the coordination and efficiency, and the support for the implementation of modern enterprise management. Therefore, in order to fully play the role of internal control in the modern enterprise system, it is necessary to constantly improve and standardize the internal control system, start from the actual development needs of enterprise to establish a modern enterprise

operating mechanism that combines corporate governance and internal control and suitable for the development of small enterprises.

Standardize and Optimize Corporate Governance Structure. The normalization of the corporate governance structure is depend on whether the board can fully play its role. Good corporate governance helps the company to develop, enables the board to make better decisions, and senior management runs the company more effectively. More importantly, it can provide a good environment for the construction and implementation of the internal control system. So, should learn from the international corporate governance practices in corporate governance, and clearly define the rights, responsibilities, and interests of shareholders' meetings, boards of directors, and managers in light of the actual situation of the enterprise, so that organizations at all levels have different powers to ensure layer-by-layer control of the production and operation activities of the enterprise and the correct implementation of business decisions and business plans. Through effective restraint mechanisms to reduce or eliminate internal control and limit the behavior of rights holders through institutional and procedural restrictions.

Build A Multilevel Internal Control System. Internal control is enterprise risk management. Corporate internal control is a process that is influenced by corporate boards, executives and some other employees. Internal control is the foundation of risk management and is at the front end of the entire control system.

In accordance with the requirements of standardization, standardization and sequencing, the enterprise establishes a complete and operable internal control system that covers the economic business process and is probable for the characteristics of small enterprises, and carry out timely feedback and adjustment of information for the continuous revision and improvement of the internal control system with the change of external environment, the adjustment of unit business functions and the improvement of management requirements, and gradually form a dynamic and perfect internal control system. Clearly stipulate the scope, authority, procedures, responsibilities of the authorization and approval of each level and each kind of work. The executives at all levels in the enterprise must exercise its powers and take the responsibilities within the scope of authorization.

Strengthen Internal Audit and External Oversight Mechanism. As a part of the internal control system's supervisory review, internal audit evaluates and improves the effectiveness of risk management, internal control and governance processes through systematic and standardized methods to help organizations achieve goals. Internal

audit is an evaluation of internal control, risk management and corporate governance to ensure that the organization operates normally and does not deviate from the goals of enterprises. Audit is an post factum, which are post-action assessment, post-action control. Therefore, enterprises should set up internal audit institutions under the board of directors. Internal audit is directly responsible to the board of directors. Its main responsibilities are checking for fraud prevention, paying equal attention to supervision and service, and helping executives to conduct effective and comprehensive internal audit of the internal control system to supervise the effectiveness of procedures and implementation of internal controls and reduce the distortion of accounting information.

Conclusion

Enterprise is a combination of multiple contractual relationships. The principal-agent relationship between the shareholders' meeting and the board of directors, the board of directors and the manager's team is the most basic contractual relationship. The internal control of the enterprise should start from the construction of the corporate governance structure. Establishing and improving the corporate governance structure itself is internal control, and the essential function of the board of directors is internal control. To this end, except the above countermeasures, the author proposes three points of thinking as below:

Extend Corporate Legal Boundaries when Necessary. Studies have shown that problems in some enterprises are related to the failure of board functions and the proliferation of insider control. Due to the economic ties and contractual relationships between the enterprise and external stakeholders, internal control of the enterprise should extend beyond the legal boundaries of the enterprise if necessary, and it is necessary to incorporate supplier resources, customer credit and demand, and government regulation into the internal control system of the enterprise.

Treat the Relationship between Corporate Governance and Internal Control Dialectically. In view of the corporate governance and internal control from the balance of rights to the scientific decision-making, the interests of all parties in the enterprise are reflected in the enterprise entity. Only by rationalizing the rights and responsibilities of all parties can the effective operation of the enterprise be guaranteed. The premise of effective operation of enterprises is the scientific management of enterprises and the scientific internal control of enterprises. So, the

ultimate goal of corporate governance is to improve the modern management level of enterprises and ensure the sustainable development of enterprises. The purpose of internal control of enterprises is to ensure the continuous and orderly operation of various types of contractual relationships, so that they can make sure the enterprises can have good strategic goals and management team, and continue to develop and create value in accordance with the set purposes.

It's Important to Improve the Quality of Salesmen and the Level of Professional Ethics. The efficiency and effectiveness of any job will be influenced by the quality of business and professional ethics of decision makers and executors. People are the decisive factors of corporate governance and corporate management, especially the quality of corporate decision makers directly affects the survival and development of enterprises. The relatively poor quality of employees in small and micro enterprise is an unquestionable fact. Accountant plays an important role in the formulation and implementation of internal control system. Therefore, improving the professional quality of corporate accountants and strengthening their professional ethics education are the conditions for ensuring effective implementation of internal control.

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