Corporate Governance Role of Auditors

Introduction

Corporate Governance is usually looked upon as a process or system related to management of an entity. Similarly overlooked is the contribution of auditors to the corporate governance. The essay evaluates the corporate governance role of auditors. Initially it defines and illustrates the term corporate governance which is followed by a consideration of the different processes and others included in auditing, the work of auditors. It is succeeded by defining of the role that auditors play in the model of corporate governance. Finally the essay concludes on a conclusion on the issue considered.

Corporate Governance

Corporate Governance is normally defined to include the different processes and procedures which the corporations follow to direct and control their organizations. Xie, Davidson III and DaDalt provide that majorly the corporate governance is in the hands of board. (Xie, Davidson III and DaDalt, 2003) It is because corporate governance is the manner in which an organization operates. And since Board of directors is the highest authority in the whole entity, usually they decide alone or with the consult of top level management the manner in which entity would operate. This decision needs to be made on the basis of interests of several stakeholders. These stakeholders not only include internal stakeholders like management, employees, etc., but also the external stakeholders like shareholders, bondholders and others. Once they have considered all of them, they decide about the operations. On the basis of their decision, they direct the top management to further direct and control whole organization. Daily, Dalton and Cannella Jr. pronounce that one issue which is highly relevant to corporate governance is consideration of different stakeholders with intersecting and contradicting interests in one policy. (Daily, Dalton and Cannella Jr, 2003) Since many times, this contradictions are high the board or top management decides a middle policy. At other times they have to prefer one stakeholder on the other based on their personal bias and then on that basis define the organizational policy.

Auditors responsibility within the organization

There are two types of auditors; internal auditors and external auditors. While internal auditors are included in the employee list of the organization, external auditors are independent. Arens present that the operations of the entity are carried out with the oversight of these auditors. (Arens, 1999) However this is not their main responsibility within the organization. They are required to carry out an examination of financial statements and accounts to identify whether there is any misstatement in them. This initiates with them identifying the factors which can predict or indicate the existence of any misstatement. Follow up on those factors led them to carry out different processes like substantive audit procedures, analytical audit procedures and others to identify the actual existence or not of the misstatement. Bedard, Chi, Graham and Shanteau highlight that the efficiency of an auditor is related to whether he is able to identify the misstatements existing in the financials or not. (Bedard, Chi, Graham and Shanteau,

1993) This level of efficiency increases as the auditor gains experience is specified industry or field. This efficiency is required equally by both the kinds of auditors. Internal auditors require this efficiency to determine misstatement and bringing the same to management action so that the issue can be resolved at the earliest. Against them, the external auditors have to use this efficiency to determine misstatements to report in their audit report. Therefore though there goals are different the major responsibility of both types of auditors is same. Beside this major responsibility auditors have some additional duties which can change as per organizational policies and legal requirements. The Internal auditors may have to support the management in terms of issues as to how they can govern the organization to achieve organizational goals. The same work can also be extended to external auditor however this duty is at lower part for external auditors to not let this assistance impact their independence. Thus these together aggregate the auditor's responsibility within the organization.

Auditor in Corporate Governance Role

Though the auditor is not engaged in the work of management, but still he has the oversight of management. Also at times he is the one who supports management on different tasks. These roles together also lend the auditor a corporate governance role. Among the major corporate governance roles that an auditor may presume are included the following –

- Incorporation in the audit plan – Rossiter highlights that one method by which the auditor can presume corporate governance role is by incorporating the same into their audit plan. (Rossiter, 2011) Auditors get an insight of several acts being carried out in the organization this exposes them to several direction and control issues being handled by entity. This allows flow of information from auditors side to the entities in relation to different stakeholders whose interests might have been overlooked by management. This information sharing can led to better level of corporate governance by management. Ernst and Young in their publication give example of impact of incorporation of corporate governance in audit plan on the entity's corporate governance achievement. (Ernst and Young) They state that it results in achievement of corporate governance at the ultimate possible level.

- Accountability – The auditors while identifying material misstatements may encourage the management to determine accountability of issues. Keith writes that it may result in the management recognizing the importance of accountability and on same lines including it in their controlling process. (Keith, 2002) It can be reasonably considered to be substantially acceptable, because the board of directors at their own level for management also need to identify people behind every activity being carried out. An example of it is Volkswagen where due to lack of accountability establishment, corporate governance was defeated through a scam which negatively impacted several entities. Therefore the inclusion would not only benefit the other stakeholders but also allow the main authority, board of director to get benefitted in their task of management.
- Check on corporate governance aspects – Broadley presents that in any case the auditor doesn't owns a responsibility to ensure existence of efficient corporate governance. (Broadley, 2006) However, he can put a check on

different aspects on corporate governance. The reason that the author presents is that the auditor hold a social responsibility. An audit is carried out to ensure that the public, who is stakeholder in different names in the entity, gets a true and fair view about the operations of the organization through financial statements. Until the organization is considerate towards its stakeholders, it would be indifferent towards their interest and the employees or management would value their interests more. This can lead to inefficient corporate governance as well as chances of misstatements. Though the auditor merely has the responsibility to keep a check on misstatement, since non effective corporate governance can also lead to misstatement, they can keep a check of the same. However to be successful it is needed that there be a free open dialogue between management and auditor on the same.

- Internal Auditors contribution – Though external auditors can help the entities in ensuring effective corporate governance, the support that the internal auditors can provide is highly effective. Ojo presents that internal auditors have a grip over several issues within management. (Ojo, 2009) This earns them a respectful position which they can utilize in relation to corporate governance. They can identify the different interests of different stakeholders. Once they have recognized the same, they can help the management identify the same and also determine the possible steps in relation to corporate governance which can be effective when the interests contradict.
- Risk management – Risk management is one of the necessities to ensure effective corporate governance. The auditors can include a risk assessment

procedure within their audit procedure. Such a procedure would require the management to keep a check on issues which can result in increase in risk assessment made by auditor. Cohen highlights that the fear of being caught with any risk factor kept open due to the check kept by auditor can encourage the management to ensure risk management. (Cohen, 2002) And this fear to keep the risk under check can result in management taking up risk management procedures in their governance procedures. Therewith it would result in management being able to carry out one necessary corporate governance process.

If an analysis be made of the role of auditor in terms of corporate governance, it presents that the major role is related to the management fear in relation to audit reports. However in case the same is effective, it can lead to considerable achievement of entity in terms of effective corporate governance while giving the auditor a credit for the same.

Conclusion

Corporate governance is the responsibility of management. It includes directing and controlling the organization in such a manner that organizational objectives can be achieved. Since it is the board which directs the top management for effective operation, corporate governance is also managed by them. Besides, the auditors have the responsibility of examination of accounts for identifying any potential misstatements. The auditors this responsibility which allows them to list any unusual transaction or account in the audit report gives them the major role in relation to corporate governance. They can incorporate corporate governance in their audit plan and keep a check on corporate governance aspects in their audit. Also they can encourage the management to ensure accountability and manage risks. Finally the internal auditor can provide management support in their being able to manage effective corporate governance. In the above manner the auditors take on corporate governance role in the organization.

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