

Internal Control, Management Power and Accounting Information Quality: Based on Chimeric Perspective

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Abstract: This paper selects 3,673 a-share manufacturing companies listed in Shanghai and Shenzhen from 2016 to 2018 as the research objects for empirical analysis. Based on the empirical results, it is concluded that ICindex is positively correlated with disclosure of accounting information, while management Power is negatively correlated with disclosure of accounting information. To some extent, internal control can inhibit the manipulation of earnings by management. This conclusion provides reference for enterprises to improve the quality of accounting information, and also provides ideas for the government to formulate corresponding accounting laws and regulations, which has certain practical significance.

Keywords: Enterprise, Internal Control, Management Power, Accounting Information Quality.

1. Introduction

Accounting information reflects the financial situation of an enterprise, the efficiency of operation and the level of cash flow. It is the result of accounting work, and also an important reference for the decision of enterprise performance management and managers to organize production. The real and reliable quality of accounting information is the prerequisite and important guarantee of economic decision-making. High-quality accounting information can provide decision-makers with a variety of decision information, which is of great value to the development of enterprises.

In recent years, domestic and foreign accounting fraud cases occurred in succession, causing high vigilance of all sectors of society. The quality of accounting information is questioned by the public. Accounting fraud cases have caused serious adverse effects, sending wrong signals to managers and even relevant management departments to mislead managers to make wrong decisions; Destroy the seriousness of accounting laws and regulations, destroy the operating environment of market economy; Damage the interests of the owners, creditors, employees and customers of the enterprise and cause them to suffer heavy economic losses; The distortion of accounting information will damage the capital market that is developing and improving in our country, affect the investor's decision making, not conducive to enterprises to invest and finance, destroy the external environment that enterprises survive, cause enterprises to operate difficult, and seriously affect the social stability and harmony.

Through the investigation and research of accounting fraud, it is found that the management plays an important role in the process of enterprise operation. As the actual operator of the company's business and operation, the management plays an important role which can not be ignored in the internal activities of the company, such as controlling the surplus, exaggerating the profit, changing the accruals, etc., and manipulates the financial statements by accounting means to achieve the purpose that no one knows. Theoretically, the excessive concentration of power at the top of a company will reduce the quality of accounting information. As we know, the separation of management and ownership exists in modern enterprises. As the trustee, the management is responsible for managing the daily operation of the enterprise and making

decisions on the big and small affairs of the enterprise. It also influences the accounting department and accounting personnel of the enterprise, and has the ability to influence the final presentation of financial statements, so as to control the final quality of accounting information. If the power of the management is excessively concentrated, the management has the ability and methods to pursue the interests of the managers and damage the interests of the owners, and achieve their own goals through earnings manipulation. So too much management power will lead to distortion of accounting information, make its quality decline.

In our country, there are many problems in the accounting information of enterprises, such as increasing the income and concealing the loss, concealing the major events, using accounting methods that do not conform to the regulations, and so on. Thinking about the reasons, human factors and policy factors. Subjectively, for the sake of personal interests and the overall financial performance of the enterprise, the manager may deliberately inflate the income and conceal the loss to present the good information of the enterprise to the enterprise owners and investors, thus reducing the quality of accounting information. Objectively, because of the development status of Chinese market economy and the insufficient understanding of accounting in the academic circle, our current accounting laws and regulations, accounting methods and so on still have some loopholes and limitations, so that the accounting information can not fully reflect the actual situation of enterprises. One of the key factors causing the distortion of enterprise accounting information is the lack of reasonable and effective internal control. It is the enterprise internal control is not perfect, ineffective operation makes the enterprise existing problems, potential risks can not quickly and effectively identify and take measures, affect the business of the enterprise, increase the possibility of financial fraud, resulting in the low quality of accounting information. Internal control is in order to improve the overall operation efficiency of the enterprise, the design and implementation of various restrictions and adjustment activities in the enterprise, help the enterprise to achieve the goal faster and better, can greatly protect the quality of accounting information, has attracted the wide attention of scholars from various countries.

Therefore, it is of both theoretical and practical

significance to study and analyze the interaction mechanism of enterprise internal control, management power and accounting information quality. By strengthening internal control, the management can restrain earnings manipulation and improve the quality of accounting information, which can really help enterprises develop better.

2. Research Hypothesis

2.1. Internal Control and Accounting Information Quality

Research and analysis of enterprise internal control and accounting information quality interaction mechanism, first from the elements of internal control analysis. Internal control environment refers to the working atmosphere provided by the enterprise for the majority of staff, which is the guarantee for the effective implementation of other elements. Good internal control environment can ensure the implementation of relevant systems, ensure the production and operation and financial management activities to get a true and accurate reflection, so as to improve the quality of accounting information. Risk assessment is to judge the risks that the enterprise will face in a timely and effective manner and formulate effective countermeasures. Effective risk assessment system can help enterprises timely discover the existing or will be faced with problems, so that the management can make preparations in advance, take scientific measures to deal with risks, avoid the enterprise to suffer significant losses, protect the interests of the enterprise, and then reduce the possibility of business managers in order to cover up business failures and manipulate the profit whitewash statements, to ensure the quality of accounting information. Control activities are to conduct scientific and reasonable control over the various business activities and procedures of the enterprise, so as to make the operation process of the business more standardized and scientific, reduce the possibility of enterprise employees taking advantage of system loopholes to practice favoritism, and ensure the quality of enterprise accounting information. The control procedure with mature system design and effective implementation can greatly improve the reliability of accounting information and thus improve the quality of accounting information. Information and communication means that the enterprise should establish and improve the information transmission mechanism, so that the important information of the enterprise operation can be transmitted in time, so that the managers can know the situation in time, and the various departments can exchange what they have. Perfect information transmission mechanism can speed up the feedback speed of relevant information of enterprises, enterprises can make faster response measures to protect the interests of enterprises, so as to improve the quality of accounting information. Internal supervision can make enterprise managers know the extent of the implementation of other procedures under internal control in time. The design of mature internal supervision can guarantee the implementation effect of the relevant system of the enterprise, make the internal control really play a role, improve the quality of accounting information. Therefore, it is speculated that internal control has a positive impact on the quality of accounting information as a whole, which can improve the quality of accounting information.

Based on theoretical analysis, the research hypothesis is proposed:

H₁: Enterprise internal control is positively correlated with accounting information quality.

2.2. Management Power and Accounting Information Quality

With the continuous development and perfection of enterprise structure, ownership and management are generally separated in modern enterprises. With the development of enterprise economy and the continuous development of enterprise scale, enterprise owners are unable to manage themselves in the whole process like a small workshop. Whether in terms of ability or professionalism, managers need a professional manager to help enterprise owners. Therefore, the owner will transfer the management right of the enterprise to the professional personnel, who will conduct the operation and management. This greatly improves the efficiency of the enterprise. At the same time, there are agency problems. Managers, as direct participants in the business activities of enterprises, have more detailed information about enterprises than the owners. However, shareholders can only understand the information of the enterprise through financial statements or shareholders, and do not know much about their own enterprises. Management has an information advantage over shareholders. In order to reduce the information difference between shareholders and managers, shareholders often carry out corresponding equity incentives. With the equity incentive, the power of management is further expanded and more able to influence corporate earnings. However, the interests of shareholders and management are quite different. Shareholders hope to maximize corporate profit and corporate value. And management is more concerned about their own compensation, benefits, etc. So when management has too much power, it may sacrifice owner's equity for its own sake. Especially when the performance of the management is related to the net profit of the financial statements, the management has a strong motivation to manipulate the corporate earnings and whitewash the financial statements to create the illusion of corporate prosperity. Management often reduces the quality of accounting information by reducing the quality of accounting information to different degrees of earnings management, whitewash the real financial information and other ways to reduce the quality of accounting information.

Based on the above theoretical analysis, this paper proposes the following hypothesis:

H₂: There is a negative correlation between management power and accounting information quality.

2.3. Internal Control, Management Power and Accounting Information Quality

When management has too much power, it may sacrifice owner's equity for its own sake. Especially when the performance of the management is related to the net profit of the financial statements, the management has a strong motivation to manipulate the corporate earnings and whitewash the financial statements to create the illusion of corporate prosperity. Management often reduces the quality of accounting information by reducing the quality of accounting information to different degrees of earnings management, whitewash the real financial information and other ways to reduce the quality of accounting information. A well-run internal control can effectively curb the problems caused by excessive management power. Internal control can

restrain the excessive power of the management through the system, rationally allocate the power structure of the management, and give full play to the supervisory role of the board of directors for the enterprise. Internal control can restrain the motivation of management to manipulate earnings, reduce the opportunity of management to manipulate, and block the way of management to make mistakes from the process and system. The various elements of internal control can play a role in the normal operation of the enterprise from different aspects, restrain the power concentration of the management, solve the agent problem between the management and the shareholders, so as to improve the quality of accounting information.

Based on the above analysis, this paper proposes the following hypothesis:

H₃: Internal control can alleviate the negative effect between management power and accounting information quality.

3. Research Design

3.1. Sample and Data Source

This paper takes Shanghai-Shenzhen A-share manufacturing listed companies from 2016 to 2018 as samples. In order to enhance the reliability of empirical data and the persuasiveness of empirical research, the sample data is screened as follows:

- (1) Remove ST, *ST, PT and other samples
 - (2) The samples newly listed and discontinued in the selected year are excluded, and the samples normally listed are selected
 - (3) Eliminate data missing and discontinuous samples
- Finally, a total of 3,673 sample data were selected,

including 960 state-owned enterprises and 2,713 non-state-owned enterprises.

In this paper, the accounting information quality of the explained variable, the authority of the manager of the explained variable, and the asset-liability ratio of the control variable are all from CSMAR database. The explanatory variables measure the internal control data from Shenzhen Dibo Company Risk management database (DIB). Excel and Stata15 are used for data processing and statistical analysis in this paper.

3.2. Variable Design and Model

3.2.1. Variable Definition

This paper selects the modified Jones model to calculate the quality of accounting information disclosure, and reflects the quality of accounting information disclosure through the absolute value of discretionary accruals. The greater the value of |DA|, shows that the higher the extent of enterprise surplus management, manipulation profit, the more the lower the quality of accounting information disclosure. The enterprise internal control composite index in Shenzhen Dibo Risk Management Database (DBI) is selected to measure the internal control. The higher the score, the better the internal control quality of the enterprise, the mature and effective implementation of the system. In this paper, the following two indicators are adopted to measure management power. It is expressed by the total number of management power obtained by the sum of the two dummy variables of equity dispersion and integration of two positions. The higher the value, the more power management has.

The definition and description of variables studied in this paper are shown in Table 1:

Table 1. List of Variable Definitions

	Name	Symbol
Explained Variable	Accounting Information Quality	Disclose
	Internal Control	ICindex
Explanatory Variable	Management Power	Power
		power1
		power2
	Enterprise Scale	Size
Control Variable	Asset-liability Ratio	Lev
	Income Growth Rate	Growth
	Rate of Return on Total Assets	Roa
	Nature of Enterprise	State owned

3.2.2. Research Model

There are three regression models in this paper, which are

formula (1), (2) and (3).

$$Disclose_{i,t} = a_0 + a_1 ICindex_{i,t} + a_2 Size_{i,t} + a_3 Lev_{i,t} + a_4 Grown_{i,t} + a_5 Roa_{i,t} + a_6 State_owned_{i,t} + \zeta_{i,t} \quad (1)$$

$$Disclose_{i,t} = a_0 + a_1 Power_{i,t} + a_2 Size_{i,t} + a_3 Lev_{i,t} + a_4 Grown_{i,t} + a_5 Roa_{i,t} + a_6 State_owned_{i,t} + \zeta_{i,t} \quad (2)$$

$$Disclose_{i,t} = a_0 + a_1 ICindex_{i,t} + \alpha_2 Power_{i,t} + \alpha_3 ICindex \times Power_{i,t} + a_4 Size_{i,t} + a_5 Lev_{i,t} + a_6 Grown_{i,t} + a_7 Roa_{i,t} + a_8 State_owned_{i,t} + \zeta_{i,t} \quad (3)$$

4. Empirical Analysis

4.1. Descriptive Statistics

According to the analysis in Table 2, the maximum value of absolute value of maneuverable accruals (Disclose) is 1.471 and the minimum value is 0.0000199, which vary greatly among different enterprises. Meanwhile, the average value of absolute value of maneuverable accruals (Disclose) is 0.0744, which is far smaller than the maximum value. Therefore, it is speculated that there may be special values in the data. Its standard deviation is 0.0725, and the degree of data dispersion is small. The maximum value of internal control is 6.795, and the minimum value is 4.884, indicating that different enterprises have different levels of internal control. Its average value is 6.472, which is not much different from the maximum value. It is speculated that the data distribution is relatively uniform and roughly normal, and there may be small special values. The standard deviation is 0.139, and the degree of data dispersion is small, indicating that most sample enterprises have good internal control, which corresponds to the good quality of accounting information mentioned above. Management Power is an integral variable, with a maximum value of 2, a minimum value of 0, an average value of 0.756, and a standard deviation of 0.692. It is speculated that most sample enterprises have the phenomenon of management power concentration. If the

average value is less than 1, it may be inferred that the management power concentration degree is small and the data dispersion degree is small.

Among the control variables, the maximum value of the enterprise Size (Size) index is 27.39 and the minimum value is 19.20, with a large range and a few extreme values. It can be seen that there is a large dispersion degree of sample enterprises and a large gap in the overall size of enterprises. The average is 22.07; The standard deviation is 1.145, reflecting the large degree of dispersion of the enterprise size of the sample enterprises. The maximum value of asset-liability ratio (Lev) was 1.352, and the minimum value was 0.0216. The average value is 0.373, far less than 0.5, and the standard deviation is 0.182. The degree of sample dispersion is small, indicating that most sample enterprises have little debt and decent solvency on the whole, and only a few enterprises have high asset-liability ratio index. The average rate of return on total assets (Roa) is 0.0507, the maximum value is 0.466, the minimum value is -0.593, and the standard deviation is 0.0623. The dispersion degree of sample data is small, but there are large differences among individuals, and there are lossmaking enterprises. The maximum value of Growth was 55.04, the minimum value was -0.862, the mean value was 0.259, and the standard deviation was 1.235. It is speculated that there is a large degree of data dispersion and negative growth of enterprises.

Table 2. Descriptive Statistics

	Obs	Mean	Std.Dev.	Min	Max
Disclose	3, 673	0.0744	0.0725	1.99e-05	1.471
ICindex	3, 673	6.472	0.139	4.884	6.795
Power	3, 673	0.756	0.692	0	2
Size	3, 673	22.07	1.145	19.20	27.39
Lev	3, 673	0.373	0.182	0.0216	1.352
Roa	3, 673	0.0507	0.0623	-0.593	0.466
Growth	3, 673	0.259	1.235	-0.862	55.04
State_owned	3, 673	0.261	0.439	0	1

4.2. Correlation Analysis

It can be seen intuitively from the correlation coefficients of variables in Table 3 that the coefficient of explained variables and explanatory variables is -0.034, indicating that internal control (icindex) is negatively correlated with absolute value of maneuverable accruals (Disclose), that is, the better the internal control, The lower the absolute value of

operational accruals, the higher the quality of accounting information. It shows that good internal control can restrain the management of enterprise earnings manipulation, so as to improve the quality of accounting information. The coefficient of disclosure variable and explanatory variable is 0.016, indicating that management Power is positively correlated with absolute discretionary accruals. This is consistent with our general analytical understanding.

Table 3. Correlation Analysis

	Disclose	ICindex	Size	Lev	Roa	Growth	Power
Disclose	1.000						
ICindex	-0.034**	1.000					
Size	0.057***	0.076***	1.000				
Lev	0.131***	-0.054***	0.530***	1.000			
Roa	-0.053***	0.272***	-0.014	-0.332***	1.000		
Growth	0.212***	0.065***	0.071***	0.060***	0.047***	1.000	
Power	0.016	-0.004	-0.151***	-0.077***	-0.013	0.027*	1.000

4.3. Regression Analysis

As can be seen from Table 4, internal control has a significant impact on discretionary accruals at the significance level of 5%. This indicates that good internal control can reduce the absolute value of discretionary accruals. The higher the quality of accounting information, the verification of hypothesis 1. Further test shows that in state-owned enterprises, the coefficient is -0.006, although the sign

is still negative, but not significant. In the regression of non-state-owned enterprises, the coefficient is -0.026, and the correlation is negative at the significance level of 5%. Therefore, it is speculated that the influence of internal control on the quality of accounting information is more obvious in non-state-owned enterprises, and non-state-owned enterprises should strengthen the construction of internal control.

Table 4. Internal Control and Accounting Information Quality Regression Coefficient

VARIABLES	Full sample	State-owned enterprise	Non-state-owned enterprise
	Disclose	Disclose	Disclose
ICindex	-0.019** (2.21)	-0.006 (0.48)	-0.026** (2.27)
Size	-0.002 (-1.39)	-0.004* (-1.95)	-0.002 (-1.32)
Lev	0.050*** (6.11)	0.048*** (3.20)	0.058*** (5.90)
Roa	-0.036* (-1.73)	0.234*** (4.99)	-0.092*** (-3.93)
Growth	0.012*** (12.83)	0.018*** (7.93)	0.011*** (10.64)
Constant	-0.030 (-0.50)	0.105 (1.20)	-0.069 (-0.86)
Observations	3, 673	960	2, 713
R-squared	0.062	0.099	0.070

t-statistics in parentheses
*** p<0.01, ** p<0.05, * p<0.1

As can be seen from Table 5, when management Power is taken as explanatory variable, its full sample coefficient α_1 is 0.002, the coefficient of state-owned enterprises is 0.001, and the coefficient of non-state-owned enterprises is 0.004. However, only non-state-owned enterprises are positively

correlated at the significance level of 10%, while the other two groups are not significant, but the coefficient signs are positive. It shows that in non-state-owned enterprises, the management is more likely to manipulate earnings profits when its power increases.

Table 5. Management Power and Accounting Information Quality Regression Coefficient

VARIABLES	Full sample	State-owned enterprise	Non-state-owned enterprise
	Disclose	Disclose	Disclose
Power	0.002 (1.10)	0.001 (0.21)	0.004* (1.84)
Size	-0.001 (-1.10)	-0.004* (-1.91)	-0.002 (-1.07)
Lev	0.050*** (6.09)	0.047*** (3.19)	0.057*** (5.89)
Roa	-0.024 (-1.20)	0.238*** (5.12)	-0.075*** (-3.35)
Growth	0.012*** (12.89)	0.018*** (7.97)	0.011*** (10.69)
Constant	0.086*** (3.32)	0.142*** (3.36)	0.089*** (2.64)
Observations	3, 673	960	2, 713
R-squared	0.061	0.099	0.069

t-statistics in parentheses
*** p<0.01, ** p<0.05, * p<0.1

In the third regression model, management power, internal control and their cross terms are added, and the regression is carried out again, and the previous results are compared and analyzed. Compared with the previous model results, it can be seen that the regression significance is significantly

improved under all samples. Internal control changes significantly from 5% in the first model to significantly negative correlation at 1% level; management power changes significantly from insignificant in the second model to significantly positive correlation at 1% level. The cross term

is negatively correlated with the controllable accruals at 1% level, indicating that the management can be supervised through reasonable allocation of authority under the condition of perfect internal control system and effective execution, so as to reduce the negative effect of excessive power of the

management on the quality of enterprise accounting information. However, this relationship is not significant in state-owned enterprises, indicating that in state-owned enterprises, the strength of earnings manipulation through internal control to improve the management is relatively weak.

Table 6. Internal Control, Management Power and Accounting Information Quality Regression Coefficient

VARIABLES	Full sample Disclose	State-owned enterprise Disclose	Non-state-owned enterprise Disclose
ICindex	-0.040*** (-3.39)	-0.015 (-0.99)	-0.065*** (-3.56)
Power	0.198*** (2.78)	0.113 (0.98)	0.245** (2.56)
ICindex*Power	-0.030*** (-2.76)	-0.017 (-0.98)	-0.037** (-2.52)
Size	-0.002 (-1.43)	-0.003 (-1.39)	-0.002 (-1.05)
Lev	0.053*** (6.86)	0.026* (1.91)	0.062*** (6.62)
Roa	-0.011 (-1.10)	0.071*** (4.37)	-0.061*** (-4.63)
Growth	0.012*** (12.76)	0.018*** (7.89)	0.011*** (10.63)
Constant	-0.169** (-2.12)	0.034 (0.33)	-0.331*** (-2.72)
Observations	3, 672	960	2, 712
R-squared	0.064	0.094	0.076

t-statistics in parentheses

*** p<0.01, ** p<0.05, * p<0.1

5. Conclusion

This paper theoretically analyzes how enterprise internal control and management power affect the quality of accounting information and proposes hypotheses. A total of 3,673 data data of Shanghai and Shenzhen A-share manufacturing industry from 2016 to 2018 are selected as samples for analysis and extreme values are removed. This paper uses the absolute value of operational accruals to measure the quality of accounting information (Disclose) as the explained variable and internal control (ICindex) and management Power as the explanatory variables to conduct an empirical study. Based on the empirical results, it is concluded that ICindex is positively correlated with disclosure of accounting information, while management Power is negatively correlated with disclosure of accounting information. To some extent, internal control can inhibit the manipulation of earnings by management.

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