INTERNAL AUDIT AS A PILLAR OF CORPORATE GOVERNANCE: A LITERATURE REVIEW

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Abstract- In an era of increasingly complex global business competition, good corporate governance (GCG) is a crucial factor in maintaining the sustainability and competitiveness of organizations. Internal audit, as an independent and objective function, plays a strategic role in supporting the implementation of GCG by strengthening transparency, accountability, risk control, and fraud prevention. This study aims to comprehensively examine the role of internal audit as a key pillar of corporate governance using a literature review method. Data sources were obtained from textbooks, journal articles, and professional standards, such as the International Professional Practices Framework (IIA, 2017) and the OECD Principles of Corporate Governance (OECD, 2015). The analysis was conducted using a content analysis approach to identify key themes, categorize internal audit contributions, and evaluate implementation challenges. The study results indicate that internal audit is no longer limited to a compliance function but has transformed into a strategic partner of management oriented towards value-added creation. However, there are a number of challenges, such as limited independence, internal resistance, and competency demands in the digital era. This study confirms that optimizing the role of internal audit is key to strengthening sustainable corporate governance, while also opening up space for further research related to digitalization and the role of internal audit in sustainability governance.

Keywords: Internal audit, Good Corporate Governance, Transparency, Accountability, Sustainability Governance.

I. INTRODUCTION

In the era of globalization and increasingly complex business competition, companies are required to pursue not only financial profit but also ensure business sustainability through the implementation of good corporate governance (GCG). The implementation of GCG has become a fundamental requirement for modern organizations, particularly to increase stakeholder trust, strengthen competitiveness, and maintain company sustainability amidst the dynamics of the external environment (Claessens & Yurtoglu, 2013). Good corporate governance is believed to be able to prevent abuse of authority, fraud, and various unethical business practices that can harm the company and the wider community (Solomon, 2020).

One of the key elements supporting the implementation of GCG is the existence of an internal audit function. Internal audit is an independent, objective, and systematic activity that serves to provide assurance and consultation to management regarding the effectiveness of risk management, internal control, and governance processes. The Institute of Internal Auditors (IIA, 2017) defines internal audit as an activity designed to add value and improve an organization's operations. Therefore, internal audit serves not only as a control mechanism but also as a strategic partner for management in improving efficiency, effectiveness, and compliance with applicable regulations (Gramling et al., 2020).

The presence of internal audit within a company was initially focused on monitoring procedural compliance and the accuracy of financial records. However, over time, the role of internal audit has transformed. Internal audit now not only examines compliance but also acts as a consultant, providing strategic recommendations to management to improve governance and achieve organizational goals (Arena & Azzone, 2009). In other words, internal audit has shifted from a purely supervisory function to a more proactive one oriented toward increasing value.

Effective internal audit implementation has been proven to strengthen the application of GCG principles, namely transparency, accountability, responsibility, independence, and fairness. Transparency is reflected in the assurance that financial and managerial reports are prepared honestly, openly, and in accordance with applicable standards. Accountability is realized by ensuring that each organizational unit is accountable for its performance in a clear and measurable manner (Tricker, 2019). Responsibility is evident in the company's compliance with regulations and social responsibility to the community. Internal audit independence ensures that every finding and recommendation is free from interference from certain parties. Meanwhile, fairness relates to the fair treatment of all stakeholders (OECD, 2015).

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Despite the strategic role of internal audit, practice shows that many challenges remain. These include the limited independence of internal auditors, who are often subordinate to management, a lack of competence in dealing with digital technology developments, and internal resistance to audit recommendations (Sarens & De Beelde, 2006). These challenges need to be addressed to ensure the internal audit function can truly function optimally in supporting sound corporate governance.

Through a literature review, this study seeks to delve deeper into the role of internal audit as a pillar of corporate governance. The literature review was chosen because it provides a comprehensive overview based on previous research and literature, thereby enriching our understanding of the relationship between internal audit and GCG. This approach is expected to provide a more comprehensive understanding of how internal audit contributes to the implementation of corporate governance, as well as the challenges it may face in practice (Suyono & Hariyanto, 2012).

II. RESEARCH METHODS

This research uses a descriptive qualitative approach with a literature review method. This literature review was chosen because this research does not involve direct field data collection, but rather examines, analyzes, and synthesizes various previous research findings, textbooks, scientific articles, institutional reports, and professional standards relevant to the topic of internal audit and corporate governance.

According to Snyder (2019), a literature review is a research method that aims to identify, evaluate, and interpret existing research related to a specific topic. This approach allows researchers to gain a broader and deeper understanding of the phenomenon being studied. Similarly, Webster and Watson (2002) state that a good literature review must be able to provide both theoretical and practical contributions by compiling, connecting, and critiquing the available literature.

Data Sources

The data sources for this study come from relevant literature, including:

1. Textbooks discussing internal audit, internal control, and corporate governance.
2. Indexed scientific journal articles, both international and national, that examine the relationship between internal audit and GCG.
3. International standards and guidelines, such as the International Professional Practices Framework (IPPF) from the Institute of Internal Auditors (IIA, 2017) and the OECD Principles of Corporate Governance (OECD, 2015).
4. Previous research relevant to the theme of internal audit as a pillar of GCG (e.g., Arena & Azzone, 2009; Sarens & De Beelde, 2006).

Data Collection Techniques

Data were collected by searching literature from various academic databases. Reference books and highly credible institutional documents were also used. The literature search used keywords such as "internal audit," "corporate governance," "internal control," and "fraud prevention."

Data Analysis Techniques

Data analysis was conducted using content analysis. Krippendorff (2018) explains that content analysis is a research technique used to draw replicable and valid inferences from data within its context. In this study, content analysis was conducted using the following steps:

1. Identifying literature relevant to the theme of internal audit and corporate governance.
2. Categorizing themes according to the role of internal audit, GCG principles, and challenges faced in practice.
3. Synthesizing information by connecting findings from various literatures.
4. Interpreting the results to answer the research questions regarding the role of internal audit as a pillar of corporate governance.

With this approach, the research is expected to provide a comprehensive picture of how internal audit plays a role in supporting GCG implementation, while also identifying literature gaps that can become opportunities for further research.

III. DISCUSSION

1. The Role of Internal Audit in Corporate Governance

Internal audit is a key element in supporting the implementation of good corporate governance (GCG). As emphasized by the Institute of Internal Auditors (IIA, 2017), internal audit not only provides independent assurance but also helps management improve the effectiveness of organizational operations. In the context of GCG, internal audit serves as a bridge between management, the board of directors, and the audit committee, ensuring consistent implementation of governance principles.

Claessens and Yurtoglu (2013) emphasize that the implementation of good corporate governance increases investor confidence, reduces the cost of capital, and improves long-term performance. Internal audit, with its monitoring and advisory roles, is a strategic instrument in maintaining the integrity of financial information, ensuring regulatory compliance, and encouraging ethical business practices.

Thus, internal audit cannot be viewed as merely an administrative function, but rather as a key pillar supporting corporate sustainability. Companies that integrate internal audit into their GCG systems have proven to be more resilient to business risks and are more trusted by stakeholders (Solomon, 2020).

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2. Internal Audit as a Risk Control Mechanism and Fraud Prevention

One of the significant contributions of internal audit is its role in risk management. According to Gramling et al. (2020), internal audit helps organizations identify, assess, and mitigate risks that could hinder the achievement of objectives. The audit process goes beyond simply identifying control weaknesses to providing strategic recommendations to strengthen the risk management framework.

In the context of fraud prevention, internal audit serves as a deterrent mechanism. Fraud often arises from weak internal controls and a low culture of integrity within a company. Research by Suyono and Hariyanto (2012) shows that internal audit effectiveness is positively related to the quality of corporate governance and fraud prevention. Therefore, internal audit functions not only ex post to detect irregularities but also ex ante to prevent unethical practices.

Furthermore, the OECD (2015) emphasizes the importance of transparency and independence in preventing conflicts of interest. Strong internal audit can provide assurance that financial statements reflect the true state of affairs, thereby reducing the opportunity for data manipulation.

3. Internal Audit's Contribution to Transparency and Accountability

GCG principles emphasize the importance of transparency and accountability. Internal audit plays a vital role in ensuring that company reports are presented honestly and responsibly.

Tricker (2019) states that corporate accountability can only be achieved if there is an effective oversight system. Internal audit, in this case, plays a role in ensuring that each organizational unit is accountable for its performance. For example, through performance audits, internal auditors can assess the efficiency of resource use and the effectiveness of goal achievement.

Furthermore, transparency relates not only to financial reports but also to the disclosure of information to stakeholders. Internal audit can help companies develop clearer reporting systems, minimizing information asymmetry between management and investors (Arena & Azzone, 2009). Thus, the role of internal audit is crucial in strengthening a company's credibility in the eyes of the public, investors, and regulators.

4. Transforming the Role of Internal Audit: From Compliance to Value Added

Early in its development, internal audit focused primarily on compliance, ensuring company compliance with internal policies and external regulations. However, as business dynamics have become increasingly complex, internal audit has transformed into a value-creation-oriented function.

Arena and Azzone (2009) demonstrate that internal audit effectiveness is significantly influenced by the extent to which internal auditors can add value to management. This is demonstrated through providing strategic recommendations, involvement in risk planning, and support in business decision-making.

Gramling et al. (2020) emphasize that internal auditors are now required to possess multidisciplinary competencies, spanning accounting, information technology, and risk management. Thus, internal audit is no longer simply a fault-finding function but also serves as a proactive internal consultant. This transformation aligns with the global trend where internal audit is viewed as a strategic partner for management in achieving competitive advantage (Solomon, 2020).

5. Challenges of Internal Audit Implementation in Supporting GCG

Despite its strategic role, internal audit practices in the field are not without challenges. Sarens and De Beelde (2006) identified a gap between management expectations and the capabilities of internal auditors. Some of the main challenges include:

a. Limited Independence – Internal auditors are often subordinate to management structures, potentially creating conflicts of interest.
b. Limited Competence – Developments in digital technology, such as big data and artificial intelligence, require internal auditors to possess new skills beyond traditional accounting.
c. Internal Resistance – Internal audit recommendations are often rejected by work units that feel disrupted by the audit process.
d. Limited Resources – Many organizations, especially in developing countries, still view internal audit as a cost, not a strategic investment.

These challenges highlight the need for increased internal auditor capacity, top management support, and stronger regulations to ensure the independence of the audit function.

6. Best Practices and Practical Implications

Some best practices in implementing internal audits to support GCG include:

- Audit committee involvement: The audit committee plays a crucial role in ensuring the independence of internal auditors and following up on audit findings (OECD, 2015).
- Technology integration: The use of data analytics enables internal auditors to identify anomalous patterns that could potentially lead to fraud.
- Risk-based approach: Internal audits should adopt risk-based auditing, focusing on areas that pose the highest risk to the organization (Gramling et al., 2020).
- Competency enhancement: Continuous training is necessary for internal auditors to gain cross-disciplinary insight, including technology and risk management.
- Supportive organizational culture: Companies with a culture of transparency and accountability will more easily optimize the role of internal audit.

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7. Research Gaps and Further Research Agenda

Although the literature demonstrates the important role of internal audit in supporting GCG, there are still gaps in the literature that could be addressed as further research agendas. Some of these include:

1. The impact of digitalization on internal audit – How technologies such as artificial intelligence, machine learning, and blockchain are transforming internal audit practices is still relatively new.
2. Internal audit in the public vs. private sector – Further research is needed to examine the differences in internal audit effectiveness in the context of public bureaucracies compared to private companies.
3. Organizational culture and internal audit effectiveness – Organizational culture factors often play a significant role but have not been studied in depth.
4. The role of internal audit in sustainability governance – With increasing attention to ESG (Environmental, Social, and Governance), studies are needed to examine the contribution of internal audit in supporting corporate sustainability.

IV. CONCLUSION

Internal audit has proven to play a strategic role as a key pillar in the implementation of good corporate governance (GCG). Based on a literature review, the internal audit function is no longer limited to compliance audits but has transformed into a strategic partner for management focused on creating added value. Internal audit supports the implementation of GCG principles by strengthening transparency, accountability, risk management, and fraud prevention.

Furthermore, internal audit also contributes to increasing stakeholder trust, strengthening the integrity of financial reporting, and fostering a healthy organizational culture. The transformation of internal audit's role from mere watchdog to business partner demonstrates that its function is now more proactive and adaptive to global business dynamics.

However, several challenges remain to be overcome, including limited independence, internal resistance, limited competencies, especially in the digital era, and the perception that internal audit is merely a cost. This requires top management support, strengthening the capacity of internal auditors, technology integration, and an organizational culture that supports transparency and accountability.

This research confirms that optimizing the role of internal audit is key to strengthening sustainable corporate governance. In addition, there are opportunities for further research related to audit digitalization, the role of internal audit in sustainability governance, and differences in the effectiveness of internal audit in the public and private sectors.

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