A Study on the Role of Internal Audit in the Governance of Social E-Commerce Platforms

Xiao Tan

Nanjing Audit University, Nanjing 210000, Jiangsu, China

Abstract: Community e-commerce constitutes an innovative business model within the electronic commerce sector. Despite its rapid growth, it is confronted with numerous inherent risks and challenges. This paper explores the essential function of internal audit in the risk management process for community e-commerce platforms and offers recommendations for enterprises to develop effective risk management strategies. Implementing a comprehensive internal audit mechanism enables community e-commerce platforms to better identify and mitigate potential risks, thus enhancing platform security and stability. Consequently, this bolsters user trust and supports the platform's sustainable operations.

***Keywords*:** internal audit; risk management; platform enterprise

1. Introduction

With the rise of social media and growing consumer demand for personalized products, community e-commerce has rapidly emerged and continues to evolve in China. Unlike traditional e-commerce, community e-commerce leverages social platforms and user communities to facilitate precise user targeting and personalized recommendations, demonstrating significant market potential. However, this innovative e-commerce model faces various operational risks, including compliance, market, and financial risks

Consequently, the role of internal audit in risk management for community e-commerce is essential. Internal audit provides a comprehensive analysis of potential risks within operational processes, offering valuable decision-making support to management. The pre-sale model, a key aspect of community e-commerce, requires stringent control over supply chain management and user demand. Internal audit involvement ensures compliance and effectiveness of pre-sale activities, enhancing user trust and market competitiveness. As consumer demand for personalized products increases, community e-commerce platforms must optimize product recommendations and customized services. In this context, internal audit can help platforms identify user needs, assess market risks, and develop effective response strategies, facilitating market expansion and profit enhancement.

2. Definition of Community E-commerce Platforms and Risk Identification

Community e-commerce is a digital commerce model. In this model, products are sold and marketing activities are performed through online communities hosted on social media platforms. Merchants connect with potential customers by creating or joining social groups, social media accounts, or applications. They promote product sales through social interaction, product information sharing, and purchase guidance. Typically, community e-commerce platforms provide purchase links or channels. These allow customers to complete transactions directly on the social platform. When identifying risks for such platforms, one must account for two key features of this model: social marketing and personalized product customization.

The identification of compliance risks within community e-commerce platforms requires a systematic analysis focused on policy direction and critical business process nodes. Notably, community e-commerce platforms often enable various group purchasing behaviors, and some products may involve cross-border transactions, raising concerns regarding customs procedures and taxation. Tax compliance is a crucial area of focus, necessitating close attention to the applicable tariff rates for different goods. Following the 2021 "Sky Clean" initiative, it was found that the auditing departments of mainstream platforms inadequately enforced relevant policies, leading to a lack of restrictions on minors' purchasing behaviors before the mandated corrections. This situation highlights the need for internal auditors to closely examine the operational processes of audit departments, assess age verification systems, and evaluate content filtering mechanisms to ensure that minors' consumption is effectively restricted in accordance with national regulations.

Credit risk arises from shortcomings in information disclosure and supervision during pre-sale transactions of customized goods on community e-commerce platforms. Such risk may lead to financial losses. Advance payments are often used with limited transparency. As a result, incidents have occurred in recent years in which group leaders or merchants absconded with funds—data from "Diansubao" confirm this pattern. Credit systems on these platforms remain underdeveloped. Notably, they lack a structured framework for classifying and evaluating merchant credit records. When identifying credit risk, internal auditors should carefully examine user-reported issues on complaint platforms. Communicating with the customer service center is also necessary to determine the appropriate follow-up actions.

The inherent characteristics of community e-commerce lead to a higher gross profit margin; however, the revenue-to-cost ratio reveals substantial inefficiencies. In assessing financial risks, internal auditors should concentrate on critical indicators, such as the sales expense ratio and revenue growth rate. In a pre-sale model, the platform functions as an intermediary, leading to advance payments being retained in the platform's account rather than directly transferred to the merchants. During the audit process, special attention must be paid to cases where revenue, which should be recognized under the net method in accordance with new revenue recognition standards, is improperly recognized using the gross method. This misclassification can significantly affect the evaluation of the platform’s profitability. E-commerce platforms utilize social media to engage potential consumers through strategies such as new user red envelopes, social media advertising, and payment discounts. Given that sales expenses represent a substantial share of overall costs, it is vital to assess the reasonableness of the sales expense ratio and investigate any sudden rises in sales expenses during the risk identification process.

3. Risk Assessment in Community E-Commerce: Methods and Applications

The primary objective of risk assessment within community e-commerce platforms is to rank identified risks based on their likelihood of occurrence and the severity of their potential impacts. This ranking ultimately informs the allocation of internal audit resources. The assessment process adheres to two fundamental principles: first, the availability of data, which prioritizes the use of verifiable information such as complaint data and operational metrics of the platform; second, business relevance, ensuring that assessment methods align with the distinctive characteristics of community e-commerce, including the pre-sale group buying model.

Once risks are identified, internal auditors should utilize both qualitative and quantitative analysis methodologies. In qualitative analysis, auditors must examine risk factors from internal and external perspectives, determining the nature of risks and anticipating potential consequences. For quantitative analysis, auditors should collect relevant data related to the identified risks, including transaction records, download statistics for client applications, and user complaints. A comprehensive analysis of this data is crucial for calculating specific values for various risk indicators, thereby aiding in assessing and predicting the severity of risks associated with the e-commerce platform and the possible losses incurred

When selecting risk assessment tools suitable for community e-commerce platforms, a combination of Key Risk Indicators (KRIs) and the Monte Carlo simulation method can be effectively utilized. The KRI approach involves establishing critical indicators linked to identified risks; for example, a significant predictor of credit risk occurs when a merchant misappropriates funds linked to pre-sale products. In such instances, an inventory level of "999" often indicates the potential for pre-sale goods, making "inventory at 999" a key risk indicator that can trigger an alert mechanism upon detection. To evaluate risks related to user complaints, three primary metrics can be employed: the percentage of complaints regarding false shipping, the percentage concerning product quality, and the percentage related to after-sales rights protection. These indicators provide a comprehensive framework for quantifying risks associated with user dissatisfaction and ensuring proactive risk management within the platform.

4. Risk Response on Platforms: Building a Management Framework

4.1 Comprehensive Monitoring of Internal Controls

An effective and scientifically designed internal control system is vital for enterprises to achieve more efficient resource allocation. Internal auditing is critical for evaluating these systems, as it identifies potential deficiencies and offers improvement recommendations. This process enhances control effectiveness and system reliability. These measures facilitate the timely identification and correction of risks while ensuring the platform's sustainable development.

The internal audit department utilizes multidimensional approaches for real-time supervision of platform operations, covering various processes and the entire system. This comprehensive oversight facilitates the early identification and resolution of potential risks. By analyzing control activities in detail, auditors can provide targeted optimization recommendations, thereby mitigating risks and supporting the achievement of organizational objectives. Moreover, after management implements risk control measures, internal auditing continues to assess the effectiveness of these strategies, ensuring proper execution, promptly addressing any deviations, and safeguarding the platform's robust operation

4.2 Assessment of Information Disclosure Mechanisms on Platforms

The successful execution of transactions on social commerce platforms fundamentally relies on consumer trust. Internal auditing is crucial for ensuring compliance and transparency in platform operations, thus creating a secure transaction environment for users. Internal auditors evaluate the clarity and visibility of the platform's rules and policies, ensuring they are easily understood and accessible. This evaluation includes clear disclosure of transaction regulations, user behavior standards, and privacy policies.

From the outset, internal auditing should prioritize compliance by performing rigorous sampling checks on merchant and product authenticity. In addition, the audit must verify the legitimacy of data regarding logistics and financial transactions for pre-sale items, as well as confirm the accuracy of customs declarations. When potential risks are identified — such as merchant fund misappropriation, cross-border tax issues, logistics challenges, and copyright violations — internal auditors must promptly communicate these findings to management.

4.3 Facilitating Interdepartmental Communication

During the internal audit process, auditors should engage in comprehensive communication and collaboration with employees across various departments within the platform. In-depth discussions with personnel from different sections enable auditors to gain insights into the operational practices and challenges each department faces. This understanding allows auditors to offer tailored recommendations that align closely with the specific functions of these departments, ultimately assisting employees in optimizing their workflows.

In this process, internal auditors disseminate knowledge related to risk management. This practice elevates overall risk awareness among staff, ensuring vigilance regarding potential operational risks. Through close collaboration with various departments, auditors enable timely and accurate information flow within the platform. Such cross-departmental communication and cooperation helps dismantle organizational silos, fosters teamwork, and contributes to establishing a more robust and efficient enterprise risk management framework.

5. Conclusion

With the rapid expansion of e-commerce platforms and global electronic commerce, the strategic importance of internal auditing for risk management in these platforms is increasingly recognized. Community e-commerce platforms, as an innovative model in this sector, feature a high volume of customized transactions, a significant presence of small and medium-sized enterprises, and heightened demands for platform credibility. In this context, they face numerous complex risk challenges in their operations, highlighting the need for a more sophisticated internal auditing system specifically designed to address their unique characteristics.

Internal auditing serve as a vital component of an organization's internal risk prevention and control framework. Utilizing its evaluative and supervisory functions, internal auditing is essential for identifying, assessing, and responding to risks. It allows community e-commerce platforms to swiftly detect and address potential risks, thereby improving operational efficiency and data security and enhancing the enterprise's core competitiveness. By continuously refining auditing methodologies and strengthening internal controls, e-commerce platforms are better positioned to navigate the increasingly complex and dynamic risk landscape, facilitating sustainable development and long-term success.

References

[1] Oke, A. (2018). The Role of Internal Audit in Corporate Governance. International Journal of Accounting and Financial Reporting, 8(4), 136-148.

[2] Tumwebaze, S., Nuwagaba, G., & Ntayi, J. M. (2018). Corporate governance and financial performance in Uganda’s financial sector: The mediating role of intern audit. African Journal of Business Management, 12(8), 210-220.

[3] Gorwa, R. (2019). What is platform governance? Information, Communication & Society, 22(6), 854-871.

Author Bio

Laughter (May, 2002 —), female, Han nationality, from Liyang, Jiangsu, with a bachelor's degree and a master's degree in auditing.