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Internal Control in Enterprises: Research at Construction Enterprises in Vietnam

[1] **Tat Thanh Doan,** [2] **Hoai Anh Nguyen,** [3] **Thi Tram Dinh**
[1, 2, 3] University of Labour and Social Affairs, Hanoi, Vietnam

Corresponding Author: **Tat Thanh Doan**

Abstract
Internal control aims to limit potential risks, safeguard assets, and protect business information. In the context of the current digital revolution, new approaches to internal control are emerging. A study on internal control in Vietnamese construction enterprises was conducted through a survey questionnaire. With 50 questionnaires sent to the top 5 construction enterprises in Vietnam-ContecCons, FECON, Licogi 16, Vingroup, and Vinaconex - 40 valid responses were received. The results show that Vietnamese construction enterprises are not yet effectively using internal control. The article also provides recommendations for applying elements of internal control more appropriately and effectively.

Keywords: Risk Assessment, Supervision, Control Activities, Control Environment, Information and Communication

1. Introduction

Businesses are growing more and more, expanding their operations and undertaking complex activities with high risk levels. To achieve their goals, managers need to supervise, control and evaluate the effectiveness of their work to minimize risks during operations. Internal control is always necessary and cannot be missed in the management process of each business. It holds significant importance for the survival and growth of every business.

Around the globe, internal control has been studied and implemented in businesses since the early 1990s. Depending on the research objectives, there are various approaches to internal control, especially since the release of the COSO report in 1992. Internal control has evolved in different directions, with the design of internal controls in various businesses being a key focus of the COSO report version. However, in Vietnam today, internal control is still a relatively new concept in business practice.

In the construction industry, the Vietnamese construction market hit a value of 57.52 billion USD in 2020, and it's projected to reach 94.93 billion USD by 2026, growing at a rate of over 8% during the forecast period (2021-2026) (FPTS, 2020). The Vietnamese construction market is highly competitive, with the presence of major international enterprises. Current construction businesses are on an upward trajectory but face many challenges and hurdles. The Vietnamese construction sector offers growth opportunities in the forecast period, which is expected to further fuel market competition. With a few enterprises holding a significant share, the Vietnamese construction market is showing observable consolidation.

Business managers need to grasp the potential risks their company is facing to make decisions about effective internal control activities. However, internal control in construction enterprises in Vietnam has not met the expectations of leaders. Therefore, improving effective and efficient internal control in construction enterprises is a must.

2. Literature Review

The overview of internal control is divided into three stages, as follows:

Stage 1: Pre-COSO stage (before 1992)

The first theory on internal control was introduced in 1929 by the Federal Reserve Bulletin's publication, positioning internal control as a tool to safeguard money and other assets while promoting operational efficiency; it's a fundamental tool for auditors' sampling. This theory highlighted the role of internal control; which is simply understood as a tool to prevent errors, fraud, loss or misappropriation of assets; ensuring reliable accounting figures. Later, this concept was expanded: Internal control is not only about protecting assets (not just money) but also ensuring accurate accounting records, enhancing operational efficiency and encouraging compliance with management policies. Since the 1940s, various American public accounting and internal auditing organizations have published a series of reports, guidelines and standards on understanding internal control in audits.

Back in 1985, the collapse of listed corporations caught the attention of U.S. lawmakers towards internal control in businesses, leading to the issuance of numerous guidelines on internal control by:

- The U.S. Securities and Exchange Commission in 1988
- The Institute of Internal Auditors in 1991
- The U.S. Auditing Standards Board in 1998.

Phase 2: The birth of the COSO report in 1992

The growth of the United States, in terms of both scale and speed of its economy, has had significant repercussions, causing severe damage to the global economy in general and the US economy in particular. This has sparked many debates among scholars and practitioners alike. In response to this, a committee named the National Commission on Fraudulent Financial Reporting, commonly known as the Treadway Commission (named after its leader, James C. Treadway - a lawyer and also a member of the US stock market), was established in 1985. This was a collaborative effort involving professional organizations such as the American Institute of Certified Public Accountants (AICPA), the American Accounting Association (AAA), Financial Executives International (FEI), the Institute of Internal Auditors (IIA), and the Institute of Management Accountants (IMA). The Treadway Commission quickly released a historic report in 1987, which included 50 recommendations aimed at reducing fraud in financial reporting. To implement these recommendations, another committee called the Committee of Sponsoring Organizations, or COSO for short, was established.

COSO has researched and studied frauds that cause significant damage to the economy and found that internal controls greatly influence the likelihood of fraud. In September 1992, COSO introduced a standard theoretical framework for internal controls and released the 1992 COSO Report. This is a comprehensive theoretical system on internal controls, marking a significant development in the theoretical understanding of internal controls. The main content introduces a complete concept of internal controls.

Phase 3: The post-COSO phase (after 1992 onwards)

The 1992 COSO report laid a relatively comprehensive theoretical foundation for internal control, paving the way for a series of studies in various fields. Its standout feature is its broad vision, managerial nature, and discussion of issues related to financial reporting, operations, and compliance. While it's not entirely complete, it has established a very basic theoretical basis for internal control. To keep up with current circumstances, an updated COSO report that aligns with the market economy is needed. Therefore, by 2013, the COSO 2013 report replaced the COSO 1992 report, effective December 15, 2014.

Currently, from various research perspectives, researchers have different views on internal control. According to the International Federation of Accountants (IFAC), internal control is a system of policies and procedures established within an organization to ensure the reliability of information, compliance with legal regulations, and operational efficiency. On the other hand, according to the American Institute of Certified Public Accountants (AICPA), internal control involves measures and methods accepted and implemented within an organization to protect money and other assets, and to verify the accuracy of bookkeeping.

The 2015 Accounting Law (Article 39) states: "1. Internal control is the establishment and organization of mechanisms, policies, procedures, and internal regulations in an accounting unit that comply with the law to ensure prevention, detection, and timely handling of risks to meet set objectives. 2. The accounting unit must establish an internal control system to ensure the following: a) The unit's assets are secured and protected from misuse or inefficiency; b) All transactions are approved within the right authority and fully recorded as a basis for preparing and presenting truthful and reasonable financial statements."

According to the Vietnamese auditing standard VSA 315, it mentions the concept of internal control. This refers to the process designed, implemented, and maintained by the Board of Directors, Management Board, and other individuals within an organization. It's all about providing reasonable assurance about achieving the organization's objectives by ensuring the reliability of financial reports, operational effectiveness and efficiency, and compliance with laws and relevant regulations.

According to the COSO report (1992 and 2013) [2], internal control is a process governed by the board of directors, managers, and employees of an entity, designed to provide reasonable assurance in achieving the following objectives:

- The effectiveness and efficiency of operations.
- The reliability of financial reporting.
- Compliance with laws and regulations.

Through research, it can be seen that the concept of internal control according to COSO is widely accepted domestically and globally.

So, we can summarize a general concept of internal control as follows: Internal control is a process governed by the board of directors, managers, and employees of an entity, designed to provide reasonable assurance to achieve objectives in operations, reporting, and compliance in active organizations.

Through these concepts, we can see that the essence of internal control according to COSO, is summarized in the basic content whichs is: Process, people, reasonable assurance, and objectives. Specifically:

Internal control is a process: Every activity of the unit must go through a series of processes *including* planning, implementation, and supervision. To achieve the desired goals, units must have control over their activities. The control activities take place daily and are present in every department within the unit, combined into a unified whole.

Internal control is designed and operated by people, including the board of directors, management, and staff. People set goals, establish control mechanisms, and operate them to achieve these *objectives*. Therefore, for effective internal control, everyone in the organization must clearly understand their responsibilities and authority, identify their roles and tasks, and know how to execute them to achieve the organization's goals.

Reasonable Assurance: Internal control can only provide a reasonable assurance to the directors and managers about achieving the unit's objectives, not an absolute guarantee due to potential limitations in the internal control system such as human errors, collusion of individuals, abuse of authority by managers, and the relationship between the benefits and costs of establishing an internal control system. Moreover, a fundamental principle in management is that the cost of the control process should not exceed the expected benefits from that process.

Goals: Each unit sets its own goals that it needs to achieve (general goals and specific goals for each activity and each department within the unit). These goals set by the unit can be divided into three groups:

- A group of operational goals (effectiveness and efficiency of resource utilization, information security, reputation enhancement, market expansion).
- A group of financial reporting goals (honesty and reliability of financial reports).
- A group of compliance goals (compliance with laws and regulations).

So, through the 2013 COSO report, the concept of internal control has been standardized and developed into a relatively complete theoretical system. It lays the foundation for how to organize, design, and operate an internal control system, providing a theoretical basis for applications among organizations operating in different fields, regions, and countries. According to COSO, internal control consists of five components: Control Environment; Risk Assessment; Control Activities; Information and Communication; Monitoring.

3. Research Method

Approach Method

The article primarily uses qualitative research methods to explore the components of internal control. In this approach, there are five basic elements of internal control: Control Environment; Risk Assessment; Control Activities; Information and Communication; Monitoring.

The Subjects

They are the chief accountants, accounting staff, and auditors of the top 5 construction enterprises in Vietnam: ContecCons, FECON, Licogi 16, Vingroup, Vinaconex. The author’s team sent out 10 survey forms to each of these construction enterprises.

4. Result

The research results indicate that the use of internal control factors to limit risk in order to achieve the objectives of the Vietnamese construction businesses surveyed has not met the requirements. Only the control environment and the supervisory activities of internal control have been appropriately established. Specifically:

Regarding the Control Environment

- Most managers have established a clear leadership style, emphasizing integrity and ethical values in both words and actions (80% believe that managers face pressures to report reasonable financial results, 90% conclude that the board of directors is cautious in business decisions, 95% of managers adjust reports when significant errors are discovered,...).
- All construction enterprises issue regulations on professional ethics (88% of enterprises have measures to limit or eliminate pressures and opportunities for employees to engage in unethical behavior).
- Every construction business has issued documents on the division of authority and responsibilities among various functional departments, widely disseminating this within the company.
- Recruitment is carried out openly (95%) and with clear regulations (93%).
- Construction enterprises have reward and discipline policies, however, the rewards don't seem to make a difference (48% of respondents believe that the employee reward and discipline regulations are not reasonable).

Regarding Risk Assessment

- The process of setting goals based on the proposed plan and the actual conditions of the business isn't quite balanced yet. Most managers are eager to achieve their set goals, so they only plan at a level that's within the company's reach. Although 78% of respondents believe they have identified the mission and strategy that the business is implementing, up to 45% perceive a lack of consistency between the business plan, strategic business objectives, and the actual conditions of the business.
- A majority (70%) of construction businesses haven't systematically and specifically identified potential risks. For each operation, businesses mainly identify risks that have already occurred without considering potential future risks (this applies to 30 out of 40 businesses, equivalent to 75%).
- Risk assessment isn't prioritized in risk management activities. A whopping 95% of businesses haven't proposed specific measures, plans, or procedures to minimize the damage from risks to an acceptable level.
- Risk assessments aren't carried out regularly across the system, leading to slow changes in internal controls and potential undetected losses. By the time these losses are discovered and reassessed, the business has already suffered damage.
- Telecommunication enterprises primarily identify emerging risks without considering potential ones. They've only identified and analyzed these risks through meetings without a dedicated department, and haven't properly implemented them (80% of the businesses surveyed haven't estimated the cost of risk prevention and control effectiveness).
- Besides, 88% of managers in construction businesses lack knowledge about risk management and lack the tools to quantify risk, mainly because most managers are technically skilled. Therefore, their approach to risk is quite rigid and still subjective. When they've made and chosen a risk response plan, they haven't considered other risks that might occur from choosing that plan.

Regarding Control Activities

- Only 63% of construction businesses have risk assessment reports in place, but they're not really comprehensive.
- The auditor isn't truly independent from the executor in some tasks.
- There's still a situation where access rights are shared (in 85% of businesses, employees can edit and delete data on the computer system).

Regarding Media Information

- The department responsible for receiving and sorting information isn't really effective. There's still a situation where the provided information is unreasonable and not useful (35% believe that the current information channels do not ensure that the information provided to the outside and the information received from the outside is reasonable and useful for users).

- Due to the situation of shared access rights, it's easy for unauthorized people to access information.

Regarding Supervision

In today's construction businesses, supervision is primarily carried out through regular mutual monitoring among employees and from managers. All findings are reported to higher levels and appropriate corrective measures are taken. However, in 65% of businesses, the periodic evaluation activities of managers have not been assessed for effectiveness and efficiency by the control system and adjusted to suit different periods.

5. Conclusion

The study has introduced the most general concept of internal control and its factors in businesses according to COSO 2013. The article's content shows an approach that includes the five factors of internal control, aligning with the research direction. The results indicate that the current internal control factors in Vietnamese telecommunications enterprises have not yet met user expectations. To enhance effectiveness and efficiency, Vietnamese construction enterprises should improve their internal controls. These enterprises should also establish more supervisory mechanisms to control the execution of power by subordinates or representatives. Regular meetings should be held to address lingering issues. Businesses need to proactively develop plans to deal with operational risks.

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