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Research on Internal Control System of Vietnam Construction Companies

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Abstract

Establishment and operation of an effective internal control system plays a key and crucial role to fulfil those targets. The good internal control system will help to identify and prevent the risks of frauds and impairments in order to minimize losses, improve efficiency and achieve the set

goals. This research aims to investigate the reality of the internal control system in Vietnam construction companies and provide suggestions and recommendations to enhance the system in the enterprises.

Keywords: Internal Control, Companies, COSO

1. Introduction

In recent years, the role and importance of internal control systems for businesses has been increasing. The internal control system has become a key factor in the development of enterprises. An effective internal control system will prevent potential risks and weaknesses; minimize losses, improve efficiency, and achieve goals in enterprises. Based on the summary of relevant domestic and foreign studies, and the theoretical framework of internal control from the perspective of COSO, this article presents the research on the current state of the internal control system in Vietnamese construction enterprises to supplement the research on the internal control system at a specific group of enterprises.

2. Literature Review

Research on internal control (IC) has been carried out for a long time, there have been many scholars and research institutions who have different views on internal control. One of the first concepts of IC was introduced by the US Federal Reserve in 1929, then the concept of a formal internal control system was mentioned in the Securities Trading Act which states the role of the internal control system in ensuring the objectives of the unit in 1934. By 1992, the number of companies in the United States increased very quickly, and fraud was also constantly increasing, causing great damage to the economy. Therefore, to prevent fraud, several organizations have been established including the Committee of Sponsoring Organizations (COSO). COSO is sponsored by many organizations such as the American Association of Certified Public Accountants (AICPA), the American Association of Accountants (AAA), the Financial Administrators' Association (FEI), the Internal Auditors' Association (IIA) and the Association of Management Accountants (IMA). It also promulgated the standard theoretical framework for internal control. The COSO report is the first systematic study on IC, and is the foundation for the theory of modern IC. The new point of the report is that it has identified the components of the internal control system and the specific criteria to evaluate it. The COSO report is considered a basic theoretical framework for researchers to continue to develop theoretical frameworks and applications in specific business conditions and environments. After the publication of the COSO report in 1992, there has been a series of research and development, expanding the applications of the COSO report in many different fields such as enterprise risk management, information technology, small businesses, banking sector, independent and internal auditing...

In addition, the research on internal control in several other aspects has also been interested and mentioned by many scholars. Some studies on the influence of internal control on the effectiveness and effectiveness of activities such as the study of Ashbough-Skaife *et al.* (2006), Bryan and Lilien (2005), Lin and Wu (2006), Shenkir and Walker (2006), Hammersley (2007). In the field of internal audit, some case studies can be mentioned such as the study of Victor Z. Brink on "Modern internal audit -evaluation of activities and control systems" and the study of O. Ray Wittington and Kurt Pany (1995) on "Principles of auditing". In addition, studies on the relationship between internal control and corporate governance by some other scholars such as Anthonny, R.N and Dearden, J. Bedford (1989); Yuan Li, Yi Liu, Youngbin Zhao (2006). The authors believe that internal control has a market-oriented role in enterprises and internal control has an impact on the development of new products of enterprises.

In addition to international studies, in Vietnam, studies on the application of the internal control system in a specific unit in industries are of interest to many authors such as (1) Pham Binh Ngo (2011) with the topic "Organization of the Internal Control System in the cost estimation units under the Ministry of National Defense"; (2) Nguyen Thu Hoai (2011) on "Completion of the Internal Control System in Cement Manufacturing Enterprises of Vietnam Cement Corporation"; (3) Bui Thi Minh Hai (2012) on "Completion of the Internal Control System in Garment Enterprises of Vietnam"; (4) Nguyen Thi Lan Anh (2013) on "Completion of the Internal Control System at Vietnam Chemical Corporation".

Thus, it can be seen that studies on internal control have been studied by many scholars. The studies are also quite diverse and cover many different aspects and aspects of internal control, such as studies on theoretical templates, internal control studies associated with operational efficiency, and research on the elements of the internal control system... These studies play an important role as a foundation and premise for further studies on internal control.

3. Theoretical Framework

Although there have been many studies on Internal Control, the view of the Committee of Sponsoring Organization (COSO) is widely used and accepted. In 1992, COSO introduced the concept of internal control in a report published under the title "Internal Control – Intergrated Framework" and defined: "Internal control is a process, influenced by the Board of Directors, managers and other members of the organization. It is designed to provide reasonable assurance to achieve the following objectives: (1) Efficiency and effectiveness of the operation, (2) Reliability of the Financial Statements, and (3) Comply with relevant laws and regulations. Also, according to the report of COSO in 1992, an IC system consists of five components: (1) Control environment, (2) Risk assessment, (3) Control activities, (4) Information and communication, (5) Supervisor. Inheriting the views of the 1992 report, the 2013 COSO report has expanded and added 17 interpretive principles to the basic concepts related to each of the aforementioned constituent elements.

Control environment: is a set of standards, processes, and structures that provide the basis for the implementation of internal control throughout the organization, is the conscious foundation, is the culture of the organization, reflects the general nuance of an organization, affects the sense of control of all members of the organization. The control environment includes the following elements: (1) Integrity and ethical values, (2) Commitment to competence, (3) Board of Directors and Audit Committee, (4) Management philosophy and executive style of managers, (5) Organizational structure, (6) Delegation of powers and responsibilities, (7) Personnel policy. According to COSO 2013, the Control Environment consists of five principles: (1) Commitment to honesty and compliance with ethical values; (2) The Board of management must demonstrate independence from the manager and implement the supervision of the design and operation of the internal control system; (3) The manager under the supervision of the BOM should establish an organizational structure, reporting process, delimitation of responsibilities and powers to achieve the objectives of the unit; (4) The unit

must indicate a commitment to the use of competent personnel through recruitment, maintenance and development of human resources following the objectives of the unit; (5) The unit should require responsible individuals to report on their responsibilities in meeting the objectives of the organization.

Risk assessment: Every organization faces risks from inside and outside the organization. Risk is defined as the likelihood that an event will occur and affect the achievement of objectives. Risk assessment is the process of identifying and analyzing risks affecting the achievement of objectives, thereby creating a basis for identifying ways to manage risks. According to COSO 2013, the risk assessment consists of four principles: (6) The unit must establish clear and complete objectives to identify and assess the risks arising in achieving the unit's objectives; (7) The unit must identify risks in achieving the unit's objectives, conduct a risk analysis to identify risks that need to be managed; (8) The unit should consider the types of potential fraud when assessing the risk to the achievement of the unit's objectives; (9) The unit should identify and evaluate the changes in the environment affecting internal control.

Control activities: Control activities are measures, processes, and procedures to ensure that management's directives are strictly enforced throughout the organization to minimize risks and facilitate the organization to achieve its goals. These are policies and procedures developed by businesses to help protect assets. Through operational control, managers are more confident that company assets are secured and financial reporting is reliable. According to COSO 2013, control activities comply with the following three principles: (10) The unit must select and develop control activities to contribute to limiting risks to achieve objectives within acceptable limits; (11) The unit selects and develops joint control activities with modern technology to support the achievement of the items targets; (12) The organizational unit implements control activities through the content of policies that have been established and implemented into specific procedures.

Information and communication: Information is necessary information to help each individual and department carry out their responsibilities. Communication is part of an information system but is designed to emphasize the role of communication. According to COSO 2013, information and communication comply with the following principles: (13) The unit collects, communicates, and uses appropriate and quality information to support other departments of Internal Control; (14) The unit needs to internally communicate necessary information, including objectives and responsibilities for Internal Control, to support the control function; (15) The unit needs to communicate to external parties about issues affecting internal control.

Monitoring: Monitoring is defined as a process of assessing the performance quality of an IC system over time. Supervision includes regular supervision and periodic supervision. It is often necessary to combine both regular monitoring and periodic monitoring to ensure the effectiveness of the internal control system. According to COSO 2013, the monitoring meets the following principles: (16) The unit must select, implement, and carry out continuous or periodic assessments to make sure that which components of internal control are present and operating; (17) The unit must assess and notify the weaknesses of internal control promptly to the responsible subjects

including managers and the Board of Directors to take corrective measures.

4. Current Situation of the Internal Control System in Vietnamese Construction Enterprises

In order to understand and evaluate the current state of internal control systems in Vietnamese construction enterprises, the author surveyed 96 enterprises in Vietnamese construction. The implementation of the survey is carried out through the use of surveys to investigate and collect information. The system of questionnaires in the survey is designed based on COSO's IC assessment question system combined with face-to-face interviews at some typical units. The research results on the internal control system in these units are as follows:

Firstly, in terms of control environment: The survey results indicate that businesses have paid attention to honesty and ethical values by promulgating documents regulating honesty and ethical behavior in the company or communicating through meetings, exchanges, or daily contact between managers and employees. Most businesses have communicated and instructed to concretize the ethical requirements, distinguishing what is a violation, what is encouraged and allowed, and what is not allowed. Most of the 62/96 companies, accounting for 64.5%, do not have the necessary skills and knowledge for each job position. There have been some companies that have built regulations in this regard, however, it is usually large enterprises with a high level of job specialization. All surveyed companies have not yet established an independent audit committee. The control functions at the companies are mainly performed by the supervisory board (SB) and the Internal Audit Board of the units. The survey results indicate that in the course of operation, only 35/96 companies, accounting for 36.4%, said that the supervisory board has regularly checked and controlled the activities of the company. The control issues of these companies are quite comprehensive and include operations related to stages and cycles such as buying, manufacturing, selling, and some other issues such as recruitment and financial reporting. Regarding the degree of independence of the composition of the Board of Management, the survey results indicate that 100% of the companies have members of the Board of Management who are not on the Board of Management. Thus, the level of independence of the Board of Management and the Board of Directors is quite high. The number of members of the Board of Management who are members of the Board of Management is about two people, usually including the Director or General Director. However, 100% of the companies do not have independent board members. The survey results indicate that the majority of companies (78/96) assess that managers often accept a high level of risk in business activities. In addition, the survey results indicate that the majority of companies (78/96 companies) account for 81.2%, and managers do not regularly put pressure on employees to complete assigned tasks. Through the survey, it can be seen that the organizational structure and several departments are suitable for the size, functions, and operational characteristics of the companies. The organizational structure and several departments are suitable for the size, functions, and operational characteristics of the companies. The survey results indicate that many companies have not defined clearly the rights and responsibilities of each employee. The companies only have defined clearly

the rights and responsibilities of the leaders. In addition, the 82 companies surveyed assessed that the duties and authorities of the departments were clearly defined and had no overlap or duplication and that the separation of responsibilities for employees created checks and monitoring by each other. However, 69/96 companies, accounting for 71.8% said that the company does not have clear disciplinary policies. When violations occur, they are not handled strictly, therefore errors or fraud cannot be prevented.

Second, in terms of risk assessment: The survey results indicate that almost all companies (89/96) have set common goals and objectives for each department. However, the level of linkage between the objectives of each department and strategic objectives is still limited, only 52/96 companies (54.1%) believe that there is a linkage, and the remaining 48/96 companies do not have a linkage. The survey results also indicate that 84.5% of enterprises regularly identify, analyze, and assess risks in their business activities. Through interviews and specific research in several companies, some of the main risks that construction enterprises face are risks of price fluctuations, exchange rates, interest rates, and policy risks.

Thirdly, in terms of control activities: Most companies review performance results and compare them with estimates or plans at both the top manager's review level and the department heads' review. The survey results indicate that the reviews of senior managers reached a rate of 100%, and reviews of department heads reached a rate of 86.9% of survey companies. Monthly, the review is carried out at the end of the month, and the companies review and re-evaluate the implementation of indicators such as revenue, profit, production output, and consumption output. The inventory of assets, supplies, and goods is also interested and carried out regularly. Regarding the division of responsibilities and separation of functions of asset preservation and accounting, the survey results indicate that 71/96 (73.9%) companies implemented, and the remaining companies have not done this work. Regarding the control of information processing, the implementing companies are still quite weak with only 32 companies, accounting for 33.3% of the effective control companies for input, output, and processing data. Companies that have not controlled this process account for a large proportion of 66.7% (64/96 companies).

Fourth, in terms of communication information: Through the survey, it was found that most information system companies have ensured that managers and employees understand the regulations and regulations issued, only a few information system companies have not met this requirement 11/96 companies (accounting for 13.0%). Through fact-finding, many companies evaluating information systems provided by the accounting department have not met the requirements for executive management activities of their managers mainly due to the analytical reporting system and management accounting reports. Survey results indicate that most companies have built information systems to help managers and employees clearly understand the rules and regulations issued by the company. There are a few companies whose information systems do not meet this requirement, 14/96 units (accounting for 14.6%). Through fact-finding, many companies evaluate that the information system provided by the accounting department does not meet the management

requirements of managers, mainly due to the analysis reporting and system of management accounting reports.

Fifth, in terms of monitoring: The survey results indicate that 79/96 surveyed companies have conducted monitoring policies, processes, and activities related to internal control, accounting for 82.2% of the total number of companies. In addition, the supervisory effectiveness of the supervisory board at most companies is still low, and the Board of Supervisors has not regularly evaluated the design and operation of internal controls. Supervision, reassessment of risks, and adjustment of controls to suit changes in business objectives and the external environment of companies are rarely implemented and applied. The survey results show that 82/96 (85.4%) companies do not perform and do not apply supervision for risk reassessment and adjustment of control and 75/96 (78.1%) companies do not periodically evaluate the effectiveness of control activities. These limitations can lead to a decrease in the effectiveness and efficiency of the internal control system over time and increase the risk of errors and fraud.

5. Comments and Discussions

Through the results of studying the situation of the internal control system of enterprises in Vietnam's construction, it can be seen that most companies promulgate documents regulating honesty and ethical behavior standards. The staff of the companies have trained in the right professional expertise suitable for the positions they take on. Members of the Board of Directors deeply understand all activities of the companies. The supervisory board has also performed the function of inspecting, controlling, and supervising the activities of the Board of Management and the board of director. The companies have developed policies on personnel management, and regulations related to personnel work that have been stipulated in the labor agreement. The issues of training and development to improve the qualifications of employees have been of interest to the companies. The companies have developed a risk identification mechanism that affects the achievement of their objectives and performance. Control activities have also been given importance. Every month, companies also regularly re-evaluate the achieved targets compared to the plan. Most companies have ensured that managers and employees are familiar with the regulations. The directives and orders of the managers have been conveyed to the employees. Supervision activities of the companies have been carried out by many departments from the senior level such as the Board of management, the Board of Directors, department level, and functions related to the supervision tasks. However, in addition to the advantages of the internal control system, there are also shortcomings and limitations. The companies have not developed specific regulations on honesty and ethical behavior in written form. Many companies have not specified the skills and knowledge for each job position in the unit. Inspection and control activities of the supervisory board over the activities of many companies are not regular. The planning of the companies is not specific and detailed to each job position, and most of them only plan for a few important targets and for departments directly related to production activities. Many businesses have not established an identification mechanism for external risks affecting business operations. Regarding control activities, many businesses have not implemented effectively the application of control software.

The periodic reporting system serving the management and operations of companies provided by the accounting department still does not meet the requirements of managers, especially in-depth analysis and information. management accounting. Internal information transmission is not timely and the feedback system from external partners has not been paid attention to in many businesses. The Supervisory Board has not regularly monitored activities to make timely adjustments. Reassessing risks and adjusting control activities to accommodate changes have not been taken into account. In addition, monitoring the implementation of ethical regulations has not been carried out in many businesses.

6. Some Solutions to Improve the Internal Control System in Vietnamese Construction Enterprises

Firstly, it is necessary to systematize and develop a system of specific regulations on ethical standards, permissible behaviors, and unauthorized behaviors for each department and position. Secondly, it is necessary to issue documents to specifically stipulate skills and knowledge for each job. These are the conditions and standards for recruiting and selecting suitable employees. Thirdly, The board of directors and supervisory board need to carry out control activities more regularly. Control activities performed by the supervisory board should be performed monthly instead of quarterly and annually. Fourthly, it is necessary to improve the capacity and moral quality of managers because this factor has a great influence on the effectiveness of Internal Control. Fifthly, the accounting department needs to provide a clearer analysis of the financial situation and business results. Companies need to research and apply the activity-based cost management model to improve cost management, thereby providing timely, clear, and specific information for managers to make decisions. Sixthly, enterprises need to deploy and establish channels to collect information from external subjects such as customers, suppliers, banks, and other subjects so that administrators have useful, multi-dimensional information for better governance and management. Seventh Companies need to reassess risks and adjust control activities to suit changing business goals and the external environment. In addition, the supervisory board needs to evaluate the design and operation of the internal control more regularly.

7. Conclusion

During the operation of enterprises, there is always a risk of errors caused by employees, managers, or third parties that damage and degrade operational efficiency. The design, construction, and operation of effective internal control is one of the extremely important measures to prevent and detect errors to minimize losses and improve efficiency to help the organization achieve its goals. The article has explored the current situation of the internal control system of enterprises in Vietnam's construction, pointed out the advantages, existence, and proposed solutions to help enterprises adjust to improve the efficiency of the internal control system in these enterprises.

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