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**PERFECTING INTERNAL CONTROLS IN
VIETNAMESE COMMERCIAL BANKS**

Major: Accounting

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SUMMARY OF DOCTORAL THESIS IN ECONOMICS

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INTRODUCTION TO THESIS' TOPIC

1. The rational of the thesis

Basically, internal control is an efficient management tool within an organization. The control designed and exercised helps managers efficiently achieve their business outcomes during a course of business' operations in various industries; It also contributes to the efficiency of a company's activities (Ramamoorti, 2003, [165]; Hermanson and Rittenberg, 2003, [112]); OECD, 2009a, b, [150], [151]; Senior Supervisors Group, 2009, [173]). Those findings rise the issues of internal controls underlying a variety of approaches, especially, the important role of internal controls getting business success.

Commercial banks are special corporations doing the money business and other areas related. This industry is complicated, takes higher potential risk affecting the optimal use of different sources – Efficiency, and gets planned operating targets – Effectiveness. The failures of banks in the world as well as either the corruptions or loss of some Vietnamese banks' businesses have taken bad effects on economy and political issues raised. Accordingly, it is essential that Vietnamese commercial banks pay attention to study any existing issues, assess these results and attempt to explain relevant reasons.

Basing on those analysis above, the topic of my thesis selected is ***“Perfecting internal controls in Vietnamese commercial banks”***.

2. Overview of researches concerning the topic

2.1. The oversea researches relating to the topic

According to the oversea studies, there are some relevancies under different categories following:

i). The general studies on internal controls and building control framework:

The best research on internal controls in general is the framework of an organization recommended by the *Committee of Sponsoring Organizations (COSO) – a body of Treadway Commission*. The COSO's Report on Internal Controls named, firstly launched in 1992 that is now globally accepted Framework Internal Control – Integrated Framework – which defined internal control as: A process, effected by an entity's board of directors, management and other personnel, designed to provide reasonable assurances regarding the achievement of objectives in the following categories: Effectiveness and efficiency of operations, reliability of financial reporting and compliance with applicable laws and regulations. The COSO 1992 Report continuously revised in 2004, 2009, 2013, and 2015. The newest amended report maintains major components comparing to COSO Report 1992. There had been the great change in the revised version of this Report 2015 that released 17 principles in accordance with 5 control components. COSO Report 2015 also kept those principles as well as those components under these previous reports, but this report closely focused on risk management and corporate governance.

Researches on internal control and relevant issues had been conducted in an unique operating areas, according to Gauthier, Stephen J (2006) [101]; Lakis, Vlacovas, Giriunas, Lukas (2012) [131]. D'Aquila, Jill M (2013) [91]. Some other findings of researches on internal controls' components found in publications by CHENG, Qiang; GOH, Beng Wee; and KIM, Jae Bum (2015), Karen A. Maguire (2014); Popescu, M. Dascalu, A. Bulletin (2012); Millichamp, A.H, (2002); Sultana R and Haque M. E. (2011) ([77], [127], [159], [144], [180]). Besides the COSO 1992, other frameworks for internal control such as the Criteria of Control Framework (hence CoCo) issued by the Canadian Institute of Chartered Accountants (1995) exist; Turnbull Report 1999 in the United Kingdom; Objectives for Information and related Technology model (COBIT) that does not replace COSO framework, focuses on information technology (IT) controls specifically designed for the IT environment and the COSO Enterprise Risk Management (ERM) framework extends to the broader area of enterprise risk management.

ii). The roles of internal controls in companies underlying in different industries:

Internal control closely related to a process of business management, influenced the development of new product in a company and directed the market of a company's outcomes (Merchant, K. A, 1985 [140]; Anthony, R. N and Dearden, J. Bedford, 1989 [52]); exhibited the relationships between internal controls and risk management (Laura F. Spira và Micheal Page, 2002 [132]; Faudizah, Hasnah and Muhamad, 2005 [96];

Robert R. Moller, 2005 [169]; Alvin A. Arens and James Loebke, 2000 [169]; Robert R. Moller, 2005 [50]; Internal controls affected the effectiveness and efficiency of a company's activities (Salehi et al., 2013 [170], Srisawangwong and et al., 2015 [179]); Michael Ramos, 2008 [142]. In the banking industry, researchers implemented studies on internal controls as a whole (Salehi, Mahdi; Shiri, Mahmoud Mousavi; Ehsanpour, Fatemeh, 2013 [170]) or other issues concerned (Srisawangwong, Papapit; Ussahawanitchakit, Phaprukbaramee, 2015 [179]; Qiang Cheng et al., 2015 [77]; Tseng, C.Y., 2007 [186]; Chirwa, E.W., 2003 [79]; Greenley, O.E. and Foxall, G.R., 1997 [106]; IFAC, 2012a [120]).

iii). *The quality of internal controls:*

Statements on internal control deficiencies are necessary that firstly required in the part 404 [171] of the Sarbanes – Oxley Act enforced in 2002. Some other researchers took findings about internal controls' quality in general such as Ashbaugh-Skaife et al. (2007); Bryan and Lilien (2005); Doyle et al. (2007b); Gee and McVay (2005) ([54], [70], [92], [102]). Other researches realized the interactions between internal controls' quality and other company's operations (Ashbaugh-Skaife et al., 2009 [54]; Ogneva et al., 2007 [152], Ettredge et al., 2006 [94]; Hogan and Wilkins, 2008 [114]); Hogan and Wilkins (2008); Krishnan (2005); Tang and Xu (2007); Mei Feng, Chan Li and Sarah McVay, 2009 ([54], [130], [182], [139]).

iv). *The measurement of internal controls:*

Researches on both the nature of internal control and its measurement done from different perspectives such as a popular approach (Heier, Dugan and Sayers, 2005 [111]), and the auditing approach of financial statements (Ashton, 1984) [56]; Onumah et al., 2012 [153]). For the assessment of internal controls' efficiency in an organization, COSO 1992 recommended evaluating internal controls in connection with key features of an effective internal controls; this assessment is a part of the internal control framework. In the revised report of COSO 2013, that is first time that has wrapped up all requirements contributing to internal controls' effectiveness: (i) one of 5 control components and 17 principles are together existence and continuity; (ii) all 5 control components concurrently carry on in an organization. According to Basel Statement, it said that internal control is effective if this control continuously fulfilled 13 principles suggested classifying into 5 components like the COSO Framework.

v). *Researches on internal controls in the banking industry:*

There have been few researches done on internal controls' issues in banking industry around the world. Although, some authors publicized findings about the particular aspect of internal controls, especially, internal control assessment in financial institutions: Xiaoli Liao, Tongjian Zhang và Mingxing Li (2011) [190]; Nitu (2002), Nagy (2005) ([148], [147]; Theofanis Karagiorgos, George Drogalas và Alexandra Dimou (2010) [184].

2.2. Internal publications related to the topic

Some researches on internal controls completed in Vietnamese organizations not operating in commercial banks: Building the system of internal control at Telecommunication Corporation by Ngô Trí Tuệ et al. (2004) [44]; at a special agent of the Ministry of Military by Phạm Bình Ngô (2011), in the industry of garment by Bùi Thị Minh Hải (2012), and at the Chemical Corporation by Nguyễn Thị Lan Anh (2014 ([39], [9], [2])). A few researches done relates to a given feature of internal controls like projects carried on by Phan Trung Kiên et al. (2012) [15], and Nguyễn Tố Tâm (2014) [39].

2.3. Conclusion of the void gap for my thesis

By using results of these analysis and appraisals above, I realized that there have been any researches publicized before on the topic of internal controls' assessment under control components in Vietnamese commercial banks. I made the decision to choose the void gap for my research.

3. Research objectives

The final goal of the thesis is to systematize points of view, to develop theoretical matters and to set up an appraisal model of actual internal control in Vietnamese commercial banks underlying 5 control components.

4. Objects and scope

4.1. Research objects

The research object is the 5 control components and their facts in Vietnamese commercial banks. The classification of control components under 5 categories follows the COSO Framework combining characteristics of commercial banks' operations, and requirements recommended in Basel I, II, III.

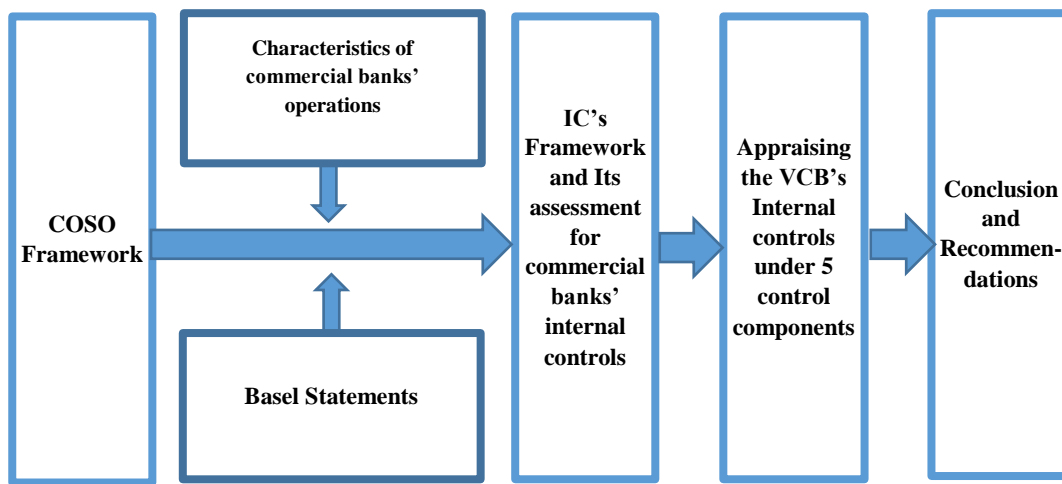
4.2. Research scope

The thesis focuses on internal controls within Vietnamese commercial banks under the auditing approach of internal auditor.

5. Research methods

To complete the thesis, I had used some different methods together to achieve these research objectives. These methods used are following: Benchmarking; Case study analysis; The analysis. Figure 1 following briefly exhibits the theoretical framework of the thesis.

Figure 1: The theoretical framework of the thesis



By mainly using the inquire of internal auditors in Vietnamese commercial banks, I gathered supporting data and analyzed this data in next step of thesis process. According to Phan Trung Kiên et al. (2012, 2017), they found that the assessment of internal controls is a major content of internal auditing works during an internal audit of Vietnamese commercial banks. ([15], [13]). Additionally, each Vietnamese commercial banks are required to build or reengineer an internal audit department. Since, I had enough chances to make a wide survey concerning the fact of Vietnamese commercial banks' internal control. I made the study on the fact of Vietnamese commercial banks' internal controls during the period from 2013 to 2016. A few contents done by using data collected in the earlier 2017. There had been 34 Vietnamese commercial banks surveyed in this period. I divided all banks into 3 different group under the amount of authorized capital for my research (Table 1).

Table 1: Classification and relevant data of banks under authorized capital

No.	Group's title	The driver of classification	Number of banks
1).	Group No. 1	Authorized capital is bigger than 20.000 billion	4
2).	Group No. 2	Authorized capital is bigger than 5.000, and less than 20.000 billion	14
3).	Group No. 3	Authorized capital is less than 5.000 billion	16
	Total		34

(Source: Author summarized and classified data relating to authorized capital of 34 Vietnamese commercial banks and basing on statements of State of Bank)

Author used the system of questions according to the COSO's 5 components to survey the fact of internal controls of Vietnamese commercial banks. Each component contained statements relevant to the

internal control component and respondents could indicate whether their bank has implemented certain control elements. A 'not true' response indicates that the control element has not been implemented.

If the specific control element has been implemented the respondents were requested to rate the perceived effectiveness of the control element on the five point likert scale (from one to five), with one being 'not true' - control element not present, two being 'not effective', three 'effective', four 'very effective' and five 'extremely effective'. The choice of a point on a scale from two to five also implied that the control element has been implemented or adopted in the bank. It is important to note that the responses indicating the presence of or use of the control elements do not imply that the system of internal control is neither effective nor not effective. Such responses (from two to five on the likert scale) only indicate the possible contribution toward the effectiveness of internal control systems.

Table 2: Number of years internal audit experience of respondents

No.	Number of years	Number of respondents	Percentage out of sample (93)
1.	Less than 3	6	6%
2.	3-5	15	16%
3.	5-10	30	32%
4.	More than 10	21	23%
5.	None	21	23%
	Total	93	100%

(Source: Summarized and computed by author)

Table 2 contributes to the reliability of the findings as all the respondents had substantial exposure to internal control systems. The seven respondents who have no internal audit experience are all Chartered Accountants (refer to Table 3). Due to this fact, the researcher deduced that Chartered Accountants have sufficient knowledge to make a valid contribution to the study.

Table 3 summarizes the professional qualifications of the respondents. It is important to note that respondents could choose more than one qualification being the reason why the total adds up to 123 instead of 93, the number of respondents of the study.

Table 3. Professional qualifications of respondents

No.	Professional Qualification	Number of responses	Percentage out of sample (93)
1.	CIA	18	19%
2.	Certified of state auditor	0	0%
3.	Certification in Control-Self Assessment	9	10%
4.	Information Systems Auditor	6	6%
5.	Chartered Accountant / Registered Auditor	57	61%
6.	Certified Management Accountant	3	3%
7.	Certified Fraud Examiner	3	3%
8.	Certified professional accountant	0	0%
9.	Certified public accountant	0	0%
10.	No professional qualification	12	13%
11.	Other	15	16%
	Totals	123	

(Source: Summarized and computed by author)

Table 4 provides a cross-tabulation of the number of year's internal auditing experience and the professional qualifications held by the respondents.

Table 4. Cross-tabulation of the respondents' number of years internal audit experience with professional qualifications

Years internal audit experience	Certified Internal Auditor	Certified Government	Certification in Control-Self Information Systems Auditor	Chartered Accountant / Chartered Certified Accountant	Certified Management Certified professional accountant	public accountant	No professional	Other	Totals			
5-10	12	0	3	3	18	0	3	0	0	3	6	30
Less than 3	3	0	3	3	12	3	0	0	0	0	6	21
More than 10	0	0	0	0	21	0	0	0	0	0	0	21
None	3	0	0	0	6	0	0	0	0	3	3	15
3-5	0	0	0	0	0	0	0	0	0	6	0	6
Totals	18	0	6	6	57	3	3	0	0	12	15	93

(Source: Summarized and computed by author)

6. The perception of the thesis

The thesis develops the theoretical issues related on the basis of COSO Framework and Basel Statement applying for commercial banks including: Creating foundations for designing and performing an effective internal control; building the appraisal model of internal controls in commercial banks that help Vietnamese commercial banks' management measuring and improving internal control deficiencies.

7. The thesis' structure:

The thesis includes 3 chapters.

CHAPTER 1: THEORETICAL BACKGROUND OF INTERNAL CONTROL IN COMMERCIAL BANKS

1.1. Internal controls and management

1.1.1. Internal controls in corporate governance

The concepts of governance and internal control are by no means new (Zannetos, 1964; Lee, 1971). Even the Bible makes explicit references to the rationale for installing internal controls and gives a number of examples of traditional controls, such as the restriction of access, the segregation of work duties and the importance of having honest and competent staff (Ramamoorti, 2003, [3]). In fact, research on the historical development of internal controls shows that signs of internal control can be found in the early duration.

Accordingly, it seems that already then "business managers" had established a system of controls where certain accounting duties were segregated in order to prevent fraud and protect assets. Traditionally, the rationale behind effective governance and control is closely related to the custody and protection of assets. Fama & Jensen (1983) [126]. Adam Smith (1776), indirectly pointed to the important roles of controls. This traditional free market view is supplemented by the stakeholder-view where additional parties are included in the governance relationships (Bhasa, 2004, [8-9]; Schachler, Juleff, & Paton, 2007, [624], Cadbury Code 1992 [172]; OECD, 1999, [11]; Lazarides and Drimpetas, 2008, [133])

There have lately been loud calls for a better governance of firms. According to Hermanson and Rittenberg (2003) these loud calls for improved corporate governance may be divided into three key drivers (Power, 1997, [160]). Control lies at the heart of academic fields such as organization, management control, management accounting and auditing. Academic fields which, with regard to control, exhibit significant overlap (Merchant and Otley in Chapman, Hopwood, & Shields, eds. 2007, pp. 786-787; also see Power, 2007, p. 62) but remain fragmented into their respective research domains (Maijoor, 2000, p. 102; also Merchant and Otley in Chapman, Hopwood, & Shields eds. 2007, p. 788; Spira and Page (2003) [178]);

COSO (2004) [160]). A management control system that will be used to maintain or alter organizational activities based on information received (Simons, 1991, p. 49). Tannenbaum (1968, p. 3), an influential writer within the area of organizational control. The necessity of control systems and internal controls may thus be explained by the need for convergence, congruence and conformity based on certain assumptions about human nature. The necessity of control systems and internal controls may thus be explained by the need for convergence, congruence and conformity based on certain assumptions about human nature.

1.1.2. The nature of internal controls

Internal control has expanded its domains significantly to form an integral part of overall management control system, and furthermore the corporate governance system of firms (Maijor, 2000; Merchant & Oxley in Chapman, Hopwood, & Shields eds., 2007). Today, internal control today is therefore as much an object and tool for the director and manager, as for the accountant and assurance specialist.

Tannenbaum (1968) Tannenbaum refers to control as “any process in which a person or group of persons or organization of persons determines, that is, intentionally affects, the behaviors of another person group or organization”. Mintzberg re-enforces this view when he refers to the levers of power as means or systems of influence. These can then be used by an influencer to control decisions and actions (Mintzberg, 1983)

The concept of internal control has been developed along with the theory and practice of accounting and auditing and its stated objectives (Brown, 1962). In this context, internal control has traditionally been regarded as a means of ensuring reliable bookkeeping procedures as well as a way of preventing and detecting fraudulent activity (see Lee ed., 1988). There has been a century of debate as to its definition and content (Heier, Dugan, & Sayers, 2005) and official definitions have often proven to be controversial (Hay, 1993). In 1992 the COSO (Committee of Sponsoring Organizations of the Treadway Commission) released their now globally accepted framework Internal Control – Integrated Framework – which defined internal control as: A process, effected by an entity’s board of directors, management and other personnel, designed to provide reasonable assurances regarding the achievement of objectives in the following categories: Effectiveness and efficiency of operations, reliability of financial reporting and compliance with applicable laws and regulations. The COSO differed from earlier definitions in at least two vital aspects. Firstly, it focused on process instead of system or structure, highlighting the loose and flexible character of internal control as opposed to it being a static and rigid system (see Kinney, 2000). Secondly, the objectives of internal control now included other objectives in addition to the financial reporting quality objective. Different internal control definitions exist, but COSO has been widely diffused and now serves as a reference point for both managerial practices and regulatory designs around the world (Power, 2007).

Agency-theory and institutional theory is described and discussed. These theoretical perspectives may be important for readers to take note of since they explain the necessity for internal controls and also how they may adapt and evolve. These theoretical perspectives will also be applied when different themes, developments and issues on internal control are treated. The agency theory provides a primarily economic explanation for the design and form of control systems. The second theoretical orientation that will be described, institutional theory (Meyer & Rowan, 1977; DiMaggio & Powell, 1983), offers a contrasting explanation for the development and form of control systems and uses a perhaps more sociological approach (see Eisenhardt, 1988).

1.1.3. The extended concept of internal controls

Internal control has always had a direct relationship with risk. After all, as long ago as in 1892 and 1905, Dicksee recommended that accountants should look for the system’s weakest points where risk exposures of accounting errors were greater. Later, the COSO included risk assessment as one of five internal control components. With the release of Enterprise Risk Management – Integrated Framework (COSO, 2004) however, the link between risk management and internal control has been made more explicit.

Researchers have discussed this development in terms of the reinvention of internal controls and its mutation into general risk management (Spira and Page, 2003; Power, 2007). Power observes that “the COSO approach requires that the design and operation of controls be linked to, and follow from, a prior

process of risk assessment, control design is explicitly related to the assessment of risk to entity objectives and sub-objectives”. Recent thought papers commissioned by COSO on how organizations embrace and embed enterprise risk management (COSO, 2011), the crucial role of the board of directors as they oversee risk management practices of firms (2009b, 2010a) and the way in which firms more effectively may identify and manage emerging risks also underscore the link between risk management and internal control.

1.2. Internal Control Framework and its components

1.2.1. The acceptance of COSO’s Internal Control Framework in a company

Although the COSO 1992 has been criticized for being confusing or not providing adequate guidance for design and implementation (Shaw, 2006, p. 75; Gupta & Thomson, 2006, p. 33), it has undoubtedly received much attention all over the world and become a key conceptual and practical framework for involved stakeholders.

With the implementation of the Sarbanes-Oxley Act in the United States and its related Section 404-requirements, the SEC required that both management and auditors use an internal control framework that meets the criteria specified in Section II.B.3a of the Section 404 Final Rules. Gupta and Thomson (2006) point out that while the SEC recognizes the existence of other frameworks and internal control guidance, the COSO 1992 also satisfies the SEC criteria (p. 28). Moreover, the IIA (the Institute of Internal Auditors), the professional body for internal auditors around the world, states in their professional practices framework that it “believes that the most effective internal control guidance available today is the report Internal Control – Integrated Framework (2004).

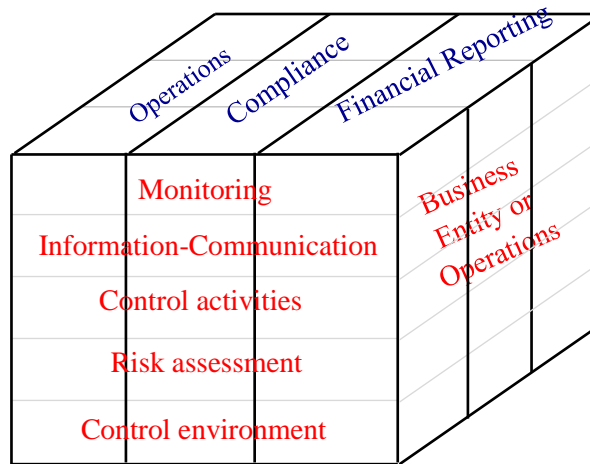
In connection with the increasing focus on risk management practices (Spira & Page, 2003; Power, 2007; Fraser & Henry, 2007; Mikes, 2009), in 2004 COSO issued a comprehensive framework on enterprise risk management (henceforth COSO, 2004). The COSO has also issued internal control guidance for smaller firms. This guidance however was directed towards the implementation of internal control over financial reporting and the specific issues facing smaller types of companies (COSO, 2006). Finally in 2009, after issuing a discussion document on monitoring controls, the COSO finalized a guidance document in this area (COSO, 2009a). More recently guidance and thought papers have also been issued on risk management oversight for board of directors (COSO, 2009b, 2010a), how firms may better identify and manage emerging risks (COSO, 2010b) and how organizations may more effectively embrace and embed entity-wide risk management practices (COSO, 2011).

COSO 1992 later became the basis for the Statement of Auditing Standard (SAS) No. 78 that subsequently amended SAS No. 55, recognizing the definition and description of internal control found in the COSO (Heier, Dugan, & Sayers, 2005,[45]). The earlier definition of internal control, which included the control environment, the accounting system and the control procedures, were thus replaced with the internal control components defined by the COSO. It is safe to say that COSO 1992 has been widely diffused all over the world and now constitutes a benchmark for firms struggling with designing, managing and overseeing their systems of internal controls. As we will see later in Sect. 5.2 COSO has also provided inspiration for Swedish guidance on internal control produced by regulatory bodies. According to IIA (2004) [122], COSO 1992 exhibited the modern definition of internal control and integrated all relevant operations pertaining to financial and non-financial operations.

1.2.2. The components of COSO’s Internal controls

The following sections highlight the specific control elements under each component which, if implemented and operating as originally intended, will result in an effective internal control system (COSO, 1992, 2013, 2015; AICPA, 2005). This study tests the perceptions of internal auditors on the effectiveness of the specific control elements listed under each of the COSO components in their organizations. The AICPA has created a comprehensive tool for control committees to obtain reasonable assurance on whether controls under the five interrelated components are operating as intended. AICPA (2005) and COSO (1994) list attributes which may contribute towards an effective internal control system. The following section provides a discussion of these attributes of the COSO components (Figure 1.1).

Figure 1.1. COSO Framework – The relationships among control components, targets, and units



(a) Control environment: (i) *Integrity and ethical values:* An organization should have a moral code of conduct and this should explain what is considered to be best business practice and what constitutes good ethical behavior; (ii) *Commitment to competence:* The level of skills needed for a specific job should be outlined for the job incumbent and management in each department should ensure that these *Board of directors and the audit committee:* A charter should be established outlining the audit committee's responsibilities and should be reviewed every year and approved by the board; (iv) *Management philosophy and operating style:* The accounting departments should be seen as a group of professionals who bring expertise to the business; (v) *Organizational structure:* Key managers such as financial managers, general managers and operation managers should be given clear description of what their responsibilities entail. The organizational structure should be applicable to the size of the organization; (vi) *Assignment of authority and responsibility:* All managers and supervisory personnel should have a copy of what their job entails. Authority should be given to appropriate persons in order to exercise responsibility as outlined in the job descriptions; (vii) *Human resource policies and procedures:* There should be written policies in place outlining procedures for employee selection and termination together with policies for staff training. Clear written policies should be in place outlining for employees the actions that will result in promotion, salary increases and when they will be compensated for certain actions.

(b) Risk assessment: The organization should consider all risks, internal and external, that could prevent objectives from being achieved. Furthermore, risks that financial statements could be materially misstated should also be considered. Management should estimate the significance of risk, determine the likelihood of risk occurring and determine the impact of the identified risks on the organization. Lastly, it is important for management to identify controls to mitigate the identified risks (AICPA, 2005; COSO, 1992, 1994, 2015). COSO recommended 3 approaches following: i) *Risk of external factors;* ii) *Risk of internal factors;* iii) *Risk under different level of operation.*

(c) Control activities: All policies and procedures should be written in the form of manuals and the procedures for each activity in the organization should be accordingly applied. Furthermore, these established policies and procedures should be reviewed and updated on a regular basis. Supervisory personnel should review the functioning of controls with reference to the relevant procedure. Any deviations identified from the procedure should be communicated to relevant parties and corrected as soon as possible. Custody over assets should be separate from the accounting function. Furthermore, operational and record keeping responsibility should be separate from each other. Physical control over assets should exist, for

example, good gate control. All policies and procedures should be subject to review by an independent party, for example the IIA (AICPA, 2005; COSO, 1992, 1994, 2015).

(d) *Information and communication:* A process should be in place to identify relevant information from external sources which could have relevance to the organization. Procedures should be established to ensure that reporting deadlines are met; ensuring relevant information is communicated to the appropriate level in a timely manner and in a format that will facilitate easy analysis of the data. New information needs should be identified and implemented. A process should exist to capture and file complaints and errors to prevent them from happening again in the future. In addition, procedures should be in place explaining what employees should do if they suspect any wrongdoing and who the relevant persons are to whom this should be communicated.

(e) *Monitoring:* Employees should be aware that the onus is also on them to communicate any deficiencies in the prescribed controls. Furthermore, organizations could use customers to identify certain weaknesses in the system by, for example, examining customer complaints and conducting customer satisfaction surveys. Management should take corrective action on recommendations made by the internal audit activity. Furthermore, the internal auditors should do follow-up audits to ensure management implemented agreed changes. Organizations should rely on the IAA for effective monitoring of controls if such an activity exists. Furthermore, organizations should use exception reports to identify any deviations from policies and procedures and use reports generated by operating personnel as a tool for identifying deviations from policies and procedures (AICPA, 2005; COSO, 1992, 1994, 2015). COSO illustrated some examples of the Monitoring conducting controls such as: (i) Normal function of operating management; (ii) Communication of external parties; (iii) Business structure and monitoring; (iv) Inventories and asset reconciliation.

1.3. The framework of Internal controls for commercial banks

1.3.1. General features of commercial banks' operations

Commercial banks basically are businesses serving a variety of services. They also concentrate on some types of fundamental transactions such as cash receipts, loan agreements and payment service. As long as products of a financial institution, banks' operations are divided into 3 dimensions following: (i) **Front Office:** In providing the following summary of business areas, it is important to recognize that there is no single blueprint for how banks organize their business areas and different institutions will set up different structures according to their own perceived strengths and business strategies. The function cover some major operations such as sales and trading, capital markets, corporate and investment banking, trade finance, research, private equity, and fund management. (ii) **Middle Office:** the middle office functions of a bank essentially serve as a link between front and back office. Originally the term was used to refer to administration functions which provide support to the trading and marketing personnel and act as liaison points for back office functions such as Operations. However, the term is now often used to incorporate key control functions such as Product Control and Risk Reporting, whose primary contact is often the front office business heads. (iii) **Back Office:** There are a number of departments which form the standard back office functions of a bank. Whilst the roles of these departments can vary from bank to bank, the following is a brief precis of their main responsibilities: operations, financial controls, credit, legal, compliance, information technology, taxation, and new business.

Banks are potentially exposed to the following areas of risk following: (1) Market risks - These risks reflect the bank's exposure to adverse movements in market rates and prices; (2) Credit Risks - These risks record the potential loss arising from the bank's counterparties failing to pay amounts due to the bank ; (3) Operational Risks - This area is currently highly topical given the focus of regulators in attempting to allocate capital requirements based on levels of operational risk; (4) Legal and Regulatory Risks - A bank's adherence to the laws, rules and regulations of the jurisdictions in which it operates is obviously of paramount importance; (5) Continuity Planning Risks - This refers to the ability of the institution to maintain its business in the event of a crisis; (6) Image/Reputation Risks - Confidence in the financial and

management soundness of banks is a critical factor in maintaining levels of business; (7) Fraud Risk - This potential risk is, in a way, a sub-set of operational risk, though impossible to quantify. For each type of risk identified, bank has to confirm that it designed and implemented appropriate controls effectively. Basel stated that internal audit is a continuity of controls over internal controls and internal assessment. As analysis, internal controls in banks is typically standardized. Therefore, the application of COSO Internal control Framework along with Basel Statement's rules as well as the installation of individual internal control framework for banks will be reality aiming at the formulation of relevant internal controls and improving banks' operating efficiency. To get understanding of these features helps author identifying concerning factors in the assessment of Vietnamese banks' internal control effectiveness.

1.3.2. Factors affecting the settlement of internal controls in commercial banks

Designing internal controls in any organization plays more important role that impacts on the maintain of the appropriateness and effectiveness of internal controls. Many researches done confirmed the differences in different organization's internal controls (Power (2007 [160]. Kinney (2000), [128]. Rae and Subrananiam (2008) [162]; Mikes (2009) [143]; Gupta, P. P., & Thomson, J. C. (2006), [107]; Chenhall (2007) [78]). These findings in researches publicized listed factors affecting the settlement of internal controls under following categories: (1) The environment of rules (COSO (2009c); Grant Thornton (2009a), ([87], [105])); (2) Professional standards and frameworks (Power (2007) [160]; (3) Văn hóa kinh doanh: Chenhall (2003) [78]. Pfister (2009 [157]); (4) Industrial characteristics (Cain (2009) [71]; Beasley, Clune and Hermanson (2005); Fraser và Henry (2007) ([60], [98]); (5) Likelihood of risk (FRC (2005) [99]; Chenhall (2003) [78]); (6) Objectives and strategies (FRC (2005) [99]. Chenhall (2003) [78]; COSO (2009c) [87]); (7) Expected risk (COSO (2004 [83]; Hofstede (1984) [113]; Chenhall (2003) [78], OECD (2009a, 2009b); Birkenshaw & Jenkins (2009), ([150], [151], [66]); (8) Viewpoints of management (Holmes, Langford, Welch and Welch (2002) [116]. Beasley, Clune và Hermanson (2005) [60]. COSO (2009c) [87]); (9) Business scope closely relates to particular features of internal controls (Wood (2009); Beasley, Clune và Hermanson (2005) [58]. COSO (2006) [84]); (10) Planned targets (Trenerry (1999) [185]. PCAOB (2007) [155]). Internal controls should cover both financial or non-financial activities and other objectives excepting the task of financial reporting (OECD (2009a, 2009b); Birkenshaw & Jenkins (2009) ([150], [151], [66]). Picket (2001) [158]).

1.3.3. Basel Framework applies for banks

Basel committee built and globally revised generally accepted standards on supervising banks. Accordingly, internal control is a group of regulations, policies, processes, internal rules, and organizational structure that are appropriately set up in a financial institution or a branch of a foreign bank in order to prevent banks from risk, to detect and solve issues related on time. Basel framework aims at 3 major objectives including tasks of operation, information, and compliance. The statement released 13 general that is a framework of internal controls' assessment in financial institutions. These principles are necessary for banks' internal controls. 13 principles are classified into 5 categories following: (1) Supervising management: 3 principles included; (2) Definition and risk assessment: 1 principle classified; (3) Control activities and segregation of duty: 2 principles attached; (4) Information and Communication: including 3 principles; (5) Monitoring and editing activities: 4 principles.

1.4. Assessment of commercial banks' internal controls

1.4.1. The nature of internal controls' assessment

The evaluation and assessment of internal controls is perhaps the most frequently occurring theme in existing research on internal controls. The importance of internal control evaluation has been highlighted in philosophical texts on auditing (Flint, 1988, [97]); While the evaluation of internal control is an important part of the auditing process, it is also becoming increasingly important for managers and directors of firms (Changchit, Holsapple & Madden, 2001, [74]; Mock, Sun, Srivastava & Vasarhelyi, 2009, [146].

As it is a part of the audit process, the assessment of internal controls forms part of professional guidance for external auditors through for example international audit standard 500 (IAASB, 2006, [119])

and internal auditors through performance standard 2120 (IIA, 2004, [122]). Both quantitative and qualitative approaches are valid for internal control assessments and no required standard format requirement exists (Bierstaker & Thibodeau, 2006, [64]). Conventionally however, auditors have adopted more qualitative methods such as the use of questionnaires, checklists and flowcharts (Mock et al. 2009, [146]; Bierstaker, 2003, [63]). As a part of the audit process the auditor may choose to document and test certain key controls. If post- testing leads the auditor to assess that the control risk is high then substantive testing has to produce all the necessary evidence (Smith, 1972 [177]), on the association between internal control evaluation and audit sample size (Sherer & Turley, 1997, [175]). For internal auditors on the other hand, sufficient, reliable, relevant and useful information should be obtained (IIA, 2004, [80]; Clikeman, 2009, [119]). As mentioned earlier, the complex mode of procedure when assessing internal control together with its growing importance, has resulted in a number of studies on the subject. Since internal control evaluation is part structure and part judgment, prior studies have sometimes been categorized accordingly. These researches pointed out above it is crucial for management to be able to assess and evaluate internal controls, simply because “it is an organization’s management, not auditors, who bear ultimate responsibility for maintaining an effective internal control” (Brown (1962) [68]; Ashton (1974) [56]; Changchit, Holsapple & Madden, 2001, [74]). The study by Chang chit shows that decision expert systems would in fact support and enable managers to better assess and evaluate internal controls. The results from the studies (by Borthick, Curtis and Sriram (2006) [67], Hunton and Thiboudau (2009) [65]) are consistent with previous studies on the subject, and provide support for the idea that the more available knowledge is, the more usable it is in a judgment task.

1.4.2. The fundamentals of internal control assessment in commercial banks

1.4.2.1. The Internal Control Environment

The research by O’Leary, Iselin & Sharma (2006) [149] suggested that for the assessment and evaluation of controls, it is necessary to know something about the following: what internal control is, the different elements of internal control, how the different elements of internal control are related, and finally, the relative importance of each element or component. Rae và Subramaniam (2008) also claim that previous studies on internal control have placed little attention on how different aspects of the internal control system affect each other [162]. Fagerberg (2008) [92] and O’Leary, Iselin & Sharma (2006), [149] found that certain internal control elements (based on the COSO-model) were emphasized; one of which was the control environment. Additional research into exactly what are the most important and significant elements of internal control evaluation and their inter-relationship to each other appears to be needed however. Entity-wide controls include controls related to the internal control environment, risk assessments, centralized processing controls, monitoring controls, management override controls and significant policies (PCAOB (2007) [155], Goldberg (2007) [104]. Bannister, Engvall và Martin (2007) [58]). Studies on the association between internal controls and organizational citizenship also provide evidence for the vital importance of management’s attitudes and behaviors (Holmes et al. 2002, [116]; Gerkes, Van der Werf and Van der Wijk (2007) [166]). It is suggested that assessing and evaluating more sophisticated entity-level controls is a complex task (Lightle, Castellano và Cutting (2007) [44]; PCAOB (2009) [58]). However, there have been some appropriate ways of assessment (Callaghan, Savage & Mintz (2007) [72]; Gerkes, Van der Werf và Van der Wijk (2007) [103]).

1.4.2.2. The management’s concentration on financial statements

Gee and McVay (2005, [102]) found that, during the period 2002–2004, the material weaknesses in internal control were mostly made up of the internal control deficiency types. As a direct result of these requirements, a number of internal control deficiencies have been disclosed by firms and it is unlikely that these deficiencies would otherwise have been disclosed to the general public (SOX 2002). SEC in the US confirmed that internal controls pertain to objectives of financial reporting and exhibit the requirements under the COSO Report. SEC also recommended appraising internal controls in connection with definite objectives and foundation bases. SEC’s guidelines suggested apply for all public listed companies including commercial banks.

1.4.2.3. Assessing and Classifying Internal Control Weaknesses

Internal control disclosure requirement often prescribes that companies should maintain a sound and effective system of internal control. Raghunandan and Rama (1994), “stating that an internal control system

exists is very different from stating that such a system has been assessed to be effective” [94]. Sarbanes-Oxley Act (the Section No. 404) in the United States prescribe an effectiveness report on internal controls by both managers and auditors. The original guidance issued by the PCAOB (2004) through Audit Standard No.2 prescribes that control weaknesses should be classified into the following categories: control deficiency, significant deficiency and material weakness [154].

1.4.2.3. Approach to assess internal controls

The top-down approach of internal controls’ assessment has become a effective tool that is not only in the consideration of risk of material misstatement in the financial reporting, but it also helps managers doing other activities concerning controls in an organization. On the basis of the process, the assessment starts the “top” and goes down following a process’ steps. As the results, that helps assessors identifying the effectiveness of internal controls as well as areas needing focused on.

1.4.3. Assessing banks’ internal controls under COSO framework’s components

1.4.3.1. The factor of Control Environment

According to the factors, the assessment pertains to 6 contents following: (i) Integrity and ethical values; (ii) Commitment to competence; (iii) Management philosophy and operating style; (iv) Organizational structure; (v) Assignment of authority and responsibility; (vi) Human resource policies and procedures.

1.4.3.2. The factor of Risk Assessment

COSO Framework considers internal controls relating to organization’s objectives released and risks of objective achievement. According to COSO, the risk assessment component appraised by applying the process of risk assessment such as: establishing objectives; identifying of risk of objectives’ achievement; evaluating risk related; and managing risk.

1.4.3.3. The factor of Control Activities

The assessment of Control Activities bases on two major categories that are (1) key attributes of internal control activities in relation to the assessment of Risk Assessment, the appropriateness of individual bank’s features, the suitability of documented policies, the implementation of control procedures, and the emphasis on key operations due to the limitation of usable sources; and (2) a variety of control activities concerning the control framework of COSO and relevant issues such as the review of top manager, information processing, physical controls, and segregation of functions or duties.

1.4.3.4. The factor of Information and Communication

COSO pertains a broader description about the attributes of an effective system of information and communication. All descriptions closely connected with the assessment of internal controls’ effectiveness, especially, the relevance to the financial reporting. Since, it becomes a base for the evaluation of information and communication as a banks’ internal controls’ element under COSO Framework. Accordingly, it suggested that considers the use of integrated sources of information, the use of information under process or non-process based, consideration of top manager’s roles, the collaboration of risk assessment and management improvements, the consideration of formal or informal state of information, and the timing of information.

1.4.3.5. The factor of Monitoring

The COSO makes the following claims for the importance of monitoring: Over time, ineffective monitoring leads to control breakdowns which reduce the efficiency of the entire internal control system. Likewise, inefficient monitoring may limit an organization’s ability of focus finite resources in the areas of greatest risk, thus reducing its effectiveness. Two fundamental principles underpin the monitoring controls framework: Ongoing monitoring and separate evaluations enable management to determine whether the components of internal control continue to function over time. Internal control weaknesses should be identified and communicated in a timely manner to those parties responsible for taking corrective action and to management and the board as appropriate. At the end of the process of monitoring, a report of internal control deficiencies should be exhibited. When rating internal control weaknesses, their likelihood and significant should be considered where likelihood is the probability that a control will fail to detect or prevent a risk’s occurrence, and significance is the potential impact of the risk if it occurs.

CHAPTER 2: THE CURRENT SITUATION OF INTERNAL CONTROLS IN VIETNAMESE COMMERCIAL BANKS

2.1. The relationships between Vietnamese Commercial Banks' operations and internal controls

2.1.1. The establishment and development of Vietnamese Commercial Banks

The formation and development of commercial banks in Vietnam associated with the development of the banking system and banking laws. Prior to the reform, Vietnam's banking system was organized as a system-level bank, including the State Bank of Vietnam and a branch network from central to local levels. In 1986, starting with the Sixth Party Congress, Vietnam began implementing economic reforms. One of the important issues that need to be reformed is the banking system. On March 26, 1988, the Council of Ministers issued Decree 53 / HDBT on the organizational structure of the State Bank. Starting from the requirement to complete the two-level banking model, on May 23, 1990 the State Council issued the "Ordinance on the State Bank of Vietnam and the Ordinance on Credit Cooperatives and Financial Companies". Effective from 1 October 1990. On December 12, 1997, the National Assembly promulgated the Law on the State Bank of Vietnam and the Law on Credit Institutions. Continuing the trend of comprehensive reform of the banking system and operation, the National Assembly promulgated the Law amending and supplementing a number of articles of the Law on the State Bank of Vietnam effective from 1 August 2003 [34] and The Law on Credit Institutions Law Amending and Supplementing a Number of Articles of Law takes effect on October 1, 2004 [35]. By the end of 2010, Vietnam had a development bank, one of the social policy banks, five state-owned commercial banks and one state-owned commercial bank, and 37 banks 50 branches of foreign banks, five banks of foreign capital, five joint-venture banks, 18 finance companies, 12 finance leasing companies, 1 central people's credit fund, people's credit and microfinance institutions first [24]. Up to the beginning of 2017, after some restructuring of the banking system, our banking system has 57 banks and credit institutions, including 34 joint stock banks.

2.1.2. The operating characteristics of Vietnamese Commercial Banks affect internal controls

i). *The scope of Vietnamese Commercial Banks*: The scope impacts on implementation and achievement of planned targets. Some facts and figures related follow: In relations to organization of banks' branches: Until the end of 2015, there have been 9200 branches and transferring departments in nationally banking system. Some of them already have branches in oversea like Viettinbank, BIDV; About authorized capital: According to State Bank's Statements in 2015, the totals of Vietnamese commercial banks' authorized capital touch the value of 487 billion VND; About the total value of assets: the values of all assets of the bank system stated by the State Bank that was nearly 5.900 billion VND in 2015. The system of banks has banks with their assets over 500.000 billion VND that are Viettinbank, BIDV, and Vietcombank; About human resource: The banks totally have 198.000 people in which 90% of them directly does business.

ii). *The capital mobilization*: Commercial banks generally recruit capital from the first market (from enterprises and citizens) and the second market (from financial institutions managed by the State Bank). Until 2015, the mobilization of banks faced many difficulties. The mobilizing proportion of different banks has discrepancies individually and different scopes among 3 groups of Vietnamese commercial banks

iii). *The credit operations of Vietnamese Commercial Banks*: Although the banks faced more difficulties, they came over and achieved goals. The period from 2013 to 2015, the rate of bad debt reduced, but it increased in 2015.

iv). *The issues of bad debts of Vietnamese Commercial Banks*: Domestic enterprises had been positively affected by the crisis in 2008. Therefore, the banks' bad debts sharply increased, especially in 2012. The statement of the State Bank disclosure that the rate of bad debts recorded at 8,8% [24].

To manage debts in the bans, the State Bank issued the Decision No. 493/2005/QĐ-NHNN about the classification of debts, the installation of provision, and the use of this fund; Circular No. 02/2013/TT-NHNN and No. 09/2014/TT-NHNN guides the banks to classify bad debts under 5 categories. Additionally, the banks also classified and recorded relevant things according to IAS 39. The State Bank sated that some of banks such as

Agribank, Vietinbank, Vietcombank, Techcombank, MB, ACB, Sacombank, Vpbank, Eximbank all had the rate of debts catching upper 83% to total bad debts in its totals in the banking system [24].

2.1.3. Những qui định trong lĩnh vực ngân hàng tài chính ảnh hưởng tới kiểm soát nội bộ

There are some regulations related to banks and other operations concerned following: Revised Law on the State Bank and Law on credit organizations backdated on 01/01/2011; Circular No. 13/2010/TT-NHNN required the assurance rate of safety in credit organizations; Circular No. 19/2010/TT-NHNN changed Circular No. 13/2010/TT-NHNN; Circular No. 44/2011/TT-NHNN settled the requirements of internal controls and internal audit in credit organizations and foreign banks' branches; Decision No. 254/QĐ-TTg dated on 1/3/2012: The Prime Minister approved the project "The restructuring of the system of credit organization during the period of 2011-2015"; Circular No. 02/2013/TT-NHNN guided the classification of debts, provision settlement and the use of provision fund for solving credit risk; Circular No. 09/2014/TT-NHNN related to this issue; Circular No. 36/2014/TT-NHNN issued the limited level of assurance in credit organizations that backdated on 1/1/2015.

2.2. The current situation of the internal controls in Vietnamese Commercial Banks

2.2.1. Assessing the component of control environment in Vietnamese Commercial Banks

Table 2.2 depicts the responses received relating to the assessment of control environment in the banks.

Table 2.2: Respondents perceived effectiveness of the control environment

No.	Control elements	Responses in percentage					Totals
		1	2	3	4	5	
1.1.4	The bank has other policies addressing expected standards of ethical and moral behaviour	3%	19%	29%	39%	10%	100%
1.1.5	Management is prohibited from overriding established controls	19%	19%	26%	29%	6%	100%
1.1.10	Management demonstrates through actions its own commitment to the code of conduct	6%	29%	26%	35%	3%	100%
1.2.1	The level of competence and the requisite knowledge and skills are defined for each job in the accounting department	0%	19%	32%	39%	10%	100%
1.2.2	The level of competence and the requisite knowledge and skills are defined for jobs in the internal audit department	6%	16%	23%	52%	3%	100%
1.2.3	Management makes an effort to determine whether the accounting and internal audit departments have adequate knowledge and skills to do their jobs	6%	19%	29%	42%	3%	100%
1.3.1	The control committee's responsibilities are defined in a charter	3%	10%	32%	52%	3%	100%
1.3.4	The control committee approves internal controls' annual control plan	6%	6%	29%	45%	13%	100%
1.3.5	Control committee members are independent of the bank and management	6%	10%	26%	45%	13%	100%
1.3.6	Control committee members have the necessary expertise to serve effectively in their role	10%	6%	32%	42%	10%	100%
1.3.11	The control committee receives key information from management in sufficient time in advance of meetings to prepare for discussions at the meetings	6%	16%	35%	39%	3%	100%

(Source: Surveyed and computed by author)

The King III report recommends that boards of directors establish ethical values in a formal code of

conduct (IoD, 2009; Jackson and Stent, 2010). This is consistent with the findings of this research (refer to 1.1.4 in Table 3.4), as 39% of respondents perceive that policies that address expected standards of ethical and moral behavior are ‘very effective’ (refer to 1.1.4 in Annexure B). The King III report further recommends that the control committee ought to be skilled and experienced in order to fulfill its responsibilities (Jackson *et al.*, 2010). This corresponds with the findings mentioned above where 42% of the respondents indicated that the control committees of their banks have the necessary expertise to serve in their role and that it is ‘very effective’ (refer to number 1.3.6 in Annexure B). Jackson *et al.*, (2010) assert that control committees should also be independent. Respondents indicated (45%) that having independent control committees are ‘very effective’ (refer to number 1.3.5 in Annexure B). The King III report suggests that the control committee should approve internal audit’s annual audit plan (IIA, 2009; Jackson *et al.*, 2010). According to the perceptions of the respondents 45% indicated that when control committees approve internal audits annual plan, it contributes to an effective internal control system.

McKenna (2010) states that one of the most difficult tasks of control committees is to determine to what extent management can override controls. Most of the respondents (29%) indicated that prohibiting management from overriding controls are ‘very effective’ (refer to number 1.1.5 in Annexure B). It would seem that banks are striving to prevent management from overriding controls, especially if this is a challenging issue and, thus, a focus of control committees. An effective code of conduct contains a commitment from the board of directors; hence the CEO should give his approval to the code and provide reports on its effectiveness (Kramer, Peterson and Johnson, 2010). This was also supported by the findings of this research in that 35% of the respondents perceive that when management is prohibited from overriding controls, this fact, contributes to an effective internal control system.

The following control elements were regarded as ‘not effective’ or not present in the bank by most of the respondents: (i) when management overrides controls, it is brought to the attention of the control committee; 32% of the respondents perceived it as not contributing the effectiveness of the internal control system; (ii) employees understand the performance criteria necessary for promotion and salary increases; 32% and 29% respectively, of the respondents perceived it as not contributing the effectiveness of the internal control system; (iii) the use of an anonymous fraud hotline; 32% of the respondents have not adopted this control element; and (iv) employee acknowledgement annually that they have read, understood and complied with the code of conduct; 35% of the respondents have not adopted this control element.

2.2.2. Respondents perceptions on the effectiveness of risk assessments Vietnamese Commercial Banks

Table 2.3 wraps up some major indicators pertaining to the assessment of the component “Risk assessment” in the banks’ internal controls.

Table 2.3: Respondents perceived effectiveness of the risk assessment

No.	Control elements	Responses in percentage					Totals
		1	2	3	4	5	
2.1.	The bank considers risks from external sources	0%	16%	39%	35%	10%	100%
2.2.	The bank considers risks from internal sources	3%	19%	52%	19%	6%	99%
2.3.	The risk of a misstatement of the financial statements is considered, and steps are taken to mitigate that risk	6%	6%	55%	26%	6%	99%
2.4.	The risks associated with foreign/offshore operations are considered	13%	16%	39%	23%	10%	101%
2.5.	Management estimates the significance of risk	0%	13%	58%	26%	3%	100%
2.6.	Management assesses the likelihood of risk occurring	0%	16%	58%	23%	3%	100%
2.7.	Magagement assesses the impact of risk occurring	0%	16%	55%	26%	3%	100%
2.8.	Management take necessary action to manage risks identified	3%	23%	42%	26%	6%	100%

(Source: Summarized and computed by author)

For data point eight, 3% responded that management of their banks does not take the necessary action to manage identified risks. When management does take the necessary action, 23% of respondents responded that it is 'not effective', 42% responded that it is 'effective', while 26% indicated that it is 'very effective'. Only 6% responded that it is 'extremely effective' (refer to number 2.8 in Annexure A).

Most of the respondents indicated that all the procedures listed under risk assessment are 'effective'. This could be due to an increased awareness of the risk management process and the pressure exerted by boards and control committees, on internal auditors, as the strategic risk management process is currently considered to be one of the top five primary responsibilities of internal auditors (Cain, 2010). It is also considered to be a great challenge for control committees in the future (COSO, 2010; KPMG, 2010; Steffee, 2010). CEOs indicated that having better risk management is a valuable lesson learned during 2009 and 2010 (Cain, 2010); hence, most respondents indicated that the procedures under risk assessment are 'effective' in increasing the effectiveness of the internal control system. These responses could also be as a result of the events of the past decade that have led to banks adopting a more focused risk management strategy, moving away from 'silo' risk managing (Aghili, 2010; Sobel, 2010).

2.2.3. Assessing the information and communication component in Vietnamese Commercial Banks' Internal controls

Table 2.5 shows the respondent rate on the effectiveness of the information and communication in the banks' internal controls.

Table 2.4: Respondents' perceptions on the effectiveness of information and communication activities

No.	Control elements	Responses in percentage					Totals
		1	2	3	4	5	
3.1.	A process is in place to collect information from external sources that could have an impact on the bank and the financial reporting process	6%	23%	48%	19%	3%	99%
3.2.	Milestones to achieve financial reporting objectives are monitored to ensure that timing deadlines are met	10%	6%	61%	13%	10%	100%
3.3.	Necessary operational and financial information is communicated to the right people in the bank on a timely basis	0%	16%	65%	6%	13%	100%
3.4.	Necessary operational information is communicated to the right people in the bank in a format that facilitates its use	0%	13%	65%	13%	10%	101%
3.5.	Necessary financial information is communicated to the right people in the bank in a format that facilitates its use	0%	13%	61%	16%	10%	100%
3.6.	A process is in place to respond to new information needs in the bank on a timely basis	10%	10%	65%	13%	3%	101%
3.7.	There is a process in place to collect and document complaints to analyse, determine cause, and eliminate a problem from recurring in the future	7%	14%	55%	17%	7%	100%
3.8.	There is a process in place to collect and document errors to analyse, determine cause, and eliminate a problem from recurring in the future	3%	23%	61%	6%	6%	99%
3.9.	A process is established and communicated to stakeholders about how to communicate suspected instances of wrongdoing by the bank	13%	26%	48%	10%	3%	100%
3.10.	The accounting system composes of different classes of transactions	3%	6%	52%	32%	6%	99%
3.11.	The accounting system ensures completeness of records	3%	19%	48%	23%	6%	99%
3.12.	The accounting system ensures accuracy of records	6%	16%	48%	23%	6%	99%
3.13.	The accounting system avoids duplicate recording	6%	13%	55%	19%	6%	99%

(Source: Summarized and computed by author)

In relation to each bank's credit operations, this component closely connected with other internal controls' elements. Banks of Group No. 1 focused on establishment of the information that helps banks preventing them from damages of risk internally or externally. Banks of Group No. 2 concentrated on the information system coming from external parties that concerns their customers. Banks of Group No. 3 used various information according to different level of risk management.

2.2.4. Assessing the monitoring component in Vietnamese Commercial Banks' Internal controls

Table 2.6 exhibits the respondents received on the effectiveness of the monitoring component in the banks' internal controls.

Table 2.6: Respondents' perceptions on the effectiveness of monitoring in the banks' internal controls

No.	Control elements	Responses in percentage					Totals
		1	2	3	4	5	
4.1.	Personnel are required to sign off, indicating their performance of critical control activities such as performing reconciliations	10%	10%	58%	16%	6%	100%
4.2.	Employees understand their obligation to communicate observed weaknesses in design with the internal control structure of the bank to the appropriate supervisory personnel	10%	29%	48%	10%	3%	100%
4.3.	Employees understand their obligation to communicate observed weaknesses in compliance with the internal control structure of the bank to	10%	32%	45%	10%	3%	100%
4.4.	The bank relies on customer complaints to identify certain control weaknesses	23%	16%	45%	13%	3%	100%
4.5.	There is follow up on recommendations from the internal auditors for improvements to the internal control system	6%	19%	55%	13%	6%	99%
4.6.	The bank relies on the internal audit department for effective monitoring of controls	16%	3%	61%	16%	3%	99%
4.7.	The bank relies on exception reports to monitor effectiveness of controls	10%	10%	61%	16%	3%	100%
4.8.	The bank relies on operating personnel generated reports to monitor controls	10%	16%	58%	13%	3%	100%

(Source: Summarized and computed by author)

There are 8 factors pertaining to the assessment of monitoring component in the banks' internal controls. There have been a variety of application of monitoring in different banks resulting from their structure, internal controls, employees, etc.

2.2.5. Assessing the control activities component in Vietnamese Commercial Banks' Internal controls

Table 2.7 summarized the results surveyed in percentage under the rate of responses.

Table 2.7: Respondents' perceptions on the effectiveness of control activities in the banks' internal controls

No.	Control elements	Responses in percentage					Totals
		1	2	3	4	5	
5.1.	The bank has a process in place to ensure that controls as described in policy and procedure manuals are applied as they are meant to be applied	3%	26%	52%	16%	3%	100%
5.2.	Policy and procedure manuals document all important policies and procedures	3%	26%	42%	23%	6%	100%
5.3.	Policies and procedures are reviewed and updated on a regular basis	3%	27%	50%	17%	3%	100%
5.4.	Supervisory personnel review the functioning of controls	6%	23%	45%	23%	3%	100%
5.5.	Timely and appropriate follow-up action is taken on exceptions reports	3%	16%	48%	26%	6%	99%
5.6.	Custody over assets are separate from accounting	6%	19%	39%	29%	6%	99%
5.7.	Operational responsibility and record keeping responsibility is separated	3%	13%	48%	29%	6%	99%
5.8.	Physical control over assets exists	0%	19%	55%	23%	3%	100%
5.9.	There is independent checks on performance	10%	10%	48%	26%	6%	100%

(Source: Summarized and computed by author)

The results summarized say that the banks almost have effective control procedures. However, the component's effectiveness is difference among different banks. Group No. 1 generally applies basic methods for credit controls such as: the policies of customer, the policies of customer selection, and the segregation of the duty of the credit risk's management. Group No. 2 built a series of criteria in approving credit agreement concerning the normal group of customers or the limited credit granting of customers. Group No. 3 designed and conducted some policies together such as the credit policy, the allowance for credit risk, and the definition of interest rate's framework. This Group separates the controls of credit risk from overall credit management and restructure it on the basis of the model of three lines of defense. This model has been actually applied for two group at the lower level.

2.3. The brief assessments of the actual internal controls in Vietnamese Commercial Banks

2.3.1. Positive conclusions on the effectiveness of internal controls in Vietnamese Commercial Banks

Results almost express the good responses at the level of "relatively effective". As the results of findings, there have been some key following conclusions:

i). Policies that address expected standards of ethical and moral behavior 39% showing the way banks' top managers pay attention to this factor. Since, they creates the effective component and takes an effect on internal controls' effectiveness positively;

ii). Management prohibited from overriding controls 29%. This finding expresses a good trend to enhance banks' internal controls effectively, but it is not a high level implying a potential risk of ineffective control procedures.

iii). Management's actions demonstrating commitment to the code of ethics (35%).

iv). Management ensuring that staff in the accounting and the internal audit department has the knowledge and skills needed to do their jobs (39% and 52% respectively). It is proved that the existence of differences under two types of essential process connecting with internal controls' effectiveness in different banks.

- v). Audit committees' responsibilities should be defined in the charter 52%.
- vi). Audit committees should approve the internal audit plan 45%.
- vii). Audit committees should have the expertise needed to serve effectively in their role (42%).
- viii). Audit committees should receive key information from management in a timely manner in advance of meetings in order to prepare effectively for the meetings (39%).
- ix). Accounting principles should be chosen that are in the long-term interests of the organisation as opposed to the short-term maximisation of income.

Most of the respondents perceived the following as 'not effective': (i) When management overrides controls, it is brought to the attention of the audit committee (32%); (ii) Employees understand the performance criteria necessary for promotion and salary increases (29% and 32% respectively); (iii) Most of the respondents regarded the following as not implemented in the organisation: The use of an anonymous fraud hotline (32%); (iv) Annual employee acknowledgement that they have read understood and complied with the code of conduct (35%).

The findings are considered in the collaboration of internal controls and risk management, this positive effects of the banks' internal controls are as follows:

(1) Almost banks surveyed has established strategy that fits the risk managements together well. Large banks such as BIDV, Vietcombank, Vietinbank had created special policies to attract powerful resources. These banks' policies had made a good effect on the effectiveness of control environment under 2 dimensions following: (i) The implementation of laws, governmental policies, relevant circular issued by the State Bank ascertains and reduces the banks' risk to the acceptable level; (ii) Individual banks' policies launched meshes with their operating conditions. Since, it assists the banks to do right things and to do things right.

(2) The model that centralizes on risk management helps banks managing their internal controls effectively. Under Section 43 of Law of credit organizations, the banks implement controls over 3 lines of the model three lines of defense.

(3) The banks have developed the assessing process of risk based on the due care affecting the effectiveness of internal controls over risks.

(4) The system of internal control procedures has continuously improved, collaborated, and fully integrated in globe standardized regulation in banking sector in the world. The application of credit ranking system helps banks avoiding, preventing, protecting them from relevant risks efficiently.

2.3.2. Limitations or ineffectiveness of Vietnamese Commercial Banks' internal controls

The medium of the environment component computed on statistical data surveyed is 3.13. This value sits on the gap of "hybrid" expressing this component might positive impact or make negative results on the banks' internal control effectiveness. Therefore, enhancement of this component could lead to improve the internal control effectiveness in the banks.

For the risk assessment in the banks' internal controls: The medium is 3.16 of "may be effective". The same trend comparing to the results of control environment above. It suggested that banks' internal control can be more effective if they focus on changes of this factor.

Banks can improve its control effectiveness by taking an effect on this factor.

The component of monitoring has low value of the medium (2.81). However, it still sits on the "hybrid" gap. Since, it also shows that banks need to change this factor better. The assessment done by internal auditor implies the negative effect on banks' internal control effectiveness. This component should be paid attention to. Banks should regard this element as a priority factor in accordance with the banks' internal control effectiveness.

The consideration of control activities exhibits that this component as the same as the first two factors. Accordingly, banks can improve their internal controls' effectiveness by changing this element.

Analyzing those findings exposes reasonable explanations relatively. Under internal auditor's perspective, reasons concerned are as follows:

- (1). The role of internal audit functions furnishing and improving banks' internal control effectiveness is not good;
- (2). The inappropriate structure of the banks badly took influences on the effectiveness of their internal controls under each component in banks' internal controls.
- (3). International standards did not customize in Vietnamese banks in general or the banks have not integrated in the banking system. Since, it is extremely hard to improve the effectiveness of internal controls in the banks keeping up with the modern management of banks in the world.
- (4). The collaborations between other control methods and internal controls faced some difficulties, especially in a changing environment.
- (5). The limitations of corporations between state administration in policy making as well as regulation issuance and banks' managements created negative effects on the internal controls in Vietnamese commercial banks.

CHAPTER 3: RECOMMENDATIONS TO PERFECT VIETNAMESE COMMERCIAL BANKS' INTERNAL CONTROLS

3.1. Rational issues of improvement of internal controls Vietnamese Commercial Banks

3.1.1. The developing strategy of Vietnamese Commercial Banks

The development of the banking sector is in the context of domestic and international economy and the complicated changes of the world economy. Over the past 20 years of reform and development, the banking sector in Vietnam has achieved results, but in the next development phase, it is necessary to improve financial capabilities and productivity. Active forces catch up the pace of development of some developed countries in the region. Up to 2020, Vietnam attempts to actively develop the dynamic banking system that supports and contributes to the development of the economy positively. This is a factor affecting the strategy of commercial banks, since it also impacts on internal controls indirectly.

3.1.2. External impacts on the enhancement of internal controls' effectiveness in Vietnamese Commercial Banks

The following external factors should be considered possibilities of enhancing the internal control effectiveness in Vietnamese commercial banks following: (i) The economic environment may face with potential risks of instability or recession; (ii) The impact of international donating organizations set up conditions to deal with an agreement; (iii) The management mechanism of monetary or financial areas affects the risk management conducted in Vietnamese commercial banks; (iv) The stock exchange sets new requirements on the banks' internal controls; (v) The Bank Credit Information Center (CIC) impacts on the internal control of Vietnamese commercial banks.

3.1.3. Internal management' requirements for improving the effectiveness of Vietnamese Commercial Banks' internal controls

Data and relevant findings found proves that there have been different factors taking changes on internal controls in Vietnamese commercial banks. It also recognized the impact on the internal controls pertaining to internal controls' components. According to COSO Framework, this effect should be deal with 5 following factors such as: control environment, risk assessment, control activities, information and communication, and monitoring.

3.2. General principles for perfecting the effectiveness of Vietnamese Commercial Banks' internal controls

3.2.1. Perfecting internal controls in Vietnamese commercial banks integrating in developing the financial market and Vietnamese banks

It is necessarily to enhance the effectiveness of the banks' internal controls that considers some factor carefully: a variety of products and services furnishing an increased market as well as changes in business operations; the compliance of international agreements on monetary and banking sectors such as the

AFAS of ASEAN or relevant requirements; The improvements of organizational structure; Changes in management, risk controls, financial capability, especially when the banks issue stocks on international stock exchange; Requirement to open or reduce technical bands in the banking sector; and the application of new credit policies.

3.2.2. Perfecting Vietnamese Commercial Banks's internal controls on the basis of corporate governance and risk management

The final task of internal controls in any organization is to detect, prevent and repair misstatements on time. Since, internal controls according to pre-controls or detection controls both play an important role in business. This factor should be considered in the way of changes in management including corporate governance and risk management.

3.2.3. Perfecting Vietnamese Commercial Banks's internal controls to assure the collaboration between the controls with other controls

Designing and installing the culture of controls on the due care in banks are significant considerations. Therefore, cross-checking or peer review work done are necessary. This leads to the design of the control to be an "open" activity. When a control activity is designed "open", it allows the implementation of monitoring, evaluation and cross-control together.

3.2.4. Perfecting Vietnamese Commercial Banks's internal controls appropriating the controls for Basel II and Basel III

Basel launched standards, operating criteria for assessment of banks' operations. In banking system, banks' internal controls recommended to use Basel Statements as a benchmark for designing and appraising banks' internal controls.

3.3. Recommendations to perfect Vietnamese Commercial Banks' internal control effectiveness

3.3.1. Recommendations to perfect Vietnamese Commercial Banks' internal control effectiveness under the control environment component

Some recommendations related are as follows:

i). Improving the way to illustrate the integrity and ethical value: to minimize pressure and opportunities for frauds; to standardize a management's attitude conveying the value of ethic.

ii). Improving organizational structure enclosing the segregation of duties and responsibilities: to maintain the management structure consistently and to keep the suitable roles of banks' managements; to organize and control the compliance of regulations and guidelines, especially the operating committee of banks including Board of directors, Control committee, Operating committees.

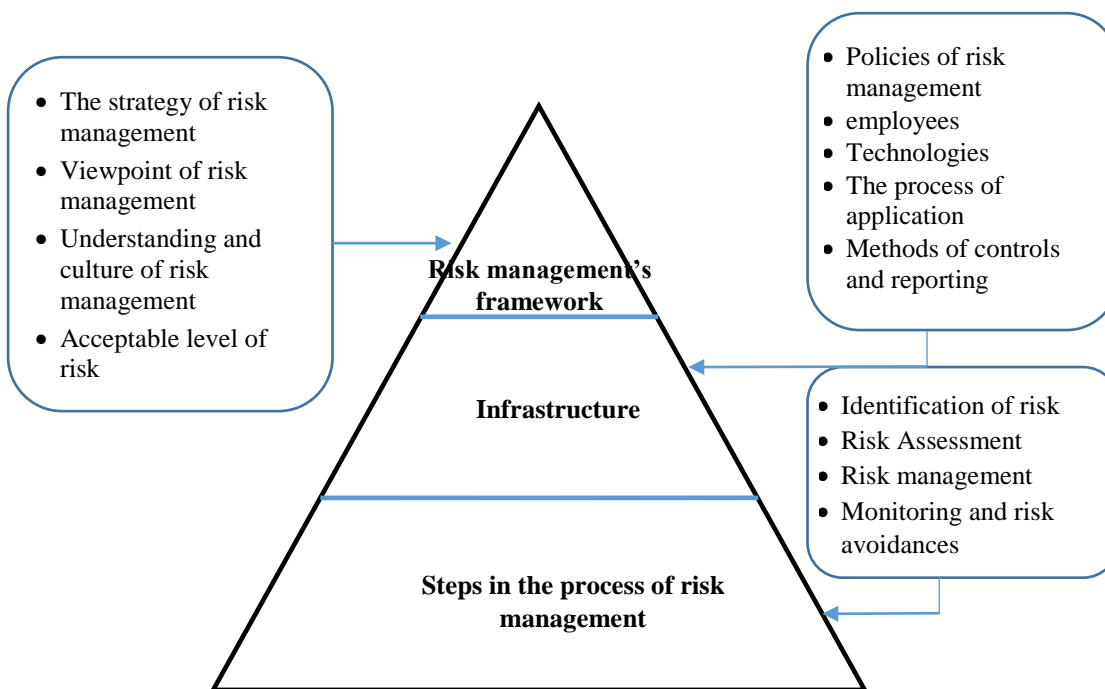
iii). Improving the understanding of internal controls changes *Management philosophy and operating style*: Changing the managers' perception will take an effect on banks' corporate governance; the relations of ownerships; Improving the roles of board of directors Considering the rights of majority shareholders as well as minority shareholders; Keeping the transparency of financial information disclosures; Enhancing the mechanism for remunerations; Solving the conflict of interest; Obtaining knowledge of internal controls and internal audit functions;...

iv). Assuring human resource supporting to banks' expectations: Banks continuously standardize competent requirements, especially in the position of management. Basically, they should consider the number of employees for controlling activities and get their operations efficiently.

3.3.2. Recommendations to perfect Vietnamese Commercial Banks' internal control effectiveness under the risk assessment component

Improving the effectiveness of the risk assessment component, the banks need to develop and ensure the three elements consistently including: the model of the risk management selected is safety, easily operate, and ensure the feature of "controllable" of internal controls; Perfecting policies and procedures related to risk management, especially credit risk management; etc. More improvements of the control environment in detail should be derived from: identification of risks, improvement of measurement, and risk assessment; the infrastructure based to manage risk; the process of risk management. The relationship between these factors is shown in Figure 3.1 above.

Figure 3.1: Relationships among risk management's factors



Source: Basel II [59]

Additionally, banks should use suitable measures of credit risk in accordance with the framework of current value such as the Value at Risk, the model of Credit-Metrics [51] or KVM-Merton model [62] in the Basel II's recommendations.

3.3.3. Recommendations to perfect Vietnamese Commercial Banks' internal control effectiveness under the control activities component

Based on the results of the assessment on the elements of control activities in Vietnamese commercial banks that raises explanations of relevant issues and recommendations realized concerning the changes to the effectiveness of banks' control activities following: (i) Improving the factor of internal accounting controls; (ii) Improving the internal control of operating process in the Vietnamese Commercial Banks. Based on the results surveyed, the banks should complete the significant controls as follows: Completing of the credit rating system; Perfecting the appraising procedures of credit contracts; (iii) Perfecting special procedures, especially the integration of controls fighting frauds under assets misappropriation and protecting banks from doing management's overreliance of internal controls.

3.3.4. Recommendations to perfect Vietnamese Commercial Banks' internal control effectiveness under the component of information and communication

Improving the collection and storage of information changes the quality and the appropriateness of information as follows: (i) Information should be provided to the appropriate users; (ii) The collection of banks' data for risk assessment is significant; (iii) Making the comparison between the expected risk and actual risk helps banks to test or assess risks concerned; (iv) Building an appropriate model of banks' capital bases on the past data that assist banks to budget their capital suitably. Technically, changes in the domestic

and international operating environment require commercial banks to have technical solutions such as: Investing in modern IT equipment; Completing the collection of information; Perfecting the process of installation and implementations uses multiple sources of information.

3.3.5. Recommendations to perfect Vietnamese Commercial Banks' internal control effectiveness under the component of monitoring

To improve the effectiveness of monitoring component needs doing following suggestions:

i). Developing measures helps banks assessing the effects of internal controls' components on general effectiveness. Guidelines recommended present in the Part B of Appendix No. 1.

ii). Monitoring is suggested to implement on the basis of banks' processes and standardized contents of verifications. To improve the effectiveness of monitoring component, banks should change contents of verifications, especially key operations, planned transactions or transactions in high risk areas.

iii). Promoting operations of internal auditing made more value added Vietnamese Commercial Banks. Internal audit is regarded as an efficient tool that helps banks achieving their goals effectively. To improve the factor as well as the effectiveness of monitoring component, banks need to improve the quality of internal auditors, the structure of internal audit departments, and the implementation of internal audit.

3.4. Conditions to conducting these recommendations to perfect Vietnamese Commercial Banks' internal control effectiveness

3.4.1. Conditions under State's changes

The activities of commercial banks are influenced by various factors in the economy. To achieve the effectiveness of Vietnamese commercial banks, therefore, it is necessary to have the supports of the State by using relevant agencies as well as taking opportunities of changes in the whole economy. The factors that need to be improved from a macro perspective will take a positive impact on the effectiveness of the internal control factors in Vietnamese commercial banks following: (i) macroeconomic environment and the stability of the monetary policies; (ii) the operations of an individual commercial bank should have a stable and synchronous legal environment; (iii) to perfect the economic information infrastructure; (iv) developing the market of bad debt trading; (v) solving the problems relating to administrative "red tape".

3.4.2. Conditions under Vietnam Banking Association

Vietnam Bank Association (HBA - VNBA) is a voluntary professional organization of Vietnamese credit institutions bases on the principles of voluntariness, self-management and self-responsibility in all aspects; Arranging and encouraging members to cooperate and support each other in business activities; To represent and protect the legitimate rights and interests of the members; to bridge the gap between members and state agencies; To stabilize and develop a healthy, effective and safe system of credit institutions in Vietnam, thus contributing to the implementation of monetary policies and promoting socio-economic development.

3.4.3. State Bank's changes

The SBV should have certain support and improvements, in particular: Firstly, to continue improving the quality of management and administration; Secondly, to step up the inspection and control work; Thirdly, the SBV should issue a set of indicators to guide the implementation of the risk warning system; Fourthly, improve the quality of the Credit Information Center (CIC); Fifthly, strictly managing the implementation of contents related to inspection, supervision, handling of bad debts and debt trading in the banks.

Final conclusions

The thesis systematizes and connects the nature of internal controls under COSO's Internal control Framework with relevant features under Basel Statement in which factors affect the installation of internal controls in commercial banks identified. My thesis launches a complete model appraising the fact of internal controls by assessing the effectiveness of 5 controls' components including control environment, risk assessment, information and communication, control activities, and monitoring activities. The model bases

on the internal audit of internal controls that combines the results of internal controls' assessment with suggestions relatively recommended.

Beside the thesis made new contributions in terms of practice following: i) Thesis wraps up significant characteristics of Vietnamese commercial banks under different categories such as scope, capital mobilizing, credit activities, the issue of bad debts and state policies regulating organizational structure, performance, and corporate governance of those banks; ii). The thesis had assessed the actual performance of the banks according to 5 components of the banks. I uncovered as follows: (1) Almost Vietnamese commercial banks surveyed have planned strategies and overall policies that direct their activities towards the congruence risk management in Vietnamese commercial banks. Accordingly, this reaction effectively impacted on the effectiveness of these banks' internal controls. (2) Firstly, a model of bank's structure mainly emphasizes risk management that takes a positive effect on the effectiveness of some banks' controls. (3) Some of these banks have developed the prudent process of risks assessment leading good changes in risk controls. Although there have been discrepancies among banks tested, those banks have mostly built standardized systematic steps relating to identifying, measuring, and evaluating risks in different areas. (4) Control procedures are increasingly better, catch up with general rules and globe integration as well. By using the system of internal credit ranking, the banks are able to face overall risk concerning a given customer. It is not only to address a risk properly and early detect this risk, but it also helps banks to assess any impacts of a risk identified. (5) Issues connecting with all components found should be enhanced following the descending order of priority such as monitoring, information and communication, control activities, control environment, and risk assessment; iii). Thesis strongly recommended that recommendations for improving the effectiveness of the banks' internal controls should rely on and collaborate with the model of effective risk management firstly launched by Basel.

Research publications of author related to the Thesis

No.	Topics	Year	Name of journal
1	Recognition of related parties' transactions concerning estates and their disclosures in financial statements	7/2011	Journal of Auditing Studies
2	The system of internal controls and internal audit and their roles in verifying and controlling activities in Vietnamese enterprises.	3/2012	Journal of Auditing Studies
3	Perfecting the income tax accounting in Vietnamese Maritime Enterprises	3/2012	Banking Science and Training Review
4	Promoting the competence of human resource in accounting and auditing professional based on methods of education	12/2012	The Proceedings of Banking Academy's Conference
5	Experiences of enterprises' restructuring activities in some countries and lessons to Vietnamese ones	5/2013	The Proceedings of Banking Academy's Conference
6	Assuring the capital fairly presented in financial statements under the accounting perspective	4/2013	Banking Science and Training Review
7	Improving qualification of employees working at auditing area in the environment of globe integration	5/2013	The Proceedings of Banking Academy's Conference
8	The relationships between the auditing activities of auditing firms and the ethical controllability of auditors' current professional	1/2014	The Proceedings of Banking Academy's Conference
9	Internal controls pertaining to risk management in Vietnamese commercial banks	11/2015	Journal of auditing and Accounting Studies
10	The effect of non-speaking communication on the attraction of customers in the banking sector	1/2016	The Proceedings of Banking Academy's Conference
11	Internal controls over cost expending in commercial banks	3/2017	Journal of auditing and Accounting Studies
12	The effectiveness of risk assessment element of Vietnamese commercial banks: Facts and relevant solutions	6/2017	Journal of auditing and Accounting Studies

Projects of author related to the Thesis

No.	Project's topic	Year	Type of project	Conducting role in project
1	Accounting solutions to the management of the income tax in Vietnam	2012-2012	Academy's Project	Co-author
2	The audit of public listed companies' financial statements listed in the HoChiMinh stock Exchange	2012- 2012	Academy's Project	Co-author
3	Studying the influences of the FDI on the sustainable development of Red river land during the period of 2003-2013	2013-2014	Academy's Project	Co-author
4	Assessing the current situation of internal auditing practices in Vietnamese construction corporations	2013-2014	Academy's Project	Co-author