

# The Role And Development Of Internal Audit In Vietnam

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Date of Submission: 12-04-2024

Date of Acceptance: 22-04-2024

## SUMMARY

Internal audit is the examination, evaluation, and monitoring of the adequacy, appropriateness, and effectiveness of internal control. The article sheds light on the goal of the study. Clarify the theoretical basis of the audit, internal audit, and its objectives. Review the formation and development of internal audits in the world and Vietnam. Assessing the role of internal audit in the organization today includes Risk management; Consulting and control; Inspection and evaluation; and reporting.

**Keyword:** Audit; Internal audit; Role; Vietnam

## I. INTRODUCTION

Internal audit activities have appeared and developed strongly in many countries around the world. In Vietnam, internal audits have been held in large-scale enterprises and public sector organizations, but in fact, internal audits in Vietnam have not been effective and revealed many shortcomings and weaknesses. The sharp deterioration of Vietnam's economy in general and public sector organizations in particular in recent years, coupled with the trend of reforming public financial management towards enhancing the efficiency of using public resources of Vietnam, requires an internal audit of Vietnamese public sector organizations to be effective. The objective of Internal Audit is to prevent, detect, and handle organizational risks; risk management of the organization to ensure efficiency and high performance, considering operational objectives and strategic objectives; plans and tasks of work achieved by the organization. Along with the goal, internal audit has roles such as: Checking the suitability, effectiveness, and effectiveness of the internal control system; Check and certifying the quality and reliability of economic and financial information of financial statements and management accounting reports before submitting for approval; Check the compliance with the principles of operation, management, compliance with the law, financial and accounting regimes,

policies, resolutions and decisions of leaders of accounting organizations; Detect loopholes, weaknesses, frauds in management and protection of assets of the organization; propose solutions to improve and perfect the management system and operate the accounting organization. The research objective of this article is to clarify the theoretical basis of auditing, internal audit, and the objectives of internal audit. Learn the evolution and role of internal audit today.

## II. THEORETICAL BASIS

### 2.1. Audit

According to Gupta (2004), an audit is "an independent examination of the financial information of any organization, whether profit-oriented or not, regardless of its size or legal form when such examination is conducted to express an opinion on it" (p.1095). The Institute Of Chartered Accountants Of India (ICAI) said, "Audits strive to ensure that accounting books are properly maintained as required by law. The auditor reviews immediate recommendations, gathers evidence, presents previous year's working papers, and evaluates the recommendations in their audit report" (ICAI, n.d.). According to the world's leading auditing firm, PricewaterhouseCoopers, "Audits provide third-party assurance to various stakeholders that the audit object is free of material misstatements" (PwC, n.d.). The term audit is "applied most often" to the "audit of financial information" concerning legal entities. Other commonly audited areas include: "compliance, internal controls, quality management, project management, water management, and energy conservation." As a result of the audit, stakeholders can assess and improve the effectiveness of risk management, control, and governance in this regard. In recent years, auditing has expanded into many areas of public and corporate life. Researcher Power (1999) argues that this expansion of auditing activities led to the formation of the "Association of Auditors".

## 2.2. Internal Audit

According to The Institute of Internal Auditors (IIA), "Internal audit is advisory and assurance activity designed to add value and improve an organization's operations. It helps the organization accomplish its objectives by offering a systematic, disciplined approach to evaluating and improving its management, control, and risk management processes" (IIA, n.d.). According to the Accounting Law of Vietnam, Law No. 88/2015/QH13, "Internal audit is the inspection, evaluation, and supervision of the adequacy, appropriateness, and effectiveness of internal control" (article 39). Wood (2012) states that an internal audit can achieve the goal of adding value and improving an organization's operations by providing insight and recommendations based on the analysis and evaluation of the organization's data and business processes (p.151). With a commitment to "integrity" and "accountability," internal audit provides value to "regulators and senior management" as an objective source of independent advice. Specialists called are employed by organizations to perform internal audit activities. Wood's (2009; 2013) studies assess that "The scope of internal audits within an organization can be broad and can involve topics such as organizational governance, risk management, and management controls for performance/effectiveness of operations (including asset protection), reliability of financial reporting and management" (p.1255; p.581), and compliance with laws and regulations. "Internal audits may also involve conducting proactive fraud audits to identify potential fraudulent practices; participate in fraud investigations under the direction of fraud investigation experts and conduct post-investigation fraud examinations to identify deficiencies in control and identify financial losses."

## 2.3. Objectives and principles of internal audit

The objectives of internal audit are specified in Article 4 of Decree No. 05/2019/ND-CP on Internal Audit. Accordingly, "Through inspection, evaluation and consulting activities, internal audit provides independent and objective assurances and recommendations on the following contents: The organization's internal control system has been established and operated appropriately for prevention, detect and handle organizational risks; The organization's governance and risk management processes ensure efficiency and high performance; The operational objectives and strategic objectives, plans and work tasks achieved

by the organization" (article 4). Also, the Decree on Internal Audit issued on Basic principles of internal audit include: "Independence: Internal audit practitioners must not simultaneously undertake tasks that are subject to internal audit. The organization shall ensure that the internal audit is not subject to any interference in the performance of reporting and evaluation tasks; Objectivity: Internal audit practitioners must ensure objectivity, accuracy, honesty, and fairness in the process of performing internal audit tasks; Comply with the law and take responsibility before law for internal audit activities" (Decree No. 05/2019/ND-CP, Article 5).

## III. THE DEVELOPMENT OF INTERNAL AUDIT IN VIETNAM

### 3.1. The development of the world's internal audit

According to ICAI, the word "audit" comes from the Latin *audire* meaning "to hear" (p.1). According to information Loeb & Shamoo (1989) published in "Data audit: Its place in auditing", auditing is said to be "a safeguard measure since ancient times" (p.23). Derek's book *History of Auditing* (2006), which studies "The changing audit process from the 19th century till date," states that "During the Middle Ages, when manual bookkeeping was commonplace, auditors in England often listened to accounts read to them and checked whether the organization's employees were negligent or fraudulent" (p.6). Speaking in his 1951 study "Early Developments in American Auditing," Moyer determined that "the auditor's most important task is to detect fraud" (p.3). Johnson (1975) quotes Chatfield as noting that "the initial audit of the United States was viewed primarily as detailed verification of the bookkeeping" (p.256). According to "The IIA-History and Evolution of Internal Auditing", "The profession of internal auditing developed steadily with the advancement of management science after World War II. However, it has only really been recognized as a modern occupation since the 40s (especially since the 60s) of the twentieth century. The Institute of Internal Auditors (IIA) was founded in 1941 in New York and the rapid development of internal audit activities in European countries in the 60s of the twentieth century. Conceptually, it is similar to financial audits of public accounting, quality assurance, and banking compliance activities. While some of the auditing techniques underpinning internal auditing originate in the profession of management consultants and public accountants, the theory of

internal auditing was formed primarily by Lawrence Sawyer (1911–2002), often considered the "father of modern internal audit"; and the philosophy, The current theory and practice of modern internal auditing as defined in the Institute of Internal Auditors' International Professional Practice Framework (IPPF) both have a huge influence on Sawyer's vision." According to "Internal Auditor Magazine", the implementation of the Sarbanes–Oxley Act of 2002 in the United States, the presence and value of this profession have been enhanced, as many internal auditors possess the skills necessary to help companies meet the requirements of the law. However, the focus of the internal audit department of publicly traded companies on SOX-related financial procedures and policies derailed the industry's progress in the late 20th century toward Larry Sawyer's vision of internal audit. Beginning around 2010, the IIA once again began advocating for a broader role of internal audit in the corporate sector, in line with the philosophy of the IPPF.

### 3.2. The development of internal audit in Vietnam

Since Vietnam applied the open-door policy, along with independent audit activities, Internal Audit has been formed and developed by the organizations themselves, from the requirements of managers. The history of the formation and development of Internal Audit is associated with the process of perception of managers towards control and management issues. Therefore, since the last century, Internal Audit has been formed as an important and effective tool for managers in organizations. However, internal audit is still a new concept in Vietnam despite the existence of internal audit departments at large state-owned enterprises. Many managers are not familiar with the concept of internal audit and are not aware of the importance of this department. Many internal audit departments in corporations and corporations act as an inspection function of the accounting department. More surprisingly, state-owned corporations tend to eliminate the internal audit function and use independent audits as a guarantee that contributes to improving their operations. Therefore, awareness of internal audit is becoming necessary not only for the board of directors and managers but also for the internal audit department and other relevant departments. Internal audit was established to meet the management requirements of businesses, non-governmental organizations, and non-profit organizations, first of all in organizations,

organizations in the stock market, banks, the public sector, and multinational companies. The research works said that, firstly, Internal Audit was born because managers in joint stock companies realized that the audit of annual financial statements conducted by independent auditors did not fully meet the requirements for the control and management process as well as timely prevent risks, Fraud may arise. After that, the Securities Exchange Commission of the countries required managers in joint-stock companies listed on the stock market to be more responsible for the reliability of published financial statements, so the managers themselves in these companies expanded and enhanced their role, and responsibilities of Internal Audit. Since then, the work of Internal Audit is not merely financial and accounting matters but also includes the analysis and evaluation of the internal control system, checking mid-term information and other information that has not been reviewed by independent auditors when conducting annual audits. The Internal Audit role is now expanded to improve internal control policies and procedures for the entire organization's operations. The development of Internal Audit can be seen in the following aspects:

As an organization, the development of an Internal Audit goes through 3 stages: in the early stages Internal audit is recognized in some places but scattered and the inspection is carried out by the owner or manager himself; The next stage of inspection and evaluation activities is officially recognized in organizations, however, internal audit is not yet widely used; In the third stage, Internal Audit is elevated to an independent organization under the direct supervision of top management to ensure strength and independence.

With the functional aspect of Internal Audit, in the past, internal audits focused heavily on accounting, mainly examining financial activities to ensure the capacity of accountants. Today, Internal Audit is not only limited to such, but also examines and evaluates operating activities, internal control systems, and other non-financial activities.

With the Internal Audit aspect evolving as a profession, it has been recognized and approved in many organizations in society. The internal audit apparatus was established due to the intrinsic needs of organizations and organizations due to the influence (advice) of independent auditors. At the same time, internal audit activities are governed by professional principles drafted and published by professional associations, and the Institute of Internal Auditors - competent professional bodies.

On the other hand, Internal Audit is professionally standardized through annual internal auditor examinations and certifications at IIA campuses in many countries around the world. In addition, there is an ethics law that has been adopted and used as the norm of conduct for internal auditors on a global scale.

The Regulation on Internal Auditing in State-owned Enterprises in Vietnam promulgated in Decision No. 832 -TC/QĐ-CĐKT of the Ministry of Finance dated 28/10/1997 is the first legal document mentioning regulations on the purpose, functions, principles, scope, tasks, contents as well as organizational and personnel issues of Internal Audit in the State-owned enterprises. In the 2000s, Vietnam had 3 more legal documents related to Internal Audit issued by the Ministry of Finance, namely: Circular No. 52/1998-TT/BTC dated April 16, 1998, guiding the organization of the internal audit apparatus at state-owned enterprises; Official Letter No. 287-TC/TCDN dated 3/8/1998 on the appointment of internal auditors and Circular 171/1998-TT/BTC dated 22/12/1998 guiding the implementation of internal audit at state-owned enterprises. The most recent is Decree No. 05/2019/ND-CP on Internal Audit issued on January 22, 01, 2019.

#### IV. THE ROLE OF INTERNAL AUDIT

Some internal audit philosophies and approaches originate from the work of Lawrence Sawyer. "His philosophy and guidance on the role of internal audit is a precursor to the current definition of internal audit. It emphasizes assisting management and the board in achieving organizational objectives through sound audits, evaluations, and analyses in areas of activity. He encourages the modern internal auditor to act as an advisor to management rather than an adversary. Sawyer sees auditors as people who actively influence events in the business rather than criticizing every degree of error. He also foresees a more desirable future for the auditor involving stronger relationships with audit committee members and the board of directors and the elimination of the direct-to-chief financial officer reporting regime" (Sawyer, 2003). Sawyer often talks about "getting the manager to do something right" and offering recognition and positive reinforcement. Writing about positive observations in audit reports was rarely made until Sawyer started talking about the idea. He understands and anticipates the benefits of providing more balanced reporting while building better relationships. Sawyer understands the psychology of

interpersonal dynamics and the need for everyone to receive validation and validation for relationships to develop (Sawyer, 2003).

Sawyer has made internal audits more relevant and enjoyable through a strong focus on operational or operational audits. He is particularly encouraged to look beyond financial statements and audits into areas such as purchasing, warehousing and distribution, human resources, information technology, facilities management, customer service, field operations, and program management. This approach helped push the audit executive into the role of a respected and knowledgeable advisor who was thought to be logical, objective, and interested in helping the organization achieve its stated goals (Sawyer, 2003).

According to the provisions of the Law on Accounting, Law No. 88/2015/QH13, Internal Audit has 4 main tasks: "Check the suitability, effectiveness, and effectiveness of the internal control system; Check and certify the quality and reliability of economic and financial information of financial statements and management accounting reports before submitting for approval; Check the compliance with the principles of operation, management, compliance with the law, financial and accounting regimes, policies, resolutions and decisions of leaders of accounting organizations; Detect loopholes, weaknesses, frauds in management and protection of assets of the organization; propose solutions to improve and perfect the management and operation system of accounting organizations" (Article 39). From these tasks, we can determine its role in the organization.

#### 4.1. Risk management

Internal audit helps identify and evaluate the effectiveness of processes, internal control systems, corporate governance, and corporate accounting. Internal auditing professional standards require the function of evaluating the effectiveness of an organization's risk management activities. Risk management is the process in which an organization identifies, analyzes, responds, gathers information, and monitors strategic risks that may actually or potentially affect the organization's ability to achieve its mission and goals. "Under the Enterprise Risk Management Framework (ERM) COSO, an organization's strategic, operational, reporting, and compliance objectives all have strategic business risks associated – negative outcomes caused by internal and external events that hinder the organization's ability to achieve its goals. Management assesses risk as part of normal

business operations such as strategic planning, marketing planning, capital planning, budgeting, hedging, incentive payment structures, credit/loan practices, mergers and acquisitions, etc. strategic partnerships, changing laws, conducting business abroad, etc. The Sarbanes–Oxley regulations require a wide-ranging risk assessment of the financial reporting process." Corporate lawyers typically prepare comprehensive assessments of current and potential litigation that a company faces. Internal auditors can evaluate each of these activities or focus on the overall process used to manage risk across the organization. For example, "internal auditors may advise management on reporting forward-looking operational measures to the board to help identify emerging risks; Or the internal auditor can evaluate and report whether the board and other stakeholders can provide reasonable assurance that the organization's management team has implemented an effective enterprise risk management program." The internal audit function can help an organization address fraud risk through fraud risk assessment, using fraud prevention principles. Internal auditors can help companies establish and maintain Enterprise Risk Management processes. This process is highly valued by many businesses for establishing and implementing an effective management system while ensuring that quality is maintained and professional standards are met. Internal auditors also play an important role in helping companies perform top-down risk assessments.

#### 4.2. Consulting and control

Internal audit advises on building processes, controlling new projects, and assessing and managing risks. Internal audit activities are primarily aimed at evaluating the internal control system. According to the COSO Internal Control Framework, internal control is broadly defined as a process, implemented by an organization's board of directors, management, and other employees, designed to provide reasonable assurance of the achievement of the following core objectives for which all businesses strive: "Operational efficacy and efficiency; Reliability of financial and management reporting; Compliance with laws and regulations; Asset protection." (Base, 2013, p.60). Management is responsible for internal control, which consists of five important components: "control environment; risk assessment; risk-focused control activities; information and communication; and surveillance activities" (Coso, 2013, p.60). Managers establish policies, procedures, and practices within these five management control

components to help the organization achieve the four specific objectives listed above. The internal auditor performs an audit to assess whether the five components of management control are present and functioning effectively, otherwise making recommendations for improvement.

#### 4.3. Testing and evaluation

Ensure the implementation of inspection activities to provide an objective assessment of effectiveness, compliance as well as control performance. "Supervise the implementation of development strategies and business plans; Supervise and evaluate the current status of business activities and financial status of the company; Supervise and evaluate the exercise of rights and obligations of members of the Members' Council and the Members' Council, the company's president, director or general director of the company; Supervise and evaluate the effectiveness and compliance with internal audit regulations, risk prevention and management regulations, reporting regulations, and other internal governance regulations of the company; Supervise the legality, systematicism and truthfulness in accounting, bookkeeping, in the content of financial statements, appendices and related documents; Supervise contracts and transactions of the company with related parties; Supervise the implementation of large investment projects; contracts, purchase and sale transactions; contracts and other large-scale business transactions; contracts, unusual business transactions of the company; Make and send assessment reports and recommendations on the contents specified at Points a, b, c, d, dd, e and g of this Clause to the owner's representative agency and the Members' Council; Perform other obligations at the request of the agency representing the owner, specified in the company's charter" (Law on enterprises, 2020, article 104).

#### 4.4. Reporting

Assess the financial situation, business, and operating system of the enterprise, then report directly to the Board of Directors and the Board of Directors. This requires the internal audit system to be constantly checked, updated, and improved. "At the end of the fiscal year, the Board of Directors must submit to the General Meeting of Shareholders the following report: Report on business results of the company; Financial statements; Report on evaluation of the management and administration of the company; Appraisal report of the Control Board" (Law on enterprises, 2020, article 175). Internal audit has

the role of evaluating the above reports, ensuring truthfulness and accuracy.

## V. CONCLUSIONS

Internal audit is an independent and objective consulting activity related to management, risk management, system and process control,...contributing to helping businesses achieve their goals. Internal audits are conducted by a department or a dedicated individual. The objective is to evaluate the effectiveness of the internal control system, and detect and propose solutions to overcome potential risks and losses, thereby helping the business achieve the set goals. This is an independent consulting activity and focuses on objectivity in the 3rd line of the organization. Internal audit plays an important role in organizational governance through basic roles such as Risk management: Identifying and evaluating the effectiveness of processes, internal control systems, corporate governance, and corporate accounting. Consulting and control: Internal audit advises on building processes, controlling new projects, and evaluating and managing risks. Inspection and evaluation: Ensure the process of carrying out inspection activities to give an objective assessment of the effectiveness, compliance as well as control performance. Report: Evaluate the financial situation, business, and operating system of the enterprise, then report directly to the Board of Directors and the Board of Directors. This requires the internal audit system to be constantly checked, updated, and improved.

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