

# *Research on the Improvement of Internal Control over Accounts Receivable of Xiaoshan Landscape Company*

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**Abstract:** In the face of the increasingly fierce market competition environment, credit sales have gradually become a means for enterprises to face competition. However, the construction period of engineering projects is long and involves a large amount of funds. If the owners fail to make payments in a timely manner for a long time, it will increase the scale of the enterprise's accounts receivable, reduce the liquidity of funds, increase the risk of bad debts, and affect the stable daily operation of the enterprise. Therefore, construction enterprises need to improve the internal control level of accounts receivable. Taking Xiaoshan Landscape Company as the research object, this paper has sorted out the current situation of the internal control of the company's accounts receivable, discovered the existing problems and causes in the internal control of the company's accounts receivable, and put forward improvement suggestions in view of the existing problems and causes to promote the healthy development of the company.

## 1. Introduction

As of the third quarter of 2024, the number of construction enterprises across the country has exceeded 160,000, with a year-on-year growth rate of 7.91%. There are a large number of construction enterprises, and the market competition is fierce. Phenomena such as price undercutting within the industry are common, resulting in the compression of enterprises' profit margins. In particular, the living space for private enterprises has become smaller. They often cannot compete with central enterprises and state-owned enterprises in the bidding for large projects and can only participate in projects as subcontractors, with their profits being further squeezed. Real estate development investment has continued to be weak[1-2]. From January to October 2024, the completed investment in real estate development across the country decreased by 10.3% year-on-year, leading to a reduction in the demand for the construction market related to it. Meanwhile, investment in some infrastructure fields is also sluggish[3-5]. For example, the fixed asset investment in the public facilities management industry and the road transport industry has performed poorly, limiting the number of projects that construction enterprises can undertake. With the continuous changes in the overall market environment, credit sales have become a means of competition. However, an increase in accounts receivable means that an enterprise's funds are

occupied and cannot flow back in a timely manner[6-7]. As a result, problems such as reduced capital liquidity, increased operating costs and bad debt risks for enterprises, and impacts on the sustainable development of enterprises in the future will arise. Therefore, improving the internal control level of accounts receivable for construction enterprises has become a "compulsory course" for enterprise development[8-9].

## **2. The relevant concepts of accounts receivable and internal control**

### **2.1. Accounts Receivable**

Accounts receivable refer to the amounts that an enterprise should collect from the purchasing units in the normal course of business operations due to the sales of goods, products, and the provision of labor services, etc., including taxes that should be borne by the purchasing units or the units receiving labor services, packaging fees and freight and miscellaneous expenses prepaid for the purchasers. In the construction industry[10-11], accounts receivable mainly refer to the project funds that construction enterprises should collect from the construction units (the employers) according to the contract but have not yet collected after completing construction projects. Through collecting the financial data of Xiaoshan Landscape Company, it is found that its accounts receivable are mainly the receivable project funds, which occur when the purchasers do not remit funds in time after invoicing and the company does not conduct timely collection.

### **2.2. Internal Control**

Internal control is the general term for a series of methods, procedures and measures adopted within an organization to achieve its business objectives, protect the safety and integrity of assets, ensure the correctness and reliability of accounting information, ensure the implementation of business policies, and guarantee the economy, efficiency and effectiveness of business activities. It mainly includes five elements: internal environment, risk assessment, control activities, information and communication, and internal supervision. The internal environment is the foundation of internal control, including governance structure, organizational setup and the allocation of rights and responsibilities, internal audit, human resources policies, and corporate culture, etc. Risk assessment is the basis of internal control. Enterprises need to identify and analyze the risks related to the achievement of internal control objectives in business activities and reasonably determine risk response strategies. Control activities are the means of internal control. Enterprises adopt corresponding control measures according to the results of risk assessment to control risks within an acceptable range. Information and communication are the carriers of the means of internal control. Enterprises need to collect and transmit information related to internal control in a timely and accurate manner to ensure effective communication within the enterprise and between the enterprise and the outside world. Internal supervision is the guarantee of internal control. Enterprises conduct supervision and inspection on the establishment and implementation of internal control, evaluate the effectiveness of internal control, discover internal control deficiencies, and make timely improvements.

### **2.3. Internal Control over Accounts Receivable of Construction Enterprises**

The internal control over accounts receivable of construction enterprises refers to the general term for a series of interrelated and mutually restrictive methods, measures and procedures adopted within enterprises to ensure the safety and integrity of accounts receivable, timely recover funds, and prevent bad debt risks. It includes multiple links such as customer credit assessment, contract

management, account tracking and collection, and bad debt management, so as to ensure the rationality of the scale control of accounts receivable and try to avoid economic losses caused by bad debts and financial risks as much as possible.

### 3. Analysis of the Current Situation of Accounts Receivable of Xiaoshan Landscape Company

#### 3.1. Introduction to Xiaoshan Landscape Company

Xiaoshan Landscape Company is a private construction enterprise engaged in construction project construction, landscaping, etc. Its main business mainly includes construction project construction, municipal project construction, and garden project construction and maintenance, etc. The company has qualifications such as the first-class general contracting qualification for municipal public works construction, the first-class qualification for urban landscaping, the first-class professional contracting qualification for ancient building projects, and the second-class general contracting qualification for construction projects.

The company has set up more than a dozen branches across the country, and its business covers more than 20 provinces. Its business scale has expanded from the Jiangsu-Zhejiang region to the Guangdong-Hainan region. It has won more than 80 excellent project awards, including 1 "Yangtze Cup" of the Jiangsu Provincial Quality Project Award, 1 "Qianjiang Award" of the Zhejiang Provincial Construction Project, 1 Grand Gold Award and 8 Gold Awards of the Excellent Garden Project of the Chinese Society of Landscape Architecture. From 2011 to 2020, the company was continuously shortlisted among the top 50 urban Landscape enterprises in the country. In 2014, it won the title of the Outstanding Enterprise in the Municipal Construction Industry and has been rated as the AAA grade of the provincial banking and financial system for many consecutive years. The company is now the executive director unit of the Zhejiang Provincial Society of Landscape Architecture and the vice president unit of the Engineering Branch. It has also won many honorary titles such as the Outstanding Enterprise in the Construction Industry of Hangzhou City and the Demonstration Enterprise of the Building Industry Modernization in Xiaoshan District. With the progress of the national ecological civilization construction, the company will continue to do a good job in projects, conduct scientific management, and carry out innovation.

#### 3.2. Analysis of Management Indicators of Accounts Receivable of Xiaoshan Landscape Company

##### 3.2.1. Analysis of Accounts Receivable and Operating Revenue

As shown in Table 1:

Table 1: Analysis of Accounts Receivable and Operating Revenue

Item	2021	2022	2023
Accounts Receivable	92064.29	91023.41	90173.87
Accounts receivable	20037.27	26461.50	28573.52
Growth rate of accounts receivable	-5.62%	32.06%	7.98%
Growth rate of business income	3.03%	-1.13%	-0.93%
The proportion of accounts receivable to Accounts Receivable	21.76%	29.07%	31.69%

Data Source: Company's financial statements

### 3.2.2. Speed of Accounts Receivable Flow

Table 2: Situation of the Scale of Accounts Receivable

Situation of the Scale of Accounts Receivable			Unit: ten thousand yuan
Item	2021	2022	2023
Operating revenue (in ten thousand yuan)	92064.29	91023.41	90173.87
Accounts receivable turnover (times)	4.46	3.92	3.28
Days of accounts receivable turnover (days)	82	93	110

Data Source: Company's financial statements

The accounts receivable turnover rate and turnover days are indicators to measure an enterprise's operating ability. Enterprises with fast collection speed and short collection periods have a higher accounts receivable turnover rate. Such enterprises have faster asset flow, fewer bad debts, and stronger debt-paying ability. The shorter the turnover days are, the shorter the debtor's default time is, the higher the creditworthiness is, and the smaller the bad debt losses are, indicating that the enterprise has stronger ability to collect accounts.

According to Table 2, the accounts receivable turnover rate of the company in 2022 slightly decreased compared with that in 2021, and it decreased to 3.28 in 2023. The turnover days increased from 82 days in 2021 to 110 days in 2023, indicating that the enterprise's collection speed became slower, the flow speed slowed down, and the collection ability weakened in 2023, and it may face bad debt risks.

### 3.2.3. Account Receivable Aging Structure

The account receivable aging reflects an enterprise's collection ability. Observing the aging period can roughly understand an enterprise's fund utilization situation and cash flow status. A relatively long aging period indicates that there may be problems such as poor fund utilization, poor cash flow and accounts receivable management in the enterprise.

Table 3: Aging Analysis Table of Accounts Receivable from 2021 to 2023

	Accounts receivable in 2021	Accounts receivable in 2022	Accounts receivable in 2023	Provision Ratio	Provision for bad debts in 2021	Provision for bad debts in 2022	Provision for bad debts in 2023
Within one year (including one year)	14286.58	17094.13	17620.42	20%	285.73	341.88	352.41
1 to 2 years	4388.16	6800.60	7284.36	5.0%	219.41	340.03	364.22
2 to 3 years	841.57	1561.23	1863.47	10.0%	84.16	156.12	186.35
Over 3 years	520.97	1005.54	1805.27	30.0%	156.29	301.66	541.58
Sum	20037.27	26461.50	28573.52	—	745.59	1139.70	1444.56

Data Source: Company's financial statements

It can be seen from Table 3 that the accounts receivable within one year (including one year) of

the company account for the majority, with a proportion of about 70% in each of the past three years. The proportion of accounts receivable with an aging of more than one year was 35.4% in 2022, which was not much different from that in 2021, but reached 38.3% in 2023. It is speculated that the enterprise realized the importance of accounts receivable collection in the early stage, took certain measures to promote the return of funds, but slackened off in the later stage and did not reasonably control the aging structure, resulting in the generation of accounts receivable with a relatively long aging. The bad debt provision ratio of Xiaoshan Landscape company is 2% for within one year (including one year), 5% for 1 - 2 years, 10% for 2 - 3 years, and 30% for more than 3 years. The bad debt reserves of the company in 2023 were relatively higher than those in the previous two years, indicating that the possibility of recovering some accounts receivable is relatively low and the possibility of finally turning into bad debt losses is relatively high.

## **4. Problems and Causes of the Existence of Accounts Receivable Risk Management in Xiaoshan Landscape Company**

### **4.1. Problems in Internal Control over Accounts Receivable**

#### **4.1.1. Unreasonable Organizational Structure Setup**

The company's organizational structure involves two types of departments, namely decision-making and execution departments, but lacks supervision departments, such as the audit department. Such a division of labor will lead to structural defects. Moreover, the power distribution between the general manager and the deputy general managers is unbalanced. The deputy general managers are at the same level as the directors of various functional departments, with a relatively small scope of power. Finance, business, and construction are all managed by the general manager, and the decision-making power is basically in the hands of the general manager. The deputy general managers cannot directly access the progress of business, which can improve the decision-making speed, but it will make the general manager unable to free himself from daily affairs and is also easy to form a "one-man show" of the leader.

#### **4.1.2. Imperfect Risk Assessment Work**

The company has not established a systematic credit assessment system. The marketing department holds business information, but does not update the information of old customers in real time. The access process for new customers is also relatively simple, lacking written documents such as customer credit rating reports as the supporting basis for business cooperation. When bidding for engineering projects without a detailed analysis of credit risks and blindly cooperating without thorough credit investigations, it will cause the company's cash flow to break. Currently, many ongoing projects of the company face the risk that the employer cannot remit funds on time due to insufficient preparation for pre-project credit assessment work. To relieve the capital shortage, the company has to pay the suppliers' payments through bank loans. The way of "borrowing new to repay old" allows the funds to circulate briefly, but the loan interest also accounts for the majority of the monthly expenditure. If this continues for a long time, the company will fall into a loan cycle and the repayment pressure will intensify.

#### **4.1.3. Lack of Real-time Monitoring of Accounts Receivable**

There is a disconnection between the formulation and implementation of the company's accounts receivable management system. The financial department can only take the initiative to check and feedback the accounts receivable situation when required by the leader. The time for reconciling

accounts with customers is not fixed. Reconciliation is usually notified orally or via WeChat when invoicing, lacking formal documents such as collection letters and reconciliation letters. The marketing department does not follow up in time when the accumulated amount of accounts receivable is large and the enterprise's capital turnover is tight. It can only conduct collection after continuous urging by the leader and does not conduct real-time monitoring of the accounts receivable situation. When a project is listed as a problem project, business managers usually have a resistant mentality, suspend exchanges with customers, and the situation that the final payment has not been received for a long time after the project is completed often occurs.

#### **4.1.4. Lack of a Sound Accounts Receivable Supervision Mechanism**

In order to survive and develop, the company cannot require the employer to prepay all project funds before construction and can only finance the construction by itself. In order to maintain a good relationship with the employer, the company cannot frequently urge it for payment. Considering that the company still needs to continue its business, the management has put forward the view that the number of winning bids can be increased while controlling costs, and then the project funds of other projects that can remit funds on time can be used to promote capital flow. Therefore, the current focus of the company's work is on increasing business volume and controlling costs, ignoring the special supervision work on accounts receivable.

Although the leader will assign and urge employees to complete the supervision work, and the financial department will also intervene in the marketing department as required by the leader to continuously track the collection situation, the audit supervision work has never been assigned to fixed personnel, and can only rely on the audit reports issued by external audit institutions. In addition, the supervision content is determined by the management, which is somewhat subjective and lacks the support of a sound accounts receivable supervision mechanism. Moreover, the company usually takes remedial measures for accounts receivable supervision work only after legal disputes arise in the project. Eventually, it can only rely on the discussion and solution by the financial department and the legal department, and the effectiveness of internal supervision is poor, which affects the stable operation of the company.

## **4.2. Analysis on the Causes of Internal Control Problems of Accounts Receivable**

### **4.2.1. Delayed Adjustment of Organizational Structure Setup**

During the start-up period of the company, the organizational structure was set up in the form of "the more capable one does more work". Necessary functional departments were retained when setting up departments. The finance department took on the auditing function, and the marketing department also took care of the project progress. As the company expanded, the original organizational structure could no longer meet the needs of new businesses. The increase in winning bids for projects and the growth in business volume left the employees in the marketing department with no time to attend to customer maintenance and the situation of progress payments, and they were unable to collect project payments in a timely manner. The focus of the financial staff was on cost accounting, and they did not continuously pay attention to the accounts receivable. At this time, the company should have established an independent credit management department to coordinate and restrain the finance department and the marketing department. However, considering that the addition of a new department would increase management costs, the management still adopted the form of one person taking on multiple jobs or multiple departments sharing one post. But one person taking on multiple jobs would increase the workload of employees, and multiple departments sharing one post would lead to confusion in the division of labor, affecting work

efficiency and teamwork.

#### **4.2.2. Lack of Risk Early Warning Mechanisms and Coping Strategies**

In order to quickly seize market resources, the company set the goal of increasing business volume. As long as the enterprise's qualifications met the standards, it would plan to bid, without systematically evaluating risks. To gain a competitive advantage, the company would sacrifice some profits in the quotation process and reduce material and labor costs to lower the quotation. This phenomenon is common among construction enterprises. The level of cost represents the quality of construction materials. Low-price competition means that the enterprise has to choose suppliers with relatively low prices, average or even poor quality when purchasing materials. There is a high probability that quality problems will occur during project construction, resulting in the risk that accounts receivable cannot be recovered and even causing the enterprise to face penalty losses. However, in the face of the temptation of winning bids and the total contract price, the company ignored the risks and did not assign professional staff to formulate reasonable risk early warning and coping strategies. Compared with the expenses invested in risk avoidance, the leadership was more willing to use this amount of money to increase the company's relevant qualifications.

#### **4.2.3. Lack of Information Communication Channels for Accounts Receivable**

Currently, the company lacks information communication channels for accounts receivable and has not built a specialized information communication platform for accounts receivable management. Information communication in this regard relies on work groups. Moreover, due to their different positions, the two departments seldom communicate with each other and do not know much about when to collect payments and the situation of payment receipts. Most of the time, information communication regarding accounts receivable needs to rely on the management to pull the two departments together. Both departments will pass information to the management, using the management as an intermediary, and seldom communicate and transmit information with each other directly. As a result, some important information is blocked. In order to maintain a good relationship with customers and easily obtain the latest market information, business managers seldom mention accounts receivable when communicating with customers. When reminding customers to pay, they simply send the amount to the customers without actively following up. This communication method is likely to lead to doubtful debts and bad debts for the enterprise.

#### **4.2.4. Imperfect Internal Supervision System**

In the early stage of the company's establishment, the manager was familiar with the company's system and operating situation and could be hands-on in the process of operation and management. While having decision-making power, the manager also took charge of internal supervision work. Therefore, no internal supervision system was formulated, and no audit supervision department was established. The audit supervision work was determined by the manager according to the situation and was usually entrusted to department leaders and financial personnel. Under the pressure of the leader, employees wanted to finish the work as soon as possible and only verified the authenticity and legality of original documents such as vouchers. The rest of the work had to rely on external audits. And hiring external audit institutions was a legal requirement. This supervision method put the enterprise in a passive position and also limited the financial personnel from giving full play to the professionalism and comprehensiveness of auditing.

## **5. Improvement Measures for Internal Control Problems of Accounts Receivable in Xiaoshan Landscape Company**

### **5.1. Improving the Organizational Structure Setup**

To address the problem of an unreasonable organizational structure setup, referring to the principle of "separation of powers" in corporate governance, the company should establish a supervision department and clearly define the responsibility boundaries with decision-making and execution departments. The three types of departments should restrict each other to achieve a comprehensive balance, avoid the leadership having absolute say and causing decision-making mistakes, and facilitate the smooth progress of internal supervision work.

### **5.2. Improving the Customer Credit Evaluation System**

The credit management department can adopt the "5C evaluation method" to determine the customer credit rating from five aspects: character, capacity, capital, collateral, and conditions. The credit management department should regularly review customers' credit situations and update and adjust customers' credit ratings in a timely manner.

### **5.3. Strengthening the Daily Supervision of Accounts Receivable**

To promote the smooth progress of the daily supervision of accounts receivable, the company should formulate an accounts receivable supervision plan. The finance department should count the capital revenue and expenditure situation at least 1 - 2 working days and count the recovered and unrecovered project payments every month, and report the data to the financial manager in a timely manner. The engineering department should report the project progress at least once a month, establish contact with the marketing department, and let the company understand the project implementation situation. When customers default on project payments, the credit management department should re-investigate and analyze the creditworthiness of the defaulting customers and re-evaluate the credit rating. Business managers should promptly connect and adopt an active collection policy. They can first communicate online to remind, then send statements, remind customers of the payment collection time. After exceeding the repayment period, they should first ask customers about the reasons for the delay, then conduct on-site visits to investigate the real situation, and send reminder notices again to remind customers and strive to recover the payments. If customers maliciously default or refuse to pay, they should be classified as Class C customers and no further cooperation should be carried out, but the collection of arrears should continue. After multiple attempts at collection are fruitless, the gains and losses between increasing collection costs and reducing the opportunity cost of accounts receivable and bad debt losses should be weighed, and then lawsuits can be filed in court.

### **5.4. Improving the Internal Supervision System**

Currently, the supervision content of the company is carried out for events that occur at a certain time. The company can establish an independent audit department and improve the internal supervision system. The special supervision work on accounts receivable can be carried out from three aspects: comprehensively sorting out accounts receivable, self-inspection and understanding of the situation, and analysis of the causes. The collection work can be organized in a way of dialectical treatment. Employees should conduct sorting and inspection work on accounts receivable project by project and unit by unit, master the detailed situation, and check whether the formation



and increase or decrease of payments are accurately recorded, and improve the business ledger. The company should analyze the account age and risk level of receivables, check and clean up on a monthly basis, control the increase in receivables, and prevent the risk of bad debts caused by blindly issuing invoices. During the payment collection stage, the company should first clarify the first responsible person, try online communication, confirmation letters, and on-site collection and other methods to carry out cleaning and disposal work, and use legal means as the last solution to disputes, and take multiple measures to solve problems. For payments with a long account age and difficult to recover, after collecting evidence and undergoing third-party verification, they should be processed in accordance with the requirements for the inventory and write-off of accounts receivable. The recovered offsetting materials or assets should be disposed of in accordance with regulations. The company should also establish a linkage mechanism to enable all departments to cooperate with each other in the special supervision work of accounts receivable and improve the progress of the collection work. For different projects of the same customer, when it is found that the customer's situation is abnormal, the construction situation of each project contracted by the customer should be promptly understood and early warning notices should be issued.

## 6. Conclusion

Xiaoshan Garden Company, being a typical private construction enterprise, is faced with a series of problems concerning the internal control of its accounts receivable. Firstly, the organizational structure is not rationally arranged. For instance, the division of labor and coordination among departments may lack clarity, leading to inefficiencies. Secondly, the credit evaluation system is far from complete. It fails to comprehensively and accurately assess customers' creditworthiness, thus increasing the potential risks of bad debts. Thirdly, real-time monitoring of accounts receivable is absent. The company is unable to promptly track and respond to changes in receivables, which might delay necessary actions. Lastly, the internal supervision mechanism is ineffective. It cannot play a proper checking and guiding role to ensure the healthy operation of the accounts receivable management.

The main reasons for these problems can be traced back to several aspects. The organizational structure has not been adjusted in a timely manner to adapt to the company's development and changes in the business environment. Risk early warning mechanisms and corresponding coping strategies are lacking. Management often overlooks potential risks and fails to take proactive measures in advance. Their risk awareness remains weak. Moreover, the internal supervision system is riddled with imperfections, lacking strict regulations and effective enforcement.

In view of the above-mentioned problems and based on an in-depth causal analysis, the following targeted improvement suggestions are proposed. Firstly, the organizational structure should be optimized. Clear lines of responsibility and cooperation need to be established among different departments to enhance overall efficiency. Secondly, the customer credit evaluation system ought to be enhanced. More scientific and comprehensive evaluation methods should be adopted to accurately gauge customers' credit conditions. Meanwhile, the daily supervision of accounts receivable must be strengthened. Timely tracking, data collection, and analysis should be carried out to ensure that any issues can be detected and resolved at an early stage. Finally, the internal supervision system requires significant improvement. Stringent rules and procedures should be formulated, and supervision work should be carried out more effectively to guarantee the proper implementation of accounts receivable control measures.

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