

**EFFECT OF INTERNAL CONTROLS ON THE FINANCIAL PERFORMANCE OF
COMMERCIAL BANKS LISTED IN THE NSE AND LICENSED BY THE CBK**

BY

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DECLARATION

I declare that this work has not been previously submitted and approved for the award of a degree by this or any other University. To the best of my knowledge and belief, the research proposal contains no material previously published or written by another person except where due reference is made in the research proposal itself.

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DEDICATION

I dedicate this project to my parents for their endless support and love.

ACKNOWLEDGEMENT

I would like to give my deepest appreciation to God for giving me the patience, courage, and strength to work on this research proposal. I would also like to acknowledge my friends, family and classmates in the completion of this research proposal for their endless support and words of encouragement.

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ABSTRACT

The effectiveness of internal controls should be of major importance to every firm due to the fact that the duty of internal controls involves prevention, detection of fraud and lastly, in a firm internal control can help in improving operational efficiency by improving the accuracy and timeliness of financial reporting. For the purpose of this study, the researcher looked to establish the effect of internal controls on the financial performance of commercial banks listed in the NSE and licensed by the CBK. Internal control was considered from the perspective of risk management, control environment, control activities, information and communication and monitoring. This study used primary data. The primary data was collected through administration of a five-point Likert questionnaire by the researcher. Descriptive statistics was used for data analysis in terms of mean and standard deviation Data was then presented by use of tables for easier understanding and interpretation. In addition, data was analyzed by the use of SPSS. From the findings of this study, it was concluded that risk management, control environment, control activities, information and communication and monitoring have a positive relationship with financial performance. This outcome aided the researcher to attain his objectives which were; to examine the effect of risk management on the financial performance of commercial banks listed in the NSE and licensed by the CBK, to establish the effect of control activities on the financial performance of commercial banks listed in the NSE and licensed by the CBK, to assess the effect of monitoring on the financial performance of commercial banks listed in the NSE and licensed by the CBK, to determine the effect of information and communication on the financial performance of commercial banks listed in the NSE and licensed by the CBK and lastly, to establish the effect of control environment on the financial performance of commercial banks listed in the NSE and licensed by the CBK.

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LIST OF ABBREVIATIONS

NSE- Nairobi Securities Exchange.

CBK- Central Bank of Kenya.

KPMG- Klynveld Peat Marwick Goerdeler.

COSO- Committee of Sponsoring Organizations.

ROA-Return on Asset.

ROE- Return on Equity.

GRA- Ghana Revenue Authority.

SPSS- Statistical Package for the Social Sciences.

CHAPTER ONE

INTRODUCTION

1.1 Background of the study

Most firms believe that in order for them to have an improvement on their financial performance, there needs to be an establishment and implementation of proper internal control systems (Kimutai, 2013). Internal controls have become of major importance today in Kenyan banks. Internal control has been recognized in most organizations as one of the most essential ingredients, necessary for the survival of the business, enterprise, or government agencies. Apart from the problem of inadequate resources, firms running a high risk of fraud, errors, misappropriation of funds and inefficient and ineffective operations. Various steps are required in order to lessen if not eradicate the risks by putting in place an internal control system (Abubakar, 2017).

Due to an increase in business failures and recurring problems of fraud, organizations have been quick to put in place their internal control systems which fit their particular operating environment to control these problems. The management of these organizations are under increased pressure to enhance the effectiveness of internal control and to effectively communicate this to the board of directors and shareholders (Kuhn & Sutton, 2010). Sound internal control systems are fundamental to the success and survival of an organization.

The quality of internal controls adopted by organizations has greatly affected the decision-making process by the board of directors and how accurate it will be (Feng & McVay, 2009). In addition, Feng and McVay (2009) suggest that firms which adopt ineffective internal control systems have experienced low returns on assets, high cases of corruption and fraud than those which have effective internal control systems. This is seen through the fall of two banks, Dubai bank and Imperial bank, in 2015. Dubai bank faced capital deficiencies and liquidity problems exposing its creditors, depositors, and the banking sector to financial risk (Abdallah, 2016). On the other hand, Imperial bank collapsed due to central bank officials colluding with some of the lender officials to steal from depositors (Masinde, 2016). The Central Bank of Kenya also pointed out that ineffective banking practices and poor business conditions as the major contributors to its collapse. This goes to show how vital internal controls are in a firm and how essential it is for commercial banks to establish watertight controls if at all it is to achieve improved financial performance.

1.1.1 Internal controls

Internal controls are mechanisms, rules, and procedures put in place by a company to ensure the integrity of financial and accounting information, promote accountability, and prevent fraud. Aside from aiding employees with complying with laws and regulations and preventing assets from being stolen or committing fraud, internal controls can help in improving operational efficiency by improving the accuracy and timeliness of financial reporting (Kenton, 2021).

Internal control is a process effected by a firm's board of directors, management, and other personnel designed to provide reasonable assurance regarding the achievement of objectives regarding operations, financial reporting, compliance with applicable laws and regulations, and protect the organization's reputation (COSO, 2013). Internal controls are measured in terms of internal auditing detection and prevention of financial fraud to the firm (Jensen, 2003).

Saleemi (2000) refers to planning of an organization as an organization chart which shows the organization structure of a company. The chart serves the purpose of showing how a firm has been divided into departments and departments into sections and of most importance to show the responsibilities and tasks that have been assigned to each employee. Employees perform their responsibilities in accordance with the organization plan. Therefore, the organizational plan is needed for effective internal control.

According to Muthusi (2017), the structure of internal controls consists of five components, control environment, this is the central component of internal control systems. Risk assessment, this involves assessment of factors that may affect attaining the firm's objectives. In addition, there is monitoring which involves assessing the quality of internal control structure over time. Also, information and communication, internal control requires that all important information be identified, captured, and communicated in a form and time frame that permits individuals to perform their financial reporting activities. Lastly, control activities which refer to Policies, procedures, and mechanisms are in place to ensure that management directives are followed correctly. According to Amudo and Inanga (2009), internal control systems operate at different levels of effectiveness, to determine if a certain internal control system is effective, the point of decision lies on these five components.

1.1.2 Financial Performance of Commercial banks in Kenya

Financial performance is a measure of how well an organization can use its assets to generate revenues, it is a general measure of a firm's overall financial health over a specified period (Kenton, 2021). Financial performance is used by internal users to determine the company's wellbeing and standing among other firms while for external users, it is used to dictate potential investment opportunities and to determine if the company will be beneficial to them.

According to Stoner (2003), performance refers to an organization's ability to function efficiently, economically, survive growth, and respond to opportunities and dangers in the environment. Companies must continually measure their profitability so as to measure their financial performance. The two most popular measures of profitability are ROA and ROE.

Financial performance of commercial banks can be affected by both internal and external factors. The internal factors are specific bank characteristics which affect the bank's performance since they are basically influenced by the internal decisions of the management and board. External factors are sector or country wide factors that are beyond the company's control and affect the banks' profitability (Al-Tamimi, 2010; Aburime, 2005).

A study by Ongore (2013) shows that financial performance of firms can also be influenced by ownership identity. Ownership identity is divided into foreign and domestic. Currently in Kenya, the number of domestically owned banks are 28 while the number of foreign owned banks are 14 in number. In regard to ownership identity, there have been a number of contradicting studies by scholars. Some scholars suggest that domestically owned commercial banks perform better than foreign banks in developing countries while others suggest that foreign owned commercial banks perform better than domestically owned commercial banks. However, in Kenya ownership identity has played an insignificant role in financial performance of commercial banks, it has mainly been internal factors (Ongore, 2013).

It's important to remember that no single metric of financial performance should be used in isolation. Rather, a comprehensive assessment of a company's success should be made utilizing a variety of performance indicators.

1.1.3 Financial performance and internal controls

An effective internal control system must ensure the protection and safeguarding of assets, prevention and detection of errors and distortions, the execution of orders and instructions by company management to ensure the completeness and accuracy of accounting records, as well as the timely preparation of credible financial statements. The effectiveness of internal control is of great importance to the firm as a whole and to enhance the efficiency of subsidiaries and departments. This is because the control function acts as a link and means of feedback between the management and staff of a company (Ekessa, 2017).

Internal control systems, such as internal audits, are designed to improve the consistency of financial performance, this can either be directly or indirectly by increasing accountability among information providers in an organization (Jensen, 2003). According to Feizal (2005), an effective internal control system is inextricably linked to an organization's ability to accomplish its revenue targets. A regular evaluation of the dependability and integrity of financial and operating information, as well as a review of controls used to safeguard assets, is required for effective internal control for revenue creation and maintenance (Ittner, 2003).

Organizations establish goals and objectives which are then assessed to know the risks that may be encountered when attaining them. A control plan and internal controls help to guarantee that operations run smoothly, that resources are protected, and that the goals are met profitably (Chester, 2003). Internal controls help an organization attain its objectives by putting in place a systematic and a methodical strategy to assess and improve the efficacy of risk management processes, resulting in improved financial performance (Bonnevie, 2003).

Commercial banks are experimenting with innovative strategies to boost profits and save operational expenses. An effective internal control system is one of the measures. Internal controls, according to a survey by KPMG (2012), provide the proper solutions for decreasing operating expenses while maximizing revenues. Internal control systems help staff meet the bank's financial objectives by responding to important business, operational, financial, compliance, and other risks (Ekut, 2011). As a result, it's critical to link internal control systems to commercial bank performance.

1.1.4 Commercial banks in Kenya

Commercial banks are financial institutions that accept deposits, offer checking account services, make various loans, and offer basic financial products like certificate of deposit and savings account to individuals and small businesses (Kagan, 2020). It is basically where most people do their banking. The Central Bank of Kenya is the sole regulator of the banking and financial institutions in Kenya.

The banking industry is so vital to the economy's stability and prosperity that the government must not allow it to operate freely. Regulations and supervisions have thus become crucial not only in the enforcement of rules and regulations, but also in the assessment of bank assets' soundness, capital sufficiency, and management (CBK, 2013). This regulatory framework ensures that banking institutions and the individuals and businesses with whom they do business are both transparent (Oloo, 2010). The goal of regulatory reforms and recommendations is to assist banks and other financial institutions in becoming stronger players, ensuring their long-term survival and, as a result, higher returns to shareholders and greater benefits on the Kenyan economy (Ndung'u, 2010).

The Covid -19 pandemic has changed the direction of the banking industry and other sectors of the economy into an unfamiliar business environment. With this continued situation worldwide, the banking sector continues to adapt to the economic dynamics imposed by the disruption. Some of the interventions that have been put in place are supporting affected customers and creating innovative solutions, including blended financing and the use of movable assets registry to address credit access to vulnerable sectors (Mukuru, 2021). Currently, there are 42 licensed commercial banks in Kenya.

1.2 Problem Statement

Internal controls that are properly designed and implemented will always result in enhanced financial performance (Mawanda, 2008). Internal control mechanisms that are weak have been reported to be ideal for committing fraud and scandals. This has been seen through the financial scandals at Enron and WorldCom. The response to these scandals brought about the Sarbanes-Oxley Act which demands that the management should take full responsibility for internal control

systems over financial reporting within the company and provide assessment of its effectiveness (Asiligwa, 2015).

Jensen and Meckling's (1976) agency theory states that principals and agents use contracting to maximize their wealth. Agents, on the other hand, may find themselves acting against the interests of the principals in order to increase their own riches. To address this agency problem, internal controls should be implemented as a safety net (Jensen & Payne, 2003).

Despite guidelines set by the Central Bank of Kenya, there have been several cases of failure in performance of banks that have been caused by fraud and weak internal controls (FLSTAP, 2011). For instance, there have been three banking institutions that have been put under receivership. The Dubai Bank of Kenya was put under receivership because it continued to operate under poor financial conditions despite being penalized by the CBK. There is also the Imperial Bank of Kenya, which was once the 19th largest bank in Kenya, which was put under receivership due to unsound business practices (Umpiantu, 2020). Due to what the regulator described as "unsafe financial conditions," Chase Bank was placed into receivership, leaving the question of the gaps that exist within the banking sector as a result of such multiple breaches unanswered (Ngigi, 2015).

Empirical studies have been carried out before, for example, Muio (2012), investigated the financial performance of private hospitals in Nairobi using internal control systems. This study, however, did not incorporate commercial banks. In addition, a study by Kamau (2014) studied on the effect of financial performance on manufacturing firms in Kenya. There was also a study by Ng'etich (2017) on the impact of internal controls on NSE-listed companies' financial performance. Mawanda (2008), internal control systems and financial performance of Ugandan higher education institutions

This study will be unique in that it will examine the impact of internal controls on the financial performance of commercial banks in Kenya that have been licensed by the CBK and listed in the NSE. Focusing on factors such as control activities, risk management, monitoring, information and communication and control environment have an effect on financial performance.

1.3 Research Objective

1.3.1 General Objective

To establish the effect of internal controls on the financial performance of commercial banks in Kenya listed in the NSE and licensed by the CBK.

1.3.2 Specific Objectives

1. To examine the effect of risk management on the financial performance of commercial banks listed in the NSE and licensed by the CBK.
2. To establish the effect of control activities on the financial performance of commercial banks listed in the NSE and licensed by the CBK.
3. To assess the effect of monitoring on the financial performance of commercial banks listed in the NSE and licensed by the CBK.
4. To determine the effect of information and communication on the financial performance of commercial banks listed in the NSE and licensed by the CBK.
5. To establish the effect of control environment on the financial performance of commercial banks listed in the NSE and licensed by the CBK.

1.3.3 Research Questions

1. What is the effect of risk management on the financial performance of commercial banks listed in the NSE and licensed by the CBK?
2. What is the effect of control activities on the financial performance of commercial banks listed in the NSE and licensed by the CBK?
3. What is the effect of monitoring on the financial performance of commercial banks listed in the NSE and licensed by the CBK?
4. What is the effect of information and communication on the financial performance of commercial banks listed in the NSE and licensed by the CBK?
5. What is the effect of control environment on financial performance of commercial banks listed in the NSE and licensed by the CBK?

1.4 Scope of the study

This research is limited to commercial banks listed in the NSE and licensed by the CBK since the researcher does not have the capacity to cover the whole banking sector. The study reviews internal control systems and the effect they have on the financial performance.

1.5 Significance of the study

1.5.1 The Management

This study is beneficial to the management as it sheds light on how internal controls are effective in helping a firm to achieve its profitability and performance targets. The management gets to see how internal control systems play a key role in maintaining and building a firm's reputation. They will be able to note that effective internal control systems help in achieving organizational goals and objectives. This study will generally contribute to the understanding of internal controls and its impact on financial performance of commercial banks listed in the NSE and licensed by the CBK.

1.5.2 The Government

The findings of this study will guide the government on the importance of an effective and efficient internal control system and how it plays a key role in the financial performance of commercial banks whose shares are traded on the NSE and are regulated by the CBK. The government will also get to understand how internal controls aid in economic growth and development of the country. The findings will therefore assist the government to assess whether the laws and regulations that have been put in place emphasize on the importance of having proper internal controls in the banking industry.

CHAPTER TWO

LITERATURE REVIEW

2.1 Introduction

This chapter focuses on the empirical and theoretical review relating to the impact of internal controls on a company's financial performance. It will also cover on the research gap and conceptual framework.

2.2 Theoretical review

The agency theory, attribution theory, and contingency theory are the three theories examined in this study.

2.2.1 Agency theory

Agency theory was developed by Jensen and Meckling (1976). They suggested a theory of how the governance of a company is based on the conflicts of interest between the company's owners (principal), its managers and major providers of debt finance (agents). The goal of theory is to solve problems that can arise in agency relationships which involve the agent and principal which is due to the fact that each of these groups has different interests and objective (Carol, 2020). A variation in risk aversion and a difference in aims are two issues that could occur. In most circumstances, the firm's agents have more information than the principals, resulting in information asymmetry that impairs the ability of the firm's owners to oversee whether the agents are protecting their interests (Jensen & Meckling, 1976).

However, the agency theory has received some criticism before. Perrow (1986), criticized the agency theory stating that it is only concentrated on the agents' side with regards to the 'principal and agent problem'. Perrow was of the opinion that the problem may also be from the principal side. Perrow observed that this theory is unconcerned about the principals who deceive, neglect, and exploit the agents. Perrow also added that agents are unknowingly dragged into work to work in a risky environment and without any scope of what limits they should not cross. Perrow's

argument became prominent in finance literature and has been developed as a theory known as the stewardship theory (Donaldson, 1990).

To ensure that the interests of the principal and agents are aligned, this theory suggests that a contract is entered for the benefit of the principal. It is looking to see that the interests of the principal are met. The relationship between the managers(agents) and owners(principal) can be further reinforced by employing experts and systems such as audit and control environment (Jussi & Petri, 2004).

In addition, the theory recognizes that any incomplete information about the agent's connection, interests, or work performance could lead to a selection dilemma. Adverse selection and moral hazard have two effects on the agent's output: not having adequate information of what should be done and not accomplishing exactly what the agent is assigned to do. As a result, the agency theory assumes that principals and agents behave rationally and use contracts to maximize their wealth (Jensen & Meckling, 1976). This hypothesis is necessary to the study because the internal controls are put in place to ensure that no agency problem exists within the firm. The internal control system further helps to reduce information asymmetry that may occur within the firm which in this case is commercial banks.

2.2.2 Attribution Theory

Attribution theory is concerned with how people explain the source of certain behavior and events. For example, people can credit results to ability, effort, or luck. Fritz Heider, first suggested that people are naive scientists who try to work out the causes of end results for themselves and other people (1958). He argues that behavior is determined by a combination of both internal and external forces. The theory examines the information gathered and how it is combined to form casual judgement. Therefore, if employees were to assume that their success is due to their own abilities and effort, they are expected to act differently than they would if they believed the success of their work was because of chance.

One of the major criticism attribution theory has faced is that it is of the assumption that people are logical and systematic thinkers hence the theory has been reduced to be mechanistic and

reductionist. The theory is also seen to have failed to take into account social, historical, and cultural factors which also shape a person's character (Shrestha,2017).

An auditor's role in a firm is to ensure financial statements have no material misstatements either due to fraud or error. The auditor's ability to detect fraud is further addressed by Reffett's (2007) study, which predicted that auditors would be held accountable by assessors if they failed to detect fraud after identifying the scam as a fraud risk.

Hence, this theory recommends that auditors report on the effectiveness of a firm's internal control. They are expected to have a greater insight on the internal controls put in place, evaluate the design and the implementation of the internal controls, and test their operating effectiveness. This is deemed necessary for auditor's reliance and possibly minimize on other substantive audit procedures that serve as a guarantee that there are no material misstatements in regard to the completeness, authenticity, and accuracy of financial records of the firm (Muhunyo,2018).

The attribution theory is for in the occurrence of fraud, the identified parties, auditors, should be held accountable incase unsatisfactory audit services were provided (Reffett, 2007). In reference to this study, this theory places the burden of fraud reporting to the relevant individual, auditors, within the firm. Despite the rampant growth in technology, that has adversely changed the internal control systems that firms have put in place, there will always be a need for people to ensure that the systems run well. As a result, individuals in authority are responsible for ensuring that all relevant regulatory and compliance requirements are met. In the context of our research, this concept implies that auditors should be among the first to disclose fraud when it occurs.

2.2.3 Contingency theory

The contingency theory was brought about by Fred Fiedler. It is an approach on leadership and management that suggests there is no exclusive or fixed way to deal with situations in a firm and the most appropriate style of management depends on the context of the situation be it internal or external (Norman, 2021). Fiedler studied the characteristics and personality of leaders and based the theory on two factors which are leadership style and situational favorableness (MacLeod, 2010). This theory suggests that organizational effectiveness is contingent on how the type of

technology, how fast the environment changes, the size of the organization, the characteristics of its structure, and its data complement each other (Woods, 2009).

One of the biggest criticisms it has received is the lack of flexibility, Fiedler believed that because people's natural leadership styles are fixed, the most effective way to deal with situations is to change the leader. Fiedler did not allow for flexibility in leaders (Dowding, 2010). Another criticism that the contingency theory has received is that it fails to adequately explain what should be done when there is a leadership/situation mismatch in the workplace (Wallace, 2016).

The contingency theory is used to describe the relationships between the context, structure, and efficacy of internal control and organizational performance, with a focus on financial reporting reliability. Previous studies suggest that internal auditors of a firm who have specialized skills and higher in internal audit ability will achieve internal control effectiveness analysis and the firm will benefit from the organizational effectiveness through internal control mechanism efficiency. (Cadez & Guilding, 2008)

Fisher (1998) argued that the contingency theory states that the design and use of internal control systems is dependent on the context of the organizational setting in which these controls are operating. Cadez and Guilding (2008), identified some factors that impact management control systems which include; technology, size and structure of the organization, external environment, organizational culture, and strategy.

Contingency indicates that one thing depends on other things," explains Daft (2012) in his book, and "Contingency theory means that it depends." Task-oriented auditing functions can be loosely structured. Auditors must carefully organize their inspections and take variables into consideration to get the work done, as the functions might vary significantly based on the area of a firm under audit and the type of business model. The contingency theory can also be applied to the structure of an audit team. Typically, audit projects are assigned to audit team supervisors. They then assemble impromptu audit teams for the projects, selecting auditors based on subject-matter competence and experience, as well as auditor availability, all of which add up to audit project contingencies.

2.3 Empirical Review

Previous studies on the influence of internal controls on financial performance are examined under the empirical review.

2.3.1 The relationship between risk management and financial performance

Hameeda and Al-Ajmi (2012) carried out a study on conventional and Islamic banks in Bahrain. The objective of the study was to find out the risk management practices of these banks. Their study found out that banks in Bahrain had a clear understanding of risk and risk management and also had efficient risk identification, risk assessment analysis, risk monitoring and credit risk analysis. In addition, they established that credit, liquidity, and operational risk were the most important risks facing both conventional and Islamic banks in Bahrain. The risk management practices were determined by the extent to which managers understood risk and risk management, efficient risk identification, risk assessment analysis, risk monitoring and credit risk analysis. From the study, risk management was seen to have a positive relationship with financial performance. This study used primary data whereby a sample of bankers were surveyed through questionnaires. The data was then analyzed by use of SPSS.

The five components of risk management used as the independent variable in a study by Wanjohi (2013) on the relationship between financial performance and financial risk management of commercial banks in Kenya were risk measurement skills, risk management environment of the institution, risk monitoring, risk mitigation procedures, and adequate internal controls of the organization. For the next five years, these five factors were related to the ROA mean (2008-2013). Financial risk management has a significant impact on commercial banks' financial performance in Kenya, according to this study. Data from both primary and secondary sources was used. Questionnaires were used to collect primary data, while several CBK Bank Supervision Annual Reports were used to obtain secondary data. Multiple regression analysis was used to examine the data from this study.

In Kenya, Kamau (2010) conducted research on the integration of risk management by commercial banks. Kamau's study was based on forty-four active banks as per the CBK in 2010. His study aimed to identify the risks encountered by commercial banks and the risk management practices adopted by commercial banks to lessen these risks. Credit, operation, reputation, and compliance

risks were identified as critical and frequently encountered in the study. The least risk they encountered was liquidity risk, and the majority of banks were found to apply both qualitative and quantitative risk measuring approaches. This study was carried out through a census survey on all licensed banks in Kenya. Also, questionnaires were handed to the risk management staff.

In addition, there was a study by Oluwafemi, Obawale, and Olawale (2013) on risk management and financial performance of commercial banks in Nigeria. Secondary data was used for this research. The data for this study was collected through annual observations of ten Nigerian banks between 2006-2009. The profitability of these firms was in ratios of their ROA and ROE. This study, like others before it, revealed that there is a significant link between financial performance and risk management. Also, this study concluded that better risk management in areas such as management of funds and reduction of unnecessary costs enhances the financial performance of firms.

2.3.2 The relationship between control activities and financial performance

Mawanda (2008) investigated the influence of internal control mechanisms on Ugandan higher education institutions. The goal of Mawanda's research was to determine the link between internal control systems and financial performance in a Ugandan institution of higher learning. The control environment, internal audit, and control activities were all considered while looking at internal controls. From the standpoint of internal controls, the researcher set out to determine the causes of persistently poor financial performance. A total of 270 Uganda Martyrs University staff members made up the target population. Both secondary and primary data were collected, and a case study research design was used. A formal interview guide and structured questionnaire were used to collect data. Data collected was analyzed using SPSS. The study acknowledged the role of control activities and its effect on the financial performance of organisation and its positive significant effect.

A study by Origa (2015), on the impact of internal controls on manufacturing enterprises' financial performance in Kenya. The functionalities that were considered under internal controls include, monitoring, risk assessment and control activities. Origa's study showed that control activities have an effect on the financial performance. Both primary and secondary data were collected. A cross sectional survey which involved 65 manufacturing firms in Kenya was carried out. The

primary data was collected by the use of a structured questionnaire. Data collected was analyzed using descriptive statistics and performance comparison done from 2011 to 2014. From this study it was seen that manufacturing firms carry out control activities as a functionality of internal controls as it has a significant effect on financial performance.

Umar and Dikko (2018) investigated the impact of internal control on commercial banks' performance in Nigeria. Control environment, risk assessment, control activities, information and communication, and monitoring were used to assess internal control, while accounting and market measurements were used to analyze bank performance. There is a favorable and significant association between control activities and bank performance, according to the findings. The study proved that performance increases if there are control activities. Data from this study was gathered from questionnaires that were administered to bank staffs of all branches of commercial banks in Nigeria. The data was then analyzed using SPSS.

In addition, a study by Oyoo (2014) on internal control's impact on the financial performance of Kisumu's microfinance institutions, showed that control activities are essential in the financial performance of micro-finance institutions. The study showed that there is a positive relationship between financial performance and control activities. The control environment, risk assessment, control activities, information and communication, and monitoring were all taken into consideration when it came to internal control while financial performance was concerned with liquidity. Questionnaires were used in the collection of data and the data collected was analyzed using correlation and presented using tables.

Also, a study by Shabari, Saad, and Bakar (2016) on the effects of internal control systems on cooperative profitability in Malaysia, showed that control activities play an important role in a firm's profitability. Control activities were found to have a good impact on cooperative profitability. Control environment, risk assessment, control actions, information and communication, and monitoring were all interconnected components of internal control. A qualitative technique was used in this study, with a case study approach being used. Interviews and documentary evidence were used to gather data.

2.3.3 The relationship between monitoring and financial performance

According to Treba (2003), periodically assessing how effective internal controls are in order to know whether or not they are correctly built, and functioning is an important part of any full internal control system. Monitoring has a favorable impact on financial performance, according to a study by Muraleetharan (2011) on the impact of internal controls on the financial performance of public and private enterprises in the Jaffna district of Sri Lanka. Internal control was evaluated using the control environment, risk assessment, control actions, information and communication, and monitoring. There were 181 respondents in the research, who worked for 47 public and private institutions in the Jaffna district. The data was collected through self-assessment questionnaire and personal interviews. The data was analyzed using SPSS where regression tools were used.

Ng'etich (2017) investigated the impact of internal controls on financial performance of NSE-listed companies. Internal control was being measured by control environment, risk assessment, control activities, information and communication and monitoring. Through his study, he was able to establish that monitoring plays a role in the financial performance of firms. This study adopted a descriptive research design and the data used was secondary data obtained from the NSE statements. From this study, it was seen that financial performance and monitoring are positively and significantly related.

Agbenyo, Jiang and Cobblah (2018) researched on the impact of government internal control systems on financial reporting on the Ghana Revenue Authority. The variables of internal controls that were considered were control environment, risk assessment, control activities, monitoring information and communication and collection performance of internal control systems. This study implied that there is a strong positive relationship between monitoring and financial reporting quality at GRA. The data from this study was collected through both primary and secondary data. The secondary data was collected by reviews from previous articles while the primary data through comprehensive questionnaires. The data was analyzed using both descriptive statistics and correlation matrix.

Lagat (2018) looked into the effect of internal control systems on the financial performance of government-owned sugar firms in Kenya. Internal controls were investigated using the control environment, risk assessment, control activities, information and communication, and monitoring

methods, while financial performance was investigated using the change in performance approach. The population consisted of five state-owned sugar companies in Kenya. The study found out that monitoring has a positive effect on financial performance. Primary data was used. The data was collected using a structured questionnaire which was then analyzed using descriptive and inferential statistics on SPSS.

There is also a study by Makut and Ibrahim (2021), on the effect of internal control on performance of cooperatives in Nigeria. Internal controls were measured using control environment, control activities and monitoring. Unlike the other studies, this study found that monitoring is of insignificance to performance of cooperatives. Data from this study was collected using a five-point Likert-scale questionnaire and used multiple-linear regression to analyze it.

2.3.4 The relationship between information and communication and financial performance.

The financial performance of higher education institutions in Puntland, Somalia, as a result of internal control systems, was studied by Abdullahi and Muturi (2016), who found a favorable association between information and communication and financial performance. Internal controls were looked at in the perspective of information and communication systems, internal audit, and monitoring activities. The data was collected using questionnaires from a sample size of 30 respondents and analyzed through SPSS.

Muhunyo (2018) investigated the financial performance of public higher education institutions in Nairobi County, Kenya, using internal control systems. Information and communication, according to the study, have a favorable and significant impact on the financial performance of higher education institutions in Nairobi County, Kenya. Primary data was acquired from 96 employees from various categories of staff in various departments of public institutions of higher learning in Nairobi County using open and closed ended questionnaires. Data analysis was carried out through descriptive statistics and multiple linear regression analysis to establish the relationship between dependent and independent variables.

In the Kurdistan area of Iraq, Ahmed, and Muhammed (2018) did a study on internal control systems and their association with financial performance in telecommunication enterprises.

Control environment, risk assessment, control activities, monitoring information, and communication were the variables for internal controls. This study revealed that information and communication have a positive and significant relationship with financial performance. Both primary and secondary data were collected for this study. The primary data was collected by use of questionnaires handed to employees of the selected companies while secondary data was collected through the audited financial statements. The data was analyzed using SPSS where regression tools were used.

Kisanyanya (2018) conducted research in Vihiga County, Kenya, on internal control mechanisms and financial performance of public higher education institutions. Information and communication have a favorable and considerable impact on the financial performance of the organizations studied, according to the research. Primary data was used for this study, it was collected using semi-structured questionnaires from a sample of 96 employees. The data was then analyzed using SPSS.

Nyagah (2014), carried out research on the effect of enterprise risk management on financial performance of pension fund management firms in Kenya. Enterprise risk management was being measured through, event identification, risk assessment, objective setting, risk response, internal environment, control activities, information, and communication. This research stated that information and communication have a negative but significant effect on financial performance. Both primary and secondary data was gathered. Primary data was collected through questionnaires based on objectives of the study while secondary data through financial statements of each pension fund management firms. Data was analyzed using both descriptive and linear regression analysis.

2.3.5 The relationship between control environment and financial performance

The impact of internal controls on the financial performance of Kenyan manufacturing enterprises was explored by Kamau (2014)., finding a strong and favorable link between control environment and financial performance. This study entailed data from both primary and secondary sources The primary data comes from structured questionnaires, while the secondary data comes from financial statements. SPSS was used to do the data analysis.

Mutesi (2016) identified a positive and significant link between control environment and financial performance in Rwandan public institutions after doing study on internal control systems' impact on financial performance. The information was gathered via data from both primary and secondary sources. The primary information was gathered from questionnaires and interviews whereas the secondary research is done using other methods. The data was analyzed using the COSO internal control integrated framework.

Kinyua, Gakure, Gekare, and Orwa (2015) looked into the impact of internal control systems on NSE-listed firms' financial performance. The research focused on objectives such as internal control activities, internal audit, control environment, risk management, and the role of corporate governance controls. The results of this study revealed that the control environment has a substantial impact on financial performance. Data was gathered from both primary and secondary sources. The primary data was gathered via structured questionnaires, while the secondary data was gathered through the review of audited annual reports, publications, and documents. The data was analyzed using SPSS.

Also, Zar (2019) researched on the effects of internal control practices on financial performance of Myanmar Interfaith Network on AIDS in Asia. The variables of internal control practices for this research were, control environment, risk assessment, control practice, information and communication and monitoring. This research showed that control environment has a positively significant relationship with financial performance. The research implemented primary data by use of five-point Likert-scale structured questionnaires and interviews both personal and telephone. The data was then analyzed by descriptive research method and multilinear regression analysis.

Uwingabiye (2019) conducted research on the internal control components and financial performance in Rwandan government organizations. Internal control systems were measured by the control environment, risk assessment, control practice, information and communication, and monitoring. Financial performance was found to have a favorable and significant association with the control environment. There was a mix of primary and secondary data used. Primary data was gathered through the distribution of questionnaires, while secondary data was gathered through the use of Rwanda Social Security Board yearly reports. The data was analyzed by use of SPSS.

2.4 Research Gap

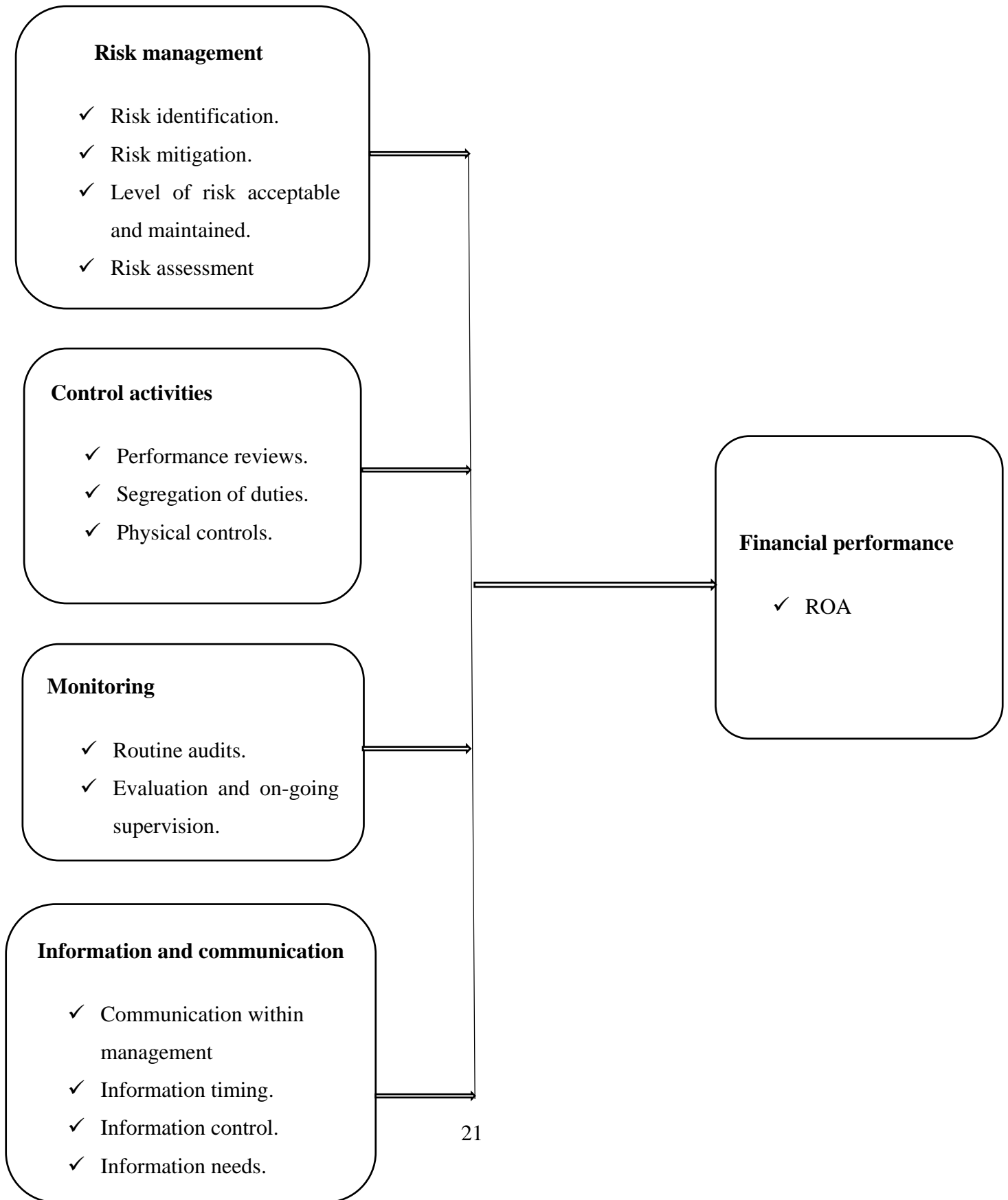
There has been a lot of research on the impact of internal controls on financial performance of businesses, but there isn't much on the impact of internal controls on commercial banks. The influence of internal controls on commercial banks' financial performance was studied in Nigeria, however this study will be conducted in Kenya. Some of the research done on commercial banks has been based on risk management and not on internal controls unlike this study. Also, some of the research looked at the impact of internal controls on factors such as financial reporting, general performance, cooperative responsibility, and institutions of higher learning unlike this study which focuses on financial performance.

This study will also specifically look at commercial banks that have been listed in the NSE and have been licensed by the CBK.

2.5 Conceptual Framework

Independent variable

Dependent variable



Control environment

- ✓ Integrity and ethical values.
- ✓ Assignment of authority and responsibilities.
- ✓ Organizational structure.
- ✓ Commitment to competence by employees.

Figure 2.1 Conceptual framework

Source: Researcher, (2021)

2.6 Operationalization of variables

This segment looks to define variables in the conceptual framework into measurable factors. Financial performance is measured using ROA. On the other hand, risk management is measured by risk identification, risk mitigation, risk assessment and the level of risk acceptable and maintained. Also, control activities are measured through performance reviews, segregation of duties and physical controls and lastly, monitoring is measured through routine audits and evaluation and on-going supervision.

Variable	Indicators	Measurement
Financial performance	✓ ROA.	Ratio scale.
Risk management	<ul style="list-style-type: none"> ✓ Risk identification. ✓ Risk mitigation. ✓ Risk assessment ✓ Level of risk acceptable and maintained. 	Likert scale.
Control activities	<ul style="list-style-type: none"> ✓ Performance reviews. ✓ Segregation of duties. ✓ Physical controls. 	Likert scale.
Monitoring	<ul style="list-style-type: none"> ✓ Routine audits. ✓ Evaluation and on-going supervision. 	Likert scale.
Control environment	<ul style="list-style-type: none"> ✓ Integrity and ethical values. ✓ Assignment of authority and responsibilities. ✓ Organizational structure. 	Likert scale

	<ul style="list-style-type: none"> ✓ Commitment to competence by employees. 	
Information and communication	<ul style="list-style-type: none"> ✓ Communication within management. ✓ Information timing. ✓ Information control. ✓ Information needs. 	Likert scale

CHAPTER THREE

RESEARCH METHODOLOGY

3.1 Introduction

This chapter discusses the research design, study population, sampling procedure and sample size, data collection methods, research quality, and ethical considerations, all of which are relevant to the field of study.

3.2 Research Design

Research design is the framework of research methods and techniques chosen by a researcher. The design allows researchers to refine on the research methods that are suitable for the subject matter and set up their studies up for success (Bhat, 2020). This study has applied a descriptive research design. Descriptive research design can be used to derive information about the current status of an occurrence and to describe “what exists” with respect to variables or conditions in a situation (De Vaus, 2011). According to Ng’etich (2017), a descriptive research design is appropriate when collecting information about people’s attitudes, opinions, and habits. Therefore, through the measures of risk management, control activities, monitoring, control environment and information and communication in this study the respondent’s attitudes, opinions or habits have shown how the financial performance of commercial banks has been affected.

3.3 Population of the study

According to Momoh (2020), a population is a group of people from which a statistical sample is taken for a study. A population can also be defined as a sum total of elements that a researcher is interested in researching and analyzing (Upagade & Shende, 2012). This study has targeted commercial banks that have been listed in the NSE and are licensed by the CBK which are 7.

3.4 Sampling technique and sample size

According to Tuovila (2020), sampling is the process used in statistical analysis in which several observations that have been determined in advance are taken from a larger population. A sample is a representative subset of a population (Wigmore, 2018).

3.4.1 Sampling technique

The sampling technique that this study has employed is non-probability sampling. The type of non-probability sampling used is purposive sampling to aid in selecting the banks and respondents. The basic goal of a purposive sample, according to Lavrakas (2008), is to develop a sample that can be logically considered to be representative of the population. Hence, for this study, purposive sampling has been used in getting data from respondent.

3.4.2 Sample size

The sample size for this study was 7. This is the number of commercial banks that are listed in the NSE and licensed by the CBK.

3.5 Data collection methods

Data collection is the act of gathering information from all relevant sources to find answers to the research problem, test the hypothesis and evaluate the outcomes (Dudovskiy, 2011). This study implemented primary data. Primary data is that which is collected firsthand by the researcher. The primary data was collected by use of a survey questionnaire which was divided into four sections containing close-ended questions. The questionnaire was self-administered whereby it was handed over to the respondents.

3.6 Data analysis

The study conducted an inferential analysis. The relationship between the independent and dependent variables was calculated using the multilinear regression model. This model will be used to see if commercial banks' financial performance is a function of the variables identified in the specific objectives.

$$Y = a + B_1 X_1 + B_2 X_2 + B_3 X_3 + B_4 X_4 + B_5 X_5 + e$$

Y = Financial performance.

a = constant.

B₁, B₂, B₃ = coefficients of independent variables.

X_1 = Risk management.

X_2 = Control activities.

X_3 =Monitoring.

X_4 =Information and communication.

X_5 = Control environment

e = error term.

3.7 Research quality

3.7.1 Reliability

Dudovskiy (2011), defines reliability as the degree to which a research method produces stable and consistent results. A particular measure is considered to be reliable if its application on the same object of measurement several times produces the same results. The aspect of reliability was brought out with the consistency that was gathered from the questionnaire.

3.7.2 Validity

According to Middleton (2019), validity refers to how accurately a method measures what is intended to measure. In simpler terms Middleton says it is about the accuracy of a measure. This study used a questionnaire as a method of data collection hence validity is of importance. The viability of my questionnaire was done by my supervisor. The accuracy of the answers from the respondents played a vital role.

3.8 Ethical considerations

This research ensured that all ethical guidelines are adhered to. Therefore, transparency was maintained. The methods used in the collection of data for this research are fully disclosed and authors of various material that have been quoted are acknowledged. The researcher ensured that the respondent's consent was acquired when administering the questionnaire, confidentiality was maintained and being just was also key during this process. Also, the questionnaire was answered

voluntarily hence no respondent was forced to provide any information. The researcher ensured that the data gathered was only being used for academic purposes.

CHAPTER FOUR

DATA ANALYSIS

4.1 Introduction

This chapter is centered on presentation of analysis of the results retrieved from the gathered data aimed to achieve the study objectives.

4.2 Sample representation

4.2.1 Response rate

The study sought data from 7 banks, and 7 banks responded, accounting for 100 percent of the respondents' rates. According to Mugenda and Mugenda (2003), a 50% response rate is enough, 60% is good and above 70% rated very good. Also, Kothari (2004) is of a similar opinion, that a response rate of 50% is adequate, while a response rate greater than 70% is very good. This suggests that based on these assertions, the response rate of, 100%, is very good hence being suitable for data analysis and reporting.

4.3 Descriptive analysis

4.3.1 General information

Table 4.1 Gender of respondents

Gender	Frequency	Percentage
Male	5	71.43
Female	2	28.57
Total	7	100

Source: Researcher, (2022)

The study aimed to determine the gender of the respondents hence requesting the respondent to indicate their gender. The research found that majority of the respondents were male as shown by

71.43% while the female respondents represented 28.57%. This serves as evidence that both genders were involved in this research and the findings did not suffer from gender bias.

Table 4.2; Age Distribution

Age bracket	Frequency	Percentage
Below 25	0	0
25 to 34	3	42.86
35 to 44	3	42.86
45 to 50	1	14.28
Above 50	0	0
Total	7	100

Source: Researcher, (2022)

The study sought the respondent to specify on their age bracket. From the findings, 42.486% of the respondents were aged between the ages of 25 to 34, 42.86% between 35 to 4, 14.28% between 45.50%. This shows that most respondents were between the ages of 25 to 50, none of them were in the categories of below 25 or above 50.

Table 4.3; Level of education

Level of education	Frequency	Percentage
Certificate/diploma	0	0

Undergraduate degree	5	71.43
Master's degree	2	28.57
PHD	0	0
Total	7	100

Source: Researcher, (2022)

The study requested the respondent to indicate their highest level of education. From the findings it is seen that 71.43% of the respondents indicated their highest level of education as undergraduate degree while 28.57% indicated their highest level of education is master's degree. This indicates that most of the respondents focused on this study had university degrees as their highest level of education.

Table 4.4; Period of service

Years of service	Frequency	Percentage
Less than 2 years	0	0
2 to 5 years	1	14.29
6 to 10 years	4	57.14
More than 10 years	2	28.57
Total	7	100

Source: Researcher, (2022)

The study requested the respondents to indicate the number of years they have served at the firm. From the information gathered the study found that 14.29% of the respondents had served for a period of 2 to 5 years, 57.14% for a period of 6 to 10 years and 28.57% had served for more than 10 years. This implies that majority of the respondents had served the banks for a considerable amount of time meaning they had adequate knowledge about the firm that could be relied upon by this study.

4.3.2 Risk management and financial performance

The study examined the effects of risk management as a measure of internal controls on financial performance of commercial banks listed in the NSE and licensed by CBK. Below are the results of the findings.

Table 4.5; Risk management and financial performance

Statements	Mean	Std. Deviation
The firm has allocated funds for the risk management function	4.2857	0.75593
Our bank has established mechanisms that aid in identifying, monitoring, and controlling various risks that may occur during the course of business	4.7143	0.48795
The management has made clear the relevant objectives for the firm	5.0000	0.00000
The management identifies the risks that may affect the achievement of the objectives put in place	4.7143	0.48795

From the above findings, it was observed that most commercial banks listed in the NSE and licensed by the CBK carried out constant risk management procedures. From the outcomes, these commercial banks have allocated funds for the risk management function, this had (M=4.286 , S= 0.7559), have established mechanisms that aid in identifying, monitoring, and controlling various risks that may occur during the course of business (M=4.714, S=0.4880), the management has made clear the relevant objectives for the firm (M=5.000, S=0.000) and the management identifies the risks that may affect the achievement of the objectives put in place (M=4.714, S=0.4880). These outcomes show that most commercial banks listed in the NSE and are licensed by the CBK have observed risk management as a measure of internal controls.

4.3.3 Control activities and financial performance

The influence of control activities on the financial performance of NSE-listed commercial banks and regulated CBKs was also looked into.

Table 4.6; Control activities and financial performance

Statements	Mean	Standard deviation
There is a clear separation of roles at our bank	4.4286	1.13389
The bank's system access is only limited to authorized personnel	5.0000	0.00000
There are corrective measures taken to address weakness in performance	4.4286	0.78680
There is supervision on the work of the junior staff by the senior staff	4.7143	0.48795

From the above findings, it was noticed that control activities were an important factor as a measure of internal controls. The results revealed that these commercial banks have a clear

separation of roles at our bank (M=4.429, S=1.134), access is only limited to authorized personnel (M=5.000, S=0.000), corrective measures taken to address weakness in performance (M=4.429, S=0.7868) and supervision on the work of the junior staff by the senior staff (M=4.714, S=0.4880). These observations reveal that most commercial banks listed in the NSE and are licensed by the CBK have observed control activities as a feature of internal controls.

4.3.4 Monitoring and financial performance

The study sought to assess the effect of monitoring on financial performance of commercial banks listed in the NSE and licensed CBK. The outcomes of this analysis are as provided below.

Table 4.7; Monitoring and financial performance

Statements	Mean	Standard deviation
The management has designated responsibilities for timely review of audit reports and resolving any defaults noted in those audit reports	4.4286	0.53452
The employees at our bank make daily reconciliation on accounts	4.5714	0.53452
Monitoring has aided in evaluating the quality of performance of our bank over a period of time	4.4286	0.53452
There are frequent external audits on our bank's financial reports	4.1429	1.46385

From the above results, it was discovered that monitoring is a functionality of internal control for commercial banks listed in the NSE and licensed by the CBK. This is evident through the outcomes of the study that illustrated that the management has designated responsibilities for timely review of audit reports and resolving any defaults noted in those audit reports (M=4.429, S=0.5345), the employees at our bank make daily reconciliation on accounts (M=4.571, S=0.5345), monitoring has aided in evaluating the quality of performance of our bank over a period of time(M=4.429,

S=0.5345) and there are frequent external audits on our bank’s financial reports (M=4.143, S=1.464). These findings show that most commercial banks listed in the NSE and are licensed by the CBK have observed monitoring as a feature of internal controls.

4.3.5 Information and communication and financial performance

The goal of the study was to see how information and communication affected the financial performance of commercial banks listed on the NSE and regulated CBK. Below are the outcomes of the findings.

Table 4.8; Information and communication and financial performance

Statements	Mean	Standard deviation
The reporting system at the bank clarifies on all the responsibilities of each department at the bank	4.5714	0.78680
Adequate information is identified and communicated in a timely manner to enable people perform their responsibilities	4.7143	0.48795
The management has identified the people who are responsible for coordinating the various activities within the bank to ensure there is proper communication on internal controls	4.7143	0.48795
All the employees comprehend the concept of internal controls, including the division of responsibilities	4.5714	0.53452
Effective communication aids to evaluate how well the guidelines and policies of the bank are working and implemented	4.7143	0.48795

From the above outcomes, it was made out that information and communication is an important measure for internal controls for commercial banks listed in the NSE and licensed CBK. This is observed from the results of the study that the reporting system at the bank clarifies on all the responsibilities of each department at the bank (M=4.571, S=0.7868), adequate information is identified and communicated in a timely manner to enable people perform their responsibilities (M=4.174, S=0.4880), the management has identified the people who are responsible for coordinating the various activities within the bank to ensure there is proper communication on internal controls (M=4.174, S=0.4880), all the employees comprehend the concept of internal controls, including the division of responsibilities (M=4.571, S=0.5345) and effective communication aids to evaluate how well the guidelines and policies of the bank are working and implemented (M=4.714, S=0.4880). These results reveal that most commercial banks listed in the NSE and are licensed by the CBK have observed information and communication as a feature of internal controls.

4.3.6 Control environment and financial performance

The study established the effects of control environment on financial performance of commercial banks listed in the NSE and licensed CBK. Below are the results of the outcomes for this study.

Table 4.9; Control environment and financial performance

Statements	Mean	Standard deviation
Roles and responsibilities are clearly outlined for the employees	4.5714	0.78680
Our bank has an accounting and financial system	4.5714	0.78680
The bank's board, management and employees are all committed to competence and integrity	4.8571	0.37796
Our bank closely monitors the implementation of internal controls	4.4286	0.78680
Our bank has an objective, independent and active audit committee	4.1429	0.89974

From the above results, it was noticed that control environment was an important factor as a measure of internal controls for commercial banks listed in the NSE and licensed CBK. This is visible from the results of the study that roles and responsibilities are clearly outlined for the employees (M=4.571, S=0.7868), our bank has an accounting and financial system (M=4.571, S=0.7868), the bank's board, management and employees are all committed to competence and integrity (M=4.857, S=0.3780), our bank closely monitors the implementation of internal controls (M=4.429, S=0.7868) and our bank has an objective, independent and active audit committee (M=4.143, S=0.8997). These outcomes show that most commercial banks listed in the NSE and are licensed by the CBK have observed control environment as a feature of internal controls.

4.4 Regression analysis

The model summary below shows the overview of the regression analysis. Below are the findings.

Table 4.10; Regression analysis

Model Summary				
Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	1.000 ^a	1.000	1.000	0.00000

Source: Researcher, (2022)

From the above outcomes of this research, it was established that financial performance and the functionalities of internal controls have a strong positive relationship. This is shown by the correlation coefficient, R, of 1.000. The adjusted R² was 1.000 serving as an indication that the variation on financial performance of commercial banks due to risk management, control activities, control environment, information and communication and monitoring was 100%. This means that changes in risk management, control activities, control environment, information and communication, and monitoring could account for 100% of variations in commercial bank financial performance.

4.5 Coefficients

Table 4.11; Coefficients

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.	95.0% Confidence Interval for B	
		B	Std. Error	Beta			Lower Bound	Upper Bound
1	(Constant)	8.882E-16	0.000				0.000	0.000
	Risk management (Our bank has established mechanisms of identifying, monitoring, and controlling various risks that may occur during the course of business)	1.000	0.000	1.000			1.000	1.000
	Monitoring (The management has designated responsibilities for timely review of audit reports and resolving any defaults noted in those audit reports)	0.000	0.000	0.000			0.000	0.000

	Information and communication (Adequate information is identified and communicated in a timely manner to enable people to perform their responsibilities)	1.000	0.000	1.000			1.000	1.000
	Control activities (There is clear separation of roles at our bank)	0.000	0.000	0.000			0.000	0.000
	Control environment (Our bank closely monitors the implementation of internal controls)	1.000	0.000	1.000			1.000	1.000

Source: Researcher, (2022)

The established regression equation is;

$$Y = 8.882E^{-16} + 1.000X_1 + 0.000X_2 + 0.000X_3 + 1.000X_4 + 1.000X_5$$

The multiple regression model found that financial performance and internal controls for commercial banks listed on the NSE and licensed by the CBK had a favorable association. The positive relationship is evident through the measures of risk management, control environment and information and communication. The constant variable also indicates that with the measures of

internal controls held constant, the value of financial performance would be $8.882E^{-16}$. The outcomes show that an increase in the unit change of risk management, control environment and information and communication would lead to an increase in financial performance by 1.000 units.

4.6 Summary of findings

From the results of the study, according to the demographic of the respondents, it is seen that most of the employees in these commercial banks listed in the NSE and licensed by the CBK are male between the ages of 25 to 34 and 35 to 44. Also, it was noticed that most of them had undergraduate degrees having served the banks for a period of 6 to 10 years.

The goal of this research was to look into the impact of risk management on the financial performance of commercial banks that are listed in the NSE and are licensed by the CBK. It was determined that most of these commercial banks have put measures in place to mitigate risks that may occur. The study also looked at the impact of monitoring on the financial performance of commercial banks that are listed on the NSE and licensed by the CBK and found that these banks monitor their activities as part of their internal controls. In addition, the goal of this study was to determine the impact of control activities on these commercial banks' financial performance. The results show that most of the banks have a clear separation of roles however some do not, the bank's system access is only limited to authorized personnel, there are corrective measures taken to address weakness in performance and there is supervision on the work of the junior staff by the senior staff.

In addition, the research was able to determine the effects of information and communication on the financial performance of these commercial banks. It was established that information and communication are an important functionality of internal controls. Lastly, there was the establishment on the effects of control environment on the financial performance of these banks. It was determined that control environment is a vital functionality of internal controls, and it plays a role in financial performance.

The results of the regression study demonstrated that internal controls and financial performance of commercial banks listed in the NSE and licensed by the CBK had a substantial positive association. The coefficient of correlation showed that the independent variables 100% contributed

to the variation in financial performance as seen by the adjusted R^2 of 1.000. The findings from the test of coefficients also revealed this positive relationship. Through the variables of risk management, control environment and information and communication.

CHAPTER FIVE

DISCUSSIONS, CONCLUSIONS AND RECOMMENDATIONS

5.1 Introduction

This chapter presents an overview of the research, its findings, and recommendations for areas that may require additional research in light of the results reached. The study's limitations are also discussed.

5.2 Summary of findings

5.2.1 Summary of risk management and financial performance

One of the objectives of the researcher was to examine the effect of risk management on financial performance of commercial banks listed in the NSE and licensed by the CBK. The results from the regression analysis and test of coefficients show that risk management, as a functionality of internal controls, and financial performance has a strong positive relationship. The findings show that an increase in the unit change of risk management would lead to an increase in financial performance by 1.000 units. These findings concur with those of Wanjohi (2013), Kamau (2010), Hameeda and Al- Ajmi (2012) and Oluwafemi, Obwale and Olawale (2013), from the empirical review, which showed that risk management and financial performance have a significant relationship.

5.2.2 Summary of control activities and financial performance

From the outcomes of this research, control activities have a positive influence on financial performance. This is demonstrated by a regression analysis that revealed that changes in control activities may account for 100 percent of variations in commercial bank financial performance. Previous studies such as those of Mawanda (2008), Origa (2015), Umar and Dikko (2018), Oyoo (2014), Shabari, Saad and Bakar (2016) also acknowledge that control activities have a positive relationship with financial performance. This also aided the researcher to attain one of the objectives of establishing the effects of control activities on financial performance.

5.2.3 Summary of monitoring and financial performance

From the empirical review on monitoring and financial performance, outcomes from Treba (2003), Ng'etich (2017), Agbenyo, Jiang and Cobblah (2018) and Lagat (2018) show that monitoring and financial performance have a positive relationship. The findings of this research, exhibit that commercial banks listed in the NSE and licensed by the CBK monitor their activities as part of a measure of internal control. Monitoring is seen to have a positive influence on financial performance, this resonates with the previous studies that were carried out. This may be shown in the regression study that revealed that variations in commercial bank financial performance could be accounted for by changes in monitoring, with a value of 100%. The researcher was also able to attain one of the objectives of assessing the effects of control activities on financial performance.

5.2.4 Summary of control environment and financial performance

Establishing the effect of control environment on financial performance was also one of the objectives. The findings from the test of coefficients shows that an increase in the unit change of control environment would lead to an increase in financial performance by 1.000 units. These results show that control environment and financial performance have a strong positive relationship. Therefore, it is important that firms put the necessary measures under control environment. The outcomes from this research also agree with those of Zar (2019), Kamau (2014), Mutesi (2016), Kinyua, Gakure, Gekare and Orwa (2015) and Uwingabiye (2019) whereby they found that control environment and financial performance have a significant and positive relationship.

5.2.5 Summary of information and communication and financial performance

Information and communication were one of the measures of internal controls the researcher considered. Most of the commercial banks had the necessary measures of information and communication put in place as per the respondents' answers to the questionnaire. Preceding studies from Abdullahi and Muturi (2016), Muhunyo (2018), Ahmed and Muhammed (2018) and Kisanyanya (2018) were of information and communication and financial performance have a positive relationship. This study came to the same conclusion as the previous one: information and communication do have a favorable impact on financial performance. This is evident from the regression analysis that was carried out by the researcher.

5.3 Conclusions

The goal of this study was to see how internal controls affected the financial performance of commercial banks that are listed on the NSE and licensed by the CBK. It is clear that changes in financial performance of these banks could be attributed to by changes in risk management, control environment, monitoring, control activities, and information and communication. These functionalities of internal controls established that there is a strong and positive relationship between financial performance and internal controls. A unit increase in each of these functionalities leads to an increase in financial performance of these commercial banks.

In addition, most of the commercial banks listed in the NSE and licensed by the CBK have put measures in place that enable them to attain these functionalities of internal controls.

5.4 Recommendations

These recommendations were made based on the findings of this study and the conclusions reached. The financial performance of commercial banks listed on the NSE and licensed by the CBK has been proven to be significantly influenced by internal control systems. Therefore, there is need for firms to improve on their internal control system by adopting a modern- integrated financial system. This system should be regularly updated in order to mitigate the constant changing techniques fraudsters employ.

Also, commercial banks should transparently report on the structure and performance of their governance, risk management and internal controls in their various reports to the external and internal stakeholders. This could be done through their periodic financial reports or the firm's websites.

5.5 Suggestions for further research

This study suggests that a comparable study and additional research be conducted. Unlike this study, which focuses on commercial banks that are listed on the NSE and regulated by the CBK, research on the study of the impact of internal controls on commercial bank financial performance is mostly focused on those licensed by the CBK. Because there is little to no information on the enterprises registered on the NSE and licensed by the CBK, there are various approaches that can be investigated.

5.6 Limitations of the research

One of the limitations the researcher faced was on the reliability of the findings from the questionnaire as only one respondent was picked from each commercial bank. This research was restricted to the precision of the data obtained from the respondents.

Also, some of the commercial banks were hesitant on disclosing some information as they considered it to be sensitive in nature. This led to a tedious process to acquire the necessary information and to carry out research from these firms.

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APPENDICES

Appendix I: Questionnaire

This questionnaire is designed to gather data in order to establish the effect of internal controls on financial performance of commercial banks. Respondents are requested to kindly answer these questions with utmost truthfulness and provide accurate information. For confidentiality purposes, respondents are not obliged to provide their names. The information you provide as responses to this survey will be solely used for academic purposes. The time taken to take part and enable in this study is highly appreciated.

Section A: General Information

1. Gender

- Female
- Male

2. What age bracket do you fall under?

- Below 25
- 25-34
- 35-44
- 45-50
- Above 50

3. Level of education

- Certificate/ diploma
- Undergraduate degree
- Master's degree
- PHD

4. How long have you worked at the banking institution?

- Less than 2 years
- 2-5 years
- 6-10 years
- More than 10 years

SECTION B: RISK MANAGEMENT AND FINANCIAL PERFORMANCE

Rank the level of extent to which your firm has put in place these risk management practices. (1- No extent, 2-Little extent, 3-Moderate extent, 4-Great extent, 5- Greatest extent.)

	1	2	3	4	5
The firm has allocated funds for the risk management function					
Our bank has established mechanisms that aid in identifying, monitoring, and controlling various risks that may occur during the course of business					
The management has made clear the relevant objectives for the firm					
The management identifies the risks that may affect the achievement of the objectives put in place					

SECTION C: CONTROL ACTIVITIES AND FINANCIAL PERFORMANCE

Rank your level of agreement to the extent to which your bank can relate to these control activities. (1-Strongly Disagree, 2- Disagree, 3-Uncertain, 4-Agree, 5- Strongly Agree)

	1	2	3	4	5
There is a clear separation of roles at our bank					
The bank’s system access is only limited to authorized personnel					
There are corrective measures taken to address weakness in performance					
There is supervision on the work of the junior staff by the senior staff					

SECTION D: MONITORING AND FINANCIAL PERFORMANCE

Rank your level of agreement to the extent to which your bank can relate to these monitoring activities. (1-Strongly Disagree, 2- Disagree, 3-Neutral, 4-Agree, 5- Strongly Agree)

	1	2	3	4	5
The management has designated responsibilities for timely review of audit reports and resolving any defaults noted in those audit reports					
The employees at our bank make daily reconciliation on accounts					
Monitoring has aided in evaluating the quality of performance of our bank over a period of time					
There are frequent external audits on our bank’s financial reports					

SECTION E: INFORMATION AND COMMUNICATION AND FINANCIAL PERFORMANCE

Rank your level of agreement to the extent to which your bank has been effective in applying these information and communication indicators. (1-Strong Disagree,2-Disagree,3-Nuetral,4-Agree,5-Strongly Agree)

	1	2	3	4	5
The reporting system at the bank clarifies on all the responsibilities of each department at the bank					
Adequate information is identified and communicated in a timely manner to enable people to perform their responsibilities					
The management has identified the people who are responsible for coordinating the various activities within the bank to ensure there is proper communication on internal controls					
All the employees comprehend the concept of internal controls, including the division of responsibilities					
Effective communication aids to evaluate how well the guidelines and policies of the bank are working and implemented					

SECTION F; CONTROL ENVIRONMENT AND FINANCIAL PERFORMANCE

Rank your level of agreement to the extent to which your bank can relate to these control environment indicators. (1-Strong Disagree, 2-Disagree, 3-Nuetral, 4-Agree, 5- Strongly Agree)

	1	2	3	4	5
Roles and responsibilities are clearly outlined for the employees					
Our bank has an accounting and financial system					
The bank's board, management and employees are all committed to competence and integrity					
Our bank closely monitors the implementation of internal controls					
Our bank has and objective, independent and active audit committee					

Appendix II: List of commercial banks listed in the NSE and licensed by the CBK

1. Co-operative Bank of Kenya.
2. Equity Bank.
3. I & M Bank.
4. Kenya Commercial Bank- KCB.
5. National Bank of Kenya.
6. NCBA Bank.
7. Standard Chartered Bank.