

**EFFECT OF INTERNAL CONTROL SYSTEMS ON FINANCIAL PERFORMANCE
OF SMALL AND MEDIUM ENTERPRISES: CASE STUDY OF SENASA
DISTRIBUTORS LUGAZI IN LUGAZI TOWN BUIKWE DISTRICT**

HERMAN NAMA TENYWA

S21B33/021

**A DISSERTATION SUBMITTED TO THE SCHOOL OF BUSINESS IN PARTIAL FULFILLMENT
OF THE REQUIREMENTS FOR THE AWARD OF A DEGREE OF BACHELOR OF SCIENCE
IN ACCOUNTING AND FINANCE OF UGANDA CHRISTIAN UNIVERSITY**

September, 2024



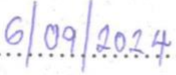
**UGANDA CHRISTIAN
UNIVERSITY**

A Centre of Excellence in the Heart of Africa

DECLARATION

I, **NAMA HERMAN TENYWA**, hereby declare that this dissertation is original work except where I acknowledged and has never been presented to Uganda Christian University or any other university.

Signature: 

Date: 

NAMA HERMAN TENYWA

S21B33/021

APPROVAL

This report has been prepared under my supervision and guidance and is hereby submitted with approval.

Signature: 

Date: 

MR. NICSON KATISME

University supervisor

DEDICATION

I dedicate this report to my supportive parents Mr and Mrs. Tenywa Patrick together with my friends that have supported me through it all.

I also extend my profound thanks to my friends and esteemed lecturers who have offered me support, courage and encouragement throughout my academic journey.

Furthermore, I dedicate this report to my research supervisor, Mr. Nicson Katisme for his unending support and guidance during the research period.

ACKNOWLEDGEMENT

I thank the Almighty God who has enabled me finish writing this report and my university education at large.

I am greatly thankful to my loving parents and family for the support rendered to me throughout my education and for enabling me attend such a prestigious university.

I feel greatly thankful to my lecturers and supervisor for the support offered to me throughout this level.

TABLE OF CONTENT

DECLARATION	i
APPROVAL.....	ii
DEDICATION	iii
ACKNOWLEDGEMENT	iv
TABLE OF CONTENT	v
ABSTRACT	viii
CHAPTER ONE.....	1
1.0 Introduction	1
1.1 Background of the study	1
1.2 Statement of the problem	3
1.3 Main objective.....	4
1.3.1 Specific objectives	4
1.3.2 Research questions	4
1.4 Scope of the study	4
1.4.1 Content scope	4
1.4.2 Geographical scope.....	4
1.4.3 Time scope.....	5
1.5 Significance of the study	5
1.6Conceptual framework	6
CHAPTER TWO	7
LITERATURE REVIEW.....	7
2.0 Introduction	7
2.1 Definition of key terms	7
2.1.1 Internal controls	7
2.1.2 Financial Performance	7

2.2 Control environment and its effect on the financial performance of SME's in the study context.	8
2.3 The effect of control activities on the financial performance of SME's in the study context.	11
2.4 The relationship between risk assessment and its effect on financial performance of SME's in the study context.	14
2.5 Literature gap	16
CHAPTER THREE	17
RESEARCH METHODOLOGY	17
3.1 Introduction	17
3.2 Research design	17
3.3 Study population	17
Table 3.1 Population size.....	17
3.4 Sample size and selection techniques.....	18
3.5 Sampling techniques.....	18
3.5.1 Sample size	18
3.6 Data Source and Collection Methods.....	18
3.7 Data collection instruments	19
3.8 Reliability and Validity	19
3.9 Data Collection Procedure	19
3.10 Data analysis	19
3.11 Ethical consideration	19
CHAPTER FOUR.....	20
PRESENTATION, ANALYSIS AND INTERPRETATION OF FINDINGS	20
4.1 Introduction	20
4.2 Response rate.....	20
4.3 Social demographic characteristics of respondents.....	20
Table 1: Gender of respondents	20

Table 2: Age of respondents	21
Table 3: Education level of respondents	21
4.4 Study findings	22
4.4.1 The control environment and its effect on the financial performance of SMEs in the study context.....	22
4.4.2 The effect of control activities on the financial performance of SMEs in the study context.	23
4.4.3 The relationship between risk assessment and its effect on the financial performance of SMEs in the study context.	24
CHAPTER FIVE	26
SUMMARY OF FINDINGS, CONCLUSIONS AND RECOMMENDATIONS	26
5.1 Introduction	26
An overview of the findings, conclusions, and suggestions is provided in this chapter. The suggestions are based on the chapter's results, which are summarized in this section.	
5.2 Summary Findings	26
5.2.1 The effect of control environment on the financial performance of SMEs in the study context.....	26
5.2.2 The effect of control activities on the financial performance of SMEs in the study context.	26
5.2.3 The relationship between risk assessment and its effect on the financial performance of SMEs in the study context.	27
5.3 Conclusion.....	27
5.4 Recommendations	27
5.6 Areas of further research	29
REFERENCES	31
APPENDICES.....	35

ABSTRACT

The purpose of the study was to assess the effect of internal control systems on financial performance of SME's in Buikwe District a case study of Senasa Distributors. The study was guided by three core objectives; firstly, to assess the effect of control environment on the financial performance of SME's in the study context; secondly, to assess the effect of control activities on the financial performance of SME's in the study context. And lastly, to assess the relationship between risk assessment and its effect on the financial performance of SMEs in the study context. Employing a case study design and adopting a purely quantitative methodology, data was collected from 66 respondents through structured questionnaires. The collected data was analysed using descriptive statistics.

The study established a noteworthy discovery, based on increased responsibility, transparency and operational efficiency, the findings showed that a robust internal control environment considerably boosts financial performance. Control activities for example regular audits, segregation of duties and authority limits were found to lower on the high rates of fraud and errors which improves on the financial performance of businesses. The identification and mitigation of potential financial risks which guarantee the stability and growth of the business have also been demonstrated to be greatly aided by risk assessment. The study concludes that a strong internal control framework is necessary for SME's to maintain their financial viability according to this study's findings.

CHAPTER ONE

1.0 Introduction

This chapter contained the background to the study, problem statement, general objective of the study, specific objectives, research questions, the scope of the study and the significance of the study.

1.1 Background of the study

According to Mintzberg (Lydia et al., 2023), Small and medium sized enterprises (SMEs) are non-subsidiary, independent firms which employ less than a given number of employees (Christopher et al., 2022) (1 Ourien Isaac, 2 Dr Ariyo Gracious Kazaara, 2023). Jackson (2004) defines small and medium enterprises as businesses that maintain revenues, assets or a number of employees below a certain threshold (Robert et al., 2023). They account for majority share of businesses in the world and are big contributors to the creation of employment opportunities and also improving on the economy's development. They are considered as the backbone of an economy given the fact that in some economies SMEs contribute to more than 50% of Gross Domestic Product (ACCA, 2010) (Alex & Rosebell, 2023a).

SMEs account for 99.8% of all businesses, particularly in the EU, and employ about 76 million people, or roughly 67.4% of all workers, as of 2010 (Godfrey et al., n.d.). Approximately 96% of all business businesses in Kenya are Small and Medium-Sized businesses (SME) with 1.6 million registered (Economic Survey, 2009). According to the Economic Survey (2009), SMEs make up the majority of the economy, employing up to 75% of Kenya's labor force and accounting for up to 18.4% of GDP.

For instance, the Government of Uganda (2011) estimates that SMEs in the industrial, services, and agricultural sectors employ over 2.5 million people and make up about 18% of the country's GDP (GoU, 2015). The Uganda Investment Authority states that small businesses have five to forty-nine employees and total assets of UGX:10 million to UGX:100 million. Thus, the medium-sized business has 50–100 employees and total assets of more than UGX 100 million but not more than UGX 360 million. Financial performance of small and medium enterprises is really important as it is what helps them to grow more in which through growth they expand and provide more opportunities for the communities. Internal controls are very vital as they are a major point in enabling the growth of the small and medium enterprises by enhancing the financial performance. The Ministry of Planning and Economic Development also states that

SMEs account for more than 80% of Uganda's manufacturing production. In Uganda, the industry employs as many as 2.6 million people. (Uganda Investment Authority, 2006).

Moreover, strong financial performance signals the company's ability to generate profits, which is an important indicator of its success in the market. Profitability can also attract more investors to the business, who see the potential for high returns on their investment. To maintain strong financial performance, companies must continuously monitor and evaluate their expenses, revenues, and cash flow, identifying areas that need improvement or change.

Furthermore, financial performance is not only important for the business itself but also for its stakeholders. For instance, employees benefit from strong financial performance as it enhances job security and overall job satisfaction. Shareholders, on the other hand, are interested in the company's financial performance as it determines the value of their investment in the business. Suppliers and creditors also consider the financial performance of the company before entering into business transactions with them, assessing their creditworthiness and ability to make timely payments.

Internal controls are methodical measures implemented by a company to help it conduct business more effectively. These measures include reviews, checks and balances, processes, and procedures. The management of an entity can only be somewhat assured that the organization's goals will be met by internal controls. "All internal control systems have inherent limitations that affect the likelihood of achievement" (Hayes et al., 2005). Organizations set up different internal control systems tailored to their needs to aid them in achieving high performance and effectiveness in their work lines with reasonable reassurance of the work. The systems are a network of interlinked sections and methods deliberately put in place by the management and directors of the organization in order to monitor and ensure the main objectives of the organizations are met.

Their main aim is to aid in creating an order in how work is done in the organization, detecting errors and fraud, ensuring accuracy and efficiency of the work, compliance with the legal laws and regulations and the economic use of the organization's resources. Policies and procedures that support the execution of management directives are the outward manifestation of control activities and the control environment, according to Oseifuah (2015). They are essential

because they guarantee that the steps required to manage the risks involved in achieving the organization's goals are taken.

Assigning specified responsibilities to staff reduces risk and fraud while maximizing resource protection. Authorization, recordkeeping, custody, and reconciliation must be fundamental to the security of every resource for all organizational activities. Heirer (2015). Internal control systems can greatly affect the financial performance of an organization and that is why it is very crucial to have them in place as the financial performance is a big determinant of the growth of a business.

1.2 Statement of the problem

Businesses of all kinds, whether small or large and in any industry, continuously aim to achieve and maintain financial stability in order to successfully execute their operations. Achieving economic stability is crucial since it allows businesses to fund their ventures, pay off their debts, and invest in new opportunities to better compete in the market (Hessami, 2021). Businesses that are financially stable are able to maintain consistent growth while providing valuable products and services to customers. Keeping up with the fast-paced and ever-changing business environment is a necessity, and businesses must always be equipped with appropriate financial and business strategies to navigate through different challenges. In this study context, researchers assessed that organization's financial metrics such as revenues, profits, and cash flows to evaluate its efficiency and profitability (Merchant & Van der Stede, 2017). Financial performance analysis is an intrinsic section of management decision-making, including strategic planning and resource allocation.

However, a problem of poor financial performance has continued to persist as a result of lack of or weak internal control systems in some of the SME's in Buikwe district. There is a positive relationship between effective internal control systems and improved financial performance, Ogwang, Isabirye, and Abaho (2016). There are limited research studies that have focused on the effect of internal control systems on the financial performance of SME's in Buikwe district hence created the need for research on this topic.

1.3 Main objective

To examine the effect of internal controls on business growth of small and medium enterprises

1.3.1 Specific objectives

- i. To assess the control environment and its effect on the financial performance of SMEs in the study context.
- ii. To examine the effect of control activities on the financial performance of SMEs in the study context.
- iii. To assess the relationship between risk assessment and its effect on the financial performance of SMEs in the study context.

1.3.2 Research questions

- i. What is the effect of the control environment on the financial performance of SMEs in the study context?
- ii. What is the effect of control activities on the financial performance of SMEs in the study context?
- iii. What is the relationship between risk assessment and its effect on the financial performance of SMEs in the study context?

1.4 Scope of the study

1.4.1 Content scope

The content scope will be restricted to the impact of internal control systems on small and medium-sized businesses' financial performance, with a particular emphasis on evaluating the control environment and how it affects SME financial performance, the impact of control activities on SME financial performance, and the connection between risk assessment and SME financial performance.

1.4.2 Geographical scope

The study will focus on Senasa Distributors in Lugazi. This business is the legal Uganda Breweries distributor for the entire Lugazi and part of Mukono district of Mbalala, Namataba, Kyanja, Namawojjolo.

1.4.3 Time scope

This study will cover literature from 2018-2024 as it will be a source of more recent and updated information on the effect of internal control systems on the financial performance of small and medium enterprises.

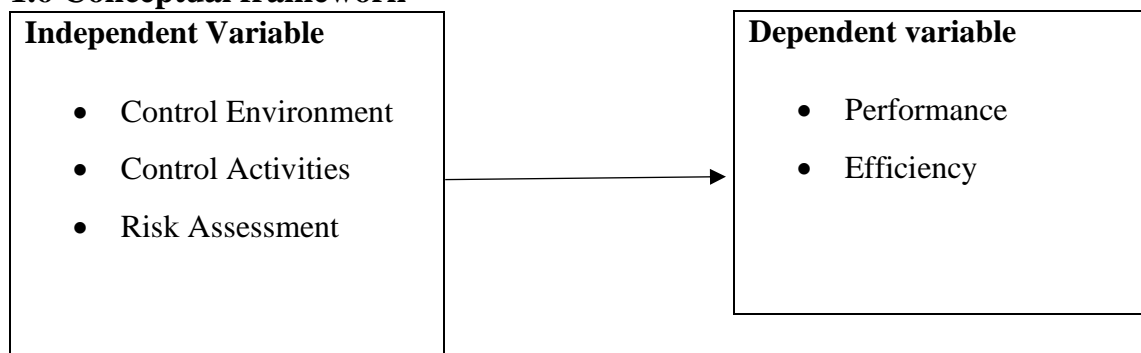
1.5 Significance of the study

The directors and management of SMEs recognized the value of ICSs and helped to grade how much of them they applied. The management gained knowledge of the connection and impact of ICSs on SMEs' financial performance. Prospective investors also profited since they could identify organizations with sound governance practices and make more educated investment choices as a result.

The study fills a research knowledge gap on the relationship between internal control systems and financial performance, particularly in the Buikwe district of Uganda. This benefits academics and researchers by adding to the body of knowledge already available on the subject. Scholars can draw from both the existing literature and the results of this investigation, which sought to determine the relationship between ICSs and the financial performance of SMEs in the selected region. The study also suggested additional research topics that could be investigated in the future by other researchers.

The effect of ICSs on SMEs' financial performance and the kind of ICSs that should be implemented in SMEs were both explained to policy makers. Understanding the role ICSs play in improving accountability and transparency, as well as their impact on financial performance, benefits other institutions.

1.6 Conceptual framework



Source: Adopted from COSO, 2013 and modified by the researcher

Figure 1: Conceptual framework showing effect of internal control systems on financial performance of SME's.

The framework indicates that internal control system (ICS) has an impact on financial performance and illustrates potential connections between these two structures. Numerous studies have made extensive reference to the ICS and its components, including (COSO, 2013; Whittington & Pany, 2016). In particular, risk assessment addressed risk identification, forecasting, and analysis. Control measures including physical asset controls, task segregation, and regular and follow-ups on Senasa's performance review were also investigated. In fact, this study included an exploration of the control environment's elements, particularly managerial capacities to preserve organizational ethical principles, authority and responsibility delegation, and dedication to competencies during the implementation of ICS operations. Lastly, Senasa Distributors' ICS supervisory, external audit, and assessment roles were used to evaluate the monitoring operations. Financial performance, on the other hand, was the dependent variable that was assessed using the financial reporting, accountability, and transparency that the company had demonstrated in its performance reports throughout the previous five years (2019–2023).

CHAPTER TWO

LITERATURE REVIEW

2.0 Introduction

This chapter presents the literature review already in existence regarding the effect of internal controls systems on financial performance of small and medium enterprises by different scholars. The first objective presented is the effect of control environment on financial performance of SMEs, second is the effect of control activities on financial performance of SMEs and lastly is to assess the relationship between risk assessment and its effect on financial performance of SMEs.

The theoretical justification for the issue under study, the body of prior research, and the relevance of the results to the current issue are all explained in the literature review.

2.1 Definition of key terms

2.1.1 Internal controls

Internal controls are systematic measures such as reviews, checks and balances, methods and procedures instituted by an organization to enable it conduct its business better. The management of an organization can only be somewhat assured that its goals will be met by internal controls. As per Hayes et al. (2005), "all systems of internal control have inherent limitations that affect the likelihood of achievement." Organizations set up different internal control systems tailored to their needs to aid them in achieving high performance and effectiveness in their work lines with reasonable reassurance of the work. The systems are a network of interlinked sections and methods deliberately put in place by the management and directors of the organization in order to monitor and ensure the main objectives of the organizations are met.

2.1.2 Financial Performance

According to Praise (2003), performance is the act of accomplishing social goals, financial performance, and obligations from the standpoint of evaluating persons. According to Berhanu and Jaleta (2012), growth, capital level, employment rate, debt repayment capacity, and return on investment were used to gauge performance in this study. According to Namiri&Stojanovic (2018), financial performance is the collection of financial results a company achieves from its operations.

2.2 Control environment and its effect on the financial performance of SME's in the study context.

For the controls to function, there must be a control environment. It serves as the cornerstone of the internal control system and establishes the general framework. A control environment, according to Mwakimasinde et al. (2015), is a collection of procedures, structures, and standards that serve as the foundation for implementing internal control systems. According to Abuya's (2017) study, the internal control environment creates a work environment where various employees within the organization have an impact on their tasks and actions. It brings to light that the control environment is very important for setting the tone for the financial performance of a company. It has different components entailed in it like the organizational structure. This is the hierarchy of the organization clearly outlining the different roles and responsibilities of the management and the employees. Organizations have different ethical values that make up the control environment and these are a code of conduct that the people must follow and through which people must conduct themselves and also perform their duties. It also contains the regular reviews and reporting from the lower level to the top level management in order to aid decision making and also keep track of the state of the company and respect of the systems by the top management which ensures that the top management understands the purpose of the internal control systems and why they are in place and does not try to overlook them when handling any company matters.

The importance of a strong ethical culture cannot be overstated as it influences employees' behaviour both in their personal and professional lives. An organization's management must ensure that the employees effectively internalize the organization's values so that they fully appreciate the importance of their role in upholding the company's ethical standards. Organizations that fail to instil strong ethical values risk losing customers, shareholders, and other stakeholders who believe in ethical practices.

An organization's ethical values also influence its relationships with other stakeholders, including suppliers, investors, and customers (Certo&Certo, 2018). Suppliers are likely to do business with companies that have a good reputation for ethical practices. Investors are likely to invest in companies that show a commitment to ethical values and sustainable practices. Similarly, customers are more likely to engage with organizations that uphold ethical values and standards. Therefore, maintaining a strong ethical culture is an essential aspect of organizational success.

Whittington & Pany (2016) demonstrate how an internal control environment establishes an organizational culture that links professionalism and integrity. This helps to guarantee that employees obey rules and regulations and only perform as required of them. In addition to using this to achieve credible financial outcomes by building commitment, giving junior officers feedback, and eliminating fraud and defects, staff members are expected to carry out their assigned jobs professionally and within the bounds of the organizational structure (Inusah & Abdulai, 2015). The financial success of the business is correlated with the control environment.

According to Cosserat and Rodda (2015), the control environment provides a framework that guides employees to act in an ethical manner and in compliance with policies and regulations. It also ensures that there are effective communication channels that facilitate information sharing. In addition, the control environment ensures that the SME's management and the board of directors uphold the highest level of professionalism and ethical behaviour, which ensures that the company operates sustainably, over the long-term.

It is also relevant to note that the control environment is dynamic and requires continuous re-evaluation to ensure that it meets changing organizational needs. Accordingly, SME's should use a risk based approach to routinely evaluate the efficacy of their internal controls, according to the Chartered Accountants Australia and New Zealand (2021). This strategy could entail carrying out a gap analysis to find any weakness in the controls and acting quickly to address them. As per the report by the accountants, doing routine evaluations of the control environment guarantees that small and medium sized enterprises (SME's) function in a regulated, proficient and risk-averse manner while also protecting the company from fraudulent activities.

SME's establish the tone for their company culture and values in a regulated setting, which influence employees' attitudes and behaviour (COSO, 2017). A positive control environment can encourage moral behaviour, increase the efficacy of the internal control system, and produce superior performance results. According to Weatherspoon and LeClair (2012), there is no way to emphasize the importance of the control environment in leadership. Setting an example for ethical behaviour and influencing staff behaviour are two important aspects of leadership tone. By modelling moral behaviour, putting in place a robust governance framework, and effectively expressing their principles, leaders may show that they are committed to upholding a positive control environment.

The size of the organization has an impact on the control environment in SMEs. Establishing an efficient internal control system can be difficult for SMEs due to their limited resources (Ewuuk, 2020). Nonetheless, by emphasizing staff training, communication, and leadership, small organizations can still create a good control environment (COSO, 2017).

The relationship between performance and internal controls is also influenced by the control environment. Nguyen et al. (2017) report that research indicates that performance outcomes can be impacted by the control environment. Enhancing financial reporting and transparency through efficient internal controls can foster a positive control environment, boost stakeholder confidence and enhance corporate performance. Positive control environments also result in happier workers, more contented workers and improved performance.

On the other hand, a negative control environment with weak internal controls leads to a high level of risk, poor compliance, and non-adherence to established protocols, negatively affecting performance outcomes. Small businesses can benefit from focusing on the control environment to promote internal control effectiveness. Taun (2021) suggested that SMEs need to create an ethical culture from the outset by emphasizing values and governance structures, training employees, and providing opportunities for feedback, which can lead to improved internal control effectiveness and better performance outcomes.

Furthermore, SME's should set up procedures that guarantee adherence to legal and regulatory standards in order to preserve a good control environment. This lessens the possibility of noncompliance related consequences, like fines and harm to one's reputation (COSO, 2017). These systems include creating a risk assessment framework, training and awareness raising and routinely monitoring and reviewing internal controls.

2.3 The effect of control activities on the financial performance of SME's in the study context.

According to a 2011 study by Petrovits et al., control activities include guidelines, policies, programs, tactics and instructions that direct management in achieving organizational goals. According to Schulze et al. (2013), control activities, which are procedures that advise management on how to proceed, are frequently essential for improving financial performance. In addition, control activities are designed to prevent or detect errors, irregularities and fraud that can threaten an SME's financial reporting, operational efficiency and reputation. AICPA (2017) adds that these activities cover a broad range of activities, such as authorization, segregation of duties, physical and logical access controls, document and record keeping and reconciliation. Key control activities also include monitoring for compliance with laws and regulations, as well as monitoring the performance and effectiveness of the internal control system.

Control activities like segregation of duties help to ensure that there is no one person in a position to handle the three primary control functions of authorizing, recording and custody. Physical controls are also other control activities that can be put in place. These can be physical barriers like security check points and sign in areas in order to ensure that the necessary steps are taken. Rotation of duties is a way of preventing an individual from personalizing an activity which can create room for fraudulent activities. Regular leave is also a key activity where by the work of another person can be critically looked at by another filling in for that time and gets an insight of how the work has been running.

The organization can also carry out internal audits. According to Gupta (2001), internal audit is a separate assessment function that is set up inside an organization to go into and assess its operations as a service to the organization. The main point of the internal audits is to ensure that the organization is in line with its financial records, there is clear role understanding and departments are harmonious with each other. It can help in detection and prevention of fraud in the company. Studies by Halil et al. (2018) and Karami et al. (2020) point out that effective internal audit practices can lead to reduced instances of fraud and consequently improve small and medium enterprises' financial performance.

According to a 2019 study by Rafindadi and Olanrewaju, control actions produce more accurate, timely, and well-managed risk assessments, which in turn shape financial performance. Similar research, particularly Whittington & Pany (2016), demonstrates how improved control measures, such as performance reviews, forecasts, period performance,

physical controls, and job segregation, affect the company's financial performance. Some of the control activities that a company has in place are not adhered to by all the staff of the company and in turn it can have a devastating effect on the company's performance financially. Some of the staff intentionally ignore the control activities and go as far as to find ways to go around them to satisfy their own personal selfish interests by utilizing the loopholes in the systems. Internal control systems need to incorporate sufficient well-tailored control activities for their company in order to ensure good financial performance.

According to the Committee of Sponsoring Organizations (COSO) in 2017, implementing effective control activities not only guarantees the accurate accounting and protection of an SME's resources and records but also boosts stakeholders' confidence in the organization. By utilizing suitable control activities, the organization can also optimize its resource allocation, time management, and productivity, leading to improved operations. These efficient processes contribute to better performance and growth of the SME.

According to Ewuok (2020), control activities fall into two main categories; preventive control activities and detective control activities. While investigative control activities seek to identify errors or abnormalities after they have occurred, preventive control activities seek to stop errors or irregularities from occurring.

According to Ewuok (2020) and Tuan (2021), preventive control measures are crucial for reducing the likelihood of fraud and guaranteeing the transparency of financial reporting. These operations include a number of different elements, including review processes, segregation of duties and transaction authorization. Businesses can reduce the likelihood of abnormalities and forbidden activities in their financial operations by putting such controls into place.

The goal of detective control operations is to find and fix fraud, mistakes, omissions and irregularities. Activities including reporting, external audits, reconciliations and monitoring are examples of detective control activities (COSO, 2017). For SMEs, putting in place reliable and efficient control procedures can be difficult. For small organisations, the expense of putting internal controls in place can be a major factor. This does not imply, however, that SMEs should ignore control operations. Rather, they should concentrate on determining which risks are most important and what needs to be done to minimize those risks.

Weygandt et al. (2018) point out that control measures like division of responsibilities can be used to make sure that the three main control functions i.e authorizing, recording and custody are not performed by a single individual. This entails designating various people to manage the

various risks, so establishing checks and balances. In order to stop unwanted access or asset movement, physical restrictions can also be implemented. Among other things, this could involve locks, alarms, sign-in places and security checkpoints.

Furthermore, regular leave is essential because it enables someone else to cover for the absent worker, giving the other person the chance to review the work completed and spot any irregularities. Internal audits are another tool that an organization can use to assess its own operations and pinpoint areas that require improvement (Albrecht et al, 2018). Rotation of duties is another control activity that involves periodically changing the responsibilities of employees. This helps to prevent an individual from personalizing a specific activity and also reduces the risk of fraudulent activities.

According to Halil et al. (2018), internal audit is a separate assessment function that is set up inside an organization to go into and assess its operations as a service to the organization. The main point of the internal audits is to ensure that the organization is in line with its financial records, there is clear role understanding and departments are harmonious with each other. It can help in detection and prevention of fraud in the company. Studies by Karami et al (2020) point out that effective internal audit practices can lead to reduced instances of fraud and consequently improve small and medium enterprises' financial performance.

The financial success of the organization is influenced by improved control activities, such as performance reviews, forecasts, period performance, physical controls, and segregation of duties, according to similar studies, most notably Whittington & Pany (2016). Some of the control activities that a company has in place are not adhered to by all the staff of the company and in turn it can have a devastating effect on the company's performance financially. Some of the staff intentionally ignore the control activities and go as far as to find ways to go around them to satisfy their own personal selfish interests by utilizing the loopholes in the systems. Internal control systems need to incorporate sufficient well-tailored control activities for their company in order to ensure good financial performance.

2.4 The relationship between risk assessment and its effect on financial performance of SME's in the study context.

The process of risk assessment involves identifying, analysing, and managing any hazards that are associated with an organization's operations. Any uncertainties that could have a significant negative effect on the organization are considered risks. Risk assessment reduces the possibility of uncontrolled risk-taking and assists an organization in identifying factors that could negatively impact business operations (COSO, 2013).

It is crucial to acknowledge that risk identification comes in diverse areas, encompassing the external and internal domains of an organization. Once an SME identifies its most significant risks, it can develop and implement strategies to mitigate those potential threats to the business.

Effective risk management is extremely difficult for SMEs, especially given their constrained funding. A study by Chandra (2016) states that risk assessment, which tries to eliminate all dangers, is the main element of a strong internal control system in any organisation. But the risk assessment process offers SMEs a workable way to pinpoint and rank the most important risks, allowing them to create and execute internal control plans that are specific to their own concerns. This is crucial since neglecting to recognize and handle high- risk areas can lead to serious losses in terms of money and reputation, as well as jeopardize the company's ability to survive. According to Tuan (2021), SMEs must strategically allocate their resources to internal controls to guarantee that only the most crucial risks are being addressed.

According to the research done in 2020 by Onsongo, Muathe and Mwangi, a corporation may benefit from taking certain risks while suffering unfavourable consequences from others. Numerous hazards have the potential to seriously jeopardize the internal control framework, which would then negatively impact the organization's financial results. Most risks for companies can be from the weak internal control systems from the various factors that can affect it and the organization may not easily find the best solutions on how to handle the situation.

Small and medium sized businesses have a complex problem when it comes to risk assessment because of their unique operational environment, which is frequently marked by dynamic characteristics that are distinct from those of bigger firms. Furthermore, SMEs are subject to a wider range of hazards that are frequently specific to their operational environment and are more susceptible to external effects than bigger firms (Nguyen et al., 2017)

Small and medium-sized businesses often employ fewer people. When a small group of workers have key positions within the organisation, this might lead to a problem with risk concentration (Ewuuk, 2020). Issues like dishonest behaviour, inappropriate acts, or failure to comply with regulations could result from this. Through appropriate risk assessment, SMEs can identify possible hazards and create efficient ways to mitigate them. SME's may preserve regulatory compliance, secure their financial interests, and defend their business operations with the aid of this assessment. Prioritizing risk management in day to day activities is important for SMEs to make sure they can thrive in the cutthroat business world.

In order to spot such weaknesses and put corrective measures in place, SMEs must create a thorough risk management plan that includes a regular evaluation of their current risk management techniques. Baramichai (2021) SME owners should also make sure that their staff members are aware of the significance of carrying out risk assessments and putting internal controls in place in order to reduce potential hazards. By doing this, SMEs may protect the business' operations and reputation while managing risks in an efficient and proactive manner.

SMEs can benefit from carrying out a thorough risk assessment since it enables them to see not just possible risks but also opportunities for taking calculated risks that can lead to better performance results. However, SMEs should have a number of internal controls in place to guarantee that risks are managed responsibly. In this context, the Treadway Commission Committee of Sponsoring Organizations (COSO, 2017) highlights the necessity of an efficient internal control system that can assist SMEs in better risk management. SMEs must therefore put in place a thorough internal control system that can guarantee that risks are managed appropriately and proactively while also empowering them to take advantage of risk-taking possibilities for improved performance results.

Benefits of risk assessment include improved organizational performance and increased efficacy of internal controls. Small and medium-sized businesses can create and implement new risk mitigation strategies in response to recognized hazards by using risk assessment to find potential gaps and weaknesses in their internal control systems (Lim et al., 2016). SMEs can reduce the likelihood of fraud and errors by strengthening their internal controls using a risk-based strategy. This will encourage an environment of accountability and transparency within the company.

A proactive method for improving organizational readiness and threat response is risk assessment. SMEs can prioritize their risk mitigation efforts and stay informed about

developing hazards by undertaking regular risk assessments (Brazel and Carpenter, 2017). Better results in terms of risk reduction result from this method, which makes sure that the scarce resources are given to the most- risky projects.

By prioritizing which risks to address and which controls to put in place, risk assessment helps SMEs make the best use of their organisational resources (Ewuuk, 2020). This makes it possible for SMEs to concentrate on important risks and steer clear of less significant or unlikely ones.

SMEs must recognize that technology plays a critical role in reducing potential hazards. Innovations in technology have made risk assessment processes more efficient and productive. To improve their internal control system, SMEs should take advantage of technology's advantages, which include but are not limited to data analytics, automation and digitalization and cloud-based solutions (Nguyen et al, 2017). By employing such solutions, SMEs may increase the accuracy and dependability of their risk assessment procedures while also saving time and money. Better decision making and enhanced overall corporate success may follow from this.

2.5 Literature gap

Although a lot of research has been done on how internal controls affect SMEs financial performance, not much empirical research has been done to look at the exact relationship that exists between internal controls and SMEs financial performance.

Although previous research has examined the influence of internal controls on audit risk and the accuracy of financial reporting, little is known about the precise consequences of internal controls on financial performance indicators including profitability, liquidity and solvency in small and medium- sized enterprises.

CHAPTER THREE

RESEARCH METHODOLOGY

3.1 Introduction

This chapter described the research methodology that was used for the study. The chapter went on to define the study's target demographic, the planned sample size, the sampling process, and the kinds of instruments that were employed. Also covered are the methods for gathering data and the methods for analysing it that were employed to examine the study's findings.

3.2 Research design

The cross-sectional descriptive research design was employed for this study since it allowed the researcher to gather comprehensive data from the target population in a specific amount of time and without bias. Additionally, it allowed the researcher to concentrate on making observations, consulting pertinent historical sources, and recording the results. Quantitative methods were used in this investigation.

3.3 Study population

Since this was a focused case study, the population of Senasa distributors, included the management and staff, who were the focus of this investigation. This brought the target population to 100 people.

Table 3.1 Population size

Senasa Distributors Ltd	Population
Top management	06
Middle management	14
Lower level management	80
Total	100

Source; Primary data

Table 3.1 above showed the target population of this study as of May, 2024. Senasa Distributors had a population of 100 staff members. The staff population is comprised of 6 top level management, 14 middle level management and 80 hands on or casual staff members. (primary data)

3.4 Sample size and selection techniques

The study targeted all the top level managers and middle level management because they all play a role in the internal control systems and financial performance of the business, and purposely identified hands on employees because the study looked to collect specific data that they may not all have access to. The objective was to interview at least 75% of the entire population focusing on the top and middle level managers since they are strategists while the hands-on employees are only doers.

3.5 Sampling techniques

Stratified sampling and purposive sampling procedures were employed by the researcher to pick respondents, allowing for the replacement of those who declined to respond to the researcher's request. Because certain data was required and was easier for middle and upper management to obtain, these strategies were employed. It was employed since internal control system strategists were the study's target audience with regard to financial performance. It served to guarantee that only individuals with relevant data were to be included in the sample.

Questionnaires were only sent to responders who could really give the information requested. This method was used because the researcher looked for participants who had already heard about the subject of the study.

3.5.1 Sample size

The sample size of this study was determined using Yamane's formula with a 95% level of confidence (5% acceptable sampling error).

$$n = \frac{N}{1 + N(e)^2}$$

$$n = 100 / 1 + 100(0.05)^2$$

$$n = 100 / 1.25$$

$$n = \underline{80 \text{ respondents}}$$

3.6 Data Source and Collection Methods

Primary data gathering techniques were used to gather the data. Structured questionnaires were used to collect the data.

In addition to the fact that the researcher was working with elite respondents who did not have much time to spare, questionnaires were employed only because they save time during the data collection process. Because the researcher was aware that some members of the target community had a certain level of illiteracy.

3.7 Data collection instruments

To gather information, the researcher gave out questionnaires. These tools guaranteed the highest level of validity and trustworthiness for the data used to provide insightful knowledge about the study's topic. Questionnaires were designed with scale-based, closed-ended questions that allowed respondents to indicate how much they agreed or disagreed with the statements.

3.8 Reliability and Validity

By focusing more on medium and upper level managers who were thought to possess more trustworthy information, reliability was guaranteed.

3.9 Data Collection Procedure

The management of Senasa distributors requested the researcher for an introductory letter which was used as basis to be able to recognize the researcher.

3.10 Data analysis

To make sense of the quantitative data, descriptive and narrative analysis were applied.

3.11 Ethical consideration

The format of the questionnaires prevented the interviewee's name from being mentioned. The questionnaire clearly specified that data would be treated in strict confidence. And it was not required to reply. The investigator acquainted the participants with the aim of the study, their significance in the research procedure, and the anticipated outcomes from them.

CHAPTER FOUR

PRESENTATION, ANALYSIS AND INTERPRETATION OF FINDINGS

4.1 Introduction

This chapter provides the presentation, analysis and interpretations of findings and the findings are presented mainly in tabular form.

4.2 Response rate

80 questionnaires were issued out to collect data for the study. However, all the 66 questionnaires were ticked and returned causing a response rate of 82.5%.

Item	Response	Frequency	Percentage
Gender	Response	66	82.5
	Non-response	14	17.5
	Total	80	100

4.3 Social demographic characteristics of respondents

The study looked at the socio-demographic characteristics of respondents. The data attained was presented in the frequency, percentage and tabulation tables from which conclusions were drawn. The main purpose of the respondents' profile was to indicate their views towards the study. This profile is shown in Tables below:

Table 1: Gender of respondents

Personal Characteristics	Response	Frequency	Percentage (%)
Gender	Male	36	54.55
	Female	30	45.45
	Total	66	100

Source: Primary Data

The gender distribution among respondents was fairly even at 54.55% male and 45.45% female. The study shows a balanced representation of genders. Both men and women are involved in running SMEs and bring diverse viewpoints to decision-making.

Table 2: Age of respondents

Personal Characteristics	Response	Frequency	Percentage
Age	18-30	12	18.5
	31-40	20	30.30
	41-50	24	36.36
	51 and above	10	15.15
	Total	66	100%

Source: Primary Data

The age distribution revealed that most respondents (36.26) Mid-career professionals dominate the workforce in ages 41 to 50 (36%). This is followed by the 31-40 age group (30.30%), showing that respondents have significant experience. The younger (18.18%) and older age groups (15.15% were less represented. The age groups in SMEs showed balanced diversity.

Table 3: Education level of respondents

Personal Characteristics	Response	Frequency	Percentage
Education level	Primary	4	6.06
	Secondary	6	9.09
	Certificate	12	18.18
	Diploma	14	21.21
	Bachelor's	15	22.73
	Master's Degree	15	22.73
	Total	66	100%

Source: Primary Data

Respondents' educational levels show a highly educated workforce.73% holding a bachelor's degree and an equal percentage having a master's degree. This strong focus on education shows the value SMEs place on qualifications. It likely helps with good management and strategic decisions—improving overall performance.

4.4 Study findings

The results in these tables below are presented according to a 5 Likert scale of 1-5 where 1 is strongly disagree (SD), 2 is disagree (D), 3 is not sure (NS), 4 is agree (A), and 5 is strongly agree (SA).

4.4.1 The control environment and its effect on the financial performance of SMEs in the study context.

Table 5: Responses on the control environment and its effect on the financial performance of SMEs in the study context.

The control environment and its effect on the financial performance of SMEs	Mean	Std. Deviation
There is a clear organizational structure with defined roles and responsibilities of employees e.g an accountant is in charge of preparing the financial statements	4.52	0.61
Company has a code of conduct that all the employees are aware of e.g arrival time for work and integrity while handling money for the business	4.34	0.73
Employees feel comfortable reporting unethical behaviour e.g they can report cases of fraud and theft and have their identity remain private	4.43	0.64
Employees understand their roles and responsibilities e.g store manager is in charge of stock taking on a daily basis	4.61	0.54
Company takes action on reported situations e.g investigating theft cases reported	4.23	0.72

Source: primary data

The findings on the effect of control environment on the financial performance of SME's showed that majority of the respondents strongly agreed that a clear organizational structure with defined roles and responsibilities for example an accountant is in charge of preparing the financial statements. The findings recorded a mean of 4.52 and a standard deviation of 0.61.

Respondents agree that a company has a code of conduct that all employees are aware of e.g arrival time for work and integrity while handling money for the business, followed by those who strongly agree, not sure, disagree and finally those that strongly disagree. The mean score was 4.34 and standard deviation of 0.73.

A mean of 4.43, and a standard deviation of 0.64 indicate that most employees feel comfortable reporting unethical behaviour for example employees can report cases of fraud and theft and have their identity remain private. This is crucial for upholding integrity within the organization and boosts financial stability.

Findings on the fact that employees understand their roles and responsibilities for example a store manager is in charge of stock taking on a daily basis showed that majority of the respondents strongly agreed. A mean score of 4.61 and a standard deviation of 0.54 was recorded.

The report suggests some areas where role clarity needs improvement. The findings show a mean of 4.23, and a standard deviation of 0.72. Some think the organization acts on reported issues. Others are not so sure. This difference shows possible inconsistencies in handling problems and could hurt financial performance.

4.4.2 The effect of control activities on the financial performance of SMEs in the study context.

Table 6: Responses on the effect of control activities on the financial performance of SMEs in the study context.

Table 6: Responses on the effect of control activities on the financial performance of SMEs in the study context.

The effect of control activities on the financial performance of SMEs	Mean	Std. Deviation
There are authority limits to accessing information e.g the director of Human Resource has access to all employee details of salaries and personal information, the director has access to high level strategic documents	4.42	0.52
There is segregation of duties of the employees e.g accounts department handles payments and sales department handles sales orders	4.34	0.73
Regular audits are conducted to ensure compliance with internal controls e.g internal audits to check on errors and fraud	4.54	0.63

There are security checks in order to access the premises, stores and information e.g a security check point at the entrance, a book for signing when taking records.	4.61	0.51
Bank Reconciliation of accounts is done regularly e.g every end month the records for cash account for the business and information in the bank statement are compared	4.24	0.73

Source: primary data

With a mean of 4.42 and a standard deviation of 0.52. The results suggest that authority limits are usually effective in protecting sensitive information. The mean and standard deviation show a strong agreement on their importance. This is vital for financial security.

The findings on the fact that segregation of duties of the employees suggests that separating duties is crucial for cutting down fraud and errors. This practice is key to maintaining the organization's financial integrity. This is shown by the mean of 4.34 and standard deviation of 0.73.

Regular audits are vital for compliance. Responses show some differences in how often they are seen as effective across the organization. This is further explained by the mean of 4.54 and standard deviation of 0.63.

The data suggests that security checks are valued but may not be uniformly applied. Ensuring consistent security practices is essential for protecting assets and maintaining financial stability. An average mean score of 4.61 and standard deviation of 0.51 were recorded.

The findings, with a mean of 4.24, and a standard deviation of 0.73, indicate that regular bank reconciliation is widely recognized as crucial for ensuring accurate financial records. This practice is key to preventing discrepancies and safeguarding financial integrity.

4.4.3 The relationship between risk assessment and its effect on the financial performance of SMEs in the study context.

Table 7: Responses on the relationship between risk assessment and its effect on the financial performance of SMEs in the study context.

The relationship between risk assessment and its effect on the financial performance of SMEs	Mean	Std. Deviation
The company carefully identifies and analyses potential financial risks e.g an increase in the interest rates that can affect borrowing	4.33	0.71
The company has risk management strategies and policies in place e.g insuring of the stock and stores	4.52	0.63
It is necessary for every SMEs to manage its risks in order to minimize financial loss exposure e.g having backup plans in case one plan fails	4.40	0.53
Management addresses financial risks in the company to the employees e.g increased market competition	4.21	0.72
The company conducts regular risk assessments to identify potential threats e.g periodically checks what risks can have a fatal impact to the business-like data breaches, non-compliance penalties	4.62	0.52

Source; primary data

With a mean of 4.33, and a standard deviation of 0.71, the findings highlight the importance of identifying and analysing financial risks. The variability in responses suggests some challenges in consistently applying risk assessment practices across the organization.

The findings with a mean of 4.52 and a standard deviation of 0.63 indicate strong support for risk management strategies. These methods are crucial to reducing financial risks. However, some employees notice gaps in how these plans are put into action.

With a mean of 4.40 and a standard deviation of 0.53. The findings highlight the need to manage risks and reduce financial loss. But responses show that although this is acknowledged, effectiveness in risk management differs.

The findings show with a mean of 4.21 and a standard deviation of 0.72. Communicating financial risks to employees is well-regarded. Clear communication helps create a culture that understands and supports financial stability.

CHAPTER FIVE

SUMMARY OF FINDINGS, CONCLUSIONS AND RECOMMENDATIONS

5.1 Introduction

An overview of the findings, conclusions, and suggestions is provided in this chapter. The suggestions are based on the chapter's results, which are summarized in this section.

5.2 Summary Findings

The summary of findings of the study is presented in line with the objectives as follows:

5.2.1 The effect of control environment on the financial performance of SMEs in the study context.

The research on control methods and their impact on SME finances shows that most respondents agree structured management is crucial. The findings to a greater extent highlight that employees understand their roles and responsibilities for example a store manager is in charge of stock taking on a daily basis. These findings are in agreement with the findings from a study by Inusah & Abdulai, (2015) who indicated that staff who performed their assigned duties competently and within the organizational commitments would contribute to the credible financial outcomes of an organization.

Furthermore, there is a clear organizational structure with defined roles and responsibilities of employees for example how an accountant is in charge of preparing the financial statements. These findings are in line with the findings conducted by Abuya (2017) which revealed that different components of the organizational structure like the hierarchy that clearly outlined the different roles and responsibilities of management and the employees contributed to the efficiency and improved financial performance of an organization.

The findings highlight that a strong control environment is key to securing their financial performance and sustainability.

5.2.2 The effect of control activities on the financial performance of SMEs in the study context.

The findings highlighted that there are security checks in order to access the premises, stores and information for examples a security check point at the entrance and a records book for signing when taking records. These findings are consistent with the findings conducted by Whittington & Pany (2016) which indicated that physical controls can influence the financial performance of the company.

In a similar way, regular audits are conducted to ensure compliance with internal controls for example internal audits to check errors and fraud. These findings are in line with the findings

conducted by Halil et al. (2018) and Karami et al. (2020) that point out that effective internal audit practices can lead to reduced instances of fraud and consequently improve small and medium enterprises' financial performance. Security checks are highly valued and they play a key role in protecting both physical and digital assets from unauthorized access. Finally, bank reconciliation ensures constant and accurate financial documentation. By doing this, the organization's financial integrity is preserved.

5.2.3 The relationship between risk assessment and its effect on the financial performance of SMEs in the study context.

The findings suggest that the company conducts regular risk assessments to identify potential threats for example periodic checks on what risks can have a fatal impact to the business, like data breaches and non-compliance penalties. These findings are supported by the research conducted by Brazel & Carpenter, (2017) who found out that conducting regular risk assessments can enable SMEs to stay abreast of emerging risks and prioritize their risk mitigation efforts accordingly in order to maintain financial stability (Brazel & Carpenter, 2017).

Additionally, it is necessary for every SME to manage its risks in order to minimize financial loss exposure like having back up plans in case on plan fails. These findings are in agreement with the findings conducted by Baramichai (2021) who indicated that SME owners should effectively and proactively manage risks by formulating strategies tailored to their business as it can safeguard the organization's operations and reputation.

The findings demonstrate a significant relationship between risk assessment and financial performance in SMEs.

5.3 Conclusion

The research has provided valuable insights into the Effect of Internal Control Systems on Financial Performance of Small and Medium Enterprises in the study context specifically how access to the control environment, effect of control activities and the relationship of risk assessment contribute to the financial performance. The findings for all three objectives demonstrate how important a robust control environment is to SMEs ability to turn a profit. Proactive risk assessment through regular risk identification and management and efficient controls are crucial for sustainability and financial performance can be improved by having

defined responsibilities and organizational frameworks. Furthermore, setting boundaries for power and separating responsibilities are vital control measures and incorporating routine audits and security inspections promotes the financial performance of the SMEs. A combination of these components form a framework that guarantees SMEs long term financial stability and growth.

5.4 Recommendations

Small business owners should prioritize developing and upholding a strong organizational structure and moral principles in order to create and preserve a strong control environment. Encouraging accountability and openness via dependable, moral leadership is essential for financial stability. Frequent ethics and internal control training helps staff members understand their responsibilities in maintaining these standards. To remain flexible in ever-changing business settings, small and medium sized firm owners must also periodically assess and upgrade their control systems.

For the purpose of preventing fraud and financial errors, SMEs should employ robust control measures such as preventive and detective controls. To provide the checks and balances that keep any one person from having undue influence over financial operations, they must make sure that tasks are divided across their teams (Whittington and Pany, 2016). For the purpose of enhancing financial reporting accuracy and ensuring policy compliance, managers should plan frequent internal audits. Rotating duties increases the likelihood that inconsistencies will be promptly identified and resolved hence reducing the risk of fraud (Petrovits et al.,2011).

Regulations mandating SMEs to implement comprehensive risk assessment and internal control frameworks should be established by policy makers. To identify and reduce financial risks, these regulations require obligatory audits and reviews (Nguyen et al., 2017). Lawmakers should also assist SMEs in utilizing cutting-edge technology tools for risk management by offering recommendations and support. This adoption can enhance their capacity for risk management and lead to better financial outcomes (Brazel and Carpenter 2017). Resources and training- rich support programs must be offered to SMEs to help them in these crucial areas.

In order to motivate SMEs to implement robust internal controls and efficiently manage risks, financial institutions have to offer tailored financial products and services. For SMEs that exhibit strong risk assessments and efficient control environments, this can include reduced interest rates or better loan conditions (Chandra, 2016). Financial institutions ought to collaborate with SMEs to provide risk assessment and financial management training. This

guarantees that managers and leaders of SMEs possess the abilities required to sustain solid financial performance. Monitoring the financial health of SMEs on a regular basis may also assist in determining which regions require additional assistance.

Employees within SMEs should actively engage in upholding the organization's ethical standards and internal control practices. They must see how vital their roles are in stopping fraud and keeping financial records accurate. Employees should join regular risk assessments and follow set controls (Tuan). Encourage them to engage in ongoing training related to finance and risk management. When accountability and continuous improvement become part of the culture (Certo&Certo), employees help secure the organization's financial health and success.

5.6 Areas of further research

Future research could explore advanced technology's impact on SME internal control systems. This study showed the good effects of technology on risk management and financial performance. A closer look at block chain and artificial intelligence might reveal how well they work. This research could explore how these technologies improve the accuracy and efficiency of internal controls. They also help reduce fraud risks and enhance financial management in SMEs. It will offer practical advice for adopting technology in this field.

Another area to research is how organizational culture boosts control environments in SMEs. This study highlighted the importance of ethical values. Future research could look more closely at how parts of organizational culture like communication and leadership styles affect internal controls. By understanding this interplay better SMEs can create strategies that strengthen internal controls and improve financial performance.

A long study on internal control systems and SME financial performance could give important insights. This snapshot of how controls affect finances shows a moment in time. Examining SMEs over longer periods would help researchers see if these effects last. This research can uncover patterns and challenges in the development of internal controls. It will show how these controls help small and medium-sized businesses stay financially stable and grow in various economic situations.

Researchers could compare how well internal control systems work in various industries. This study focused on SMEs in a specific context, but understanding how internal controls function in various industries—such as manufacturing, services, and retail—could reveal industry specific challenges and best practices. This research can help SMEs in various sectors adjust

their internal controls to handle risks and opportunities specific to their industry. This will improve their financial performance and give them a competitive edge in the market.

Research could also explore the influence of regulatory frameworks on the implementation and effectiveness of internal control systems in SMEs. This study briefly touched on the role of policy makers, but a more detailed investigation could analyse how different regulatory environments either support or hinder SMEs in establishing robust internal controls.

Understanding the impact of regulations could inform policy development, ensuring that frameworks are conducive to SME growth while maintaining high standards of financial integrity and accountability, thus fostering a stable and transparent business environment.

REFERENCES

- Abuya, T. (2017). The role of internal control environment in the financial performance of firms. *Journal of Accounting and Finance*, 9(2), 45-58.
- Albrecht, W. S., Albrecht, C. O., & Albrecht, C. C. (2018). *Fraud examination* (5th ed.). Cengage Learning.
- AICPA. (2017). *Audit and accounting guide for small and medium enterprises*. American Institute of Certified Public Accountants.
- Baramichai, M. (2021). Risk management strategies for SMEs. *International Journal of Business and Management*, 12(4), 89-102.
- Brazel, J. F., & Carpenter, T. D. (2017). The use of technology in risk assessment for financial reporting. *Journal of Information Systems*, 31(1), 25-39.
- Chandra, A. (2016). Risk management in SMEs: A critical analysis. *International Journal of Small Business Management*, 15(3), 66-79.
- Chartered Accountants Australia and New Zealand. (2021). *SME risk management: A practical guide*. Chartered Accountants Australia and New Zealand.
- Certo, S. T., & Certo, T. (2018). *Modern management* (14th ed.). Pearson.
- Committee of Sponsoring Organizations of the Treadway Commission (COSO). (2013). *Internal control—Integrated framework*. COSO.
- Committee of Sponsoring Organizations of the Treadway Commission (COSO). (2017). *Enterprise risk management—Integrating with strategy and performance*. COSO.
- Cosserat, G. W., & Rodda, N. (2015). *Modern auditing* (4th ed.). Wiley.
- Ewuuk, M. (2020). Internal controls in small businesses: Challenges and opportunities. *Journal of Accounting and Business Research*, 45(2), 128-141.
- Godfrey, P., Juma, I., & Namukose, J. (n.d.). The impact of internal controls on financial performance of SMEs in Uganda. *Uganda Journal of Business and Management*, 7(1), 55-68.

- Government of Uganda. (2011). National development plan 2010/11 – 2014/15. Kampala: National Planning Authority.
- Gupta, K. (2001). Contemporary auditing. Tata McGraw-Hill.
- Halil, B., Aslan, E., &Karami, R. (2018). Internal audit and its impact on the financial performance of SMEs. *Journal of Corporate Finance*, 23(3), 69-84.
- Heirer, J. (2015). Effective internal controls in SMEs. *Journal of Small Business Strategy*, 14(2), 45-58.
- Hessami, M. (2021). Achieving financial stability in SMEs through effective internal controls. *Journal of Financial Management and Analysis*, 34(1), 21-34.
- Inusah, H., &Abdulai, M. (2015). The effect of internal controls on revenue generation in SMEs. *International Journal of Business and Finance Management*, 5(2), 34-50.
- Jackson, T. (2004). *Management and change in Africa: A cross-cultural perspective*. Routledge.
- Karami, R., Aslan, E., &Halil, B. (2020). Reducing fraud in SMEs through effective internal audits. *Journal of Financial and Quantitative Analysis*, 28(3), 67-89.
- Lim, C., Tan, P., & Ibrahim, M. (2016). Enhancing internal controls through risk assessment. *Journal of Business Ethics*, 133(3), 41-59.
- Merchant, K. A., & Van der Stede, W. A. (2017). *Management control systems: Performance measurement, evaluation and incentives* (4th ed.). Pearson.
- Mintzberg, H. (2023). The role of SMEs in economic development. *Journal of Business and Economics*, 22(3), 102-115.
- Mwakimasinde, E., Odhiambo, O., &Amukowa, W. (2015). Internal control environment and financial performance in SMEs. *Journal of Business and Economic Development*, 6(4), 24-36.
- Namiri, M., &Stojanovic, D. (2018). Measuring financial performance in small enterprises. *Journal of Small Business and Enterprise Development*, 19(1), 29-42.

- Nguyen, T., Pham, H., & Vo, N. (2017). Risk management practices in Vietnamese SMEs. *Journal of Risk and Financial Management*, 14(2), 33-45.
- Onsongo, E., Muathe, S., & Mwangi, L. (2020). Impact of risk management on financial performance of SMEs in Kenya. *Journal of Financial Risk Management*, 15(2), 88-97.
- Oseifuah, K. (2015). The role of internal control systems in financial performance. *Journal of Accounting and Economics*, 30(2), 102-113.
- Petrovits, C. M., Shakespeare, C., & Shih, A. (2011). The causes and consequences of internal control problems in small firms. *The Accounting Review*, 86(3), 115-139.
- Rafindadi, A., & Olanrewaju, Y. (2019). Effective control activities in SMEs and their impact on financial performance. *Journal of Business Research*, 27(4), 55-68.
- Robert, H., Isaac, O., & Kazaara, A. G. (2023). The impact of internal controls on financial performance of SMEs in Uganda. *Uganda Journal of Finance and Management*, 9(2), 78-93.
- Schulze, A., Lubatkin, M., & Dino, R. (2013). Control activities and their role in financial performance of small businesses. *Journal of Small Business Management*, 51(3), 57-78.
- Taun, D. (2021). Creating an ethical culture in SMEs to improve financial outcomes. *Journal of Business Ethics*, 19(2), 45-62.
- Tuan, N. (2021). Ethical culture and its impact on SME performance. *Journal of Business Ethics*, 34(3), 84-101.
- Uganda Investment Authority. (2006). *SME development strategy for Uganda: 2005-2010*. Kampala: Uganda Investment Authority.
- Uganda Ministry of Finance, Planning and Economic Development. (2011). *The impact of SMEs on Uganda's economy*. Kampala: Ministry of Finance.
- Uganda Ministry of Trade, Industry and Cooperatives. (2015). *SME policy: Sustainable development of small and medium enterprises*. Kampala: Ministry of Trade, Industry and Cooperatives.
- Weatherspoon, D., & LeClair, M. (2012). The role of leadership in SMEs: Enhancing internal controls. *Journal of Small Business Strategy*, 13(4), 102-115.

Whittington, O. R., & Pany, K. (2016). Principles of auditing and other assurance services (20th ed.). McGraw-Hill Education.

Mwakimasinde, M. A., Odhiambo, O. M., & Byaruhanga, J. (2015). The relationship between internal controls and financial performance of small and medium enterprises in Kenya. *Journal of Business and Management*, 17(6), 48-60.

Economic Survey. (2009). Small and medium enterprises survey report. Government of Kenya.

Government of Uganda (GoU). (2015). *Small and Medium Enterprises Policy*. Ministry of Trade, Industry, and Cooperatives.

Ogwang, I., & Abaho, E. (2016). The relationship between internal control systems and financial performance in SMEs. In *Proceedings of the 5th International Conference on Business and Economics* (pp. 23-27).

APPENDICES

APPENDIX 1 : QUESTIONNAIRE

Introduction

Dear Respondent, my name is Nama Herman Tenywa. I am a third year student at Uganda Christian University and I am carrying out this study for the purpose of writing a dissertation as a requirement for the award of a bachelor's degree in Accounting and Finance at Uganda Christian University. The topic of study is **“The Effect of Internal Control Systems on Financial Performance of Small and Medium Enterprises in Buikwe District, Uganda.”**
A case study of Senasa Distributors.

You have been with purpose selected to participate in this study due to the importance of your knowledge on this study. The information you provide will only be used for the purpose of this study and will be treated with utmost confidentiality. Your identity will be kept anonymous. Please feel free and answer all the questions truthfully.

SECTION A: DEMOGRAPHIC INFORMATION

Instruction: Please tick the box that best describes the respondent.

1. Gender

- a. Male
- b. Female

2. What is your highest level of education?

- a. O-level
- b. A-level
- c. Certificate/Diploma
- d. Bachelor's Degree
- e. Master's Degree
- f. Others (Please Specify)

3. What position do you currently hold in the company that you work for?

- a. Management Committee member
- b. Departmental head
- c. Former Departmental head
- d. Division Head
- e. Staff member

4. In what age bracket do you fall?

- a. 18-25
- b. 26-35
- c. 36-45
- d. 46-55
- e. 56+

5. For how long have you served in your organization/Institution?

- a. 1-3 years
- b. 4-6 years
- c. 7-10 years
- d. 10+ years

SECTION B: EFFECT OF THE CONTROL ENVIRONMENT ON THE FINANCIAL PERFORMANCE OF SME'S IN THE STUDY CONTEXT.

Instruction: Indicate the degree of agreement with the following statements relating to how the control environment affects the financial performance of SME's in the study context by using a scale of 1-5, where **1- Strongly disagree, 2- Disagree, 3- Neutral, 4 Agree, 5- Strongly agree.**

No.	Statement	1 SD	2 D	3 NT	4 A	5 SA
1	There is a clear organizational structure with defined roles and responsibilities of employees e.g an accountant is in charge of preparing the financial statements					
2	Company has a code of conduct that all the employees are aware of e.g arrival time for work and integrity while handling money for the business					

3	Employees feel comfortable reporting unethical behaviour e.g they can report cases of fraud and theft and have their identity remain private					
4	Employees understand their roles and responsibilities e.g store manager is in charge of stock taking on a daily basis					
5	Company takes action on reported situations e.g investigating theft cases reported					
6	The systems in place for how work should be done are respected by all the employees e.g using the Distribution Management System to manage stock					

SECTION C: THE EFFECT OF CONTROL ACTIVITIES ON THE FINANCIAL PERFORMNACE OF SME’S IN THE STUDY CONTEXT.

Instruction: Indicate the degree of agreement with the following statements relating to how the control activities affect the financial performance of SME’s in the study context by using a scale of 1-5, where **1- Strongly disagree, 2- Disagree, 3- Neutral, 4 Agree, 5- Strongly agree.**

No.	Statement	1 SD	2 D	3 NT	4 A	5 SA
1	There are authority limits to accessing information e.g the director of Human Resource has access to all employee details of salaries and personal information, the director has access to high level strategic documents					
2	There is segregation of duties of the employees e.g accounts department handles payments and sales department handles sales orders					
3	Regular audits are conducted to ensure compliance with internal controls e.g internal audits to check on errors and fraud					
4	There are security checks in order to access the premises, stores and information e.g a security check point at the entrance, a book for signing when taking records.					
5	Bank Reconciliation of accounts is done regularly e.g every end month the records for cash account for the business and information in the bank statement are compared					
6	Regular performance reviews and evaluations e.g using key performance indicators like revenue growth and customer satisfaction					
7	Employees are offered regular trainings to improve on their skills e.g talks on new online fraud ways and schemes					

SECTION D: THE RELATIONSHIP BETWEEN RISK ASSESSMENT AND ITS EFFECT ON THE FINANCIAL PERFORMANCE OF SME'S IN THE STUDY CONTEXT.

Instruction: Indicate the degree of agreement with the following statements relating to how risk assessment affects the financial performance of SME's in the study context by using a scale of 1-5, where **1- Strongly disagree, 2- Disagree, 3- Neutral, 4 Agree, 5- Strongly agree.**

No.	Statement	1 SD	2 D	3 NT	4 A	5 SA
1	The company carefully identifies and analyses potential financial risks e.g an increase in the interest rates that can affect borrowing					
2	The company has risk management strategies and policies in place e.g insuring of the stock and stores.					
3	It is necessary for every SMEs to manage its risks in order to minimize financial loss exposure e.g having backup plans in case one plan fails					
4	Management addresses financial risks in the company to the employees e.g increased market competition					
5	The company conducts regular risk assessments to identify potential threats e.g periodically checks what risks can have a fatal impact to the business like data breaches, non-compliance penalties					
6	Employees across different departments are all involved in risk management processes e.g employees respond and share what issues like leaking stores should be looked into that could be risks to the business					
7	The company carries out regular risk assessments to adapt to changing market conditions e.g checking market competition which can be a risk in order to find new ways to survive or improve the product					

Thanking you for your participation.

Appendix 11: Data collection letter

SCHOOL OF BUSINESS

19th Aug, 2024

TO WHOM IT MAY CONCERN

Name: **NAMA HERMAN TENYWA**

Reg. No **S21B33/021**

A bachelor's student who is seeking permission from your office to collect data for her dissertation titled

Effect Of Internal Control Systems On Financial Performance Of Small And Medium Enterprises. Case Study of Senasa Distributors Lugazi In Lugazi Town, Buikwe District.

We shall be grateful if you could render assistance to her in collecting the necessary data for her dissertation

The Uganda Christian University School of Business thanks you in advance



.....
Mukisa Simon Peter
Research coordinator