THE EFFECT OF INTERNAL CONTROL ON FINANCIAL PERFORMANCE

CASE STUDY CENTENARY BANK ENTEBBE BRANCH

Submitted by:

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ABBREVIATIONS

AAS	-	Audit and Assurance Standard 6
CA	-	Control Activities
CE	-	Control Environment
CIMA	-	Cynam Island Monetary Authority
CIV	-	Coefficient of Validity Index
COSO	-	Committee of Sponsoring Organizations
ICS	-	Internal Control System
RA	-	Risk Assessment
SOX	-	Sarbenes-Oxley ACT
USA	-	United States of America

DEFINITION OF KEY TERMS

Internal control is designed and affected by those charged with governance in the entity management and other personnel to provide reasonable assurance the achievement of the entity's objectives.

Control environment refers to the management's attitude towards controls, sets the stage for attitude and actions of the entire company.

Control activities encompass both policies and procedures that management has established to ensure management directives are carried out in the organization.

Financial performance is the ability to operate efficiently, profitability, survive, grow and react to the environmental opportunities and threats.

Risk assessment is management's identification and analysis of risks relevant to the preparation of financial statements in conformity with generally accepted accounting principles.

Population involves an entire group of individuals, events or objects having common observable characteristics.

ABSTRACT

This paper seeks to find out how the different commercial banks manage the internal controls using Centenary Bank Entebbe Road Branch as a case study; this paper will focus on commercial banks in Uganda. The internal control objectives include; control environment, risk assessment and control activities and how they affect financial performance of the organization. Internal controls help a company to have controls designed to make operations effective and efficient. They also ensure that all transactions are promptly and properly recorded at the correct amount in the appropriate accounts and in the proper accounting period so as to permit preparation of financial statements in accordance with relevant legislation and accounting standards hence improving on the organization's welfare and reduction on the rate of fraud in the financial sector. Hence there is a close relationship between internal control on financial performance since controls still help the organization to ensure errors and irregularities are avoided or made apparent.

A cross sectional survey was used in the course of the study. Both qualitative and quantitative data was gathered in order to establish the relationship between the independent and dependent variables, so as to examine how internal controls are used in Centenary Bank and therefore account for the performance levels. The study comprised of 35 employees in centenary bank. Simple random approach was used during the study. Purposive sampling was also used to select only respondents for the researcher to attain the purpose of the study. Data was collected using both primary and secondary sources. After collecting data, the researcher organized well-answered questionnaire, data was edited and sorted for the next stage. The data was presented in tabular, bar graphs with frequencies and percentages. The researcher used Statistical Package for Social Sciences (SPSS) to analyze the relationship between the variables under study.

Therefore I intend to find out how commercial banks can use the internal controls systems so as to maintain the financial performance of the banks including control fraud and monitoring employees and how they should carry out their activities so as to achieve the desired goals and activities.

CHAPTER ONE

INTRODUCTION

1.0 Introduction

This chapter shall cover the background of the study, statement of the problem, purpose of the study, objectives of the study, research questions, research hypotheses, scope of the study, justification of the study and definition of key terms. The reason as to why I chose this topic is because I want to know whether there was a close relationship between internal control and financial performance since controls still help the organization to ensure errors and irregularities are avoided. Therefore I intend to find out how commercial banks can use the internal controls systems so as to maintain the financial performance of banks including control of fraud and monitoring employees and how they should carry out their activities so as to achieve the desired goals and activities.

When a company suddenly collapses, the question that comes to mind is “what went wrong?” A break down in the internal control is the usual cause. According to Gupta (2001), internal control is the plan of an organization and all methods and procedures adopted by management of an entity to assist in achieving management’s objective of ensuring, as far as applicable, the orderly and efficient conduct of the business including adherence to management policies, the safe guarding of assets, prevention and detection of fraud and error, the accuracy and completeness of accounting records and timely preparation of reliable financial information. Some objectives include; efficiency and effectiveness, reliability of financial reporting, and compliance with relevant laws and regulations. Therefore the absence of these variables may often result in organizational failure. However, Goh and Li (2011) demonstrate that firms having material internal control weaknesses exhibit lower financial performance compared with the firms that do not have such weaknesses and that the subsequent remediation of internal control weakness leads to greater financial performance. The findings should suggest that effective internal controls lead to the adoption of a reporting strategy that is based on more financial performance.

According to Lobbecke (1997), internal control is designed and affected by those charged with governance in the entity (for example an entity's board of directors), management and other personnel to provide reasonable assurance about the achievement of the entity's objectives in the following categories; reliability of financial reporting, effectiveness and efficiency of operations and compliance with applicable laws and regulations. It is worth noting that internal controls only provide reasonable but not absolute assurance to an entity's management and board of directors that the organization's objectives will be achieved. "The likelihood of achievement is affected by limitations inherent in all systems of internal control" (Hayes et al., 2005). Organizations establish systems of internal control to help them achieve performance and organizational goals, prevent loss of resources, enable production of reliable reports and ensure compliance with laws and regulations.

1.1Back ground of the study

Globally, according to American International Federation of Accountants (2012), internal control is a crucial aspect of an organization's governance system and ability to manage risk and is fundamental to supporting the achievement of an organization's objectives and creating, enhancing and protecting stakeholders' value. On the other hand, high-profile organizational failures typically lead to the imposition of additional rules and requirements, as well as to subsequent time - consuming and costly compliance efforts. However, the International

Federation of Accountants (2012)say that this obscures the fact that the right kind of internal control enabling an organization to capitalize on opportunities, while offsetting the threats, can actually save time, money and promote the creation and preservation of value. Ideally, effective internal control also creates a competitive advantage, as an organization with effective controls can take an additional risk.

In contrast, according to COSO (1992), internal control is a process that guides an organization towards achieving its objectives which include; operational efficiency and effectiveness, reliability of financial reporting and compliance with relevant laws and regulations. Absence of these variables often results in organizational failure.

Furthermore, the findings of the Tread way Commission Report (1987)carried out in the United States (USA) confirmed absence of, or weak internal controls as the primary cause of many cases of fraudulent company financial reporting. The widespread of global corporate accounting scandals that assumes near epidemic proportions in recent years inform this study. Notable cases include; Enron and WorldCom in the United States of America, Parmalat in Europe and ChuoAoyama in Asia(Shelton and Whittington, 2008).Naturally, no business will sit idle and watch fraudsters loot its resources away; there will be effort made to control the situation. Analytically, there are many methods adopted by business entities and the method that has proved very successful is internal control system. The ICS comprises the plan of; organization and all of the co-coordinating methods and measures adopted within a business to safe guard its assets.

Similarly, Jajanthi and Krishran (2001) argue that the emphasis on good internal controls arises because it is considered to be an important factor in achieving good quality financial performance. It is therefore important to examine monitoring mechanisms that corporations can use to ensure the effectiveness of their internal control. Absolutely, the quality of an entity's internal control is a function of the quality of control environment which consists of the board of directors and audit committee.

According to Stoner (2003), financial performance refers to the ability to operate efficiently, profitability, survive, grow and react to the environmental opportunities and threats. In agreement with the above, Stoltenberg and Anderson (1995), asserts that performance is measured by how efficient the enterprise is in use of resources to achieving its objectives.

Regionally, in the late 1990s and early 2000s, the Ugandan banking industry underwent significant restructuring. Several indigenous commercial banks were declared insolvent, taken over by the central bank and eventually sold or liquidated. These included; Uganda Cooperative Bank, Greenland Bank, International Credit Bank, Teefe Bank and Gold Trust Bank, which were closed or sold. Uganda Commercial Bank was initially privatized through a sale of its majority shares to a purported company from Malaysia. However, it later came to light that the actual buyer was a partnership between Greenland Bank, which was insolvent at the time and some politically connected individuals. A second privatization sale was conducted, with the Standard Bank of South Africa emerging as the winner.

Besides, the privatized Uganda Commercial Bank was merged with the former Grindlays Bank which Standard Bank of South Africa already owned and had renamed Stanbic Bank. The merged new bank is now known as Stanbic Bank (Uganda) Limited. As of 2008, Stanbic Bank(Uganda) Limited was the dominant commercial bank in Uganda, with about 27% of all bank assets and about 20% of all bank branches. Akin, Nile Bank Limited, an indigenous institution, was acquired by the British conglomerate, Barclays Plc, in January 2007 and merged with its existing Ugandan operations to form the current Barclays Bank (Uganda).

Even then, a moratorium on new commercial bank licenses was declared in 2004, with the passage of a new banking bill in Parliament, which established new banking institution classification guidelines.

Eventually, Centenary Bank started as an initiative of the Uganda National Lay Apostolate in 1983 as credit trust and it began operations in 1985. In 1993, it was registered as a fully-fledged commercial bank. Today Centenary bank is the leading Micro Finance and commercial loans provider serving over 1,000,000 customers. Ownership is as follows 31.3%-The Ugandan Secretariat, 0.3%-individual Ugandans, 18.3-StichtingHivos-TridosFonds, 11.6% SIDI, 38.5%.

Internal controls used in commercial banks in Uganda today face a challenge of inadequate management oversight. They face a challenge of accountability and failure to develop a strong culture within banks. In addition, there is inadequate assessment of risk of certain banking activities whether on or off balance sheet. That is why this affects the financial performance of banks in Uganda. Nevertheless a system of effective foundation is for the safe and sound operations of banks in Uganda. This requires all banks on-and-off-balance sheet activities and that responds to changes in bank's environment and condition (Cohen; 2002).

1.2 Statement of the problem

Effectiveness of internal control on financial performance should be considered most important in every organization, because the task of internal control is to prevent, detect and investigate fraud in an organization (Doyle, 2007). In as much as internal control systems are wide and numerous, for the sake of this study, internal control is limited to; the control activities, risk assessment and control environment. Control activities occur throughout the organization at all levels and all functions (Junner, 1993). They include; authorization, verifications, reconciliations, reviews of operating performance security of assets and segregation of duties (Ernst and Yong, 1995).

The majority of commercial banks in Uganda seem to have weak internal controls making the availability of information for risk analysis by the bank and micro lenders inadequate (Bukenya; 2011).Additionally, the most common internal control weaknesses include; too much trust in employees, lack of proper procedure for authorization, lack of personal financial information disclosure (for bank frauds), lack of separation of transaction authority from custodian of assets, inadequate independent checks on performance, lack of adequate attention to detail, failure to separate asset custody from accounting for assets, failure to separate accounting duties, absence of clear lines of authority, relaxed or absence of audit activities or reviews, no conflict of interest statement required and lack of adequate documents and records.

Finally, internal control systems of most commercial banks are not developed basing on theories/ models such as Agency theory which would promote the philosophy and management style, organizational structure and methods of imposing control. Assignment of authority and responsibility are all key aspects of the control environment (Jones, 2007).

Therefore the researcher intends to find out the effect of internal control on financial performance of Centenary Bank Entebbe Road Branch.

1.3 Broad objective of the study

Find out the relationship between internal controls and financial performance of Centenary Bank.

1.4 Objectives of the study

1. To investigate the effect of risk assessment on the financial performance in Centenary Bank.
2. To examine the relationship between control environment and the financial performance in Centenary Bank.
3. To find out the effect of control activities on the financial performance in Centenary Bank.

1.5 Research questions

i. How does risk assessment affect the financial performance of Centenary Bank?
ii. How do control activities affect the financial performance of Centenary Bank?
iii. What is the effect of control environment on the financial performance of Centenary Bank?

1.6 Scope of the study

The research shall focus on the effectiveness of the internal control systems in Centenary bank. Centenary bank has several branches; the research shall however focus on Centenary bank Entebbe branch. This is mainly due to the fact the other branches use similar internal controls to those that is used at Entebbe branch.

1.6.1 Subject matter

The study focused on effectiveness of internal control on the financial performance of commercial banks in Uganda (Centenary Bank Entebbe Road branch).Internal control consist of;

control environment, risk assessment and control activities and financial performance consisted of; liquidity, profitability and accountability.

1.6.2 Geographical coverage

This study was carried out in centenary bank located in Kampala along Entebbe Road Talent House Plot7. Centenary Bank was chosen as the case study because it is one of the commercial banks in Uganda which is unexceptional when it comes to problems of poor internal controls. This is mainly due to the fact that majority of other centers are just coming up and the internal controls implemented at other centers of centenary bank are a replica of the controls at the main center.

1.6.3 Time period

The research covered the period from 2008 and 2012.

1.7 Justification of the study

Financial performance is one area that is given a lot of prominence all over the world, it has been widely researched. A lot of literature has been written on financial performance and external auditors normally place a lot of emphasis on internal controls as a measure to ensure sustainability. This study shall therefore try to establish the linkage between internal controls and improved financial performances measured by liquidity, accountability and financial reporting.

1.8 The significance of the study

The findings of the study would help the management of the bank to maintain an enhanced controlled environment by helping management and employees to establish and maintain an environment throughout the bank that sets a positive and supportive attitude towards internal control, reliable management, operating personnel for effecting internal control and internal audit for evaluating whether appropriate controls have been implemented and whether the internal controls are functioning as intended. Other significance of the study includes;

The study established the relationship between the dependent and the independent variables. The relationship will institute the link between internal controls and financial performance of the employees in Centenary bank.

1.9 Conceptual frame work

Over view of the objectives

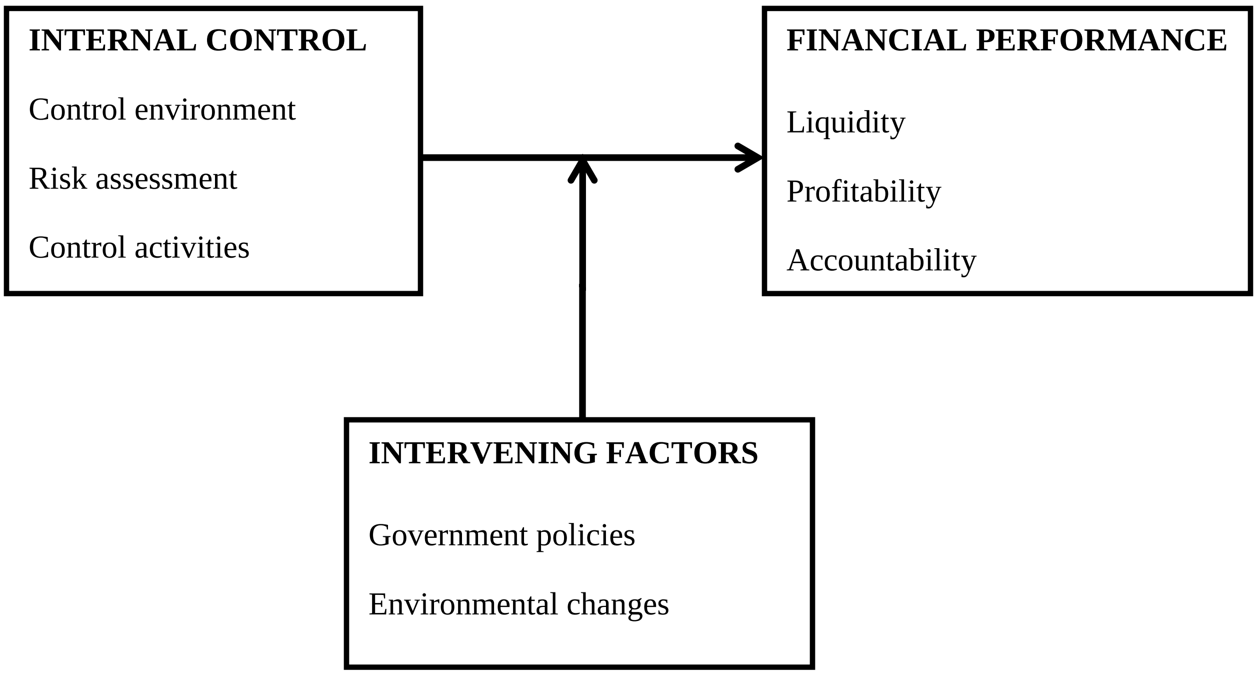
According to Douglas, (1996), is the process of identifying and responding to business risk.

Control activities encompass both policies and procedures that management has established to ensure management directives are carried out in the organization, (Douglas 1996).

According to Arens, et al, (2000), control environment consists of actions, policies and procedures that reflect the overall attitude of top management, the directors and the owners of an entity about control and its importance to the entity.

Figure 1: Conceptual Framework

Independent variable **Dependent variable**



Source: *Douglas, 1996and Arens, et al, 2000*

From the above conceptual framework, it is clear that internal controls as an independent variable (as measured by the control environment, monitoring and the risk assessment) affects financial performance a dependent variable (as measured by liquidity of an entity, accountability and profitability). However, there are also moderating factors like government policies and environmental changes

CHAPTER TWO

LITERATURE REVIEW

2.0 Introduction

This chapter seeks to bring out the relevant works of different authors about internal controls.

The research was intended to assess the effect of internal controls on financial performance with emphasis on commercial banks. The review of available literature therefore endeavored to establish whether there is a correlation between internal control systems as an independent variable and financial performance as a dependent variable. The review particularly focused on risk assessment, control environment and control activities as the main variables of internal control. The review also examined financial performance and in particular focusing on Liquidity, Accountability and Profitability. The review examined the common systems of internal controls employed by organizations. The review also determined the main objective systems of internal control that are normally intended to achieve. The ultimate objective of this review was therefore to examine the relationship between internal controls systems and financial performance.

Therefore the chapter involves the review of related literature and summary.

2.1 Theory frame work

Agency theory

According to Berle and Means (1935), agency theory is a concept that explains why behavior or decisions vary when exhibited by members of a group. Specifically, it describes the relationship between one party, called the principal that delegates work to another, called the agent. It explains their differences in behavior or decisions by noting that the two parties often have different goals and independent of their respective goals, may have different attitudes toward risk. The theory essentially acknowledges that the different parties involved in a given situation with the same given goal may have different motivations and that these different motivations can manifest in divergent ways. It states that there will always be partial goal conflict among parties, efficiency is inseparable from effectiveness and information may always be somewhat asymmetric between principal and agent.

Hoitash andKarlam (2012)agency theory focuses on the conflict that arises from the separation between principals(shareholders) and agents (managers). The essential conflict,that while the principal engages the agent to take actions on his or her behalf and the agent's interests are sometimes not well aligned with those of the principal. To alleviate this conflict, the principal can write a contract tying the agent's compensation to observed performance (Jensen and Meckling 1976). Enforcing such contracts requires that theprincipal engage in costly monitoring of the agent's effort (Fama and Jensen 1983), but such monitoring is essential because agents that are not monitored are more likely to behave opportunistically and extract greater firm resources (Fama; 1980).

2.2An overview of internal control

According to Doyle, Weili and Vay (2007), internal control is the process that provides reasonable assurance regarding reliability of financial reporting. Today, organizations are less able to perform many internal controls (for example multiple layers of authorization, cross-checking, supervision and segregation) because, as previously argued, they employ less people due to technological advancement and changing management techniques. However, the revised professional guidance highlights opportunities to strengthen overall control. The audit is acknowledging the importance of revised control criteria in achieving effective internal control (Aimar 2001; Kinney 2000).

Jajanthi and Krishran(2001) add that the emphasis on good internal control a risesbecause it is considered to be an important factor in achieving good quality financial performance. It is therefore important to examine monitoring mechanisms that corporations can use to ensure the effectiveness of internal control. The implication is that an entity’s internal control should be under the purview of the audit committee quality and internal control. Also the quality of an entity’s internal control is the function of the quality of control environment board of directors and audit committee. Thereforethe mechanism of ensuring high-quality audit committee would ensure a high quality internal control which could differ across entities. It could directly engage in overseeing the company’s financial and accounting staff.

Pan and Weon(2001) argue that the economic consequences of auditor’s legal liability in a setting where the quality of the firm’s internal control system and auditor’s effort jointly determine the in formativeness of the auditors export on firm’s financial statements. The costly nature of internal control raises a question of how to balance the owner’s investment in the internal control system with the auditor’s effort. It shows that when the auditor is legally liable to financial statement users, there is a nontrivial strategic interaction between the auditor’s provision of effort and firm owner’s investment internal controls systems. The distinguishing feature of the study is the in formativeness of audit report depends not only on the auditor’s effort but also on the owner’s costly investment in the internal control system. This shows that, if the auditor’s expected liability loss is sufficiently large, the owner under-invests efforts leading to an efficiency loss. While reducing the owner’s legal liability in this situation, improves social efficiency by alleviating the misallocation of the owners and auditor’s investment.

2.3Actual review of the literature

2.3.1 Control environment and financial performance

The control environment is the foundational context within which the other aspects of internal control operate (Konrath, 1999). The philosophy and management style, organizational structure, methods of imposing control, assignment of authority and responsibility are all key aspects of the control environment (Jones, 2007).

According to Rick, et al(2005), controlenvironment means the overall awareness, attitude and actions of directors and management regarding the internal control system and its importance in the entity. The control environment has persuasive influence on the way business activities are structured, the way objectives are established and the way risks are assessed. Management can show a positive attitude by including internal control in performance evaluations, discussing internal controls at management and staff meetings and by rewarding employees for good internal control practices. Commitment to competence includes;a commitment to hire, trains, and retain qualified staff. It encompasses both technical competence and ethical commitment. Management's commitment to competence includes; both hiring staff with the necessary skills and knowledge and ensuring that current staff receives adequate on-going training and supervision.

According to Minnesota management and Budget (2013),discovered that control environment is the foundation of an effective internal control system and begins with the "tone at the top" - the words and actions of the agency's leadership. Under an effective control environment, employees view internal control as an essential and integral to doing their day-to-day job duties. It can also be useful in prompting discussion among agency senior management and help determine what, where and how improvements can be implemented in the agency's current control environment.

Control environment consists of; actions, policies and procedures that reflect the overall attitude of top management, directors and owners of an entity about control and its importance to the entity. If top management believes that control is important, others in the organization will sense that and respond by conscientiously observing the controls established. The essence of an effectively controlled organization lies in the attitude of its management (Arens andLobbecke, 1997).

Savens and Beelde (2006b) argued that control environment encompasses the policies, procedures and skills that exist within a department to ensure that only valid financial transaction are recorded accurately and the rules and regulations are compiled with. While Savens and Beelde (2006a) found out that control environment (for example level of risk and control awareness extent to which responsibilities related to risk management and internal controls are clearly defined and communicated) are significantly related to the role of internal audit function with an organization.

According to Arens et al (2000), the control environment contains the actions, policies and procedures that reflect the overall attitudes of top management, the directors and the owners of an entity about control and its importance of the entity. C E includes general controls which are actual activities (policies and procedures) used to implement the control systems henceeffect the culture of the organization in so far as it relates to internal control and is part of the corporate governance.

Furthermore Eilifsen, Messeir, Glover, and Prawitt (2010) found out that control environment sets the tone of the organization, influencing the consciousness of its people. It is the foundation for all components of internal control providing discipline and structure. Therefore importance of control to an entity is reflected in the overall attitude to, awareness of and actions of those charged with governance, management and owners regarding control. This can be thought of as umbrella that covers the entire entity, and establishes the frame work for implementing the entity's accounting systems and internal control.

William and Messier (2000) emphasize that control environment (CE) is the foundation for all other components of internal control, providing discipline and structure and encompassing both technical competence and ethical commitment. Managers must evaluate the internal control environment in their own unit and departments as the first step in the process of analyzing internal controls. Many factors determine the CE and are listed below for consideration. This list is not all-inclusive, nor will every item apply to a particular unit. First, management's attitude, actions and values set the tone of an organization, influencing the control consciousness of its people. Internal controls are likely to function well if management believes that those controls are important and communicates that view to employees at all levels. Conversely, if management believes that controls are unrelated to achieving objectives or are obstacles then this attitude will be communicated.

The Institute of Standard Chartered Accounts in England (2005) refer to control environment as the client's culture and deals with matters such as ethics competence, management's philosophy, operating style, the organizational structure and operating policies of the business. Therefore, an agency's internal controls and structures underpin a strong control framework; management should also have an understanding of the importance of the agency's culture in influencing the effectiveness of the controls. For example, an agency may have a well-documented risk management process, but without active management support, the process may not be adopted to the extent required to ensure best practice concerning risk identification and management.

Similarly Taylor and Millichamp(2008) discovered that the control environment includes the attitude, awareness and actions of the directors and senior managers of the organization. It is, in effect, the culture of the organization in so far as it relates to internal control and is part of corporate governance In addition Carmichael (1996) said that control environment in most cases deals with the management's attitude towards control, sets the stage for attitude and actions of the entire company. Unless employees perceive that control is no important to top management, there will be little nor an effective application of accounting and control procedure. Therefore control environment sets tone for company.

Whittington and Pany (1996) were of the view that control environment sets the tone of an organization. This is done by influencing the control consciousness of people which may be viewed as foundation for the other components of internal control. CE factors include integrity and ethical values, commitment to competence, board of directors or audit committee, organizational structure and assignment of responsibilities. Therefore if auditors are to use control environment must obtain sufficient knowledge to understand management's attitudes, awareness and actions concerning the control environment. It is important that auditors concentrate on substance of control, rather than their form for example an organization may have, but not enforce, code of conduct prohibiting unethical activities.

Doyle and Vay (2007) argued that where there is weak control environment in the internal control, there is more likely hood that material misstatement of the annual or interim in financial statement will not be prevented. While according to Statement on Standard Attestation (2012) control environment helps to provide the necessary structure and discipline which helps to establish a "tone at the top" within an organization.

According to Hayes et al. (2005),the control environment means the overall attitude, awareness, and actions of directors and management regarding internal control system and its importance in the entity. The CE has a pervasive influence on the way business activities are structured, the way objectives are established, and the way risks are assessed. The control environment is influenced by the entity's history, culture and the control consciousness of its people. Hence effectively controlled companies set a positive "tone at the top" and establish appropriate policies and procedures.

O'Reilly et al. (1998) have established that an entity's management can foster control environment that encourages control consciousness on the part of employees and contributes to the quality of the other components of internal control. Such control environment has pervasive influence on the way (an entity's) business activities are structured objectives established and risks assessed. This enables the auditor to determine whether it appears to be conducive to maintaining effective internal control and whether it minimizes the incentives and opportunities for management to deliberately distort the financial statements. Understanding the control environment gives the auditor an indication of management's and the board of directors' attitudes towards control and their approach to directing the business.

According to Douglas et al. (2010),the control environment sets the tone of an organization, influencing the control consciousness of its people. It is foundation of all components of internal control, providing discipline and structure. The importance of control to an entity is reflected in the overall attitude to, awareness of and actions of those charged with governance, management and owners regarding control. The control environment can be thought of as an umbrella that covers the entire entity, and establishes the frame work for implementing the entity's accounting systems and internal control.

Carmchael, Willingham and Schaller (2009) state that control environment is the management's attitude towards control, sets the stage for the attitude and actions of the entire company. If employees perceive that control is not important to top management there is little hope for an effective, conscientious application of accounting and control procedures. The control environment sets a tone of an organization. Therefore CE influences the control consciousness of all organizational personnel and is the foundation for all other components

Beneish et al (2008) discussed the control environment as the tone of an organization and the way it operates. He further says that it concerns the establishment of an atmosphere in which people can conduct their activities and carry out their control responsibilities effectively. Likewise, COSO (2004) looks at the ethical environment of an organization to encompass aspects of upper management's tone in achieving organizational objectives, their value judgments and management styles. The control environment represents the control atmosphere for the entity and is the foundation for the other components (Nicolaisen, 2004).

Bates (2001) considers the factors relating to the control environment to include the integrity, ethical values, and competence of employees and management, management's philosophy and operating style, the manner in which authority and responsibility are assigned, the organization and development of employees, and the attention and direction of the board of directors towards organizational success.

Lou (2008) concurs that higher level administrators of an organization are responsible for establishing the appropriate control environment.

Control Environment (CE) is the philosophy, style and supportive attitude, as well as the competence, ethical values, integrity and morale of the people of the organization (DiNapoli, 2007). The CE is further affected by the organization's structure and accountability relationships. Whereas DiNapoli, (2007) found out control environment (CE) as the attitude and actions of council and management regarding the significance of control. In addition control environment also provides the discipline and structure for the achievement of the primary objectives of the System of Internal Control.

INTOSAI (2004)assert that control environment is the foundation of the (internal control system) ICS and sets the tone of an organisation, influencing the control consciousness of its staff. Similarly Thuy (2007) said control environment provides the discipline and structure as well as the climate which influences the overall quality of the Internal Control Systems. Elements of the control environment are; the personal and professional integrity and ethical values of management and staff, appropriate culture in the organisation, attitude towards

Rajkumar (2009) reports control environment as the underlying foundation for the success of all the other elements of the internal control. Furthermore as per Auditing and Assurance Standard 6 issued by ICAI (AAS6), the control environment means the overall attitude, awareness and actions of directors and management regarding the internal control system and its importance in the entity. The control environment has an effect on the effectiveness of the specific control procedures and provides the background against which other controls are operated. Therefore a strong control environment, for example, one with tight budgetary controls and an effective internal audit function, can significantly complement specific control procedures. However, a strong control environment does not, by itself, ensure the effectiveness of the internal control system.

2.3.2 Control activities and financial performance

William and Messier (2000) expressed control activities as policies and procedures that help ensure management's directives are carried out and are implemented to address risks identified in the risk assessment process. It sets the tone of the organization, influencing the control consciousness of its people. It includes range of activities, including approvals, verification and reconciling of duties.Therefore control activities should be an integral part of the daily activities of a bank. An effective internal control system requires that an appropriate control structure is set up with control activities defined at each level. These include top level reviews and appropriate activity controls are for different departments or divisions.

Douglas et al. (2010), report that control activities are policies and procedures that ensure that management's directives are carried out and are implemented to address risks identified in the risk assessment process. They include a range of activities, including approvals authorizations, verifications, and reconciliations. CA facilitate a registered entity's ability to monitor, identify, assess, and take corrective action with respect to actions that effect compliance with Reliability Standards, and, therefore, promote compliance with the Reliability Standards.

Similarly Rick et al (2005) term control activities as policies and procedures that help ensure management directives are carried out. They help ensure that the necessary actions are taken to address risks to the achievement of the entity's objectives for operations and financial reporting. CAs are divided into two elements policy establishing what should be done and procedures to affect that policy. A policy, for example, securities dealer retail branch must monitor customer trades. The control procedure is a review of a computer printout of daily trade activities by the customer, performed in a timely manner and with attention given to the nature and volume of securities traded.

CorrespondinglyWhittington and Pany (2001) agree with the above authors that to control activities as policies and procedures that help ensure that management's directives are carried out. These policies and procedures promote actions that address the risks that face the organization. Therefore they are designed and implemented to address the risks that the bank identified through risk assessment process. For smaller clients, it is common to identify few or no control activities because controls are often ineffective due to limited personnel. In that case, the auditor sets a high assessed control risk. For clients with extensive controls where the auditor sets a high assessed control risk believes controls are likely to be excellent, it is often appropriate to identify many controls during the understanding phase.

According to Millichamp (1996), control activities are policies, procedures, techniques, and mechanisms that help ensure that management's response to reduce risks identified during the risk assessment process is carried out. In other words, control activities are actions taken to minimize risk. The need for a CA is established in the risk assessment process. When the assessment identifies a significant risk to the achievement of an agency's objective, a corresponding control activity or activities is determined and implemented. CA can be preventive or detective: Preventive activities are designed to deter the occurrence of an undesirable event. The development of these controls involves predicting potential problems before they occur and implementing procedures to avoid them while detective activities are designed to identify undesirable events that do occur and alert management about what has happened. This enables management to take corrective action promptly.

According to Millichamp and Taylor (2008), the control activities are detailed policies and procedures that help ensure management directives are carried out, for example necessary actions are taken to address the risks that threaten achievement of the organization's objectives. Also control activities are tools, including policies, procedures, actions and other mechanisms, that help ensure actions are taken to address risks ("what can go wrong?"). They are essential for proper stewardship and accountability of government resources and for achieving program goals and objectives. Control activities should be recognized as an integral part of each business process, rather than a separate system. CA encompass a wide array of actions, from simple steps such as locking a filing cabinet; to more complex measures like analyzing and approving grant applications. Control activities occur at all levels and functions of an organization, from data entry to management reviews In short, control activities represent sound business practices but control activities benefit, rather than hinder, the agency by helping to achieve organizational goals. They are not intended to limit or interfere with an agency's duly granted authority related to legislation, rule-making or other discretionary policy-making.

According to Carmchael, Willingham, and Schaller (2009), emphasize that control activities encompasses both policies and procedures that management has established to ensure management directives are carried out. Control activities relevant to an audit are often called control procedures. The concepts underlying control activities are likely to be similar across all agencies, but the form and formality with which they operate will vary. Therefore, smaller agencies rely on highly effective management controls instead of other types of control. For example, management's retention of authority for approving significant purchases can provide strong control over this activity, lessening the need for more detailed or redundant control activities. Setting up an appropriate segregation of duties can also be challenging in a smaller agency. However, even agencies with only a few employees can assign responsibilities to achieve appropriate segregation, or use management oversight of the incompatible activities to achieve a strong control structure.

O'Reilly et al. (1998) argued that control activities are established only for high-volume or high-risk classes of transactions. The design of control activities is influenced by the size, complexity, and nature of the business as well as the nature of the entity's internal control as a whole. Control activities can actually help ensure the agency is acting within their authority and complying with legislative requirements. The implementation of control activities must always consider costs and benefits, especially since most agencies struggle with limited resources, such as staffing, funding, and time. Excessive or duplicative control activities should be avoided; attempting to completely eliminate a risk is generally not achievable, would be prohibitively expensive and would most likely slow down productivity. As a general rule, the cost of implementing and sustaining a control activity should not exceed the benefits derived from that control activity. For example, purchasing an expensive locked cabinet to limit access to basic office supplies may not be considered cost effective. Alternatively, using a locked cabinet to secure highly negotiable assets such as daily cash receipts would be considered cost effective.

Fiscal Officer Development Series (2008) control activities are policies and procedures that help ensure that actions identified as necessary to manage risks are carried out properly and in a timely manner.This must be implemented thoughtfully, conscientiously and consistently unusual conditions identified must be investigated and appropriate corrective action taken.

According to RAI Internal Controls Working Guide (2013),control activities are a part of business (or management) functions within a registered entity and are typically characterized within its policies, procedures, and activities. Well-designed control activities increase the likelihood that compliance with reliability standards will be achieved. Some of these activities may include; approvals, reviews, analysis, self-assessment, or automated processes (for example control system alarms and work order management systems). Hence a well-designed control activity generally consists of mechanisms; that provide oversight and supervision of the process, identify instances of deficiencies, assess both the reason for the deficiency and the related risk, determine the level of correction (if one is required) and finally communicate the information to the proper level of management and when necessary the appropriate regulatory body.

Control activities are the policies and procedures implemented by an organization to ensure that management's directives are carried out. These activities are often grouped into the three categories of objectives to which they relate, namely, operations, financial reporting, and compliance (Shelton and Whittington, 2008). They further argue that these control activities include a range of activities which include; diverse a approvals, authorizations, verifications, reconciliations, reviews of operating performance, security of assets, segregation of duties and authority.

The Sarbanes-Oxley Act SOX (2002) states that control activities comprise of policies, procedures, and systems relating to the reliability of financial reporting. They include; authorizations and approvals, verifications, reconciliations, review of performance, security of assets, segregation of duties, and controls over information systems (Laura, 2002). The elements of control activities include; policies regarding reconciling bank statements with cheques issued, procedures governing the counting and valuation of inventory, the procurement and disposal. Systems and codes of conduct to guide employee behaviour (Kaplan, 2008; Thuy2007, SOX, 2002). CA can be preventive or detective. Corrective actions are a necessary complement to internal control activities in order to achieve the organisations objectives.

Rajkumar (2009), noted that control activities as the policies and procedure that ensure that bank personnel are following the management directives for achieving the bank’s objectives. Control activities are basic tools through which management ensures that its internal control objectives are realized by controlling the risks assessed as above. As per AAS6, Internal control system includes control procedures which are the policies and procedures in addition to the control environment which management has established to achieve the entity's specific objectives.

In summary control activities are most effective when they are reviewed by management and all other personnel as an integral part of, rather than an addition to the daily activities of the bank. When controls are reviewed as an addition to the day-to-day activities, they are often seen as less important and may not be performed in situations where individuals feel pressured to complete activities in a limited amount of time. In addition controls that are an integral part of the daily activities enable quick responses to changing conditions and avoid unnecessary costs. As part of the fostering the appropriate culture within the bank, senior management should ensure that adequate control activities are an integral part of the daily functions of all relevant personnel.

2.3.3 Risk assessment and financial performance

According to Washington and Pany (1995), the risk assessment needs management to carefully identify and analyze the factors that affect the risk that the organization's objectives will not be achieved, and then attempt to manage those risks. The following are the factors that might be indicative of increased financial reporting for an organization; changes in the organization's regulatory or operating environment, changes in personnel, implementation of anew or modified information system, rapid growth of the organization, changes in technology affecting production processes and corporate restructuring.

Millichamp, and Taylor (2008) risk assessment involves management's identification and analysis of risks relevant to the preparation of financial statements in the conformity with generally accepted accounting principles.

Risk assessment (RA) is the process of identifying and analysing relevant risks to the achievement of the entity's objectives and determining the appropriate response (DiNapoli, 2007, INTOSAI, 2004). It involves risk identification; risk evaluation (estimating the Impact of a risk; assessing the likelihood of the risk occurrence); assessment of the risk appetite of the organisation; and development of responses. A should be performed and should identify; controllable risks (risk son which Internal Control procedures can be established) and uncontrollable risks (risks that are caused by the external environment that the entity operated in).

According to the Cadbury Report (1992), the risk management should be systematic and also embedded in company procedures. And there should be a culture of risk awareness in the organisation. As governmental, economic, industry, regulatory and operating conditions are in constant change, risk assessment should be an ongoing iterative process. RA implies identifying and analysing altered conditions and opportunities and risks (risk assessment cycle) and modifying internal control to address changing risk. Bank needs to pay attention to total risks, which is sensitive to the choice of service delivery mechanism (Heald, 2003).

Cayman Island Monetary Authority (CIMA), (1998) state that an effective internal control system requires that the material risks that could adversely affect the achievement of the bank's goals are being recognised and continually assessed. This assessment should cover all risks facing the bank and the consolidated banking organisation (that is, credit risk, country and transfer risk, market risk, interest rate risk, liquidity risk, operational risk, legal risk and reputational risk). Internal controls may need to be revised to appropriately address any new or previously uncontrolled risks. Added that banks are in the business of risk-taking. Consequently it is imperative that, as part of an internal control system, these risks are being recognized and continually assessed. From an internal control perspective, a risk assessment should identify and evaluate the internal and external factors that could adversely affect the achievement of the banking organization's performance, information and compliance objectives.

According to Carmchael, Willingham, and Schaller (1996), effective risk assessment identifies and considers internal factors (such as the complexity of the organization's structure, the nature of the bank's activities, the quality of personnel, organizational changes and employee turnover) as well as external factors (such as fluctuating economic conditions, changes in the industry and technological advances) that could adversely affect the achievement of the bank's goals. This risk assessment should be conducted at the level of individual businesses and across the wide spectrum of activities and subsidiaries of the consolidated banking organization. This can be accomplished through various methods. Effective risk assessment addresses both measurable and non-measurable aspects of risks and weighs costs of controls against the benefits they provide.

Agreeing to above Millichamp (1996) asserted the risk assessment process includes evaluating the risks to determine which are controllable by the bank and which are not determine which are controllable by the bank and which are not. For those risks that are controllable, the bank must assess whether to accept those risks or the extent to which it wishes to mitigate the risks through control procedures. For those risks that cannot be controlled, the bank must decide whether to accept these risks or to withdraw from or reduce the level of business activity concerned.

Laura. (2002) discovered that in order for risk assessment to remain effective, senior management needs to continually evaluate the risks affecting the achievement of its goals and react to changing circumstances and conditions. Internal controls may need to be revised to appropriately address any new or previously uncontrolled risks. For example, as financial innovation occurs, a bank needs to evaluate new financial instruments and market transactions and consider the risks associated with these activities. Often these risks can be understood when considering how various scenarios (economic and otherwise) affect the cash flows and earnings of financial instruments and transactions. Thoughtful consideration of the full range of possible problems, from customer misunderstanding to operational failure, will point to important control considerations.

According to Rajkumar (2009),risk assessment is an effective internal control system requires that all material risks, internal and external, controllable and uncontrollable, that could affect the achievement of the bank's objectives, are recognized and continually assessed. Management must identify, measure and analyse the various kind of risks faced by the bank at all levels including credit risk, country and transfer risk, market risk, interest rate risk, liquidity risk, operational risk, legal risk, reputational risk etc. This risk assessment process helps the management to be aware of the risks faced by the bank and determine the internal controls required to manage these risks. Risks are not static phenomenon and keep on changing with time and circumstances. In order to ensure that the system of internal controls that address the risks faced by the banks is effective, the management needs to continuously evaluate its risk profile.

2.4.4 Financial performance

According to Stoner (2003), financial performance is the ability to operate efficiently, profitability, survives, grow and react to the environmental opportunities and threats. Financial accountability is a necessary condition for efficient public management and hence for the management of funds. In agreement with the above, Stoltenberg and Anderson,(1995), asserts that performance is measured by how efficient the enterprise is in use of resources to achieving its objectives. Financial performance is a subjective measure of how well a firm can use assets from its primary mode of business and generate revenues. This term is also used as a general measure of a firm's overall financial health over a given period of time and can be used to compare similar firms across the same industry or to compare industries or sectors in aggregation. There are many different ways to measure financial performance, but all measures should be taken in aggregation. Line items such as; revenue from operations, operating income or cash flow from operations can be used, as well as total unit sales. Furthermore, the analyst or investor may wish to look deeper into financial statements and seek out margin growth rates or any declining debt.

2.5.5 Conclusion of the chapter

From the literature review, several researchers seem to concur that there is a relationship between internal control systems and financial performance of an organization. These conclusions will however be confirmed or dispelled after empirical evidence has been obtained from the research.

CHAPTER THREE

RESEARCH METHODOLOGY

3.0 Introduction

In this chapter the researcher describes the procedures that were followed in conducting the study. These includes; the research design, the study population, sample size and sample selection, sampling techniques, data collection and analysis methods, ethical consideration and limitations to the study.

3.1 Research design

According to Wangusa (2007), research design involves all the issues involved in planning and executing a research project. The research design that was used to structure the research, to show how all of the major parts of the research ,project the samples or groups, measures, treatments or programs and methods of assignment work together to try to address the central research questions. The researcher used the case study design to carry out the research and the case study used was Centenary bank Entebbe road branch was chosen as a representative of all commercial banks. Where results of the study can be replicated and applied to other centers including the main branch. Case study is “an Intensive descriptive and holistic analysis of a single entity or a bounded case.

The researcher also used both quantitative and qualitative approaches to carry out the research. Wangusa (2007) found out that quantitative research approach consists of those studies in which the data concerned can be analyzed in terms of numbers. It is based more directly on its original plans and its results are more readily analyzed and interpreted. The researcher used quantitative approach in order to be able to quantify the data collected, in other words getting the figures about the data which ranged from the number of people that were interviewed, the sample size and the statistics.

According to Wangusa (2007), the qualitative approach of research in one that describes events, persons and so forth scientifically without the use of numerical data and she was of a view that qualitative research is more open and responsive to its subject. The qualitative approach helped the researcher to explain data in form of figures and describing the opinions of the respondents. The researcher used qualitative research approach in order to provide a systematic description of data collected and this happened after had been transformed in to figures. So, the qualitative approach was used to describe those figures.

3.2 Study population

Creswell (2009) reported that Population involves an entire group of individuals, events or objects having common observable characteristics. This part of the research shows the particular group of respondents that the researcher was interested in the field of the study. The total population employee was sixty.

The study focused on human resource and finance related departments of the banks targeting particularly general banking and loans department of the bank. All those are expected to be given questionnaire. The financial management process of the bank involves a cross section of individual and most importantly the departmental heads of the bank (especially during the budgeting process).

3.3 Area of the study

The study focused on Centenary Bank Entebbe branch and focusing particularly on internal controls (particularly control environment, risk assessment and control activities) operated at the branch.

3.4 Sample size and selection of sample size

Wangusa (2007) discovered that sample size is a small group people obtained from the accessible population. The researcher chose a sample size that was big enough to generate enough data that the researcher carefully analyzed to get information out of it.

The study basically targeted top and middle level management members because they are the custodians of internal control. Accordingly, all departmental heads were targeted as respondents, however, greater emphasis was laid on capturing members in human resource and finance related offices. The objective was to give questionnaires to at least 75% of the human resource department and all staff in finance and accounts related offices.

Purposive sampling the researcher consciously decides who to include in the sample. It was used simply because the study was targeting basically custodians of the internal control systems. It also ensured that only people with relevant information are sampled.

3.4.1 Sample size selection

The researcher selected a sample size of 40 (four) respondents out of the 60(sixty) workers. In determining this sample size, the researchers used solve n's formula as shown below;

n = N/1+N(e)2

n represented the sample size

‘N’ represented the total population and ‘e’ represented the allowed probability of committing an error in selecting a small representative of the sample, which is either 0.5/0.05 95%/99% respectively, but here an error margin of 0.05 was used.

After the application of the above formula, the researcher used the simple random sampling method which was applied on the selected respondents in the sample to collect data from them. Under this method, every worker in the sample stood a chance of being chosen at random to collect data from him or her. The researcher also used the purposive sampling method. This was purposely used to collect data from the chief accountant and some managers of the bank.

3.5 Sampling techniques

Sekaran and Bougie (2013) noted that sampling techniques are the types or methods of sampling that the researcher used. The researcher used probability sampling. Probability sampling is a sampling method used to obtain a reasonable number of the subjects, objects or cases that represent the target population. For instance out of the 60workers, the researcher used this method to come up with 40 members in a sample size.

Table 1: Number of Respondents

Category of respondents	**Number of respondents**
Employees	**20**
Management (banking officer, management committee members)	**14**
Total	**34**

Source; primary data

3.6 Methods of data collection

Sekaran and Bougie (2013) there are two types of data collection methods, that is to say primary and secondary sources of data. The researcher used both methods.

3.6.1 Primary sources of data

Under this type of data source, questionnaires and interviews were used/applied on the respondents.

3.6.2 Questionnaires

The researcher designed questions that were presented to the workers at the bank to answer them. The questions were both closed and open ended. The closed ended questions required the respondents to tick or mark their answer of choice whereas the open ended questions required the respondents to write down the answers or explain a little adding on the answers they had given to justify. The researcher gave the respondents some time to answer the questions and after, the questionnaires were collected for analysis. Questionnaires enabled the researcher get different opinions of different respondents from Centenary bank that acted as the basis of data analysis.

3.6.3 Secondary source of data

Sekaran and Bougie (2013) asserts that secondary sources refer to information gathered from sources that already exist. Under the secondary source, the researcher looked at what other researchers found out about the performance of Centenary bank. The researcher also used academic journals, articles, text books, pamphlets and the internet as other secondary sources of data. By looking at the secondary sources, the researcher was in position to compare these sources with what the other researchers had found out which assisted the researcher in time of analyzing the collected data.

Data was basically collected from loans and general human resource department.

3.7 Data management and analysis

According to Creswell (2009), the data management involves the way data is handled and treated after collection and data analysis involves checking data to see the level of correctness. Data was kept intact after collection before analysis could start. The researcher used SPSS during the course of data analysis. This helped in generating the tables, graphs and pie-charts that consisted of quantitative data. Then the qualitative approach was used to describe data embedded in figures.

3.8 Data validity and reliability

Wangusa (2007) noted that data validity is the accuracy and meaningfulness of inferences, which are based on the research results. It is the degree to which results obtained from the analysis of data actually represent the phenomenon under study.

To ensure the validity of data, the researcher used the coefficient of validity index (CVI) below which is used to test the extent to which data is accurate.

CVI = Item rated/Total number of items multiplied by 100 (Abel and Olive 2003).

The reliability was ensured by testing the instruments for the reliability of values (Alpha values) as recommended. Alpha values for each variable under study should not be less than 0.6 for the statements in the instruments to be deemed reliable. Consequently, all the statements under each variable were subjected to this test and were proven to be above 0.6.

Abel and Olive (2003) data reliability is a measure of the degree to which a research instrument yields consistent results or data after repeated trials. To ensure the reliability of data, the researcher used the test-retest method. This involved administering the same instrument to the same group of instruments.

Under quantitative data, the researcher used correlation which enabled to show the relationship between the dimensions of the independent variable and dependent variable. Researcher also used frequency tables to find out the trend, nature, sample mean and standard deviation of collected data.

3.9 Ethical consideration

- Under ethical consideration, the researcher first sought for permission from the study area. This enabled the respondents to prepare in advance for the researcher to provide the data that the researcher needed. The researcher also offered to give a copy of the research report to the concerned people of the case study.
- The researcher tried very much to avoid causing physical and emotional harm to the respondents. This was adopted in all the data collection methods used, that is questionnaires and interviews. This created a free environment for the respondents to give the researcher all the information required.
- The researcher tried to be objective enough both in the questionnaires and the interviews. Personal biases and opinions were done away with here and the respondents gave the data to the researcher as required.

- ❖ In reporting the results of the data collected, the researcher relied so much on accuracy of the data. The data collected was presented the way it was given by the respondents from the field. This made the results more objective and less subjective.

3.10 Study limitations

- ❖ Research was an expensive venture yet the researcher was constrained financially.
- ❖ Time constraint was yet another challenge for the researcher to accomplish this study.

3.11Conclusion

In conclusion, this chapter focused more on the area of the study, data collection and the techniques used in data collection. This was followed by data analysis as well as testing the validity and reliability of the data collected. This chapter was very necessary in determining the quality of data the researcher collected from the field of the study.

CHAPTER FOUR

DISCUSSION AND INTERPRETATION OF FINDINGS

4.0Introduction

This chapter presents empirical findings in reference to research objectives in chapter one. They are presented and analyzed using frequency tables, percentages (graphs) and finally SPSS was used to establish a relationship between the variables. Interpretation and analysis of the data collected was done basing on the objectives which include: to investigate the effect of control environment on the financial performance of centenary bank Entebbe branch, to find out the effect of risk assessment on the financial performance of centenary bank Entebbe branch, and to find out the effect of control activities on the performance of centenary bank.

4.1 Sample Characteristics

The sample characteristics of the respondents include: age, gender, level of education and duration in employment of the respondents. Statistical tools such as, frequencies and percentages are presented in Tables 1 – 16.

4.2 Background information of the respondents

4.2.1 Gender of respondents

Table 2: Gender of respondents

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Male	22	64.7	64.7	64.7
	Female	12	35.3	35.3	100.0
	Total	34	100.0	100.0	

Source: Primary Data

The tables 1 above shows that male respondents were 22 (64.7%) where as female were12(35.3%), representing more male respondents than female at the bank.

4.2.2 Educational level

Table 3: below shows the percentage of employees who filled and returned the questionnaires include; bachelor holders, 67.6% and 32.4% master's holders.

education level of respondents					
		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Bachelor	23	67.6	67.6	67.6
	Masters	11	32.4	32.4	100.0
	Total	34	100.0	100.0	

Source: primary data

Findings in table 2 above show that 67.6% of the respondents hold bachelors, 32.4% masters. Majority were degree holders indicating that Centenary bank Entebbe Road branch performance is mainly influenced by skilled andlearned staff, thus they can easily evaluate the effectiveness of internal controls used in the organization.

4.2.3 Position of respondents

Table 4: Position of respondents

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	management committee	5	14.7	14.7	14.7
	finance and accounts officer	5	14.7	14.7	29.4
	banking officer	7	20.6	20.6	50.0
	Employee	17	50.0	50.0	100.0
	Total	34	100.0	100.0	

Source: primary data

According to table 3 above; majority of the respondents in the study were employees of Centenary bank totaling 50.0%, with the least being the management committee and finance officer who each had a total of 14.7%. This implies that employees were involved in the daily activities of the organization at all levels such as strategic, programmatic and operational levels.

4.2.3 Age

Table 5: Age of respondents

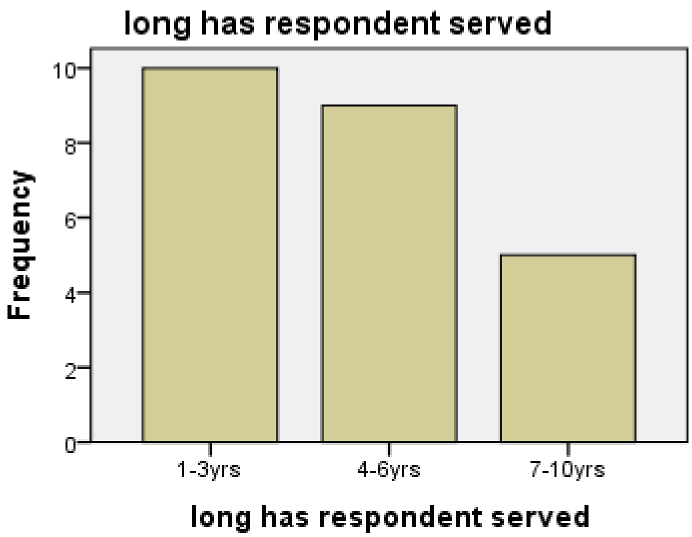
		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	18-25yrs	10	29.4	29.4	29.4
	26-35yrs	16	47.1	47.1	76.5
	36-45yrs	8	23.5	23.5	100.0
	Total	34	100.0	100.0	

Source: primary data

In table 4; majority of the respondents between 26-35 years represented 47.1%, 36-45years were 23.5% and 18-25 years being 29.4% years. The results show that most respondents were capable of making informed decisions which enhance internal controls.

4.2.4 Period respondents have served in Centenary bank

Figure 2: Long has respondent served



Source: primary data

Findings in figure2above show that 10% of the respondents served for 1-3 years, 8% served for 4-6 years, 4% served for 7-10 years. Majority served for 1-6 years indicating that Centenary bank Entebbe road branch is managed by experienced staff.

4.3 To examine internal control systems in Centenary bank Entebbe road branch

Descriptive statistics were used to examine internal control systems in Centenary bank. The results were analyzed and interpreted basing on the anchor of the instrument scale which was ordered such that a mean close to 5-represents strong agreement, 4-agreement, and 3-Undecided, 2–disagreement and 1-Strong disagreement. The researcher based on internal control objectives which include control environment, risk assessment and control activities. These include;4.4Objective 1: The effect of control environment on financial performance

4.4.1 Organizational structure

Table 6: Organizational structure

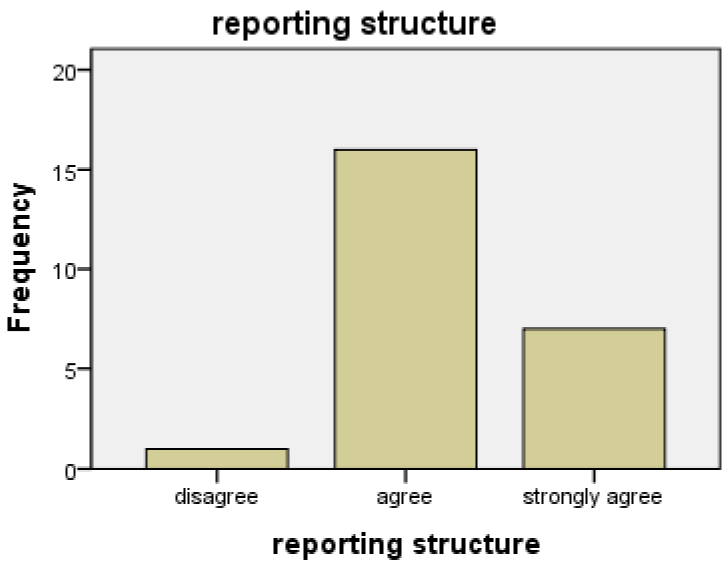
		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Disagree	1	4.2	4.2	4.2
	not sure	1	4.2	4.2	8.3
	Agree	16	66.7	66.7	75.0
	strongly agree	6	25.0	25.0	100.0
	Total	24	100.0	100.0	

Source: primary data

Table 5 above represents how the researcher asked a question to establish whether the bank had a clear reporting structure. It is clearly stipulated that most of the respondents agreed with the reporting structure in the organization and represented with 66.7%, those who strongly agreed were 25.0% strongly while those who disagreed were 4.2%. This indicates that communication within the organization was based on the control environment as the foundation of an effective determinant of what, where and how improvements can be implemented in the institution (Minnesota Management and Budget, 2013)

4.4.2 Reporting structure

Figure 3: Reprting structure



In figure 3, the findings indicate that reporting structure in the bank is evidence based and the financial reports are generated basing on accurate, consistent data. This prevents misstatement of the annual or interim financial statement (Doyle and Vay, 2007)

4.4.3 Knowledge and skills needed to perform the job.

Table 7: Knowledge and skills needed

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Disagree	2	8.3	8.3	8.3
	not sure	2	8.3	8.3	16.7
	Agree	17	70.8	70.8	87.5
	strongly agree	3	12.5	12.5	100.0
	Total	24	100.0	100.0	

Source: primary data

Table 6: above indicates that the knowledge and skills were analyzed by the entity since 61.8% of the respondents agreed while 8.8% disagreed. This promotes establishment of an atmosphere in which people conduct their activities and responsibilities effectively (Beneish et al, 2008

4.4.4 Segregation of roles

Table 8: Segregation of roles

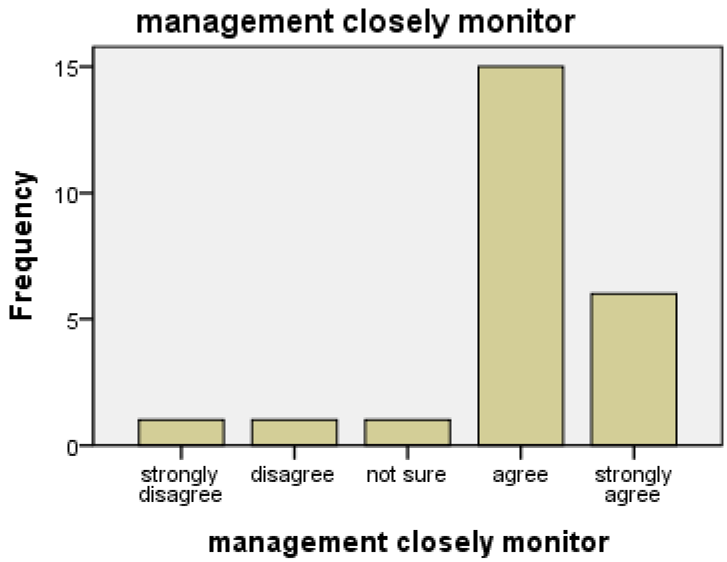
		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Disagree	3	12.5	12.5	12.5
	not sure	4	16.7	16.7	29.2
	Agree	13	54.2	54.2	83.3
	strongly agree	4	16.7	16.7	100.0
	Total	24	100.0	100.0	

Source: primary data

From the results above, the scale showed that 54.2% agreed that in the organization there was segregation of duties where as 16.7% disagreed. This enhances policies, procedures and systems relating to the reliability of reporting systems which includes authorization, approvals, verifications, reconciliations, reviews of performance, security of assets, segregation of duties and controls over information systems (Laura, 2002).

4.4.5 Management closely monitors internal controls

Figure 4: Management closely monitor



In the figure 4 above, it showed that management closely monitors the internal controls in the organization since respondents agreed with the highest frequency of 15 followed by strongly agreed.

According to Hayes, Dassen, Schilder and Wallage (2005) if management believes control is important; others in the company will observe the control policies and procedures. If the employees in the organization feel control is not important to top management, it will not be important to them. However control environment in which there is no motivation, misstatement of financial statements may lead to problems.

4.5 Objective 2: the effect of risk assessment on financial performance of Centenary bank Entebbe Road Branch

This objective indicates whether management assesses the risks in the bank.

4.5.1 Design of system

Table 9: Design of system

The first question put to the employees is whether management designs a system to offer an appropriate response to skills? The answers to this question were displayed in the table below:

Design of system

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Disagree	1	4.2	4.2	4.2
	not sure	6	25.0	25.0	29.2
	Agree	12	50.0	50.0	79.2
	strongly agree	5	20.8	20.8	100.0
	Total	24	100.0	100.0	

Source: primary data

The results shown in table 8 above indicate that management designs the system since 50.0% agree while 25.0% were not sure and 20.5% strongly agreed. This shows that management actively engages in the activities of the organization hence this helps management to identify risks a head of time. In contrast with Whittington and Pany (2001), they state that management designs and implements policies and procedures to address risks that the bank identifies through risk assessment process.

4.5.2 Review risk register

Table 10: Review risk register

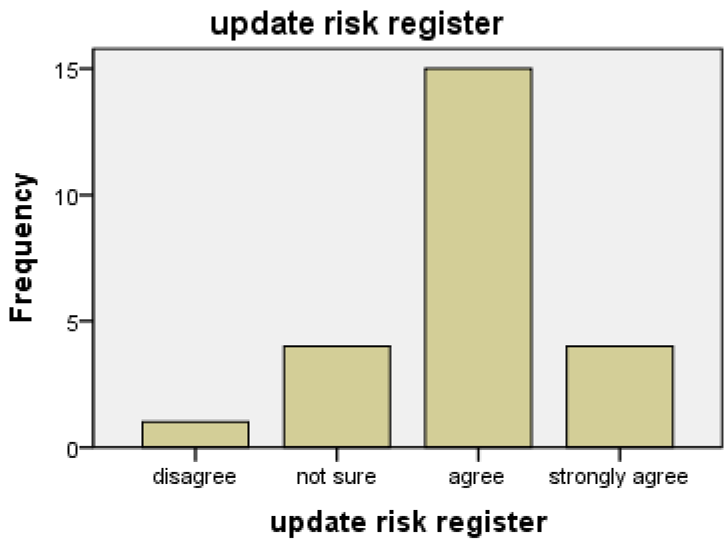
		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Disagree	1	4.2	4.2	4.2
	not sure	4	16.7	16.7	20.8
	Agree	17	70.8	70.8	91.7
	strongly agree	2	8.3	8.3	100.0
	Total	24	100.0	100.0	

Source:primary data

Table 9 indicates that managemnet reviews the risk register since most of the employees agree with 70.8% while 16.7% were not sure. Reviewing of therisk register helps managemnt to know which risks have they faced and incase the same risk comes up they know how to handle it.Risks are not static phenominon but keep changing with circumstances and time. In order to ensure that the system of internal control system addresses the risks faced by the bank is effective, management needs to continuosly evaluate its risk profile (Rajkumar, 2009)

4.5.3 Update risk register

Figure 5: Update risk register



The figure above shows that management updates its risk register since agree appears to be the highest frequency of 15

4.5.4 Evaluate and respond to risk

Table 11: Evaluate and respond to risk

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	strongly disagree	1	4.2	4.2	4.2
	Disagree	2	8.3	8.3	12.5
	not sure	3	12.5	12.5	25.0
	Agree	14	58.3	58.3	83.3
	strongly agree	4	16.7	16.7	100.0
	Total	24	100.0	100.0	

Source: primary data

From table 10 shows that management evaluates the risk register since most of the employees agree with 58.3% hence this helps management to know the different risks they face. From an internal control perspective, a risk assessment should identify, evaluate internal and external factors that could adversely affect the achievement of the banking organization's performance, information and compliance objectives (Cayman Island Monetary Authority, 2008)

4.5.6 Risk register

Table 12: risk register

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Disagree	2	8.3	8.3	8.3
	not sure	2	8.3	8.3	16.7
	Agree	14	58.3	58.3	75.0
	strongly agree	6	25.0	25.0	100.0
	Total	24	100.0	100.0	

Source primary data

Results in table 11 above show that 25.0% of the respondents strongly agreed that there was a risk register in the bank, 58.3% agreed, 8.3% were not sure, 8.3% disagreed. Majority of the respondents agreed that there was a risk register in the organization**.** According to Hayes, Dassen ,Schilder and Wallage (2005) management assesses risks as part of designing and operating internal control system to minimize errors and irregularities. However certain conditions may increase risk and deserve special consideration. These conditions include: changed operating environment; new or revamped information systems; rapid growth; new technology; new lines, products and activities; corporate restructuring; and foreign operations.

4.6 Objective 3: the effect of control activities on financial performance of Centenary bank Entebbe Road Branch

4.6.1 Policies and procedures

Table 13: Policies and procedures

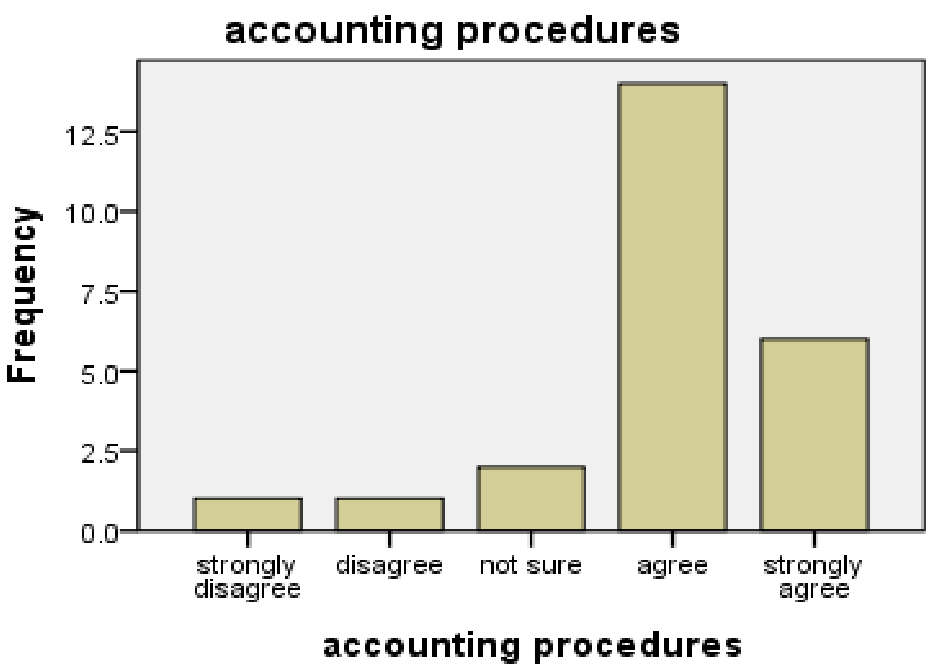
		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Disagree	2	8.3	8.3	8.3
	not sure	1	4.2	4.2	12.5
	Agree	17	70.8	70.8	83.3
	strongly agree	4	16.7	16.7	100.0
	Total	24	100.0	100.0	

Source: primary data

Results in table 12 above depict that 70.8%% of the respondents agreed the bank has policies and procedures, 16.7% strongly agreed, 4.2%% were not sure, 8.3%% disagreed and 21% strongly disagreed. This implies that activities carried out in the bank go through procedures. Similarly, Rick et al, 2005 terms control activities as policies and procedures that help ensure management directives are carried out.

4.6.2 Accounting procedures

Figure 6: Accounting procedures



From figure 6 above indicates that accounting procedures of bank are clearly segregated since frequency shows that agree had the highest with 12.5. Management's retention of authority for approving significant purchases can provide appropriate segregation of duties to achieve a strong control structure (Carmichael, Willingham and Schaller, 2009)

4.6.2 Bank asset

Table 14: Bank asset

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	strongly disagree	1	4.2	4.2	4.2
	Disagree	2	8.3	8.3	12.5
	not sure	1	4.2	4.2	16.7
	Agree	17	70.8	70.8	87.5
	strongly agree	3	12.5	12.5	100.0
	Total	24	100.0	100.0	

Source: primary data

Results in table 13 above show that 12.5% of the respondents strongly agreed that bank asset movement is always recorded, 70.8% agreed, 4.2% were not sure, 8.3% disagreed and 4.2% strongly disagreed. Majority of the respondents agreed showing that asset movement is always recorded.

4.6.3 Prepares reviews T

Table 15: Prepares reviews

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Disagree	2	8.3	8.3	8.3
	not sure	2	8.3	8.3	16.7
	Strongly agree	13	54.2	54.2	70.8
	Agree	7	29.2	29.2	
	Total	24	100.0	100.0	100.0

Source primary data

Results in table 14 above reveal that 54.2% of the respondents strongly agreed that someone other than the preparer reviews and approves bank reconciliations, 29.2% agreed, 8.3% were not sure and 8.3% disagreed. Majority of the respondents agreed this implies that management prepares reviews and approves bank reconciliation. Control activities ensure that the necessary activities are taken to address risks to the achievement of the entity's objectives for operations and financial reporting (Whittington and Pany 2001).

4.6.4 Employees work check

Table 16: Employee's work check

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	strongly disagree	1	4.2	4.2	4.2
	Disagree	4	16.7	16.7	20.8
	not sure	3	12.5	12.5	33.3
	Agree	12	50.0	50.0	83.3
	Strongly agree	4	16.7	16.7	100.0
	Total	24	100.0	100.0	

Source: primary data

Results from table 14 above illustrate that employees check on the fellow employees work this is shown 50.0% agree, 16.7% strongly agree, 12.5% not sure, 16.7% disagree and 4.2% strongly disagree. This helps management know which employee is performing well or poor.

4.6.5 Corrective action

Table 17: corrective action

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Disagree	1	4.2	4.2	4.2
	not sure	3	12.5	12.5	16.7
	Agree	13	54.2	54.2	70.8
	strongly agree	6	25.0	25.0	95.8
	Total	24	100.0	100.0	100.0

Source: primary data

Results in table 15 above show that 10% of the respondents strongly agreed that cost of production has been reducing dramatically for the past two years, 26% agreed, 8% were not sure, 33% disagreed and 23% strongly disagreed. Majority of the respondents disagreed; this implies that any employee who defies the rules and regulation of the bank, an action is taken against him. Hayes ,Dassen, Schilder and Wallage (2005) asserts that control activities help ensure that necessary actions are taken to address risks to the achievement of the entity's objectives for operations and financial reporting. On the other hand if an individual has custody of assets and also accounts for them, there is a high risk of that person dispensing the asset for personal gain and adjusting the records to cover theft.

CHAPTER FIVE

RECOMMENDATIONS

5.0 Introduction

This study was designed and carried out to establish the effectiveness of Internal

Control Systems (ICS) in achieving financial performance in Centenary bank Entebbe Road Branch. This chapter gives the discussions, conclusions and recommendation of the research findings presented and interpreted in chapter four. Also suggested areas for further research are also presented. All of which are presented in accordance to the research objectives.

5.1Conclusion

From the study findings, it is concluded that the internal controls used in Centenary bank Entebbe road branch were effective and satisfactory, the level of financial performance was found to be significant and a vital positive relationship between internal controls and financial performance was established to exist. This had a positive and negative impact on employees this is shown below;

5.1.1 The effect of control environment on financial performance of Centenary Bank Entebbe Branch

From the findings above showed that control environment had a positive impact on the bank that is to say since most of the respondents were in agreement with; clear organizational structure, reporting structure is clearly stipulated, entity analyzes the knowledge and skills needed to perform job adequately, segregation of lead to minimizing of costs and management closely monitors the implementation of internal control. The communication of the company integrity and ethical values to employees and reinforcement in practice affects the way in which employees view their work. However poor control environment can lead to; employees disrespecting of top management since they may not know who is in higher position. Therefore Centenary Bank Entebbe Road Branch top management should that there are proper.

5.1.2 The effect of risk assessment on financial performance CRDEB

From the results it is found out that there is a statistically significant positive relationship between risk assessment and internal control. This is because most of the respondents agreed with what was put across by the researcher. They include; the bank management designs a system to offer appropriate response risks, management reviews the risk register, management update its risk register, management's role to identify and the bank has risk register. It entails the identification and prioritization of objectives, the identification of risks and assessment of their likelihood and impact. Consequently Jones (2007) looks at risk assessment as the identification, evaluation and management of risks. He further notes that risks can relate, to financial statement fraud or to the misappropriation of assets. Therefore management must identify measure and analyze the various risks faced by the bank. In case management does not plan for the risks, it might end up incurring costs when the risk occurs.

5.1.3 The effect of control activities on financial performance

The findings of the study revealed that control activities are duly approved in advance by appropriately authorized persons. Cheque authorization, processing, and signing and the accounting functions are clearly segregated under the internal control system. (Shelton & Whittington, 2008) argue that control activities include a range of activities as diverse as approvals, authorizations, verifications, reconciliations, reviews of operating performance, security of assets and segregation of duties, segregation of duties and authority. Management should ensure control activities are an integral part of the daily functions of all relevant personnel. However if control activities are not regularly reviewed employees may feel lay to perform their duties, management might not recognize the level at which commodities leave the organization.

5.1.4 General conclusion

Generally, this research examined the effectiveness of Internal Control Systems in achieving financial performance in bank. The findings revealed that Internal Control Systems have a significant positive effect in achieving financial performance. This means that when Internal Control Systems improve, there will be attainment of financial performance in banks.

The study further reveals that there a significant positive relationship between the control environment, control activities, risk assessment, and financial performance in banks. Control environment, risk assessment and control environment were revealed to have more significant predicator financial performance. This implies that the more sound the internal control systems and the more the Internal Control Systems are adhered too, the higher the chances that bank will achieve good financial performance.

5.3 Recommendations

5.3.1 To examine the effectiveness of internal controls used Centenary Bank Entebbe Road Branch

The management of Centenary Bank Entebbe Road Branch should design effective internal control systems by ensuring that adequate asset listings is done by management, staff should be motivated, capital assets purchased are approved by appropriate level of management and asset numbering is done to show location and protection of the assets.

5.3.2 To establish the level of financial performance in Centenary Bank Entebbe Road Branch

The management of Centenary Bank Entebbe Road Branch should ensure that it strengthens strategies aimed at improving financial performance in all categories of staff and this should be used to ensure that the financial performance in the bank improves.

5.4 Areas for further research

The study did not exhaust all the independent variables that influence financial performance thus the need for other researchers to conduct an exhaustive study on variables under listed.

Monitoring

Information and communication

In addition, further study should concentrate on the examination of other factors that contribute to attainment financial performance not included in this study other than Internal Controls.

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APPENDICES

Appendix I: Questionnaires

The effect of internal control on financial performance of banks

Case study: Centenary Bank Entebbe road branch

Dear Respondent, my name is Namwebe Caroline. I am currently carrying out a study for the purpose of writing a dissertation as a requirement for the award of Bachelor of Business Administration and Management of Uganda Martyrs University. The topic of study is the Effect of internal control on financial performance of commercial banks. You have been selected to participate in this study due to the importance of your information in the study. The information you provide will only be used for the purpose of this study and will be treated with utmost confidentiality.

Please feel free and answer all the questions.

Section A

RESPONDENT'S BACKGROUND

1**. Gender (Please tick appropriately**)

Male ☐

Female ☐

2. What is your highest level of education?

Certificate/Diploma ☐

Bachelor ☐

Masters ☐

Other (Specify)…………………………………………………………………...

3. What position do you currently hold in the Organization/Institution that you work for?

Management Committee member ☐

Finance and Accounts staff ☐

Banking officer ☐

Employee ☐

4. In what age bracket do you fall? (Circle where appropriate)

18-25yrs ☐

26-35yrs ☐

36-45yrs ☐

46-55yrs ☐

56 and above ☐

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

1-3 yrs ☐

4-6 yrs ☐

7-10 yrs ☐

10yrs and above ☐

Section B:

To examine the functionality of Internal Control systems of Centenary banks in Uganda

Please rank the following statement on likert scale ranging from strongly disagree to strongly agree

Where;

1= strongly disagree

2= disagree

3= not sure

4= agree

5= strongly agree

Control environment	5	4	3	2	1
The bank has a clear organizational structure.					
The reporting structure is clearly stipulated.					
The entities analyze the knowledge and skills needed to perform jobs adequately?					
Segregation / separation of roles can lead minimizing of costs.					
Management closely monitors implementation of Internal control systems in our bank.					
Ethical values are upheld in all management decisions.					

Risk assessment	5	4	3	2	1
The bank management design a system to offer appropriate response to risks.					
Management review risk register.					
Management updateits risk register.					
It is management's role to identify, evaluate and respond to risk in bank.					
The bank has a risk register.					
Management is concerned with the development of responses to risks.					

Control activities	5	4	3	2	1
Bank policies and procedures can lead to producing financial reports.					
Accounting procedures of bank are clearly segregated.					
Bank Asset movement is always recorded.					
Someone other than the preparer reviews and approves bank reconciliations.					
Every employee's work check on the others.					

Corrective action is taken to address weaknesses.					

Section C:

What are some of the other factors that affect financial performance in your organization?

………
………

How else does your organization promote its financial performance to improve quality and quantity?

………
………

Appendix II: Budget

No.	Activity	Quantity	Price per unit	Amount
1.	Typing and Printing			200,000
2.	Binding	3Copies	3,000	80,000
3.	Stationery			100,000
4.	Transport			100,000
5.	Communication			100,000
6.	Photocopying questionnaires		40	40,000
7.	Miscellaneous			100,000
	Total			**720,000**

Appendix III: Work Plan

Time	Activity
Sept.- Dec-2013	Dissertation writing
May-Sept.2013, and Febraury , 2014	Data collection
March 2014	Data analysis
April , 2014	Presentation