EFFECT OF INTERNAL CONTROLS ON THE FINANCIAL PERFORMANCE OF MANUFACTURING FIRMS IN KENYA

BY;

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DECLARATION

I declare that this Research Project is my original work and has not been submitted for examination in any other university or institution of higher learning.   .

Signed ……………………………..   Date………………………

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This Research Project has been submitted for examination with my approval as the University Supervisor

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DEDICATION

I dedicate this research project to my family members most specially my wife Rita Mishi and my children, for their love, support, patience, encouragement and understanding. They gave me the will and determination to complete my masters.

ABSTRACT

Effectiveness of internal control on performance should be considered most important in every firm because the task of internal controls is to prevent and detect fraud in the firm. Internal controls are put in place to ensure safe custody of all assets; to avoid misuse or misappropriation of the firm's assets and to detect and safeguard against probable frauds. Every firm whether manufacturing or non-manufacturing, should have management of the highest qualifications, caliber and dedication since its inception. Thus the purpose of this study is establishing the effect of internal controls on the financial performance of manufacturing firms in Kenya. The findings of this study would be crucial in informing the policy makers in Kenya on the effect of internal control on financial performance of manufacturing firms. A cross sectional survey was used which targeted 65 manufacturing firms in Kenya. The primary data was collected by use of a structured questionnaire. A Statistical Package for Social Sciences (SPSS) version 21.0 was used to analyze the data. From the findings of the study, it was concluded that manufacturing firms which had invested on effective internal control systems had more improved financial performance as compared to those manufacturing firms that had a weak internal control system. Hence it was recommended that Kenya Association of Manufacturers should monitor and supervise manufacturing firms to ensure that the accountants comply with accounting regulations and requirement as provided by the Institute of Certified Public Accountants to ensure proper implementation and compliance with accounting standards and principles, organizations should develop a mechanism to incorporate relevant feedback from the various stakeholders into their internal control system; and also that the governing body ensure that the internal control system is periodically monitored and evaluated

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ABBREVIATIONS AND ACRONYMS

CEO	Chief Executive Officer
COMESA	Common Market for Eastern and Southern Africa
EAC	East African Community
GAAPs	Generally Accepted Accounting Principles
GDP	Gross Domestic Product
IAS	International Accounting Standards
ICS	Internal Control
MVA	Market Value Added
NSSF	National Social Security Fund
ROA	Return on Assets
ROS	Return on Sales
SPSS	Statistical Package for Social Sciences
VFM	Value for Money

CHAPTER ONE: INTRODUCTION

1.1 Background of the Study

Internal control as "Comprising the plan of an organization and all the co-ordinate methods and measures adopted within a business to safeguard its assets, check the accuracy and reliability of its accounting data, prorate operational efficiency and adherence to prescribed managerial policies." The definition of internal control is divided into financial internal control and non-financial (administrative) internal control. Financial internal control pertains to financial activities and may be exemplified by controls over company's cash receipts and payments financing operations and company's management of receipts and payments. Non-financial internal control on the other hand deals with activities that are indirectly financial in nature i.e. controls over company's personnel section and its operations, fixed assets controls and even controls over laid down procedures (Reid and Ashelby, 2002).

A sound internal control helps an organization to prevent frauds, errors and minimize wastage. Custody of assets is strengthened; it provides assurance to the management on the dependability of accounting data eliminates unnecessary suspicion and helps in maintenance of adequate and reliable accounting records. This study therefore attempts to establish the effectiveness of internal control in manufacturing firms in Kenya (Amudo and Inanga, 2009).

Despite the fact that internal control is expensive to install and maintain, it gradually evolved over the years with the greatest development occurring at the beginning of 1940's. Not only have the complexities of the business techniques contributed to this development but also the increased size of business units which have encouraged the adoption of methods which while increasing efficiency of business, acts as a safeguard against errors and frauds.

Mawanda (2008), states that "there is a general perception that institution and enforcement of proper internal control s will always lead to improved financial performance". It is also a general belief that properly instituted use of internal control improves the reporting process and also gives rise to reliable reports which enhances the accountability function of management of an entity. Preparing reliable financial information is a key responsibility of the management of every public company. The ability to effectively manage the firm's business requires access to timely and accurate information.

Moreover, investors must be able to place confidence in a firm's financial reports if the firm wants to raise capital in the public securities markets. Management's ability to fulfill its financial reporting responsibilities depends in part on the design and effectiveness of the processes and safeguards it has put in place over accounting and financial reporting. Without such controls, it would be extremely difficult for most business organizations especially those with numerous locations, operations, and processes to prepare timely and reliable financial reports for management, investors, lenders, and other users. While no practical control can absolutely assure that financial reports will never contain material errors or misstatements, an effective of internal control over financial reporting can substantially reduce the risk of such misstatements and inaccuracies in a company's financial statements (Kaplan, 2008; Cunningham, 2004; INTOSAI, 2004).

1.1.1 Internal Controls

Internal control is a process, effected by an entity's board of directors, management and other personnel, designed to provide reasonable assurance regarding the achievement of a firm's objectives in the effectiveness and efficiency of operations, reliability of financial and management reporting, compliance with applicable laws and regulations and protect the organization's reputation (Kaplan,2008).

Effective internal control operates when some specific procedures are adopted by the management. International Accounting Standards (IAS) categorizes internal control types as a plan of organization, segregation of duties, control of documents, safeguarding of assets, competence of staff, arithmetic and accounting controls, recording and record keeping , supervision, authorization and approvals, vocation and rotation of duties, cost feasibility , routine and automatic checks.

Saleemi (2000) refers to plan of organization as an organization chart showing the organization structure of a company. The purpose of this chart is to show how the company has been divided into departments and departments into sections and most important to show what responsibilities and duties are assigned to each officer. Authority and responsibilities are clearly defined. Employees perform their duties according to the organization plan. This plan allocates and defines responsibilities and identifies lines of reporting for all aspects of business operations. The plan of organization is needed for effective internal control.

Internal controls consist of five components namely: Control environment- This is the foundation for all the other components of internal control. It comprises of factors like integrity and ethical values of personnel tasked with creating, administering and monitoring the controls, commitment and competence of persons performing assigned duties, board of directors or audit committees, management philosophy and operating style and organizational structure, Risk assessment process, this refers to the careful assessment of factors that affect the possibility of objectives of the organization not being achieved. It refers to the identification and analysis of relevant risks associated with achieving the objectives of the organization.

1.1.2 Financial Performance

Positive financial performance in a manufacturing firm can be achieved by eradicating waste in benefits services processes and systems. The "critical success factor" for a manufacturing firm is the degree to which it fulfills its set objectives and mission in terms of being efficient, effective and economical. The information obtained from a sound internal control as reflected from financial statements will provide a report on a firm's financial performance and position that is useful to a wide range of users for assessing the stewardship and making economic decisions (Davies, 2007).

Internal Control is very instrumental in achieving the firm's set mission and objectives; hence Value for Money. The main approach to VFM is the firm's control over the use of resources in order to achieve its set objectives. Heads of departments should establish sound arrangements for planning, appraising, authorizing and controlling operations in order to achieve positive Financial Performance. Financial Performance and Value for Money are used to assess whether or not a firm has obtained the maximum benefit from the goods and services it acquires and / or provides, within the resources available to it (LGIAM, 2007).

Value for Money is not paying more for a good or service than its quality or availability justifies, as well public spending implies a concern with economy (cost minimization), efficiency (output maximization) and effectiveness (full attainment of the intended results). The most effective way to improve Financial Performance is by reducing the level of irregularity and fraud through improvements in the firm's use of internal financial control. Shareholders need to be assured that their resources are being used efficiently and effectively in providing the right service at the least cost. Financial Performance analysis needs to pay attention to total risks and is related to concepts of efficiency and effectiveness (Deakin, 2003).

1.1.3 Internal Controls and Financial Performance

Internal control including internal audits are intended primarily to enhance the reliability of financial performance, either directly or indirectly by increasing accountability among information providers in an organization (Jensen, 2003). Internal control therefore has a much broader purpose such that the organization level of control problems associated with lower revenues, which explore links between disclosure of material weakness and fraud, earnings management or restatements internal controls provide an independent appraisal of the quality of managerial performance in carrying out assigned responsibilities for better revenue generation (Beeler et al, 2006).

Fadzil et al (2005) said that an effective internal control unequivocally correlates with organizational success in meeting its revenue target level. Effective internal control for revenue generation involves; regular a review of the reliability and integrity of financial and operating information, a review of the controls employed to safeguard assets, an assessment of employees' compliance with management policies, procedures and applicable laws and regulations, an evaluation of the efficiency and effectiveness with which management achieves its organizational objectives (Ittner, 2003).

Most organizations no longer set up internal control as a regulatory requirement but also because it helps in ensuring that all management activities are appropriately carried out (Kenyon and Tilton, 2006). Further, organizations are making it a point of duty to train, educate, and sensitize their employees on how to use this internal control system since its effectiveness depends on the competency and dependability of the people using it. All these control actions ensure that any risks that may affect the company's ability to achieve its goals are appropriately avoided and should occur at all levels and in all functions of the organization (Doyle et al, 2005).

There are three major classifications of internal controls; preventive, detective, and corrective. Preventive controls predict potential problems before they occur, make adjustments, and prevent an error, omission or malicious act from occurring. The detective controls are used to detect and report the occurrence of an omission, an error or a malicious act. Finally, the corrective controls help in ensuring that the impact of a threat is minimized, identify the cause of a problem as well as the correct errors arising from the problem. Corrective controls correct problems discovered by detective controls and modify the processing to minimize future occurrence of the problem (Singleton, 2006).

1.1.4 Manufacturing Firms in Kenya

The manufacturing sector in Kenya in which the study is based on is one of the major contributors to the economic development of the country. According to the National development Plan 2002-2008 it contributes to employment of a large population of the country's workforce and also contributes about 13% of Gross Domestic Product (GDP). According to the Kenya Economic Survey 2010, the manufacturing sector grew by 4.4% in 2010 when compared to prior year. This was mainly driven by; reliable power supplies arising from favorable weather conditions that bolstered electric power generation, favorable tax policies, including the removal of duty on capital equipment and some raw materials, increased credit to the manufacturing sector increased availability of raw agricultural materials, Growth in the regional market (EAC, COMESA).

In Kenya, the manufacturing sector is divided into 14 sub-sectors which are: Food and Beverages, Tobacco, Building, Construction and Mining, Chemical and Allied, Energy, Electrical and Electronics, Leather Products and Footwear, Metal and Allied, Paper and Paperboard, Motor Vehicle and Accessories, Pharmaceutical and Medical Equipment, Plastics and Rubber, Textiles and Apparels, Timber, woods Product and Furniture (Manufacturing in Kenya: a Survey of Kenya's Manufacturing Sector 2006- KAM).

Although Kenya manufacturing sector is still small when compared to those of industrialized countries it is still the largest in East Africa (Aosa, 1992). Ownership of manufacturing firms is a major dimension because it has a strong bearing on the organization's performance and control. In terms of sector concentration, large companies in Kenya account for a large proportion of manufacturing sector's output and employment. From the above arguments, provides reason why the manufacturing sector is important to be studied. Specifically, the study will look into the effect of internal control on financial performance.

1.2 Statement of the Problem

Effectiveness of internal control on performance should be considered most important in every firm because the task of internal controls is to prevent and detect fraud in the firm. Internal controls are put in place to ensure safe custody of all assets; to avoid misuse or misappropriation of the firm's assets and to detect and safeguard against probable frauds. Every firm whether manufacturing or non-manufacturing, should have management of the highest qualifications, caliber and dedication since its inception. The management should meet regularly to review the affairs of the firm and to direct the strategic path of the firm and also ensure continued goal congruence (Reid & Smith, 2000).

Controls in a manufacturing firm should evolve over time and all the departments and units of the firm should undergo positive transformations. The firm should also employ world class professionals to fill all the keys departments and units. This should probably be ensured by having a transparent and open of selection and recruitment aided by an ably staffed Human Resource Department of the firm. All departments and units should be adequately staffed with qualified and competent staff. The firm's records and accounting systems should be refined overtime and be audited by professionally trained and recognized auditors with a good reputation (Chenhall, 2003).

A firm should always have an internal audit department to help in compliance with the internal policies and procedures. Most firms put the above efforts in order to achieve positive performance. However, despite all these efforts, firms still struggle with liquidity problems, untimely financial reports, inefficient accountability for the firm's financial resources, frauds and misuse of the firm's resources as well as a number of decisions made not yielding the expected results. Furthermore, business transactions are not carried out according to the Generally Accepted Accounting Principles (GAAPs). This leaves the assets of a firm being improperly safeguarded, records being incomplete and information being inaccurate which often results in misleading financial statements that cannot be relied on by the stakeholders of the firm.

Jeremiah Munene (2013) conducted a study and found out that some of the challenges experienced in regard to internal controls include; struggles with liquidity problems, financial reports are not made timely, accountability for financial resources is wanting, frauds and misuse of institutional resources have been unearthed and a number of decisions made have not yielded the expected results.

Moraa Ondieki (2013) conducted a study and stated that internal controls can have features built into them to ensure that fraudulent truncations are flagged or made difficult, if not impossible, to transact. Internal control audits provide assurance that controls are working, but they do not necessarily detect fraud or corruption. The objectives of internal controls audit relate to management's plans, methods, and procedures used to meet the organization's mission, goals, and objectives.

Ndegwa E. Wanjohi (2013) stated that measurement and evaluation of performance is central to control, and addresses three questions namely; what happened, why it happened and what to do about it. Financial performance provides short term feedback to the control s as they monitor the implementation of strategic objectives by checking the organization's position, communicating the position, confirming priorities and compelling progress. It can therefore be construed that internal controls are the means while financial performance is the end.

This study attempted to investigate the persistent poor financial performance of manufacturing firms in Kenya from the perspective of internal controls which has hitherto been ignored. The effectiveness of internal controls on a firm's financial performance should be a key concern for most firms. Since internal controls help to prevent and detect fraud in an organization, manufacturing firms in Kenya should give much importance to internal audit which is generally a feature of large companies. It's a function provided either by employees of the entity or it can be sourced from an external organization in order to assist management in achieving corporate objectives.

1.3 Objective of the Study

The main objective of this study is to establish the relationship between internal control and the performance of manufacturing firms.

1.4 Value of the Study

This study is of interest to academicians and future researchers who will be undertaking other researches related to this. This is because it increases their knowledge on internal control and provides the necessary information to be incorporated into their work. The study also helps them come up with better proposals on internal control and their effects on financial performance of manufacturing firms. The recommendations of the study are of interest to the management of manufacturing firms because they point out the areas ignored in the internal control systems as well as the ways of improving the quality of the internal control. Furthermore the study helps to inculcate scientific and inductive thinking and promotes the development of logical habits and thinking by all staff in the organization.

The findings of this study would be crucial in informing the policy makers in Kenya on the effect of internal control on financial performance of manufacturing firms.

CHAPTER TWO

LITERATURE REVIEW

2.1 Introduction

This chapter focuses on the effect of Internal Control s (ICS) in achieving performance of firms in view of what other scholars have studied.

2.2 Review of Theories

Various theories have been formulated on internal audit and performance. They include Agency theory; Contingency theory and Theory of the firm. These are discussed below.

2.2.1Agency Theory

Agency theory is concerned with resolving problems that can exist in agency relationships; that is, between principals such as shareholders and agents of the principals for example, company executives. The two problems that agency theory addresses are: the problems that arise when the desires or goals of the principal and agent are in conflict, and the principal is unable to verify what the agent is actually doing and the problems that arise when the principal and agent have different attitudes towards risk. Because of different risk tolerances, the principal and agent may each be inclined to take different actions.

Adams (1994) in his article stated that agency theory can provide for richer and more meaningful research in the internal audit discipline. Agency theory contends that internal auditing, in common with other intervention mechanisms like financial reporting and external audit, helps to maintain cost-efficient contracting between owners and managers. Agency theory may not only help to explain the existence of internal controls and internal audit in firms but can also help explain some of the characteristics of the internal audit department, for example, its size, and the scope of its activities, such as financial versus operational auditing. Agency theory can be employed to test empirically whether cross-sectional variations between internal auditing practices reflect the different contracting relationships emanating from differences in organizational form.

2.2.2 Contingency Theory

Contingency theory is an approach to the study of organizational behavior in which explanations are given as to how contingent factors such as technology, culture and the external environment influence the design and function of organizations. The assumption underlying contingency theory is that no single type of organizational structure is equally applicable to all organizations. Rather, organizational effectiveness is dependent on a fit or match between the type of technology, environmental volatility, the size of the organization, the features of the organizational structure and its information. Contingency theories were developed from the sociological functionalist theories of organization structure such as the structural approaches to organizational studies by (Woods, 2009).

Contingency theory is used to describe the relationships between the context and structure of internal control effectiveness and organizational performance, especially reliability of financial reporting. Empirical study suggests that internal auditors who are specialized and higher in internal audit ability will achieve internal control effectiveness analysis and that the firm will benefit from the organizational effectiveness via internal control mechanism efficiency (Cadez and Guilding, 2008).

Cadez and Guilding (2008) identified some factors, which impact management controls; these are: external environment, technology, structure and size, strategy and national culture. It suggests that the demands imposed by technical tasks in the organization encourage the development of strategies to coordinate and control internal activities. The location of information in relation to technology and environment has an important influence on organization structure. In uncertain environments with non-routine technology, information is frequently internal. Where environments are certain, or where technology is routine, information is external. The dimensions of structure and control include authority structure and activities structure, i.e., rules and procedures that determine the discretion of individuals. Authority relates to social power. In the contingency model, decentralized authority is more appropriate where uncertain environments or non-routine technology exist. Centralized authority is more appropriate when environments are certain.

Contingency theory states that "the design and use of control system is contingent upon the context of the organizational setting in which these controls operate," (Fisher, 1998). Therefore the idea of contingency theory is that the selection and use of a management control is contingent on a variety of internal and external factors. It is therefore clear that, factors such as external environment, technology, structure and size, strategy and national culture impact management control system. The theory suggests that the demands imposed by technical tasks in the organization encourage the development of strategies to coordinate and control internal activities.

Daft (2012) in his book writes: "Contingency means: one thing depends on other things" and "Contingency theory means: it depends." Audit functions are task-oriented and can be loosely structured. The functions also can vary considerably, depending on the area of a company under audit and the type of business model, so auditors must carefully manage their inspections and take variables into account to get the job done. The contingency theory also can be applied to an audit team's structure. Typically, audit team managers receive audit projects. They then create ad hoc audit teams for the projects, selecting auditors based on expertise and experience in the subject areas, and on auditor availability, all of which add up to contingencies for any given audit project.

2.2.3 The Theory of the Firm

In simplified terms, the theory of the firm aims to answer these questions: Existence, Boundaries, Organization, why are firms structured in such a specific way, for example as to hierarchy or decentralization?, heterogeneity of firm actions and performances, what drives different actions and performances of firms, and lastly, the evidence, what tests are there for the respective theories of the firm (Thomas, 2008). The theory of the firm consists of a number of economic theories that describe, explain and predict the nature of the firm, company, or corporation, including its existence, behavior, structure, and relationship to the market.

This theory affirms that a firm is a "black box" operated so as to meet the relevant marginal conditions with respect to inputs and outputs, thereby maximizing profits, or more accurately, present value. The theory helps to explain why an entrepreneur or manager in a firm which has a mixed financial structure containing both debt and outside equity claims will choose a set of activities for the firm such that the total value of the firm is less than it would be if he were the sole owner and why this result is independent of whether the firm operates in monopolistic or competitive product or factor markets (Kantarelis, 2007).

This study will thus be guided by three theories namely; agency theory, contingency theory and the theory of the firm. Agency theory shows the relationship between the principal and agent and the agent's responsibilities which include financial reporting, budgeting and providing any other additional information to the principal. The contingency theory on the other hand explains that organizations' behavior and functions are dependent on factors such as technology, culture and the external environment that the organizations operate in while the theory of the firm asserts that, a firm is operated so as to meet the relevant marginal conditions with respect to inputs and outputs, thereby maximizing profits, or more accurately, present value.

2.3 Determinants of Financial Performance of Manufacturing Firms

Bessis (1998) defines financial performance as a management initiative to upgrade the accuracy and timeliness of financial information to meet required standards while supporting day to day operations. Lyman and Carles (1978) also defined it as the operational strength of a firm in relation to its revenue and expenditure as revealed by its financial statements. Financial performance is characterized of a bad debt policy, sales turnover, profitability level, client's dropout rate, growth, reduction in fixed assets, and physical visitation by commercial staff, debt age analysis, and public media.

Dixon et al (1990) said that appropriate performance measures are those which enable organizations to direct their actions towards achieving their strategic objectives. Kotey, Reid and Ashelby (2002) contends that performance is measured by either subjective or objective criteria, arguments for subjective measures include difficulties with collecting qualitative performance data from small firms and with reliability of such data arising from differences in accounting methods used by firms.

Whittington and Kurt (2001) found out that objective performance measures include indicators such as profit growth, revenue growth, return on capital employed. Financial consultants Stern Stewart and Co. created Market Value Added (MVA), a measure of the excess value a company has provided to its shareholders over the total amount of their investments (John and Morris, 2011). This ranking is based on some traditional aspects of financial performance including: total returns, sales growth, profit growth, net margin, and return on equity.

Dwivedi (2002) however, mentions other financial measures to include value of long-term investment, financial soundness, and use of corporate assets. John and Morris (2011) mentions accounting based performance using three indicators: return on assets (ROA), return on equity (ROE), and return on sales (ROS). Each measure is calculated by dividing net income by total assets, total common equity, and total net sales, respectively.

Some other useful measures of financial performance are wound into what is referred to as CAMEL. The acronym "CAMEL" refers to the five components that are accessed: Capital adequacy, Asset quality, Management, Earning and Liquidity. Ratings are assigned for each component in addition to overall rating of banker's financial conditions (Jose, 1999).

2.3.1 Capital Adequacy

Capital adequacy is the determination of the minimum capital amount required to satisfy a specified economic capital constraint (Miccolis, 2002). Ultimately it determines how well financial institutions can cope with the shocks to their balance sheet. Thus it's useful to track capital adequacy ratios that take financial risks, foreign exchange credit and interest rate risks, by assigning risks ratios established by the International Settlement (BIS). Capital adequacy is measured in relation to the relative risk weight assigned to the different category of assets held both on and off to control the incentive to take on excessive risk and to absorb a reasonable amount of losses.

2.3.2 Asset Quality

The solvency of financial institutions is typically at risk when their assets become impaired, so it is important to monitor indicators of the quality of their assets in terms of overexposure to specific risks trends in non-performing loans and the health and profitability of borrowers. It arises when a borrower defaults on the loan payment agreement. A financial institution whose borrower defaults on their payment may face cash flow problems, which eventually affects its liquidity position. Ultimately, this negatively impacts on the profitability and capital through extra specific provisions for bad debts (BOU, 2002).

2.3.3 Management

Management quality (approximated by cost efficiency scores) has been associated with firm failures in a number of recent studies, for example, Barr and Siems (1994), Wheelock and Wilson (2000), and Kick and Koetter (2007). Cost efficiency is approximated by a simple ratio of Operating Expenses to Total Revenues, denoted as Efficiency Ratio, measures management flexibility to adjust costs to changes in the business development signaled by revenues. The higher is the Efficiency Ratio, the higher is the default risk.

2.3.4 Earning

The continued viability of a firm depends on its ability to earn an adequate return on its assets and capital. The evaluation of earnings performance relies heavily upon comparison on the key profitability measures (such as return on assets and return on equity) to industry bench mark and peer group norms (Federal Reserve, 2002). Most bank studies emphasis is placed on profitability in terms of ROE and ROA. Profitability as a measure of performance is widely accepted by financial institutions, management, company owners and other creditors as they are interested in knowing whether or not the firm earns substantially more than it pays by way of interest (Sadakkadulla & Subbaiah, 2002).

2.3.5 Liquidity

Initially solvent financial institutions may be driven towards closure by management of short term liquidity. Indicators should cover funding sources and capture large maturity mismatches. Liquidity is the degree to which debts obligations coming due in the next 12 months can be paid in cash or assets that will be turned into cash .The mismatching and controlled mismatching of the maturities and interest rate of assets and liabilities is fundamental to the management of manufacturing firms.

2.4 Empirical literature review

Mawanda (2008) conducted a research on effects of internal control on financial performance in institution of higher learning Uganda. In his study he investigated and sought to establish the relationship between internal controls and financial performance in an Institution of higher learning in Uganda. Internal controls were looked at from the perspective of Control Environment, Internal Audit and Control Activities whereas Financial performance focused on Liquidity, Accountability and Reporting as the measures of Financial performance. The Researcher set out to establish the causes of persistent poor financial performance from the perspective of internal controls. The study established a significant relationship between internal control and financial performance. The investigation recommends competence profiling in the Internal Audit department which should be based on what the University expects the internal audit to do and what appropriate number staff would be required to do this job. The study therefore acknowledged role of internal audit department to establish internal controls which have an effect on the financial performance of organizations.

Case studies on internal controls in Belgium illustrate the importance of the control environment when studying internal auditing practices. Sarens and De Beelde (2006) found that certain control environment characteristics like tone-at-the-top, 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 the internal audit function and fraud detection within an organization.

Using the analytical approach and focusing on control activities and monitoring, Barra (2010) investigated the effect of penalties and other internal controls on employee's propensity to be fraudulent. Data was collected from both managerial and non-managerial employees. The results showed that the presence of the control activities, separation of duties, increases the cost of committing fraud. Thus, the benefit from committing fraud has to outweigh the cost in an environment of segregated duties for an employee to commit fraud. Further, it was established that segregation of duties is a "least-cost" fraud deterrent for non-managerial employees, but for managerial employees, maximum penalties are the "least-cost" fraud disincentives. The results suggest the effectiveness of preventive control activities such as segregation of duties is dependent on detective controls.

Ewa and Udoayang (2012) carried out a study to establish the impact of internal control design on bank's ability to investigate staff fraud and staff life style and fraud detection in Nigeria. Data were collected from 13 Nigerian banks using a four point likert Scale questionnaire and analyzed using percentages and ratios. The study found that Internal control design influences staff attitude towards fraud such that a strong internal control mechanism is deterrence to staff fraud while a weak one exposes them to fraud and creates opportunity for staff to commit fraud.

Kakucha (2009) evaluated the level of effectiveness of internal controls of enterprises operating in Nairobi. The study was quantitative and was conducted between September 2007 and June 2009 using a sample of 30 small businesses as listed in the National Social Security Fund (NSSF) Register of Kenya. Primary data was collected from the managers of the small business using interviews and examination of documents pertaining to internal controls. The study established that there are deficiencies in the s of internal controls, with the degree of deficiencies varying from one enterprise to another. The components of internal control that were missing in most businesses surveyed were: firstly, risk analysis, and secondly lack of proper flow of information.

In addition, the study established that the sample population had limited awareness of what constituted an effective of internal control. The study also found that there is a negative relationship between the age of an enterprise and the effectiveness of its of internal control while a negative correlation between the resources held by an enterprise and its internal control weaknesses exists. The recommended that these were need to enlighten the operators of small business of what constitutes an efficient and effective of internal control through forums and seminars.

Amudo and Inanga (2009) also carried out a study in Uganda to evaluate the internal control s that the regional member countries of the African Development Bank Group institute for the management of the Public Sector Projects that the Bank finances. There are 14 projects of the bank's public sector portfolio in Uganda. The data received and analyzed is for eleven projects. Three projects were omitted because they were not fully operational to install effective internal control. The study identified the following six essential components of an effective internal control: control environment, risk assessment, control activities, information and communications, monitoring and information technology. The outcome of the evaluation process was that some control components of effective internal control s were lacking in those projects. These rendered the control structures ineffective.

Wee Goh (2009) studied 208 firms on audit committees, boards of directors, and remediation of material weaknesses in internal control. He measured the effectiveness of the audit committee by its independence, financial expertise, size, and meeting frequency, and the effectiveness of the board by its independence, size, and meeting frequency, and by the duality of the chief executive officer (CEO) and chair positions (CEO duality). He also examined other factors that can affect firms' timeliness in the remediation of material weaknesses, such as the severity of material weaknesses, firms' profitability, the complexity of firms' operations, and so on. He found out that the proportion of audit committee members with financial expertise is positively associated with firms' timeliness in the remediation of material weaknesses. Second, firms with larger audit committees are more likely to remediate material weaknesses in a timely manner. Third, that a more independent board is less susceptible to the undue influence of management and more likely to exert pressure on management to remediate material weaknesses.

Jones (2008) compared internal control, accountability and corporate governance in medieval and modern Britain. He used a modern referential framework (control environment, risk assessment, information and communication, monitoring and control activities) as a lens to investigate medieval internal controls used in the twelfth century royal exchequer and other medieval institutions. He demonstrated that most of the internal controls found today were present in medieval England. Stewardship and personal accountability were found to be the core elements of medieval internal control. The recent recognition of the need for the enhanced personal accountability of individuals is reminiscent of medieval thinking.

Romar and Moberg (2003) conducted a case study that showed the following could have contributed to WorldCom scandal in 2002: unrealistic growth targets when expectations were low, management philosophy was aggressive; inadequate assessment of internal and external factors, and objectives before setting aggressive targets; poor segregation of duties; access to data entry and manipulation was not properly segregated and there was a lack of stringent monitoring of the internal control and therefore quality of the controls around the posting of journal entries to the general ledger was not identified as weak.

Olumbe (2012) conducted a study to establish the relationship between internal controls and corporate governance in commercial banks in Kenya. The researcher conducted a survey of all the 45 commercial banks in Kenya. It was concluded that most of the banks had incorporated the various parameters which are used for gauging internal controls and corporate governance. This was indicated by the means which were obtained enquiring on the same and this showed that the respondents agreed that their banks had instituted good corporate governance with a strong of internal controls and that there is a relationship between internal control and corporate governance.

A study conducted by Wainaina (2011) examined the internal control function. He established that, other than the prevention and detection of fraud, internal controls should reflect the strength of the overall accounting environment in an organization as well as the accuracy of its financial and operational records.

2.5 Summary of Literature Review

From the literature reviews done it has been found out that realization of positive financial performance and value for money depends on whether firms have Internal Controls. Non-compliance to the internal controls are one of the major hindrances to the attainment of positive financial performance in manufacturing firms. Whereas a lot has been done on control environment and control activities there is little done about internal audit in relation to value for money; what is greatly studied is value for money audits. Weak, non-compliance, non-existent or absent public financial management functions (Internal Control s) are likely to negate any advantages that might be inherent in achieving positive Financial Performance of a firm. Therefore, there is need to establish the relationship between the internal control s and performance of manufacturing firms in Kenya. It can be concluded from the literature that Control Environment, Control Activities, Risk Assessment, Information and Communication and Monitoring are significant predictors of financial performance.

CHAPTER THREE

RESEARCH METHODOLOGY

3.1 Introduction

This chapter provides an account on how this study was conducted. The methodology include the research design, the target population, the sampling design and the sample size, the data collection instruments as well as the data analysis techniques that will be used to analyze the data.

3.2 Research Design

A cross sectional survey was used in the course of the study. The researcher conducted a survey of 65 manufacturing firms register with the Kenya Association of Manufacturers (KAM). According to Mugenda, (2003), Descriptive research design allows the researcher to study the elements in their natural form without making any alterations to them. The design also allows the researcher to come up with descriptive statistics that can assist in explaining the relationship that exists among variables. Descriptive research design is the most applicable for the study, as the study focused on describing independent variables. This scientific method of investigation involved collection and analysis of data in order to describe a phenomenal in its current condition or status, Mugenda, (2003), continues to indicate that this design is preferred because it is time saving, it is possible and easy for the researcher to obtain current factual information from the employees in the organization.

3.3 Population

A study population is a well-defined or specified set of people, group of things, households, firms, services, elements or events which are being investigated. The population should fit a certain specification, which the researcher is studying. A target population is one that the researcher wants to generalize the result of the study. The population chosen for this study is 65 manufacturing firms registered with the Kenya Association of Manufacturers (KAM). A census survey was conducted to establish the relationship between internal control and financial performance of the 65 manufacturing firms.

Census is a procedure of systematic acquiring and recording information about all members of a given population. Conducting a census research requires an adequate response which in turn leads to high degree of statistical confidence in the results due to great accuracy and reliability. (Mugenda, 2008). A census survey was conducted to target 65 senior managers manufacturing firms in Kenya

3.4Data collection method and instrument

Both primary and secondary data was used in the study. Primary data is information gathered directly from the respondents (Mugenda, 2003). The primary data was collected by use of a structured questionnaire. The questionnaire is considered because it is easy to administer. The questionnaire contained both open and closed ended questions; it was self-administered through a drop-and-pick method. The questionnaire was divided into fours ections. Section A to C contained questions relevant to internal controls while section D contained questions on financial performance assessment. Secondary data that was collected included annual reports and financial statements.

3.5 Data Analysis

Data was analyzed on the basis of descriptive statistics and performance comparison done across time between the years 2011-2014. Statistical Package for Social Sciences (SPSS) version 22.0 was used as an aid to analysis. SPSS is preferred because of its ability to cover a wide range of most statistical and graphical data analysis and is attic. In order to determine the relationship between internal controls and financial performance, a multiple regression was conducted to establish the relationship that existed between three independent variables of internal control and the dependent variable – financial performance.

The researcher intended to take one respondents from each firm – one top management. The study will adopt the following model to conduct its analysis:

$Y = \beta 0 + \beta 1X1 + \beta 2X2 + \beta 3X3 + \epsilon$

Where, Y –Performance of Manufacturing Firms in Kenya

$\beta 0$ - Constant

X1 – Risk Assessment

X2 – Control Activities

X3 –Monitoring

$\beta 1 - \beta 3$= Measure of sensitivity of variable X to changes in Performance

Є= Error term

Financial performance was measured by Return on Investment (ROI). Risk assessment and monitoring was measured by the level of business knowledge of the entrepreneurs in internal control as per the questionnaire in appendix one. Control activities was measured by how the entrepreneurs review and verify internal controls

3.6.1 Tests of Significance

The study conducted an F- test to establish the significance of the independent variables (risk assessment, control activities, and monitoring procedures) against the dependent variable (Financial Performance). The significance of variables was observed at 95% confidence level whereby, variables with a 'p' value of 0.05 and below was deemed significant while those with 'p' values above 0.05 deemed insignificant.

CHAPTER FOUR

DATA ANALYSIS AND PRESENTATION OF FINDINGS

4.1 Introduction

This chapter presents analysis and findings of the study as set out in the research objective and research methodology. The study findings are presented on the effect of internal controls on financial performance of manufacturing firms in Kenya. To achieve the objective of this study the respondents were encouraged and persuaded to respond to the statements in the questionnaire objectively to ensure validity and reliability.

4.2 Response Rate

The study sought to collect data from 65 respondents, a total of 59 respondents‟ responded constituting 90.8% of the respondents rates. According to Mugenda and Mugenda (2003) a 50% response rate is adequate, 60% good and above 70% rated very good. This also concurs with Kothari (2004) assertion that a response rate of 50% is adequate, while a response rate greater than 70% is very good. This implies that based on this assertions; the response rate in this case of 90.8% is very good.

4.3 Descriptive Statistics

Descriptive statistics are concerned with explaining the sample of data that the researcher is concerned with. They are used to describe the main features of a collection of data quantitatively. Below are the findings:

4.3.1 Gender of the respondents

Table4.1:Gender

Category	Frequency	Percentage
Male	39	66.1
Female	20	33.9
Total	**59**	**100.0%**

4.3.2 The Level of Education Attained by the Respondents

The respondents were asked about their level of education in order to determine whether they understood the internal control systems and its effect on financial performance of the firm.

Table 4.2: Education

Category	Frequency	Percentage
Certificate/Diploma	4	6.8
Undergraduate degree	43	72.9
Masters	11	18.6
PhD	1	1.7
Total	**59**	**100.0%**

From the findings in table 4.2 above, the results showed that most of the employees were degree holders at 72.9%, 18.6% of the respondents had attained a master's level, 6.8% certificates or diplomas and only 1.7% of the respondents had attained PhD. This clearly shows that most of the employees in manufacturing firms were degree holders at the managerial level.

4.3.3 Age bracket of the respondents

Table 4.3: Age

Category	Frequency	Percentage
Below25	1	1.7
25-34	22	37.3
35-44	33	55.9
45-50	3	5.1
Total	**59**	**100.0%**

4.3.4 RISK ASSESSMENT AND FINANCIAL PERFORMANCE

The researcher examined the effects of risk assessment as functionality internal controls of the organization affects the financial performance of manufacturing firms in Kenya. Below are the results of the findings:

Table 4: Risk Assessment

	Mean	**Standard Deviation**
Management has defined appropriate objectives for the organization	3.78	0.730
Management identifies risks that affect achievement of the objectives	3.85	0.819
Management has a criteria for ascertainment of which fraud-related risks to the	4.11	0.882

organization are most critical		
Management has put in place mechanisms for mitigation of critical risks that may result from fraud	3.24	0.597

From the above findings, it was observed that most of the manufacturing firms carried out regular risk assessment procedures. From the results, manufacturing firms defined appropriate objectives for the organization, this had (M=3.78, S.D=0.730), the management identifies risks that affect achievement of the objectives (M=3.85,S.D=0.819), the management has a criteria for ascertainment of which fraud-related risks to the organization are most critical had (M=4.11, S.D=0.882), the management has put in place mechanisms for mitigation of critical risks that may result from fraud had (M=3.24, S.D=0.597).It was also established that the management had put in place mechanisms for mitigation of critical risks that may result from fraud. These results are clear indication that most manufacturing firms observed risk assessment procedures as functionality of internal control of the manufacturing firms.

4.3.5 CONTROL ACTIVITIES AND FINANCIAL PERFORMANCE

The study examined the effect of control activities on the financial performance of manufacturing firms in Kenya. Below are the results of this study in table 4.5

Table 4.5: Control Activities

	Mean	**Standard Deviation**
Our organization has clear separation of roles	4.51	0.911
Every employee’s work check on the others	3.85	0.506
Corrective action is taken to address weaknesses	4.19	0.882
Staff are trained to implement the accounting and financial management	3.24	0.556
Our organization has a well-developed Chart of Accounts	4.10	0.603
It is impossible for one staff to have access to all valuable information without the consent of senior staff	3.42	0.619
Controls are in place to exclude incurring expenditure in excess allocated funds	3.14	0.712
Departments have budget reviews where actual expenditure is compared with budgeted expenditure and explanations for the variances given	3.22	0.845
Our security identifies and safeguard organizational Assets	4.20	0.972

From the above findings, it was revealed that control activities were carried out regularly by most manufacturing firms. The findings showed that most manufacturing firms had clear separation of roles (M=4.51, S.D=0.911), corrective actions were taken to address weaknesses (M=4.19, S.D=0.882).The results also found that the staff were trained to implement the accounting and financial management system (M=3.24, S.D=0.556), the security system identified and safeguarded organizational assets (M=4.20, S.D =0.972).It was concluded that manufacturing firms carried out control activities as a functionality of internal control of the manufacturing firms in Kenya.

4.3.6 MONITORING PROCEDURES AND FINANCIAL PERFORMANCE

The study sought to establish the effect of information and communication on financial performance in relation to the length of operation of the organization. The results of this analysis are as provided below in table 4.6

Table 4.6: Monitoring procedures and financial performance

	Mean	**Standard Deviation**
There are independent process checks and evaluations of controls activities on ongoing basis	3.21	0.993
Internal reviews of implementation of internal controls in units are conducted periodically	3.03	0.502
Monitoring has helped in assessing the quality of performance of the organization over time	4.11	0.811
Management has assigned responsibilities for the timely review of audit reports and resolution of any non-compliance items noted in those audit reports	2.05	0.830

From the above findings in table 4.6, it was found that that monitoring was a functionality of internal control of manufacturing firms. This was demonstrated by the results of the study which showed that there was independent process checks and evaluations of controls activities in the operation of the firm (M=3.03, S.D=0.993), internal reviews of implementation of internal controls in units were conducted periodically (M=3.21, S.D=0.502), monitoring has helped in assessing the quality of performance of the organization over time (M=4.11, S.D=0.811). Some of the manufacturing firms did not assign their responsibilities in a timely manner and this negatively affected compliance in audit report, this is explained by (M=2.05, S.D=0.830). This shows that even though monitoring is an important functionality activity of the internal control of the firm in its operation period, not all manufacturing firms implemented this practice. This therefore, negatively impacted on the financial performance of some manufacturing firms.

4.4 Regression Analysis

A study was conducted on the relationship between internal control and financial performance of manufacturing firms in Kenya. The analysis applied the statistical package for social sciences (SPSS) version 21.0 to compute the measurements of the multiple regressions for the study. The findings are provided below:

4.4.1 Model Summary

The model summary shows the summary of the regression analysis as shown in the regression model. Below are the findings in the table 4.7

Table 4.7: Regression Model Summary

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.957(a)	.916	.757	.250

In order to explain the percentage of variation in the dependent variable financial performance as explained by the independent variables. The researcher used coefficient of determination that was obtained from the model summary in the table 4.7.Coffecient of determination was used to explain whether the model is a good predictor.

From the results of the analysis, the findings show that the independent variables (risk assessment, control activities and monitoring procedures) contributed to 75.7% of the variation in financial performance as explained by adjusted R2 of 0.757% which shows that the model is a good prediction.

4.4.2 Analysis of Variance

The study conducted an Analysis of Variance, in order to test the impact of the relationship between internal controls and financial performance of manufacturing firms in Kenya. The findings were as shown below:

Table 4.8: ANOVA (Analysis of Variance)

	Sum of Squares	df	Mean Square	F	Sig.
Regression	2.117	3	.706	4.888	. 001(a)
Residual	1.213	14	. 0.086		
Total	5.24	17			

Source: Author (2015)

The results of the findings above revealed that the level of significance was .001(a) this implies that the regression model is significant in predicting the relationship between internal control and financial performance. By the help of an F-test table, the tabulated value for F (5%, 3, 14) is 2.96 which was less than 4.888 meaning that the model was statistically significant.

4.4.3 Test for Coefficients

This table shows the level of significance on the variables, it also provides the standardized and unstandardized coefficients are sho: wn below:

Table 4. 9: Multiple Regression Analysis

Model		Unstandardized Coefficients		Standardized Coefficients	T	Sig.
		B	Std. Error	Beta		
1	(Constant)	0.989	2.163		5.331	0.000
	Risk Assessment	0.101	0.200	0.328	-.815	0.001
	Control Activities	0.213	0.133	0.637	1.609	0.003
	Monitoring	0.892	0.224	0.843	.542	0.005

From the above table 4.9, the researcher sought to establish the extent to which internal control impact on financial performance of manufacturing firms‟. The following regression equation was obtained: ROI= 0.989+.101X1+.213X2+.892X3

From the above regression model holding all the other factors constant, financial performance is measured by the efficiency and effective implementation of internal controls. The results of the multiple regression model shows that there is a positive relationship between internal control and financial performance of manufacturing firms in Kenya. This implies that a single unit increase in any of the independent variables results into a corresponding increase in financial performance of manufacturing firms.

The regression analysis was undertaken at 5% significance level. The criteria for comparing whether the predictor variables were significant in the model was through comparing the corresponding probability value obtained and α=0.05. If the probability value was less than α, then the predictor variable was significant but from the above analysis. The results above shows that the variables were significant since their corresponding predictor values were below 5%.

4.5 Summary and interpretation of the findings

According to the respondents' demographics, it was revealed that most of the employees in manufacturing firms were males with university degree. It was further revealed that most respondents were aged of 35-44 years.

The researcher examined the effects of risk assessment as functionality internal controls of the organization affect the financial performance of manufacturing, it was established that the management had put in place mechanisms for mitigation of critical risks that may result from fraud. These results are clear indication that most manufacturing firms observed risk assessment procedures as functionality of internal control of the manufacturing firms. The study examined the effect of control activities on the financial performance of manufacturing firms in Kenya. The results revealed that that the staff was trained to implement the accounting and financial management systems, the security system identified and safeguarded organizational assets. It was observed that manufacturing firms carried out control activities as a functionality of internal control of the manufacturing firms in Kenya.

Further, it was found that manufacturing firms monitored their activities as part of the functionality of internal control systems; however some of the manufacturing firms failed to assign their responsibilities in a timely manner and this negatively affected compliance in audit report. This showed that even though monitoring was an important functionality activity of the internal control of the manufacturing firms, all manufacturing firms did not implement this practice. The statistical results from the regression analysis show that there is a positive relationship between internal control and financial performance of manufacturing firms in Kenya. This is demonstrated by the level of significance attained by each of the independent variables. All the independent variables have a significance of less than 5%. This is an indication that the variables are statistically significant.

The regression results revealed that there is a positive relationship between internal controls and financial performance of manufacturing firms in Kenya. The coefficient of determination proved that the independent variables contributed to 75.7% of the variation in financial performance as explained by adjusted R2 of 0.757% which shows that the model was a good predictor. This is supported by a study by Kakucha (2009) who evaluated the level of effectiveness of internal controls of enterprises operating in Nairobi. Data was analyzed using a regression model and the results of the analysis exhibited a positive relationship between internal controls and financial performance. This study therefore seeks to investigate whether internal control affects financial performance. These findings are also supported by a study of Olumbe (2012) who did a study to establish the relationship between internal controls and corporate governance in commercial banks in Kenya concluded that strong internal control systems led to improved corporate governance.

CHAPTER FIVE

SUMMARY, CONCLUSIONS AND RECOMMENDATIONS

5.1 Summary of findings

The main objective of this study was to establish the relationship between internal control and the financial performance of manufacturing firms in Kenya. Descriptive research design was adopted for this study. The study used a sample of 65 manufacturing firms in Kenya. To ensure that all levels of employees are represented, the study used stratified random sampling technique. The study used primary data collected from semi-structured questionnaires. Quantitative data was analyzed using descriptive statistics while qualitative data was analyzed using content analysis. Quantitative data was coded and entered into Statistical Packages for Social Scientists (SPSS Version 21.0). Analysis was, then, based on descriptive statistics. Multiple regression analysis was used to establish the relationship between internal controls and financial performance of manufacturing firms in Kenya.

From the study findings, in regard to their gender, most of the participants were males as opposed to their female counterparts who most of them had university degrees.

The results of the regression model show that there is a positive relationship between internal controls and financial performance of manufacturing firms. Holding all the other factors constant, financial performance is measured by the efficiency and effective implementation of internal controls. The results of the multiple regression model shows that there is a positive relationship between internal control and financial performance of manufacturing firms in Kenya. This implies that a single unit increase in any of the independent variables results into a corresponding increase in financial performance of manufacturing firms. The study established the internal controls affect financial performance of manufacturing firms in Kenya to a great extent.

5.2 Conclusions

From the findings of the study, it was concluded that manufacturing firms had invested on effective internal control systems had more improved financial performance as compared to those manufacturing firms that had a weak internal control system. From the findings, it was revealed that those manufacturing firms that observed integrity, ethical values, risk assessment, control activities, and monitoring procedures recorded high financial performance. Most large scales manufacturing firms that fully invested in strong internal control systems were able to mitigate fraud. Based on the study findings, the results indicated that some small scale manufacturing firms faced challenges in effective implementation of internal control due lack of sufficient resources to hire competent staff and to invest in modern technologies. The findings of the study found that control activities had a significant positive relationship with financial performance indicators. Similarly the other variables for instance, risk assessment was also found to have a positive relationship with financial performance of manufacturing firms in Kenya apart from monitoring that revealed a negative relationship with financial performance of manufacturing firms. From the findings of the study internal reviews of internal control units of most manufacturing firms were not conducted periodically, monitoring was not carried out regularly and untimely assigning of audit reports leading to lack of compliance of audit reports.

5.3 Recommendation to Policy and Practice

The study recommends that both internal and external auditor should be constantly updated and well-grounded on international financial reporting standards (IFRS) and principles in order to enhance their knowledge and skills in application of accounting practices and to keep them updated on the contemporary issues.

Kenya Association of Manufacturers should monitor and supervise manufacturing firms to ensure that the accountants comply with accounting regulations and requirement as provided by the Institute of Certified Public Accountants to ensure proper implementation and compliance with accounting standards and principles. Manufacturing firms should develop and organize constant seminars and workshops to train and educate auditors and accountant on matters pertaining proper implementation of accounting policies and procedures to enhance their skills and expertise in their practice as professionals. The study further recommends that the governing body, possibly supported by the audit committee, should ensure that the internal control system is periodically monitored and evaluated. The actual assessment can be executed by the organization's management. A staff person who is sufficiently independent from those responsible for the system, such as the internal auditor, could provide additional assurance on the effectiveness and cost efficiency of the internal control system. The manufacturing firms should transparently report on the structure and performance of their governance, risk management, and internal control in their various reports to internal and external stakeholders, such as through their periodic accountability reports or on the organization's website.

5.4 Limitations of the Study

The research met with various challenges when conducting the research that included the fact that the firms ordinarily do not want to give information due to client confidentiality. The findings of the study may not be generalizable to other manufacturing firms in Kenya to differences in social, political and economic environments in different parts of the country. In addition, some of the respondents would not find the subject to be of interest. Additionally, some respondents would not want to give the information as they considered it of competitive importance. Time limitation made it impractical to include more respondents in the study. This study was also limited by other factors in that some respondents may have been biased or dishonest in their answers. More respondents would have been essential to increase the representation of manufacturing firms in this study and to allow for better check of consistency of the information given. However, the researcher did look for contradictions in the information given and no inconsistency were found.

5.6 Suggestions for Further Study

Due to the turbulent nature of the business environment a similar study should be conducted after a period of ten years in order to investigate whether there are any areas of commonalities or unique factors this is because the level of technology is very dynamic and keeps on changing. It would be interesting to conduct a study on the determinants of internal control and their implications on financial performance; this will shed more light on the appropriate model to choose when implementing better internal control systems that enhance financial performance of firms.

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APPENDICES

Appendix I: Questionnaire for the respondents

This questionnaire is designed to collect data on to establish the effect internal control s on performance of manufacturing firms. The data shall be used for academic purpose only and it will be treated with confidentiality it deserves. The respondents are highly encouraged and persuaded to respond to the statements in this questionnaire in the most truthful and objected way possible. Your participation in facilitating this study will be highly appreciated. Kindly tick in the space provided with the correct answer or supply the required information. Where required, please specify and elaborate.

SECTION A: General Information

1. What is your gender?

Male [ ] Female [ ]

2. What is your highest level of education? Certificate/Diploma [ ] Undergraduate degree [ ] Masters[ ] PhD [ ]

3. What is your age bracket?

Below25[ ]

25-34[ ] 35-44[ ]

45-50 [ ]

Above 51[ ]

SECTION B: RISK ASSESSMENT AND FINANCIAL PERFORMANCE

5. Rank the extent to which your organization's management is involved in risk assessment (1- Very great extent, 2- Great extent, 3- Moderate extent, 4- Little extent, 5- No extent)

	1	2	3	4	5
Management has defined appropriate objectives for the organization					
Management identifies risks that affect achievement of the objectives					
Management has a criteria for ascertainment of which fraud-related risks to the organization are most critical					
Management has put in place mechanisms for mitigation of critical risks that may result from fraud					

SECTION C: CONTROL ACTIVITIES AND FINANCIAL PERFORMANCE

6. Rank the extent to which your organization practices the following control activities (1- Very great extent, 2- Great extent, 3- Moderate extent, 4- Little extent, 5- No extent**)**

	1	2	3	4	5
Our organization has clear separation of roles					
Every employee's work check on the others					
Corrective action is taken to address weaknesses					
Staff are trained to implement the accounting and financial management					
Our organization has a well-developed Chart of Accounts					
It is impossible for one staff to have access to all valuable information without the consent of senior staff					
Controls are in place to exclude incurring expenditure in excess allocated funds					
Departments have budget reviews where actual expenditure is compared with budgeted expenditure and explanations for the variances given					
Our security identifies and safeguard organizational Assets					

SECTION D: MONITORING PROCEDURES AND FINANCIAL PERFORMANCE

8. Rank the extent to which the following statements relate to your organization "monitoring procedures (1- Very great extent, 2- Great extent, 3- Moderate extent, 4- Little extent, 5- No extent)

	1	2	3	4	5
There are independent process checks and evaluations of controls activities on ongoing basis					
Internal reviews of implementation of internal controls in units are conducted periodically					
Monitoring has helped in assessing the quality of performance of the organization over time					
Management has assigned responsibilities for the timely review of audit reports and resolution of any non-compliance items noted in those audit reports					

Appendix II: List of Manufacturing Firms in Kenya

Acme Container Ltd

Adhesive Solutions Africa Ltd

Africa Kaluworks (Aluware) Division K

Africa Oil Kenya B.V

African Cotton Industries Ltd

Agni Enterprises Ltd

Ali Glaziers Ltd

Alpha Dairy Products Ltd

Alpha Fine Foods Ltd

Apex Steel Ltd

Aquva Agencies Ltd -Nairobi

Arrow Rubber Stamp Company Ltd.

Artech Agencies (KSM) Ltd

Ashut Quality Products

ASL Ltd – HFD

Athi River Mining Ltd

Atlas Copco Eastern Africa Ltd

Bamburi Special Products Ltd

Beta HealthCare

BIDCO Oil Refineries Limited Bilco Engineering

Biodeal laboratories ltd Blowplast Ltd Blue Triangle Cement

Bobmil Industries Limited

British American Tobacco Kenya Ltd

C. Dormans Ltd

Chandaria Industries Limited

Chevron Kenya Ltd

Chloride Exide Kenya Limited

Colgate-Palmolive(East Africa) Ltd Commercial Motor Spares Ltd

Cosmos Limited

Creative Fabric World Co Ltd

Creative Innovations Ltd.

Crown-Berger (K) Ltd.

Cuma Refrigeration EA Limited

Doshi Group of Companies

East Africa Glassware Mart Ltd

East African Breweries Limited

East African Cables Ltd.

East African Portland cement

Eastern Chemical Industries Ltd

Eco Consult LTD

Ecolab East Africa (K) Ltd

Ecotech Ltd

Energy Pak (K) Ltd

Eveready East Africa Limited

Excel Chemical Ltd.

FairdealUpvc, Aluminium and Glass Ltd

Farmers Choice Ltd

Foam Mattress Ltd.

Furmart Furnishers 42 Geomatic Services Ltd

Goldrock International Enterprises

Hydraulic Hose & Pipe Manufacturers Ltd

JET Chemicals (Kenya) Ltd

Kapa Oil Refineries Limited

Kenbro Industries

Kenya Electricity Generating Company Ltd

Kenya Fluorspar Company Ltd (KFC)

Kenya Grange Vehicle Industries Ltd

Kenya Petroleum Refineries Ltd

Kenya Power and Lighting Company Ltd

Kenya Solar