Effect of internal control activities on financial performance of Rwanda Association of Local Government Authorities

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Abstract

Globally, internal control mechanism is a tool for ensuring that an organization realizes its mission and objectives. Internal controls are often thought to be the domain of accountants and auditors; it is actually management that has primary responsibility for proper controls. A critical element of any comprehensive Internal Control mechanism is regular monitoring of the effectiveness of internal controls to determine whether they are well designed and functioning properly. The current study was analyzing the effect of internal control activities on financial performance of public entities in Rwanda. The research project used mixed method named qualitative and quantitative approach and the research design was descriptive survey design with 133 respondents. The data was analysed using IBM/SPSS version 20.0. The questionnaire was the main tool to collect information, and interview was also used. The results was presented in tables for presenting frequencies. From the findings, holding the various components consistent, internal control activities is measured by proficient and powerful usage of monitoring and risk assessment. Monitoring has a positive beta coefficient of 0.977, which indicates that one unit increase in monitoring will cause to increase internal control system by 0.977 and the other indicators remaining constant. Moreover, the consequence of the examination demonstrates that internal control system, risk assessment and monitoring influence financial performance of public entities Rwanda (RALGA). In addition, a critical period for conducting internal control system should lead to regular monitoring for the effectiveness of internal controls to determine properly well-functioning of an organization. Finally, Finally, the researcher recommended that to enhance collaboration and regular internal control should be put under consideration of any organization as it is required and regular internal auditing and self-application of regular monitoring are also necessary for the internal control effectiveness of public entities.

1. Introduction

Globally, and especially in Africa, there are calls for governments to be accountable for the huge resources they hold on trust and manage for the people who gave them the political and administrative authority. The public sector represents a principal-agent relationship. The officials or administrators act as the agents while the citizens are the principals. In the words of Achua (2009), government spending is a very big business and the public demands to know whether the uge outlays of money are being spent wisely for public interest. Those in authorities assume fiduciary status with the attendant responsibilities requiring them to render accounts of their stewardship to the citizens for whom the authority is held in trust. (Rapani and Malim, 2018).

Ashbaugh Skaife *et al*., (2008) documented that firms reporting internal control weaknesses have more complex operations; have experienced recent changes in organizational structure; are at increased exposure to accounting risks; and have fewer resources to invest in internal control. Furthermore, Doyle et al., (2005) indicated that firms with material

weaknesses have a lower earnings quality than those that do not report material weaknesses. Additionally, Hamersley *et al*., (2007) showed a negative market reaction to firms that had reported material weaknesses in internal control per the requirement of Sarbanes-Oxley Act Section 302

Internal controls are a problem that is not limited to developing countries. Businesses in Ghana, Africa, use internal management extensively. Internal management practices have been conducted in the administration of various sectors of Ghana's economy. When proper mechanisms are set in place, according to Mensah. The co-founder of the ABM Attorneys, it would be easy for the nation to track records dating back to the independence period. What companies (especially state-owned enterprises) must do is maintain proper market controls, he continued. They need adequate internal regulation in order to function within the legal system and perform business (Byiringiro and Mahabaleswara, 2016).

However, in Rwanda there have been a few instances where the execution of these internal controls has been ineffective. Niyonshimye, (2013) a senior research fellow continues to keep tracking of similar cases of public funds within government corporations. He pointed out that one of Rwanda rooted governance bottlenecks when it comes to internal regulation is a lack of efficient financial reporting, which exacerbates the public corporations' poor internal control structure. Despite these scrubbing concerns, there is a lack of understanding of internal controls activities and their efficacy in Rwanda, especially in the public sector, necessitating the analysis of internal control activities and effective of financial management at RALGA. Over the years, many efforts have been made to eliminate financial inaccuracies in Rwanda public sector

According to the study conducted by Barr and McClellan, (2018) on tracking inventory at a regular basis often means that it adheres to the monitoring documents, found that RALGA organization tends to get the control systems, actively participates in monitoring and supervision of the activities of the technical training organization, all the activities of the Institution are initiated by the top level management, that the internal audit department is not efficient, is understaffed, does not conduct regular audit activities and does not produce regular audit reports although the few reports produced by the internal audit department address weaknesses in the system. It was from this context; the current study was important to find out the effect of internal control system on financial performance of public entities Rwanda: A case of Rwanda Association of Local Government Authorities (RALGA)

2. Review of Literature
Internal Control Activities

Any business faces risks that might prevent it from achieving its goals. Some are under the organization's supervision, while others are not. Internal controls however are any of the measures taken by the organization to avoid, identify, or correct certain risks that are under its jurisdiction. Internal controls include management checks such as reviewing financial reports; limiting access to unauthorized individuals; doing reconciliations in positions that should ideally be the same, such as a cash count to the actual cash; physical verification, such as of fixed assets; authorizations and approvals of transactions; use of standard documents as well as segregation of duties (Caleb *et al*, 2019).

Internal control is a continuous action or a sequence of activities, not just an occurrence or a procedure, that occurs in every business activity and should be a fundamental part of every business organization rather than an add-on structure. Individuals make the internal control mechanism work, as top-level management is largely responsible for successful internal control, with all other players playing important roles. No matter how well planned and executed internal controls are, they can only offer fair security, not utter assurance (Brigham and Ehrhardt, 2013).

Internal control is a mechanism influenced by workflow and jurisdiction, as well as corporate structure, individuals concerned, and management information systems, both of which are intended to assist an organisation in achieving certain aims or goals. It is the method of using, tracking, and evaluating an entity's usable or assigned capital. Internal management is respected for its role in identifying and avoiding theft as well as preserving the entity's accessible tangible and intangible capital. Machinery and real estate are examples of tangible wealth. Intellectual property, like patents, is an example of an intangible assets (Baharud-din, Shokiyah and Ibrahim, 2014).

Internal management is critical in an organization's attempts to accomplish its priorities and objectives, particularly in the public sector. The public sector is made up of non-profit organisations, ministries, offices, and institutions that aim to fulfill and provide the country's citizens' social needs, such as health, healthcare, and education (Udeh and Nwadialor, 2016).

3. Materials and Methods
Research Design

This research used descriptive survey as its research design, which examines the effect of internal control system on financial performance of public entities Rwanda conducted in Rwanda Association of Local Government Authorities (RALGA). Research design

can be classified in different ways. According to Rezigalla, (2020). The descriptive research design serves as a blue print of a project and this links the data collection and activities to the research questions ensuring that the research aim and objectives are achieved. For a research study to be credible, useful and feasible, the design should be implemented. This study was a mixed method research study meaning it combines the use of quantitative and qualitative research to confirm previous research and explore new areas as well as to observe the internal control system

Target Population

The target population of the research was mainly consisted of the Finance and accounting department as well as the administrative staff of Rwanda Association of Local Government Authorities (RALGA). However, not all staff members of the Rwanda Association of Local Government Authorities (RALGA) were relevant to the study. Based on the literature review and understanding what internal controls are, a researcher focused on the employees who are directly related to internal control activities and they were in the departments of Finance and accounting as well as Human Resource. The population was composed of both male and female of different levels of education and ages as well as experience.

Table 3. 1 Target population

Category	Population
Administrative staff	6
Finance/audit/accountant	9
Human resource	1
Staff members	23
Consultants	209
Total	248

Source: RALGA (2022)

Sample size

It is not possible to use the whole population due to a number of reasons, including limited time given by the institution for completion of the research. It is therefore possible to select a group of representatives through a variety of research techniques in the study. A portion of the target population referred to as a sample (Andrew and Orodho, 2014). This means a finite part of a statistical population whose properties are studied to gain information about the whole population is a representative sample.

Stratified sampling was used in this research, since the parent population was made up of sub-sets of known size. The subsets were the various departments at Rwanda Association of Local Government Authorities (RALGA), which was involved to ensure that the results are proportional, and a representative of the whole. The purposive sampling technique was used for the study. A purposive sample is a non-probability sampling technique used for a research work on the basis of the objective of the study. It is also known as

subjective sampling or selective sampling (Andrew and Orodho, 2014). The purposive sampling was used because of its relevance to the study.

In order to determine the sample size, the study employed the formula by Alain Bouchard, that illustrates that for a population between 100 and 500 individuals, the sample can be 285 with an assumed error of 5% and 95% within precision of 99 of 100 (Mualuko, Mbabazi and Shukla, 2016). This can be elaborated in the following numbers:

N = total population size is 248

No: Sample size when the population size goes towards infinite is 285

Nc: Corrected sample size

$$Nc = \frac{N \times No}{N + No} = \frac{248 X 285}{248 + 285} = 132.60 \cong 133$$

Thus, the sample size was 133 individuals in total including administrator staff.

The respondents from RALGA were well identified in Table3.2.

Table 3. 2 Distribution of Sample size of the Study

Category	Population	Sample size
Administrative staff	6	6
Finance/audit/accountant	12	10
Human resource	1	1
Staff members	233	116
Total	248	133

Source: RALGA (2022)

In this illustration, one hundred and thirty-three respondents among 248 was purposively selected and studied. To collect quantitative and qualitative data and formulated questionnaires was administered to one hundred thirty-three (133) purposively selected including administrative staff, finance/audit/accounting, human resource and staff.

Sampling Techniques

In this research utilized three techniques to get a sample size of the population. These techniques were purposive sampling which was deliberately focused on Finance and accounting department as well as the administrative staff of Rwanda Association of Local Government Authorities (RALGA). According to Mualuko, Mbabazi and Shukla, (2016). Purposive sampling technique allows the researcher to target a group of people supposed to have reliable contribution for the study. The simple random sampling was used to get a sample from finance and human resource. Also, representative samples of staff was selected randomly. The domination of simple random sampling lies on the fact that respondents are given equal chance to participate in the study. About data from RALGA administrative staff, all was sampled to give out the all information needed about effect of internal control system on financial performance of public entities Rwanda. The sampling technique was used in this study was therefore the same for each category of population. Participation in the survey was voluntary, although a motivation talk from the RALGA administrative staff was carried out to give confidence the participants in the research and ensure confidentiality of their responses.

Procedures of Data Collection

A well-developed questionnaire helped a researcher to answer all research questions and link them with the independent variables so as to meet the research objectives. The questionnaire had one sets of questions, which targeting the relationship between internal control activities and effective of financial management at Rwanda Association of Local Government Authorities (RALGA). The number of

Socio - demographic characteristics of respondents

This section of socio-demographic characteristics indicated the frequencies of socio-demographic

questionnaires to be administered was calculated referring the Alain Bouchard formula. These was distributed and administered to the respondents by the researcher in person and picked later and this was preferable because it is found to be easy to present and collect.

Data Analysis

The data was gathered from the questionnaires and used descriptive statistics to analyze the data in order to have clarity and easily explain the study. The data was analyzed using simple percentages, Tables, and correlation coefficient. Thus, descriptive analysis was also used in the analysis of the questionnaires while the information obtained from the interviews was presented in qualitative form. Questionnaires was administered to help in the quantitative methods which emphasize objective measuring and statistical analysis of the data collected. Interviews were conducted to help explore more and gain an understanding of underlying reasons and opinions that improved the insight of the research.

Analysis of qualitative data from questionnaires was converted into written texts. This procedure was pursued by selecting, coding, simplifying units into themes, making clusters of partitions and condensation of data in order to sharpen, sort, discard and organize in such a way that final conclusions was drown.

As indicated by Abdulghani, *et al*., (2014) quantitative data analysis is a process of presenting numerical data. Quantitative data in this study used both descriptive and inferential statistics, hence the process involved cleaning of data to make sure that the data was correctly identified in order to gain knowledge about the data, lists of data was made to produce descriptive statistics. For example, means and standard deviations was used. Furthermore, graphics such as histograms and pie charts to show the study's data distribution was employed. In calculating coefficient measuring strengths and coefficient that describe percentages or variance the use of Statistical Package for Social Sciences (SPSS 20.0) was employed

4. Results and Discussion

characteristics especially sex, age, education and profession experience.

Table4. 1 Presentation of socio-demographic characteristics

Gender	Frequency	Percent
Males	73	54.9
Females	60	45.1
Total	133	100
Age		
20-30 years	34	25.6
31-40 years	76	57.1
41-50 years	23	17.3
Total	133	100
Education level		
Post graduate	37	27.8
Bachelor	79	59.4
Diploma	17	12.8
Total	133	100
Experiences		
0-2 years	41	30.8
2-4 years	59	44.4
4 years and above	33	24.8
Total	133	100

Source: Primary Data (2022)

Table 4.1, indicated that the males were represented by 54.9% of respondents while females were 45.1% of respondents. The group of age is presented in the Table 4.1. The respondents with 20-30 years was 25.6%, the respondents (31-40 years) was 57.1% and the respondents with 41-50 years was 17.3%.

The education level presented are postgraduate (27.8%), bachelor (59.4%) and Diploma (12.8%). The findings shown that the experience varied between 0-2 years (30.8%), 2-4 years (44.4%) of respondents and 4 years and above 24.8%.

Internal control activities and financial performance in Rwanda Association of Local Government Authorities

Table4. 2 Presentation of the effect of internal control activities on financial performance

Variables	SD (%)	D (%)	N (%)	A (%)	SA (%)	Mean	STD
Auditing standards and the offices/sector's policy.	9.8	6.8	1.5	49.6	32.3	3.88	1.219
Internal control activities without the interference	6.8	23.3	3.8	43.6	22.6	3.52	1.259
Effective internal control activities are actually base line in the internal control system	2.3	12	1.5	51.9	32.3	4.00	1.015
Board of directors, management of an entity, and other staff, to provide internal control activities	5.3	10.5	4.5	38.3	41.4	4.00	1.168
Examples of financial reporting controls	14.3	25.6	6.8	31.6	21.8	3.21	1.409

Source: Primary Data (2022)

Table 4.2 presented the findings of internal control activities and financial performance in RALGA.

The scope, time and extent or auditing procedures based on the auditing standards and the offices/sector's policy agreed by 49.6% of respondents, All internal control activities without the interference or influence of another party or from the office/sector agreed 43.6% of respondents, Effective internal control activities are actually the very base line in the internal control system agreed this with 51.9% of respondents. 41.4% of respondents strongly agreed that board of directors, management of an entity, and other staff, to provide fair certainty that the achievement of a corporate goal in terms of financial reporting reliability, quality and quality of operations, and compliance with relevant laws and regulations will be accomplished and 31.6% of respondents agreed that Authorizations and licenses, verifications, asset protection, and reconciliations are all examples of financial reporting controls.

Relationship between variables

To establish whether there was any statistical relationship between effects of internal control activities and the financial performance in Rwanda Association of Local Government Authorities. Regression analysis between the scores of the two variables was conducted. The SPSS output shows the correlation results.

Table4. 3 Internal Control activities and financial performance

Model Summary

Model Summary						
Model	R	R Square	Adjusted R Square	Std. Error of the Estimate	F Change	Sign. Change
1	.950[a]	.902	.901	.320	1203.198	0.000

Source: Primary Data (2022)
a.Predictors: (Constant), Internal control activities

R square is the coefficient of determination which illustrates the variation in the dependent variable is due to changes in the independent variable. From the findings in Table 4.3.1 above the value of R square was 0.950, $P<0.05$ an indication that there was variation of 90.2% on the financial performance of RALGA is due to changes in internal control activities.

Table4.3. 1 ANOVA

ANOVA[a]					
Model	Sum of Squares	df	Mean Square	F	Sig.
1 Regression	123.216	1	123.216	1203.198	.000[b]
Residual	13.415	131	.102		
Total	136.632	132			

Source: Primary Data (2022)
a. Dependent Variable: Financial performance
b. Predictors: (Constant), Internal control activities

From the ANOVA statistics, the processed data, which is the population parameters, had a significance level of 0.000 which shows that the data is ideal for making conclusions on the population's parameter as the value of significance (p-value) is less than 5%. The significance value was less than 0.05, an indication that the model was statistically significant.

Table4.3. 2 Coefficients of internal control activities and financial performance

Coefficients[a]					
Model	Unstandardized Coefficients		Standardized Coefficients	t	Sig.
	B	Std. Error	Beta		
1 (Constant)	.820	.094		8.697	.000
Internal control	.168	.005	.950	34.687	.000

Source: Primary Data (2022)
a. Dependent Variable: Financial performance
For the model $Y = a + bx$ is explained from the results in such a way that; financial Performance (Y) $= 0.830 + 0.168X$ (X: Internal Control activities). This implies that one-unit increase in financial performance is associated by 0.168 units of internal control activities. At 5% level of significance and 95% confidence level, internal control activities had a 0.000 P-value. Therefore, the RALGA should engage in provision for internal control activities practices. There is high potential of the financial performance of the organization increasing.

The respondent found that effective internal control activities are actually the very base line in the internal control system, this is also accepted by Shabri, Saad, and Bakar, (2016) noting that internal control is a major part in managing an organization which is helps manager achieved desired results.

The respondents strongly agreed that board of directors, management of an entity, and other staff, to provide fair certainty that the achievement of a corporate goal in terms of financial reporting reliability, quality and quality of operations, and compliance with relevant laws and regulations will be accomplished, this is supported by Zulkifli, Alagan and Ibrahim (2014) reporting that internal audit unit has the responsibility to determine internal control activities and is in place by reviewing policies and practices in the organization.

5. Conclusion

Effective internal controls and defining the individual(s) responsible for conducting a control activity is segregation of duties, which prevents one person from controlling all phases of a transaction and the respondents agreed that there is procedures of dealing with detecting, evaluating, as well as reacting to risk. Therefore, there is significant relationship between internal control activities and financial performance in Rwanda Association of Local Government Authorities

Acknowledgments

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