KAMPALA INTERNATIONAL UNIVERSITY
SCHOOL OF BUSINESS AND MANAGEMENT
RESEARCH PROJECT

THE ROLE OF INTERNAL CONTROL SYSTEMS ON BUSINESS PERFORMANCE A CASE STUDY OF KENYA COMMERCIAL BANK TRANS-NZOIA DISTRICT- KENYA

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A PROJECT SUBMITTED TO THE SCHOOL OF BUSINESS AND MANAGEMENT IN PARTIAL FULFILLMENT OF THE REQUIREMENT FOR THE AWARD OF A DEGREE OF BACHELORS OF BUSINESS ADMINSTRATION FINANCE AND BANKING - OPTION.

DECEMBER: 2007

DECLARATION

I LINAH MUKAMI NJIRU, declare that this research report is my own work and that it has never been submitted before by any other researchers in any other higher learning institution or university for any purpose.

Signature ..... Date 23/09/08

Linah Mukami Njiru

APPROVAL

This research report has been submitted to the school of Business and Management of Kampala International University after being supervised and approved by

Signature .....

MICHAEL MUSANA

Date .....22/09/08.....

DÉDICATION

This work has been dedicated to my parents, brothers, friends and to my supervisor Mr. Musana for his tireless contribution for the success and development of this research project. I also thank my dear parents and brothers for the financial support in my research.

God bless you all.

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ABSTRACT

The study was aimed on the internal control and the organization's effectiveness in the accounts. A sound internal control system is important as it enables it to carry on the business of the enterprise in an orderly manner, safeguards the organization's assets and ensures completeness and accuracy in their records to achieve high performance.

The study aimed at documenting and evaluating the adequacy of internal control and its performance of Kenya commercial Bank by comparing them with a sound theoretical framework and thereafter offering recommendation for its improvement. Both primary and secondary techniques of data collation were used.

During analysis of data, quantitative, qualitative and descriptive techniques such as graphs, pie charts were used. Controls in the areas of cash, wages and salaries, debtors were examined. The data was eventually analyzed by comparing with an ideal system which exhibited that some controls were weak and other strong.
For effective and sound internal control system which will ensure an organizational good performance, the research recommended that the company should review its existing control measures and come up with a workable plan to reinforce them.

According to my findings it shows that internal control systems play an important role in the banks performance though. According to the researcher there is a probability of cash controls been weak while there is a reasonable strong measures being taken to control wages and salaries as well as debtors. However more needs to be done to reduce the risk of fraud and any malpractices which can lead to losses. Hence an internal control plays a major role in measuring and evaluating banks performance.

CHAPTER ONE

1.0 INTRODUCTION

Despite the fact that an internal control system is expensive to install and maintain it has gradually evolved over the years. The greatest development occurred In the mid of 1940's owing to the complexities of the business techniques that has not only contributed to business development but also the increased size of businesses units which has encouraged the adoption of the methods which while increasing efficiency also acts as safeguards against fraud and errors.

Internal control systems have achieved great importance in the recent years. It ensures that the company's personnel are efficiently utilized, ensure compliance with the laid down procedures and policies to ensure that the company runs in an orderly manner. Therefore all entities have some sort of accounting systems with some internal control of the transactions and other business activities.

Internal control system is not only an internal check and internal audit but the whole system of controls, financial or otherwise (non-financial) instituted by the organization to ensure that the business of the company run in an orderly manner. The definition of internal control is therefore divided into financial internal controls and non financial (administrative) internal control.

Financial internal controls pertain to financial activities and may be exemplified by controls over the organization's cash receipts and payments, financing operations and the organizational management of receivables and payables. Non financial internal controls on the other hand deal with activities that are not directly financial in nature. This includes control over personnel and organization's operations, fixed assets control, and control over the laid down procedures and policies.

In recent years this aspect of internal control systems has greatly achieved significance. It is designed to safeguard the organizations' assets against misuse, ensure that the organization's laid down policies are complied with ,ensure that the personnel force is efficiently utilized ,the company runs in an orderly manner and ensure maintenance of reliable records which are a source of information necessary for managerial decision making process. It's evident therefore that the adoption of a sound internal control system is not only helpful to management but also to the external auditors and users of financial information and other organizational records.

Banking institutions are for example formed to promote the economic interests of the public and offer relevant banking services. But the scarcity of resources, mismanagement of the depositors' funds and poor records can inhibit the attainment of the said objectives. Separation of ownership from management of the daily duties of the business threatens these objectives.

Both administrative and accounting controls are an integral part of the internal control design, implementation and operation which are functional to the business environment. No system should be utilized without adequate internal controls. In addition the absence of a critical internal control systems has left many organizations to fraudulent activities, provision of un -reliable data which is of little use in assisting management in decision making in harmony with the organization's objectives. Therefore to ensure efficient utilization of resources a sound internal control system is needed

1.1 Background to the case study

The history of the Kenya Commercial Bank date back to 1896 when its predictors the National Bank of India opened a small branch at the coastal town in Mombasa. In 1958 Grindlays Bank of Britain merged with the bank of India to form a national and Grindlays bank.

In the 1970's the government of Kenya acquired 60% shareholding in national and Grindlays bank and renamed it Kenya Commercial Bank. In 1976 the government

acquired 100% of the shares to take control of the largest commercial bank in Kenya. The government has over the years reduced its shareholding to its current 26% and the public owning 74% of the Kenya commercial bank shares.

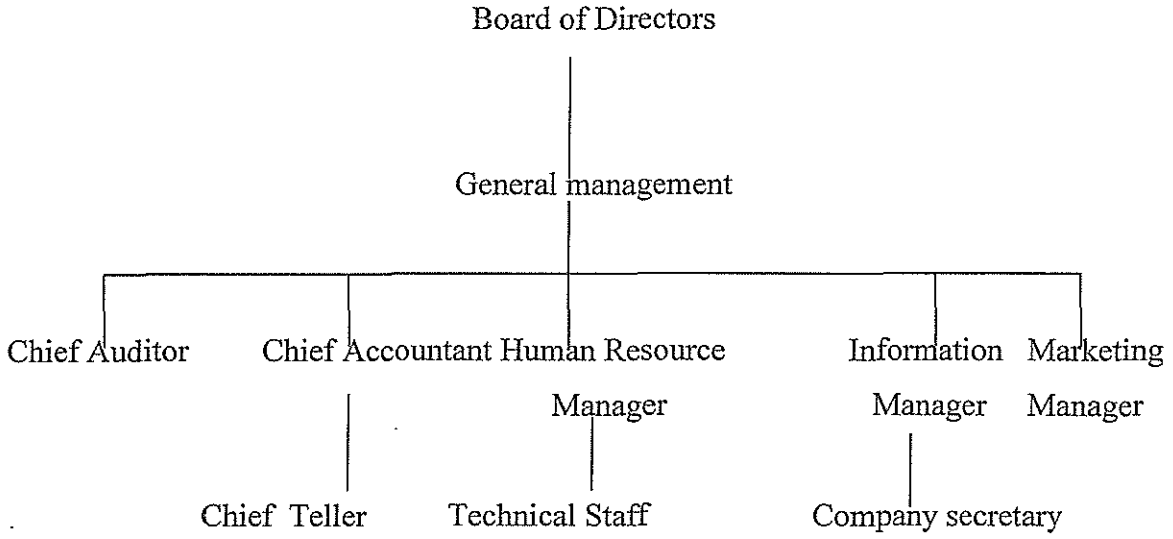
A wholly owned subsidiary savings and loans (k) limited was acquired in 1972 to provide mortgage finance. In 1997 another subsidiary Kenya Commercial Bank (TZ) _ was incorporated in Dares-lam to provide banking and financial services and to facilitate cross border trade within east Africa region.

Since inception Kenya Commercial Bank has endeavored in provision of banking services geared towards meeting the ever changing customer needs. This has ensured consistence growth in customer deposits that have in return provided a strong recover for steady growth in customer borrowings every year.

1,1.1 Current Developments

Since incorporation the bank has achieved tremendous growth to emerge as a leader in Kenya's banking and financial sector. In 1970 the bank had thirty two full time branches of which twenty five were located in rural areas, five in Nairobi and two in Mombasa. Today the Kenya Commercial Bank groups has the widest network in the country comprising of ninety five full time branches and thirty five satellite branches all of which represents fifty five percent of the total banking outlets. The company's mission statement is to provide a whole range of retail banking and financial services apart from acting as agents of development. The group recently opened up branches in the southern Sudan as one of the ways of development. In recognition of the need to strengthen the interdependence between domestic and external economies the bank has continued to expand working arrangements with other countries. To-date the bank has over four hundred correspondent banks throughout the world.

ORGANISATIONAL STRUCTURE OF KENYA COMMERCIAL BANK LIMITED TRANS-NZOIA DISTRICT KENYA -2006



SOURCE: DATA SURVEY 2008

1.2 Statement of the problem

Organizations both small and large, profit making and non profit making are faced with different problems. Among these problems are misappropriations of cash, fraudulent manipulation of accounts, embezzlement of funds and suppression or omission of effects of transactions from records or documents. All these have made it difficult for business enterprises-cooperatives in particular, incapable of controlling their financial obligations. The situations continues to prevail due to factors which includes a complex corporate structure whose complexity does not seem to be warranted ,high turnover in the key accounting personnel and the unusual transactions at the end of the year. Business transactions do not take place as per the Generally Accepted Accounting Principles (GAAP). The assets are not properly safeguarded; records are incomplete and inaccurate thus providing inadequate and unreliable information for the preparation of financial statements and reports. Despite attempts by most organizations to come up with good

policies to streamline the business operations through the initiative of the reform program, less has been achieved and therefore a likelihood of poor performance unless a good and effective financial practices are put in place.

A sound internal control system helps organizations to prevent frauds, errors, correct and complete records of all transactions and minimize wastage of the organization's resources. It ensures custody of fixed assets, provides assurance to the management on the dependability of accounting data, eliminates suspicion and helps in maintenance of adequate and reliable accounting records.

This research therefore aimed at establishing the effectiveness of internal control systems on record management in Kenya Commercial Bank Limited-Kenya.

1.3 Research objectives

The research intended to achieve the following objectives:

- To establish effectiveness of the existing internal control instruments in Kenya Commercial Bank Limited -Kenya
- To evaluate the adequacy of existing internal control system of Kenya Commercial Bank Limited based on a theoretical sound internal control system.
- To suggest some methods and devices to improve on the organization's internal control

1.4 The purpose of the study

The purpose of the study was to evaluate the effectiveness of the existing internal control systems of Kenya Commercial Bank Limited and its effects on the record management of the organization.

1.5 Research questions

- How effective are the organization's internal control systems?
- What are the instruments of internal controls employed by the organization?
- What is the impact of internal control systems on financial records of the organization?
- What are methods and devices to improve on the organizations internal control systems?

1.6 Research hypothesis

There is a significant relationship between the effectiveness of the internal control system and attainment of the organizational goals.

1.7 Scope of the study

The research basically aimed at documenting and evaluating the internal control systems of Kenya Commercial Bank Limited. This was done by comparing it with the theoretically sound internal control systems and thereafter a recommendation for improvement of the same. The study therefore aimed at the types of internal controls employed by the organization. The targeted controls include; cash control, purchase control, wages and salaries control, debtors control, fixed assets control and internal audit control. The researcher also considered other factors such as employee relations and annual leaves that were not considered by the previous researchers.

1.7.1Geographical scope

The research was carried out in trans-Nzoia district mainly in Kenya commercial bank which is located in trans-nzoia shopping centre.

1.7.2 Time scope

The time of the study is limited to 4 months (January to May 2008)

1.8 Significance of the study

a) To study will help me to build my ability and acquire more knowledge on internal control system as well as applying IAS practically thus integrating the theory and practical.
b) The study will help in the identification of the risks associated in internal control management.
c) The study will help me to know how banking institutions carry out their business for future references.
d) The study will help in identifying the relationship between internal controls and business performance.
e) The study will point out the key areas ignored in the internal control system as the ways of improving the quality of their internal controls system.

f) The study will be a good base for policy makers in different organizations including the government.

g) The study will act as a review in implementing of various internal controls in their institution.

h) Partial fulfillment of the undergraduate degree.

CHAPTER TWO

LITERATURE REVIEW

2.0 Introduction

Banking is interesting enough to merit a 118 page booklet entitled *History of the Eighties—Lessons for the Future* first published in 1997. This booklet is the culmination of a massive FDIC study project which included participation from bank regulators, academics and the FDIC's Division of Research. Ricki Helfer, then-Chairman of The FDIC, opened her keynote address with these words, "It has been said that experience is a tough teacher—first you get the test, then you learn the lesson." From 1980 through 1994 1,617 banks failed or received financial assistance from the FDIC. During the same period 1,300 savings and loans failed. L. William Seidman, Publisher, CNBC Chief Commentator and former Chairman of both the FDIC and the RTC asked, "How can this wealth of experience be used to give us a transformation strategy for core competence in the financial system of the next decade?" He answers by saying, "internal control will be the most important requirement of the day. Constant vigilance and the development of even more sophisticated systems will be the challenge to both the financial institutions and their regulators. The search for the most effective backup system of internal control will be the never-ending duty of those in charge.

The present Provisions establish the objectives of the bank's internal control, the main principles of its organization, and minimum requirements established for banks. Banks may establish more detailed and tight requirements for their systems of internal controls

The Basel Committee is distributing this paper to supervisory authorities worldwide in the belief that the principles presented will provide a useful framework for the effective supervision of internal control systems. More generally, the Committee wishes to emphasise that sound internal controls are essential to the prudent operation of banks and to promoting stability in the financial system as a whole. While the Committee recognises

that not all institutions may have implemented all aspects of this framework, banks are working towards adoption.

The guidance previously issued by the Basel Committee typically included discussions of internal controls affecting specific areas of bank activities, such as interest rate risk, and trading and derivatives activities. In contrast, this guidance presents a framework that the Basel Committee encourages supervisors to use in evaluating the internal controls over all on- and off-balance sheet activities of banks and consolidated banking organisations. The guidance does not focus on specific areas or activities within a banking organisation. The exact application depends on the nature, complexity and risks of the bank's activities.

In his paper titled "Internal Control, Fraud Prevention and Security Management," the Head of Internal Control of the First Bank of Nigeria Plc, *Ademola Adewale* observed that the greatest contributor to fraud occurrence in the Nigerian banking industry were the employees.

Other factors mentioned were absence of fraud detection mechanism, collusion between fraudsters and bank staff, mis-match between the competence level of bank staff and the nature of products or services offered, societal acquisitive instinct and insatiable lust for wealth, inadequate deterrent punishment for fraudsters, external influence on bank staff and delay in prosecuting fraudsters.

Yet, other factors included inadequate or lack of training, circumvention of rules and regulations, porous recruitment system, over-centralization of authority, poor security features on bank instruments or documents, industry inertia and lack of discipline.

ISA 315- understanding the entity and its environment and accessing the risk of material mis- statement defines the internal control system as the process designed and affected by these charged with governance, management and other personnel to provide reasonable assurance about the achievement of the entity objectives with regard to reliability of financial reporting effectiveness and efficiency of operation and compliance with applicable laws and regulations. Internal control consists of:

- Control environment.
- Entity risk assessment process
- Information system including the related business processes relevant to financial reporting and communication
- Monitoring of controls.

The statement of Auditing Standards No. 30'Accounting and Internal Control Systems and Audit Risk Assessments-defines internal control systems as the one that comprises the control environment and control procedures. It includes all policies and procedures adopted by the organization's management to achieve their said objectives of ensuring orderly and efficient conduct of its business, including adherence to its internal policies, safeguarding of assets, prevention and detection of errors and fraud, the accuracy and completeness of accounting data and records and timely preparation of financial reports. America Institute of Certified Public Accountants (1984) defines internal control as "comprises the plan of 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, promote operations efficiency and adherence to prescribed managerial policies".

Batra et al (1992) said that internal controls involves actions taken within the organization to protect the assets against improper assets distribution, assures the accuracy and dependability of all financial and operating information, judge operating efficiency and measure adherence to the organizational established policies. He further noted that designing and maintaining of the internal control system is the responsibility of the management. But it's a matter of great concern for auditors although they have no authority, to recommend and prescribe that certain rules and procedures be adopted by the organization. They may be involved to assist management in designing, installation and modification of the system.

According to *Official Gazette "Valstybės žinios", 2001, No. 107-3894* (Bank of Lithuania) The present Provisions establish the objectives of the bank's internal control, the main principles of its organisation, and minimum requirements established for banks. Banks may establish more detailed and tight requirements for their systems of internal controls.

Batra et al (1992) finally emphasized that in order to arrive at the conclusion on the internal control system's effectiveness; answers to the following three questions provide the solution to accomplish the effective internal control systems: What are the procedures normally followed? How far are the prescribed procedures effective in creating a good and satisfactory internal control of the organization's records? does the organization actually follow the prescribed procedures?

Milichamp (1999) said that the internal check and internal audit are the two broad areas that fall under the scope of internal control systems. He defined the internal audit as an independent appraisal of activities within an organization for the review of accounting, financial and other business practices. This helps the management to evaluate on the performance and efficiency of various established procedures. It provides information whether the established procedures are followed or not.
Manasseh (1990) defines internal check as a continues audit carried out by staff itself by means of which work of each employee or individual is independently checked by other members of the staff.

Price et al (2003) noted that accountants recommend that all businesses no matter their size, establish an effective internal control procedures. These procedures are designed to protect the resources and financial records of the business. Internal controls also benefit employees because they commit the temptation to misuse the assets. Internal controls pinpoint responsibility which prevents suspicion from falling on honest employees.

William Kenney (2000) claims that internal control can improve the quality of information for management but it may not be a complete assurance service. It's only a

process that is implemented by the organization's board of directors and management to provide reasonable assurance regarding effectiveness and efficiency of operations and financial records and compliance with the applicable organizational policies and regulations

William Kenney (2000) comments further that management wants a high level of assurance that each of its information processing and related record maintenance is carefully and competently applied in an un-biased fashion. Management also wants that its assets are protected in order to fulfill its steward obligation to stockholders. Internal control over business measurement thus helps to achieve real-world activities for management decision making and it's periodically compared with real world counterparts.

Emilsyee (1993) did a case study on internal control of the Nyayo Bus Services Corporation –Nairobi. Its objective was to document and evaluate the internal control systems of the corporation and provide recommendation towards the improvement of the existing internal controls. He used personal interviews to gather data and evaluated the same by comparing it with a sound theoretical framework of internal controls. He found out that fairly good internal controls were in place in the cash cycle. The researcher however established that the stores department had weak controls due to the less adequate segregation of duties and poor record keeping.

William and Colby (1978) studied internal controls of small businesses and concluded that there are contrasting factors affecting accounting controls in large and small business. They went on to suggest ways in which such controls can be strengthened. They observed that auditors should be too wary of too much reliance on executive controls in a small business. Instead the auditors should recognize the need for designing other audit procedures that will compensate for the dominance of the executive controls in the business setting.

1992, the Committee of Sponsoring Organizationsof the Treadway Commission (COSO)2 outlined five essential components of any internal control system. The five components are:

1. control environment
2. risk assessment
3. control activities
4. accounting, information, and communication systems, and
5. self-assessment or monitoring

Each component is discussed below in more detail and is accompanied by a series of questions that address fundamental control activities. While this list is not all-inclusive, negative answers to these questions can help identify fundamental internal control weaknesses.

According *to Bank of Lithuania* the major elements of control of the bank internal control shall consist of five interrelated elements:

- The management oversight and the control culture
- risk recognition and assessment;
- internal control procedures and segregation of staff duties;
- information and communication;
- Assessment of internal control system and correcting deficiencies.

The effective functioning of these elements is essential in achieving the principal objectives of internal control.

2.1 PRINCIPLES FOR INTERNAL CONTROL SYSTEMS

The main principles of this instruction are derived from: the A Framework for Internal Control Systems in Banking Organizations, Publication No. 40, dated September 1998, of the Bank for International Settlements, Basel Committee on Banking Supervision and are supplemented with specific requirements of the CPO for implementation by banks. Through this instruction, the CPO does not prescribe in detail the manner in which each individual bank should implement its own system of internal controls. The applicability of the main principles of this instruction to each individual bank depends on the nature,

complexity and risks of each bank's activities. However, the CPO requires that each bank have an appropriate system of internal control, which adheres to these fundamental principles.

A. Management Oversight and the Culture of Control

According to the Basel committee of banking Governing Board is responsible for:

(1) Approving and periodically reviewing the overall business strategies and policies of the bank

(2) Understanding the major risks faced by the bank, setting acceptable levels for these risks, and ensuring that bank administrators take the steps necessary to identify, measure, monitor and control these risks;

(3) Approving the organizational structure;

4) Ensuring that bank administrators monitor the effectiveness of the internal control system. Board of directors is ultimately responsible for ensuring that an adequate and effective system of internal controls is established and maintained.

Pursuant to Section 19.1 of the Regulation, the audit committee can assist The Governing Board In fulfilling these responsibilities; however, pursuant to Section 16.5, the Governing Board and its members cannot delegate their responsibilities to others.

Senior bank administrators are responsible for:

(1) Implementing strategies and policies approved by the Governing Boards;

(2) Developing processes that identity, measure, monitor and control risk incurred by the bank;

(3) Maintaining an organizational structure that clearly assigns responsibility, authority and reporting relationships;

(4) Ensuring that delegated responsibilities are effectively carried out;

(5) Setting appropriate internal control policies;

(6) Monitoring the adequacy and effectiveness of the internal control system.

The Governing Board and Senior bank administrators are responsible for promoting high ethical and integrity standards, and for establishing a culture within the organization of the bank that emphasizes and demonstrates to all levels of personnel the importance of internal controls. Bank personnel must be informed of, and held responsible for, their role in the internal controls process.

B. **Risk Recognition and Assessment**

According to **Fernando De Peralto** all material risks that could adversely affect the achievement of the bank's goals should be recognized and continually assessed. This assessment should cover all risks facing the bank and the consolidated banking organization (credit risk, country and transfer risk market risk, interest rate risk, liquidity risk, operational risk, legal risk and reputation risk). Internal controls should be revised to appropriately address new or previously uncontrolled risks.

C. Control Activities and Segregation of Duties

According to Central Payments Office of East Timor

Sections 23.1, 27.1(e), and 31.1 of *Regulation No. 2000/8* on *Bank Licensing and Supervision* Control activities should be an integral part of the daily activities of a bank. An appropriate control structure should be established with control activities defined at every sector of the bank's operations. The control structure should include:

a) Top level reviews -An adequate management information system should exist for the Governing Board and senior bank administrators to review the bank's progress toward established goals.

b) Appropriate activity controls for each unit and sub-unit of the bank - Administrators in charge of units and sub-units of the bank should

2.1 Types of internal control system

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

a. Plan of organization

According to *Saleemi (1989)* it is an organization charts which shows the organization structure the purpose of drawing an organizational plan is to show how the organization is divided into departments and sections and the responsibilities charged thereof. Authority and responsibility is clearly defined. Employees perform their duties according to organizational plan on allocated duties and responsibilities it also identifies lines of reporting for all aspects of business operations. The plan of organization therefore is needed for effective internal control.

Spicer and Pegler (1978) referred it as a control of the organization personnel. It defines who is who in the business. This therefore acts as a guiding tool to avoid duplication of efforts, avoid conflicting duties, facilitate delegation of duties and harmonize operations in the business. This further ensures that a chain of command and flow of authority is respected and followed.

b. Segregation of duties

Adewale said that despite banking consolidation, organisational structure and reporting lines of some banks lacked clarity and this way provided opportunities to employees to cover up fraud and losses from unauthorised activities.

The head of internal control also mentioned inadequate segregation of duties as a challenge. He also explained that due to high remuneration by some banks, fewer

numbers of staff were employed to carry out multiple tasks that should be handled by separate persons.

Thus, he said that segregation of duties was lacking in those banks, which created avenue for employees with such exposure to defraud.

As per *Millchamp* (1999) the term segregation of duties is used to mean the internal duties. One of the prime means of control is the separation of duties which would if combined enable one individual to record and process a complete transaction. Segregation of duties reduces risks of intentional manipulation of accounts and increases the element of checking. Division of duties thus makes frauds more difficult to be committed because one transaction is completed by different employees.

Manasseh (1990) noted that any internal control system will only be strong if duties and responsibilities are segregated. This reduces the risk of frauds and errors. It also increases efficiency in the organization's operations due to specialization and facilitates supervision. The duties which must be segregated are recording, authorization, execution of duties, custody of organization assets and system development for computer operations.

c. Control of documents

As per *Batra et al (1992)* control of documents involves the control of the organization's sensitive documents which includes receipts, cheques, local purchase orders, debit and credit notes and payment vouchers. These documents must be handled by a responsible person and should be pre-numbered to ensure control and minimize misuse. They must be kept under key and lock and must be controlled from the central point.

d. Physical controls

De Paula et al (1990) noted that the internal controls also require that assets of the business like machinery, equipment, motor vehicles and cash should be kept safely. The access to these assets should be limited to authorize personnel only. The procedures designed and security measures taken for safeguarding these assets should be

comprehensive and adequate. For instance cash and stock should be under the custody of somebody who is reliable. The physical controls common in businesses are employment of security personnel, alarm systems, strong electrified gates, strong rooms and safes, strong fences and security lights.

This involves the actual process by which an asset is used for its intended purpose and ensuring it contributes a lot to the organization before it can be disposed or written off. It involves securing assets against and misuse and physical attack. The objectives of physical controls are to ensure proper authorization, ensure assets are properly maintained and used rightfully, proper accountability and record management of these assets.

e. Competence of staff

According to *Spicer and Pegler (1978)* the proper functioning of any system depends on the competence and integrity of those operating it. The staff employed in the organization should be competent and experienced.

Manasseh (1990) said that the organization should employ qualified, experienced, competent and motivated employees who have interest in what they are doing and the organization should regard its employees as its valuable assets. These employees must be reliable and responsible in order to ensure efficiency in the business operations. Any good internal control system must be manned by reliable personnel who are qualified and competent.

Competence of the staff refers to the willingness of the staff to perform duties as required without any close supervision. To instill this spirit of competence among them it requires that the staff should be motivated through rewards, promotions and recognition element in the course of executing their duties.

f. Arithmetic and accounting controls

Woolf (1997) noted that these are internal controls aimed at ensuring the accuracy of transactions and also ensures proper recording of the organization's transactions according to the Generally Accepted Accounting Principles (GAAP). He further argued that internal controls are usually boosted by the use of calculators and computers. He noted also that while examining the system of internal control the auditors should consider the possibility of collusion between close relatives working in related parts or departments of the organization.

According to *Saleemi (1989)* the recording of business transactions should be accurate and arithmetically correct. For this purpose some controls are introduced for example checking totals, reconciliation, control accounts and trial balance. An effective internal control requires proper implementation of arithmetical and accounting controls. He concluded by saying that the auditor has to examine the adequacy of the internal control system differently for different organizations.

g. Supervision

Manasseh (1990) suggested that any system of control should include supervision of day-to- day transaction by responsible officer and according to these transactions for instance the working hours of employee recorded and should be checked or inspected by the supervisor.

According to *Millichamp (1999)*, supervisors must be vigilant in their duties and ensure that people under their supervision perform their duties as per the laid down organizational policies and this supervision must be done in the human way so as to promote morale among the employees and avoid apathy or frustration among those under supervision. He further noted that management should check internal statements, budget controls and standard costing statements and review departmental procedures and functions. This gives operational efficiency and should be done by higher authorities like internal auditors and managers

h. Authorization and approval

Woolf (1997) said that all transaction must be authorized and approved by the right and responsible organizational officer. This is aimed at preventing fraud and safeguarding the assets of the organization. It stimulates the flow of authority to avoid bureaucracy and conflicting authorized activities. For example the purchase order should be approved before money is paid. Similarly payment of wages should be approved before money is withdrawn. Internal control requires a proper system of authorization and approval. The basic objectives of authorization and approval are to avoid fraud instances and safeguard the company assets.

De Paula et al (1990) said that the organization should ensure authorization of sensitive assets in the hands of highly responsible people who cannot misuse such authority due to their position and precaution of professional ethics which they are bound to observe.

i. Vocational and rotation of duties

Manasseh (1990) noted that the organization must give a compulsory leave especially to the accounting staff who should not overstay their leaves. This is aimed at checking the efficiency of the officer in the business in their absence thus minimizing errors and fraud and boosting the efficiency of the employees. The employees should be rotated in different departments but doing jobs which are related to areas of their specialization.

j. Cost feasibility

Batra et al (1992) noted that the system to be installed must be within the limits affordable by the organization and its costs must not out weigh the cost benefits to be derived from such type of internal control. Regarding cost feasibility, the cost benefit analysis should be used to weigh the advantages and disadvantages of the undertaking.

k. Routine and automatic checks

According to *Saleemi (1989)*, the internal controls should take room for surprise checks especially for such items as petty cash, stock control, salaries and wages payment. These will prevent errors and frauds, promote morale and efficiency.

2.2 Internal check

Batra et al (1992), internal check refers to the checks of the day-to-day transactions which operate continuously as part of the routine system whereby the work of one person is proved independently or is complementary to the work of another. The object is the prevention of or early detection of errors and fraud. It includes matters such as delegation and allocation of duties, authority and division of work, the method of recording transactions and the use of independently ascertained totals against which a large number of individual items can be proved.

Spicer and Pegler (1978) defined the internal check as an arrangement of staff duties whereby no one person is allowed to carry through and record every aspect of a transaction so that without the collusion between the two or more persons fraud is prevented and possibilities of errors are reduced.

On the basis of the above definitions, internal check means the arrangement of the staff in a scientific way so that no one person is allowed to handle all aspects of a transaction. No single person can authorize, conduct and record the transactions. Also the duties of employees are arranged so that work of one employee is checked with the other employee.

Batra et al (1992), noted that the objectives of internal check is to make chances of fraud on part of any staff difficult, speed detection of any act of dishonesty and irregularity, detection of errors and assurance that all material facts are promptly recorded in their books of prime entry and included in the final financial records of the organization for managerial decisions.

2.3 Internal audit

Millichamp (1999) noted that internal audit is aimed at ensuring that management operates efficiently so as to manage the business better. It's a managerial tool that acts as watch dog over the organization's entire internal control system.

Woolf (1997) defined it as an independent appraisal of activities within an organization for the review of accounting, financial and other business practices. It's conducted by the employees of the organization and helps management to evaluate the performance and efficiency of established procedures.

Batra et al (1992) said that internal auditing is an evaluation and analysis of the business operations conducted by the internal audit staff. The objective of the internal audit is to assist all members of the management in the effective discharge of their responsibilities by furnishing them with analysis, appraisals, recommendations and pertinent comments concerning the activities reviewed. The attainment of the overall objective includes activities such as reviewing and appraising soundness and adequacy of internal control procedures and adherence to the laid down policies and plans of the organization.

2.4 Evaluation of internal controls systems

Batra et al (1992) said that the system of internal control should be reviewed at the beginning of the audit. This should be done in order to arrive at a decision regarding the amount of detailed examination. It's to be performed during the audit to ascertain the weakness or strength of the system as one of the basis of expressing the opinion concerning their presentation of financial statements and record management. An auditor will normally initiate his review of internal control before engaging the check. Conclusions concerning the internal controls affect the scope of the examination by an auditor. Many auditors interweave their review and evaluation of internal control with the audit process.

A proper system of internal control which is effectively operated save an audit time, reduces examination costs to the client, assures the auditor on reliability of the financial transactions and reduces the work of the internal auditor. Auditing standards also provides for reliance upon the effectiveness of internal control systems as a guide to the auditor in determining the amount of detailed verification necessary during the course of

the audit. In view of such reliability the auditor must have a sound basis for formulating an opinion on the effectiveness of the system relied upon.

2.5 Tools used for internal control system evaluation

a. Internal control questionnaires (ICQ'S)

Manasseh (1990), stated that a questionnaire is a standard pre-printed documents designed by the audit firm. It comprises a series of questions on the internal control. They are to be completed by senior members of the audit staff after putting the questions on the client company's officers responsible for each of the sections into which the internal control questionnaires are targeting. The questions should be in series.

Generally the questionnaire is so worded that a 'NO" answer suggests an undesirable practice relative to achieving a good internal control. The advantage of using these questionnaires is that they are comprehensive and an all inclusive method of ascertaining, recording and evaluating systems of internal controls.

b. Substantive tests

Saleemi (1989) describes substantive tests as the tests of the transaction balances and other procedures such as analytical review which seeks to provide audit evidence as to completeness, accuracy and validity of the information contained in the financial records and statements.

The nature and timing the extent of substantive tests is determined by the degree of reliance which the auditor can place on the operations of the internal control systems. The substantive tests produce evidence that the information being incorporated in the production of financial statements and other records is correct in all aspects. If there is any difference from balances with the original entries then it indicates a weakness of an internal control system.

According to Woolf (1997), substantive tests constitute the weakness tests which are used to refer to any additional tests considered necessary in view of the number of errors or weakness which become apparent during execution of the audit programs. It's an extension of work originally planned due to the discovery of high proportion of errors than was anticipated.

Basically substantive tests are designed to help organizations produce evidence as to the completeness, accuracy and reliability or validity of the financial records. This helps to assess the strength or weakness of the internal control system of the organization.

c. Flow charts

Spicer and Pegler (1978) said that the audit flow charts are dramatic representations of a company's accounting systems and procedures. It consists of horizontal lines which indicate the movement of items across departments and the vertical line which indicate the movement of items in the same department. They are designed to simplify the recording of internal control systems to the understanding of the new audit staff, managers and other administrators. It also highlights the relationship between different parts of the internal control systems in a simple diagrammatic manner.

The flow chart will help to ascertain the flow of authority and dissemination of instructions downwards and upwards through all internal channels of communication. This will ensure that the information flow is adequate, sufficiently detailed, accurate and up-to-date.

d. Walk through tests

Mellichamp (1999) noted that walk through tests are applied in any situation where the auditor has not obtained his description of the system from a personal investigation of the system by questioning the operating staff and examining documents and records. It can also be applied at the final audit when he needs to review the system from the date of interim completion to the end year.

Saleemi (1989) said that after obtaining information about the organizational structure of the client, the auditor would also like to confirm this information and increase his comprehension of the whole system. Walk through tests are used to trace small number of transactions. This is mainly to ensure correct recording in the accounting system and to give preliminary evaluation of the system.

e. Compliance tests.

Batra et al (1992) said that compliance is necessary because sometimes the prescribed controls tend to be disregarded or modified when applied in practice unless there is a strict supervision by a responsible officer. The compliance of the procedures can be tested by selecting samples at random from different categories of transactions and examining them in depth. For example the auditor may test a few items of inventory right from the stage of their purchase to final stock taking. He may also verify some aspects of control by direct observation.

2.6 Internal control and technology

Woolf (1997) said that with the rapidity changing technology, there is need to restructure the controls of various organizations to support these developments. The auditors' work is to evaluate the performance directly with the computer and computer records as they exist in suitable machine sensible form. The auditors therefore concentrates on proving the initial inputs and checking there validity and then calculate output manually which is then compared with the computer output.

Bialy (1989) developed a computer assisted model for designing, analyzing and evaluating the internal control systems. The internal control model was implemented and found feasible. It is designed to aid the auditors with vast modern internal control systems and to aid them evaluate the systems.

De Paula et al (1990) noted that there are some systems developed to ensure that satisfactory standards are maintained in designing, testing, implementing and documenting new systems and programs. He further noted that an auditor has to review

internal controls to ensure that there are clear definitions of duties and division of responsibilities between these sections.

Ravian (1997) carried out research to determine if control to data represents a major difference between file systems and data base systems. He found out that certain general control programs developments and maintenance is different over access to data represents a major difference between file and data base systems. A data base requires a broad control than the file system.

In particular therefore the auditor should ensure that the computer routine have been properly documented ,un authorized persons are not allowed into computer files, programmers should not have access to computers except when its necessary and that computer operators do not have access to source documents and also not allowed to amend programs.

2.7 Internal controls and business performance

Saleemi (1989) said that the adoption of a sound internal control will ensure success in business. The information obtained from a sound internal control as reflected on the financial statements will provide a report on entity's financial performance and financial position that is a reflection of proper stewardship.

Salih (1983) did a case study of Ethiopian Airlines- Nairobi and evaluated its internal controls. He used interviews to gather the information and analyzed it by comparing with a theoretical sound and generally accepted internal control systems. He found out that there was lack of segregation of accounting and custodial function on the branch. He therefore concluded that its records were not effective for decision making.

Ochieng et al (1990) carried out a study with objectives of documenting the existing internal control systems of Seal Honey Limited and compared it with ideal internal control systems. They found the following deficiencies; there was no documented organizational charts, no procedures for manual duties and responsibilities for each

employee, there were no discount policies for reference which would lead to collusion between the customers and sales supervisors. Analysis of purchase order procedures showed that the financial controller had many responsibilities over purchases at the expenses of the purchasing control personnel.

2.8 Detection of errors and frauds

De Paula et al (1990) said that the impact of a sound internal control system is to detect and prevent errors affecting the financial statements and hence financial performance of the enterprise. He added that the reasonability of detecting and preventing errors and frauds rests with management of an organization.

Haylas and Aston (1992), researched on the effectiveness of particular audit techniques in detection of errors that affects the financial statements and their causes. They concluded that the intentional errors are concentrated on a few audit areas and that large portions of financial errors are signaled by less rigorous audit procedures such as analytical reviews and discussion with the client.

CHAPTER THREE

RESEARCH METHODOLOGY

3.1 Introduction

For this research to be effective, research design, data collection and analysis was used to arrange the information in such a way that enabled the researcher to come up with the reliable recommendations and conclusions. The following are the methodology employed starting with the research design, study population, sampling design, research instruments and analysis of data.

3.2 RESEARCH DESIGN

The study design is cross section the role of the internal control system on business performance. The study will focus on the view of strategic managers, accountants and internal auditors of the bank. It will employ both quantitative methods to generate in depth information and qualitative methods to show magnitude and the scope of the problem to be studied.

3.3 Area of study

Kenya Commercial Bank-Trans-nzoia district, Kenya.

3.3 The study population

The study mainly focused on the staff of Kenya Commercial Bank-Trans-nzoia district, Kenya. They included different managers of departments, internal auditor and twenty five subordinate staff of the organization. The organization was selected because of its convenience in accessibility, the financial resources available to the researcher and the researcher's familiarity to the organization.

The targeted population consisted of fifty employees of the organization. The primary respondents for this research included the managers, accountants, internal auditor and ten subordinate accounts staff working in the accounts and audit departments.

3.4 Sample design

A stratified random sampling technique was used in picking the employees on which the data was collected. The population was stratified into a number of strata and the sample of employees was selected from each stratum. Simple random sampling technique was used in selecting the employees to constitute the sample from each stratum. All the sampled employees were contacted personally to obtain answers.

3.5 Types of data

The researcher used two types of data in the study. The primary data and the secondary data were used by the researcher. The primary data is the data that was collected for the first time for the purpose of this research. The secondary data involved the analysis of various internal and external documents in order to obtain the information and other control measures that wee necessary for the production of this research report. The internal documents included reports from internal auditors, current and previous departmental reports and the organizational regulations. External data documents included the external auditors' reports.

3.6 Data collection Techniques

Both primary and secondary techniques were used. The primary techniques like the questionnaires, interviews and observation of the respondents were employed.

3.6.1 Methods used

a. Questionnaire technique

Data was collected by the use of structured questionnaires designed by the researcher. The questionnaires were sent to the department heads, internal audit staff and other subordinate staff. This technique was used because all the respondents were literate. The questionnaires were aimed at investigation purchase control, salaries and wages control, debtors control, internal audit control, cash, transactions control and fixed assets control. The major advantage of this method includes; free of biased information and enough time for the respondent to consider his/her points carefully than in an interview.

b. Interviewing method

The personal interviews were carried out by the researcher as a follow up of the questionnaires so that the interviewee could be aided in the areas of difficult and seek an in depth discussion and explanation on matters missed on the questionnaires. Among the staff interviewed are the system development officer, internal auditor and commercial manager. They were aimed to investigate internal audit, computer controls, and general overview of the organization. The method has an advantage of immediate response, room for clarification and in depth information and collection of other complementary data.

c. Non participant observation method

Observation was focused on the practical aspect of the normal tasks carried out in the organization by the staff. They included mail registration by the registry clerk, cash receipts by the cashier, salary payments, preparation of payment vouchers, posting of journal entries to the ledger and the approval by the senior officials and observation of the operational procedures of the whole organization. The advantage of this method is that it protects the confidentiality of information and better recommendations based on personal observation.

3.7 Analysis of data

Once the data had been collected, it was analyzed by the researcher both qualitatively and quantitatively. The analysis involved the determination of the effectiveness of the existing controls in the organization. The data obtained was analyzed under a stated research design so as to answer the questions with the collected data. It's from this analysis and observation that the researcher came up with a comprehensive conclusion and recommendations on the effectiveness of internal control system on record management.

3.8 Limitations of the study

The researcher faced the following limitations in the process of this research:

Some of the respondents were unwilling to answer the questionnaires thus leading to the delay in data collection

.

There was the problem of information denial to the researcher by the management Kenya Commercial Bank Trans-nzoia district, Kenya with the excuse of confidentiality and internal use only.

There were financial constraints due to inadequate resources to finance the research however this remains confidential to the researcher.

CHAPTER FOUR

FINDINGS AND ANALYSIS

4.0 Introduction

This chapter analyses the findings obtained from the field collected by the outlined methodologies such as questionnaires, interviews and researchers analysis.

4.1 Cash control

Cash control means the steps which are undertaken to ensure that cash receipts are handled properly and cash payments are duly authorized by some responsible officials. It relates to bank notes, cheques and drafts.

Respondents were asked to state whether the cash control of the company was strong or weak. 65% of the total respondents said that the cash control was weak while the other 35% said that it was strong.

One major reason that was stated why the cash control was weak is;

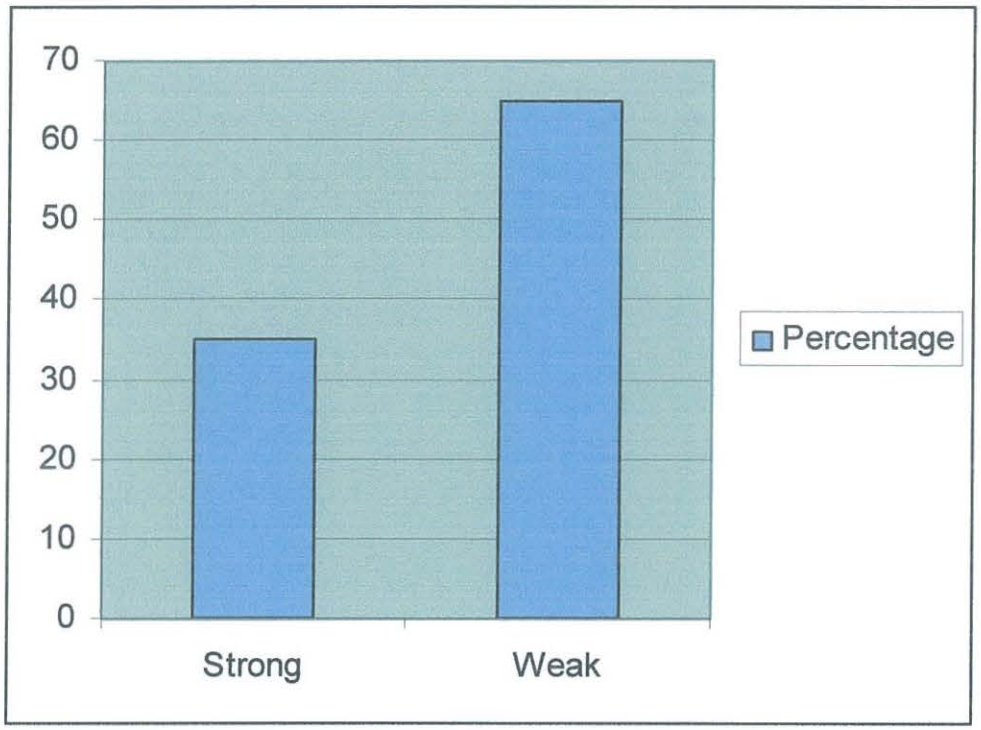
- Internal auditors do not regularly audit the account. This in itself shows that the existing control on cash is not effective and calls for corrective measure to be done since this could lead to fraudulent malpractices regarding cash.

4.1.1 Presentation of data on cash control

Management	Internal audit staff	Other subordinates	Total	Reponses	Percentage
4	2	6	12	Strong	35
2	1	15	18	Weak	65

SOURCE : DATA SURVEY 2008

Figure 4.1.1 of data on cash control



SOURCE: DATA SURVEY 2008

According to the research it shows that the cash controls are weak which means there is a room to fraud in the bank. This can lead to loss of cash or misuse of funds especially when it comes to petty cash.

4.2 Debtors control

The respondents were asked to comment on the effectiveness of debtors control whether they were strong or weak and if weak give reasons.

According to their response, 75% of all the respondents noted that the debtors control was strong while the remaining 25% said that the debtors control was weak. The reasons they give why the debtors control was weak included;

- No adequate procedures are laid down to establish the credit worthiness of people when granting loan.
- No clear or specific procedures are taken to recover the amount due from debtors.
- Internal auditors rarely audit their accounts.

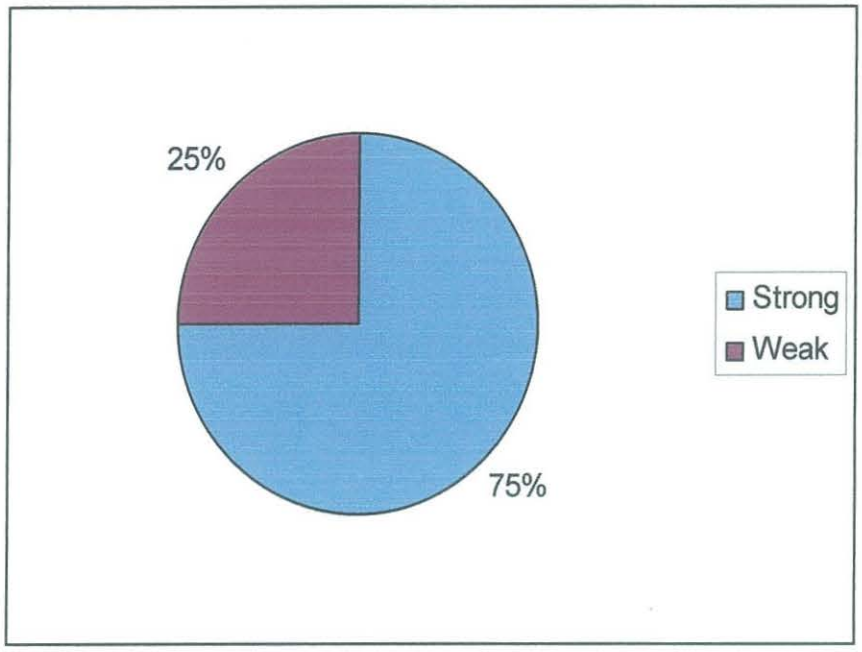
The above reasons indicate that the debtors control is not fully effective and thus calls for corrective measures to be done.

4.2.1 Presentation of data on debtor control

Management	Internal audit staff	Other subordinates	Total	Reponses	Percentage
9	7	7	23	Strong	75
4	1	2	7	Weak	25

SOURCE: DATA SURVEY 2008

Figure 4.2.1 of data on debtor control



SOURCE: DATA SURVEY 2008

The pie chat illustrates that the debtor controls are strong but the 25% of respondent think that enough is not been done to control debtors and this can lead to ghost debtors as well as increased bad debts which will in turn affect the banks performance. Thus effective controls should be put in place to reduce the risk of bad debts.

4.3 Internal control on wages and salaries

The respondents who were interviewed in the organization gave comments as; 40% of internal control on wages and salaries strong while 60% of the respondents said that it was weak. This is presented in table 4.3.1. Some of the respondents who sad that internal control on wages and salaries gave reasons as:

- Procedures relating to transfers and discharge of employees are not clearly defined.
- Control accounts for PAYE, NSSF, NHIF, are not clearly maintained.
- Payroll deductions are not clearly stated by the management
- Transactions in the accounting records are not checked on regular basis

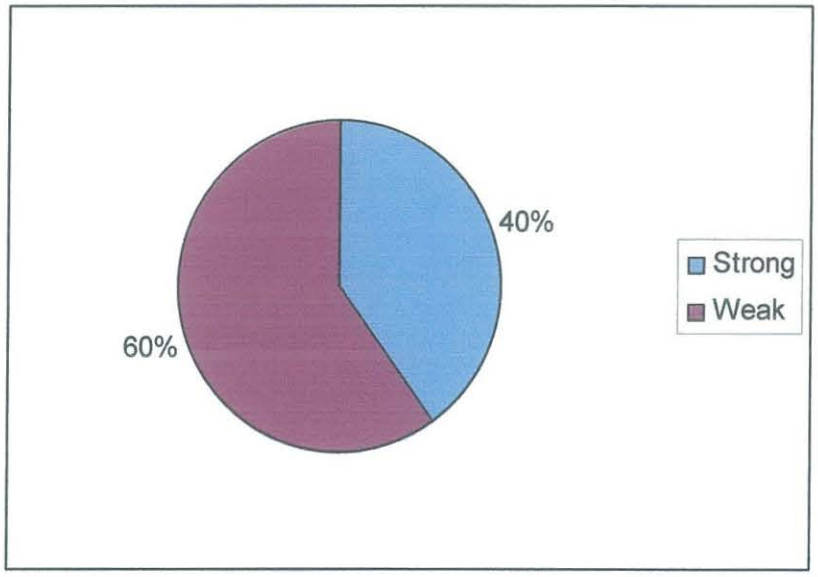
This has therefore indicated that the internal control on wages and salaries is not sufficient and effective.

4.3.1 Presentation of findings on wages and salaries

Management	Internal audit staff	Other subordinates	Total	Reponses	Percentage
5	4	3	12	Strong	40
9	5	4	18	Weak	60

SOURCE:DATA SURVEY

Figure 4.3.1 of findings on wages and salaries



SOURCE: DATA SURVEY 2008

The wages and salaries is relatively strong but the 40% of respondent think that the the controls are weak. This means that the that the bank can be loosing relatively a large amount of money due to inaccuracy in salaries and wages calculation as well as an increased level of ghost workers in the bank. Sufficient measures need to be taken and independent auditor conducted.

4.4 General overview

The commercial manager was interviewed by the researcher and found out that there was not a good working relationship between the subordinates and the senior officials. However the researcher has noted that there were unqualified persons employed by the bank so as to minimize the overhead costs. There was no clear definition of duties and responsibilities of each employee especially the casual workers.

The company had its mission statement, however, the objectives of achieving it proved insufficient and require more work to achieve at the end. The turnover rate of employees in the organization is very high due to low pay being paid to lower level employees. There is also prolonged under-staffing of accounts and audit departments which has led to regular changes in accounting policies and practices.

Basing on the general overview, the system of internal control is not effective and thus calls for adequate measures to be taken in order to streamline the company's operations.

4.5 Internal audit control

After interviewing the internal auditor of Kenya commercial Bank – Trans-nzoia District, Kitale, the researcher was able to gather a variety of information. The organization had constant spot checks involving auditors from other KCB branches going for regular audit. The organization also had routine audits which they normally give five days notice to other employees to have their records in place and ready to be audited. However, it has few internal auditors who are not enough to perform their duties effectively and efficiently.

CHAPTER FIVE

SUMMARY OF FINDINGS, CONCLUSION AND RECOMMENDATIONS

5.0 Summary of findings

After a thorough analysis, the findings showed that there are several controls employed in the company. Some of the controls are cash control, debtors control and salaries and wages control. The adequacy of these controls was determined basing on a theoretical sound internal control system. The outcome of finding and analysis showed that all the controls had some weaknesses.

The Kenya commercial bank's internal control system consists of a set of measures and rules designed to minimize business risks and ensure regular, secure and efficient operation - relies on a variety of dedicated bodies and tools, which are adapted according to the object. The principles on which the internal control system rests are: clearly defined levels of responsibility; efficient internal information systems; separation of operational from control duties; standardized order of procedures; documented controls; independent internal inspectorate.

The banks internal controls are performed within the following framework:

i. management controls, bearing on the development and management of business Strategies, the choice of concrete lines of action and the verification of end results;

ii. hierarchical and functional controls, performed by the office managers themselves Or their nominees to ensure that tasks are completed as assigned and the proper Procedures followed

iii. functional confirmation controls, involving forms of cross-check between Operational areas and control areas

iv. Inspections of internal control system to ensure that they are functional and useful in the accomplishment of the banks objectives and goals.

In particular, the purpose of the controls is to verify, from the three viewpoints of effectiveness, efficiency and security, the compliance of operations with the body of external and internal regulations, the handling and stock of valuables, the correct entry of transactions in the accounts and the intactness of the Bank's physical assets. In this context, the correct performance of internal controls, the effectiveness of physical and logical security measures, the functioning of organizational structures and the quality and quantity of resources assigned are also subjected to review.

The inefficiency/effectiveness of the organizations internal controls have led to malpractices such as non reliability of financial records, embezzlement of cash, delays in salaries and wages payments. In order to improve on the organizations internal control system, the researcher came up with various suggestions, methods and devices in order to ensure a sound and effective internal control system.

5.2 Conclusion

Most bankers realize that internal control and self-policing (internal audit) are critically important to accountants and regulators. That aside, what does it really mean for shareholders, directors, senior management and employees? Is it just an expensive exercise in regulatory futility? We think not. For the shareholders, it contributes to value and the bank's bottom line. For directors, it demonstrates their recognition of their responsibilities and provides them peace of mind that they are doing their jobs. After all, who doesn't want to sleep better? For senior management, it provides a means of accountability and communication bank-wide to ensure that board-directed plans, goals and risk tolerances are achieved. For employees, it provides them the rules by which they must play and the tools to be effective.

In conclusion the researcher established that internal control system of the company is weak and thus cannot be relied upon as an instrument of good financial management.
In reinforcing ethical values, banking organizations should avoid policies and controls that may inadvertently provide incentives or temptations for inappropriate activities. Examples of such policies and practices include undue emphasis on performance targets or other operational results, particularly short term ones; high performance-dependent compensation rewards; ineffective segregation of duties or other controls that may offer temptations to misuse resources or conceal poor performance; and insignificant or overly onerous penalties for improper behaviors.
While having a strong internal control culture does not guarantee that an organization will reach its goals, the lack of such a culture provides greater opportunities for errors to go undetected or for improprieties to occur.

Yet factors such as inadequate or lack of training, circumvention of rules and regulations, porous recruitment system, over-centralization of authority, poor security features on bank instruments or documents, industry inertia and lack of discipline. Others were inflating credit interest to ledgers and withdrawing the difference fraudulently, conversion of the bank's income to customer's account and withdrawal of same, diversion of unutilised foreign exchange and inflation of statistical data of account performance to give deceptive impression of the bank performance and proper internal control systems should be taken to account

One of the preconditions of the efficient internal control system shall be adequate segregation of duties, i.e. the conflicts of interests should be avoided. The bank board as well as the heads of respective structural subdivisions shall ensure the separation of granting authorizations for financial and business transactions, their enforcement, entry in the accounting records and protection of assets. The activity spheres of likely conflicts shall be identified, reducing their number to the minimum extent and closely monitored by an independent person, i.e. a person not concerned with the spheres of conflict. Each task assigned to the staff shall be clear, logical, and the rights, duties and responsibilities discussed and co-ordinate.

It was found that management of internal audit department, professional proficiency, objectivity and review significantly influence the monitoring aspect of the internal control system. Scope of work and performance of audit work significantly influences the information and communication aspect of the internal control system while performance of audit work, professional proficiency and objectivity significantly influence the control environment aspect of the internal control system. The study also shows that management of internal audit department, performance of audit work, audit program and audit reporting significantly influences the risk assessment aspect of the internal control system. Lastly, performance of audit work and audit reporting significantly influences the control activities aspect of the internal control system.

If effective internal control system is installed within the organization, it would encourage efficient and effective use of its resources including personnel to optimize the organizations goals and mission of incorporation. This is because without a sound and effective internal control system, the organization's operations will continue to deteriorate and its performance will worsen in future.

5.3 Suggestions and Recommendations

a. The organizational structure of the company should be designed to provide appropriate division of financial responsibility and it should be strengthened by employing a qualified and competent workers.
b. The role of internal auditors should be well defined and manned by competent and motivated officer.
c. Regarding credit control management, there should be procedures laid down for verification of credit worthiness of individuals requesting or seeking loans.
d. There should be a sound or good relationship between the senior officials' and their subordinates. This also includes effective communication which is vital element in any organization.
e. Training should be enhanced to ensure that front office employees get same training as the internal auditor thus enhancing the communication.
f. Job rotation should be encouraged and job enlargement to enhance a sound and effective internal control system.
g. Advance control shall cover the framework of organizational measures aimed at preventing abuse, avoiding bank performance mistakes, entry of fraudulent and misleading data in accounting and financial statements. Hence the bank should invest in research and development so as to develop advance controls.

h. Possibility for bank staff to properly identify bank customers and beneficiaries, i.e. to ensure implementation of the principle of "customer due diligence" in the bank should be developed.

i. The bank managers should have responsibility for implementing the bank strategy established by the bank council: creation and development of the system of identification, measurement, monitoring and control of the risks run by the bank; setting acceptable levels for these risks; approving the organisational structure clearly defining the rights duties and liability of the bank staff, maintaining this structure and ensuring the discharge of such duties; effective functioning of internal control system within the bank.

j. The bank should promote high ethical and integrity standards and establish environment within the bank that emphasizes and demonstrates to all staff levels the importance of internal controls. All staff of the bank need to understand their role in the internal controls process and fully engaged in the process.

k. An effective internal control system shall ensure that material risks that could adversely affect the achievement of the bank's goals are being recognised and continually assessed. The risks assessment shall cover all risks facing the bank and the consolidated banking group covering the parent bank and its subsidiaries (that is credit risk, market risk, liquidity risk, operational risk, legal risk, reputation risk, etc.). Internal controls may need to be revised to appropriately address any new or previously uncontrolled risks.

l.

m. the bank is accumulating and analysing information on loss incurred as a result of mistakes made by the bank staff, bank customers or third parties, abuses, thefts, or inadequate performance of duties; interruptions in bank payments of settlements, malfunction of computer hardware and software and telecommunications; full or partial destruction of assets resulting from external effects; has developed a contingency plan (natural calamities, fire, vandalism, armed robbery, etc.) with a view to ensuring continuing performance of the bank and its subdivisions and minimizing contingent losses; and

n. The internal control should be an integral and sustainable part of the daily activities of a bank. An effective internal control system shall require that an appropriate control structure is set up, with control procedures defined at every managerial level. These should include: reports to the bank council and board, appropriate activity controls for structural subdivisions of a bank (departments, divisions, etc.), protection of bank assets, compliance with exposure limits and follow-up on non-compliance; granting approvals and authorizations for transactions, and verification and reconciliation of data.

o. For internal control system purposes the bank board and the heads of respective structural subdivisions instructed by it shall ensure that reliable and adequate internal (financial, operational, compliance), as well as external (market and other factors and conditions) information relevant for decision making is provided in timely manner and in consistent form.

p. The internal audit service of the bank should maintain close co-operation with a credit institutions supervision authority. Bilateral meetings organized on the initiative of either of the parties might be one of the forms of co-operation aimed at ensuring effective system of internal control of the bank.

q. In accordance with the procedure and periodicity established by the bank board, the internal and (or) external auditors should verify the effectiveness of the system of internal control, also including self-assessment (when a person responsible for a particular function determine the effectiveness of controls exercised by them). The frequency of monitoring different activities shall be determined by the risks incurred by the bank and change and nature of changes occurring in the operating environment.

[illegible] defining the principles of organization of its internal control is consistent with the nature, complexity and variety of transactions performed by the bank, the risks incurred, as well as with the minimum internal control requirements established in the present Provisions. Hence for a bank to proper and attain its goals and objectives sound internal control system should be put in place.

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APPENDICES

Appendix I

THE IMPACT OF INTERNAL CONTROL SYSTEMS ON BUSINESS PERFORMANCE
A CASE STUDY OF KENYA COMMERCIAL BANK LIMITED
TRANS- NZOIA DISTRCT- KENYA

Primary data collection questionnaire

TO THE COMMERCIAL MANAGER

Introduction

This research is being undertaken as partial fulfillment of requirement of the award of Bachelor of Business Administration of Kampala International University.

Being an official of Kenya Commercial Bank, I feel that you are in a better position to provide me with relevant information. This information is purposely for academic purposes.

(Please tick where appropriate)

1. SEX: MALE FEMALE

2. Which department do you work for?

Finance ☐

Human Resource ☐

Accounting ☐

Production ☐

Sale and Marketing ☐

Other specify

3. What is your job title?

Top-level management ☐

Middle level management ☐

First level Management ☐

Individual contributor ☐

4.In your observation do you think the duties and responsibilities you have for each employee is clearly defined?

Yes ( ) No ( )

If No, please give reasons.

a.....

b.....

5. In your own opinion are the above problems affecting commercial activities

Yes ( ) No ( )

If Yes, please in what ways?

a.....

b.....

6. Do the above problems affect organization performance?

Yes ( ) No ( )

If yes please state how.

a.....

b.....

7. Any other general comment on the effectiveness of internal controls of your organization.

a. .....

b.....

Thank you for your contribution

Appendix II

THE IMPACT OF INTERNAL CONTROL SYSTEMS ON BUSINESS PERFORMANCE

A CASE STUDY OF KENYA COMMERCIAL BANK LIMITED TRANS- NZOIA DISTRCT- KENYA

Data collection questionnaire.

TO CHIEF ACCOUNTANT

This research is being undertaken as partial fulfillment of requirement of the award of Bachelor of Business Administration of Kampala International University. The questionnaire guide will assist in gathering and evaluating the effectiveness of internal control on record management.

You as the Chief Accountant you are in a better position to provide me with relevant information that will make this report a success. The information given shall be treated with high degree of confidentiality and shall not be used for any other purposes except for this research

TICK WHERE APPROPRIATE

1). SEX: MALE ☐ FEMALE ☐

2). Which department do you work for?

Finance ☐

Human Resource ☐

Accounting ☐

Production ☐

Sale and Marketing ☐

Other specify

3). What is your job title?

Top-level management ☐

Middle level management ☐

First level Management ☐

Individual contributor ☐

4). For how long have you worked for your organization?

Less than 1 year ☐ 1-5 years ☐ 5-30 Years ☐

.1. Cash control

How is cash control in the company?

Weak ( ) Strong ( )

If weak, what are the reasons that have contributed to this?

a.....

b.....

5. Purchase control

How is purchase control of purchases?

Strong ( ) weak ( )

If weak please give reasons for this.

a.....

b.....

6. Debtors/ loan control

Comment on company's debtors/ loan control

Strong ( ) weak ( )

If weak give reasons

a.....

b.....

7. Wages and salaries control

How is the internal control on wages and salaries?

Strong ( ) Weak ( )

If weak what are the reasons that have contributed to this state?

a.....

b.....

8. Any other comment on the internal controls employed by the organization.

a.....

b.....

Thank you for your contribution.

Appendix III

THE IMPACT OF INTERNAL CONTROL SYSTEMS ON BUSINESS PERFORMANCE

A CASE STUDY OF KENYA COMMERCIAL BANK LIMITED TRANS- NZOIA DISTRCT- KENYA

Primary data collection Interview Schedule

TO THE CHIEF INTERNAL AUDITOR

This research is being undertaken as partial fulfillment of requirement of the award of Bachelor of Business Administration Kampala International University. The interview guide will assist in gathering and evaluating the impact of internal control on business performance.

As the Chief Internal Auditor you are in a better position to provide me with relevant information that will make this report a success. The information given shall be treated with high degree of confidentiality and shall not be used for any other purposes except for this research.

1. Are there control measures you have put in place to minimize instances of fraud among the employees?

   Yes ( ) No ( )

If yes, please enumerate some.

a.....

b.....

2. Do you regularly audit your areas of operations as per you specification?

   Yes ( ) No ( )

If Yes, state reasons

a.....

b.....

3. Do you constantly brief the management on the current state of the existing controls and what they should do to improve them?

Yes ( ) No ( )

If Yes, please give reasons

a.....

b.....

4. Do the employees comply with the requirements of financial and accounting principles regarding internal control in the organization?

Yes ( ) No ( )

If No give reasons

a.....

b.....

5. Any other general comment on the internal control systems of the organization.

a.....

b.....

Thank you for assisting me.

Appendix V

BUDGET

ITEMS	AMOUNT IN KENYAN SHILLINGS
Typing and printing	5,000
Literature review and collection study of materials in external libraries, inclusive of photocopies	2,500
Data collection over the internet and other sources	3,500
Transport costs	4,500
Questionnaire development	5,500
Hard cover binding of the dissertation three copies	24,000
Miscellaneous costs	4,500
TOTAL	**49,500**

Appendix VI

WORK PLAN

ACTIVITY	DURATION	DATES
Literature review and development of proposal	3 weeks	March 08
Submission of the proposal	2weeks	May-08
Study and correction of questionnaire	2 weeks	May-08
Data collection	1 week	July-08
Data processing	1 week	July-08
Data analysis	1 week	July-08
Report writing and submission	3 weeks	August08
Presentation of the project	1 week	August08

Appendix VII

LINAH MUKAMI NJIRU

P.O. BOX 453 EMBU – KENYA

TEL: 0724350020

EMAIL: Lrwann@yahoo.com

PERSONAL INFORMATION

Year of Birth: 1983

Nationality: Kenyan

Religion: Christian

Marital Status: Single

ID Number: 22620407

Sex: Female

CAREER OBJECTIVE

Being a highly motivated individual ready to work under minimum supervision, fast learner and a team player, I am ready to face challenges with confidence, to work under pressure to produce high quality results. I am seeking a job in a challenging environment that allows me to develop and utilize my qualifications, skills and talents to the full.

ACADEMIC AND PROFESSIONAL EDUCATION

Kampala International University **[2005-2007]**

- Bachelor of Business administration (majoring in finance Banking)

Strathmore university ***[2002-2004]***

- Successfully completed part one and two of Association of Chartered Certified Accountants (ACCA)]

RESPONSIBILITIES

- School prefect – Ikuu High School.
- School Prefect – kyeni Primary School.

SKILLS

- Great Team Player
- High Propensity to undertake research in any field so assigned
- Financial analysis and interpretation

HOBBIES AND INTERESTS

- Sports: basketball and badminton.
- Drama: as a way of creating awareness on the key issues affecting society.
- Avid reader of business and economic issues.
- Traveling