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EFFECT OF CONTROL ACTIVITIES ON FINANCIAL PERFORMANCE OF FARMERS' COOPERATIVE SOCIETIES IN TRANS-NZOIA COUNTY, KENYA

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Abstract: *The main objective of this paper is to examine the effect of internal controls on financial performance of agricultural producer cooperatives societies (APCSs) in Trans-Nzoia County. The study's primary goal was to assess the efficiency of the internal control systems at the private banks in Mogadishu and to examine their financial results. A cross-sectional survey design was employed to select research population. Data were collected using structured questionnaires and interviews. The data were analyzed using descriptive statistics as well as inferential statistics. The results showed that manufacturing enterprises with good internal controls outperformed those with weak internal controls in terms of their financial performance. Therefore, the research encourages the management of farmers' cooperative societies to adopt the appropriate and relevant internal control activities in financial management.*

Keywords: *control activities, financial performance, cooperative societies, internal controls*

1. Introduction and Background

Internal controls are crucial to all business units, but they are especially important for the Agricultural Producer Cooperative Societies. Agricultural Producer Cooperative Societies in Kenya rule the agricultural industry and contributes to the economic prosperity. Internal control's overarching objective is to assist the organization in achieving its objectives. Internal controls are established with the aim of achieving efficiency and effectiveness in operations, where effectiveness point towards attaining definite goals set and intended results; on the other hand efficiency deals with proper utilization of resources and thus ensuring that there is a rewarding relationship between resources employed and the results achieved (COSO, 1992).

An organization without internal controls may experience issues including but not limited to financial theft, bribery, embezzlement and tax evasion. The problem of fraud in the Farmers' Cooperative Societies is caused by inadequate knowledge on the entrepreneurs, little or insufficient employee expertise with respect to their assigned role, shortage of training and lack of internal control systems. Internal control measures would be used to curb or eliminate these errors. If implemented appropriately, internal audit, a crucial element of internal control, will examine the actions of other departments or personnel.

Amaka (2017) suggested a connection between reliable financial records and efficient internal controls. A survey research strategy was adopted for this study since data from both primary and secondary sources were employed, and a sample size was established using the Yaro Yamane sampling method. Out of the four research questions, three hypotheses were developed at a 5% level of significance using the regression co-efficient analysis method, and the Z table was also employed to compare the computed value of significance B and table value. According to Amaka's analysis, internal control is crucial to the growth and productivity of the business because it assesses managerial performance.

Kiabel (2007) conducted research on the accounting control procedures and financial results of government-owned businesses. With particular reference to enterprises controlled by the Rivers State. The study's correlational research approach employed structured questionnaires and interviews to collect data. According to the study, there is only a marginally important connection between accounting control procedures and government-owned company financial performance. This finding, according to the author, was mostly brought about by the majority of the examined firms using accounting control measures in an insufficient and poor manner. The study discovered that the financial performance of government-owned firms was not significantly impacted by accounting control measures. According to the findings, state-owned businesses should implement appropriate budgeting strategies to enhance their financial performance.

Abdi (2018) investigated the effect internal control systems had on the productiveness of the commercial banks in Mogadishu. The primary goals were to assess the efficiency of the internal control systems at the private banks in Mogadishu and to examine their financial results. 33 people who worked for private banks in Mogadishu as managers, chief cashiers, internal auditors, and financial directors were the study's intended participants. To analyze the data, descriptive statistics was utilized. As a research tool, questionnaires were distributed. The investigation's findings showed that the majority of Mogadishu's private banks have enough funds to carry out their declared objectives. There is also a clear division of labor. This poll reveals that internal auditors regularly, quickly, and efficiently carry out their duties.

Mwakimasinde, Odhiambo, and Byaruhanga (2014) conducted a second study to examine how internal control mechanisms affect the financial performance of Kenyan sugarcane out grower businesses. The study used descriptive correlational survey design. Data was gathered from both primary and secondary sources. Main informants from each of Kenya's nine out grower companies were surveyed in order to gather primary data. Secondary data was acquired through publications, yearly reports, and document analysis. Because the key informant technique was used, all of the finance managers and internal audit department heads for each out grower company were chosen to take part in the study. All nine of the institutes of sugarcane out growers received the data gathering tools. Cumulative frequencies and percentages were calculated using SPSS version 19.0, the statistical package for social scientists, to analyze the data. According to the study, the internal control system significantly and favorably impacted the financial performance.

Nyakundi, Nyamita, and Tinega (2017) examined the impact internal control systems had on the monetary results of small and medium-sized firms in Kisumu, Kenya. The study adopted stratified and straightforward random sampling techniques to select research population. The study's cross-sectional survey research design was adjusted, and it employed both quantitative and qualitative approaches. The research used both primary and secondary data. Standardized questionnaires and interviews were employed to collect primary data while financial statements from the sampled businesses were utilized to acquire secondary data. The data were analyzed using descriptive statistics as well as inferential statistics. The study findings revealed that internal control systems are related to a considerable change in financial performance. The study's findings confirmed the notion that internal control systems have a significant influence on Kenya's public water corporations' financial performance.

Njanike, Mutengezanwa, and Gombarume (2016) looked at factors in Zimbabwe that influence internal controls in financial institutions in emerging nations to ensure excellent corporate governance. The study looked at how internal control flaws affected corporate governance as well as the key components that make it successful. It became evident that bad corporate governance was significantly influenced by the adoption of ineffective internal controls. The study found that insufficient corporate governance was a result of the issue of "fact cat" directors as well as internal control structure gaining precedence.

Njeri (2014) investigated how internal controls affected the financial results of Kenyan manufacturing firms. The study's primary goal was to determine how internal control systems affected the financial performance of Kenyan manufacturing companies. The sample for the study was made up of twenty industrial companies. The study included both primary and secondary data. While primary data came from a structured questionnaire, secondary data came from the financial records of the questioned industrial businesses. The majority of the manufacturing firms surveyed had a strong control environment, which had a good impact on the firms' financial performance, the study, which employed multiple regression to evaluate data, found. The study came to the conclusion that manufacturing enterprises with good internal control systems outperformed those with weak internal control systems in terms of their financial performance. Manufacturing companies' governing body (the board) should be assisted by the audit committee in ensuring that the internal control system is routinely examined and assessed.

The 2018 report International Finance Corporation and World Bank emphasized the need for success of Farmers' Cooperative Societies to promote the government's agenda of employment creation, income generation and the overall economic expansion for the third world countries as Agriculture is the backbone of their economy. Aimable Ineza (2016) averred that 75% Farmers' Cooperative Societies in least developing countries have failed in the first three years of their establishment and operations owing to failures of omission or commission in their organizational controls systems. Republic of Kenya (2016) report on survey study also indicates that majority of APCSs ail from poor financial management practices making some to close down whereas a majority struggle to remain financially afloat without knowing causes of their financial predicaments. Compounding the problems of bureaucratic regulatory regime, increased licensing fees, high cooperate and corporation taxes and longtime taken by the judicial system to settle APCSs business disputes, APCSs in Kenya have suffered from poor or inadequate internal control practices. ROK (2019) has linked poor audit practice to entrepreneurs' illiteracy, and misconceptions about internal controls high cost relative to the benefits associated with it. As a result, this study aimed to investigate how internal controls affect financial performance, particularly for Farmers' Cooperative Societies in Trans-Nzoia County. Nearly all internal controls studies have only focused on large companies leaving out small companies.

2. Statement of the problem

In least developed countries (LDCs), particularly in the Kenyan economy, Farmers' Cooperative Societies have remained crucial for the reduction of poverty, generation of income, and creation of jobs. The Kenya National Bureau of Statistics report on Agricultural Producer Cooperative Survey 2019 noted that Agricultural sector supported more than 35% of newly created jobs in 2017, 2018 and 2019 (Republic of Kenya, 2019).

Trans-Nzoia County is known for many agricultural based producer cooperatives that have earned it respect in relation to the Kenyan economy. Trans-Nzoia is termed by many as Kenyan food store, as a result various organizations both governmental like Kenya Plant Health Inspectorate Service (KEPHIS), Kenya Agricultural and Livestock Research Organization (KALRO) and non-governmental such as International Livestock

Research Institute (ILRI) have made countless interventions to strengthen Farmers' Cooperative Societies s (Trans-Nzoia county Agricultural report 2019). Despite such interventions, over 55% Farmers' Cooperative Societies have not been performing well and thus unable to serve its stakeholders effectively, for example Fedha Producer cooperative society being the latest to collapse as it failed in its creditworthiness test, drop in sales, restructuring terms of service of employees and even retrenching others. In Trans-Nzoia County, it was crucial to highlight how internal controls affect financial performance of Farmers' Cooperative Societies in order to determine whether or not poor application of control activities, risk assessment, monitoring, risk control environments, and information and communication led to the failure of the business.

3. Study Objectives

The main objective of this paper is to examine the effect of internal controls on financial performance of APCSs in Kenya. Specifically, the paper seeks to examine the effect of control activities on financial performance of Farmers' Cooperative Societies in Trans-Nzoia County.

4. Research Methodology

This study embraced time series design employing both quantitative and qualitative data analysis methods. The Farmers' Cooperative Societies under study mostly produce coffee and tea. This study utilized Yamane Taro to sample 99 employees from the 26 Farmers' Cooperative Societies selected in Trans-Nzoia County. The research used purposive sampling to select 3 Directors from the 3 categories of Farmers' Cooperative Societies understudy in Trans-Nzoia County. Questionnaires was used to gather quantitative data while interview schedules to collect qualitative data. While theme analysis was used to evaluate qualitative data, descriptive and inferential statistics were utilized to analyze quantitative data.

5. Results and Discussion

Table 1: Descriptive Statistics of Control Activities on Financial Performance

STATEMENT	N	M	SD
Reconciliations is consistently documented and authorized by management.	90	4.87	.342
To carry out the objectives and mission of the organization effectively and efficiently, organization develops control activities.	90	4.53	.753
Management grants employees restricted permission to carry out specific tasks and complete specific transactions.	90	4.57	.498
Information from both external and internal parties is readily available.	90	4.87	.342
Internal controls are implemented by the company, which improves performance of APCSs.	90	4.93	.251
The person who performs reconciliation is the same person who approves transactions.	90	4.47	.502
The APCSs maintains a record of employees' trainings and achievement for the organization.	90	4.38	.488
Employees are encouraged to report fraud to APCSs, and adequate measures taken to prevent it in the future.	90	4.91	.286

Effective internal control is attributed to the highly regulated and structured environment in APCSs sector.	90	4.88	.329
Internal control systems are frequently implemented by APCSs which reduces exposure to risk.	90	4.40	.493
The APCSs maintain up-to-date duplicating and recording systems and have efficient staff management.	90	4.42	.497
Top management committee positively affects financial fraud prevention of the APCSs.	90	5.00	.000
OVERRAL MEAN SCORE	**90**	**4.68**	**0.406**

M-Mean; SD-Standard deviation

Source: Research Data (2021)

The objective of the study was to investigate the effects of control activities on financial performance on APCSs in Trans-Nzoia County. The descriptive data is summarized in Table 1, reveals that a majority of respondents agreed that reconciliations were always documented and approved by management (M=4.87; SD=.342),organizations develop control activities in order to carry out their objectives and missions effectively and efficiently (M=4.53;SD=.753); management grants employees restricted permission to carry out specific tasks and complete specific transactions (M=4.57;SD=.498), information from both internal and external parties is easily accessible (M=4.87; SD=.342); the organization implemented internal controls that improved the performance of APCSs (M=4.93; SD=.251);the person who performs reconciliation is the same person who approves transactions (M=4.47;SD=.502); In addition, respondents concurred that APCSs maintained records of employees' training and accomplishments for the organization (M=4.38; SD=.488); employees are encouraged to report fraud to APCSs, and adequate measures taken to prevent it in the future (M=4.91;SD=.286); effective internal control is attributed to the highly regulated and structured environment in APCSs (M=4.88;SD=.329);.management established control activities to successfully and efficiently monitor the financial statements; that APCSs frequently developed contingency risk plans and implemented internal control techniques have lower risk exposure (M=4.40; SD=.493), and that APCSs maintained adequate recording and duplicating systems have effective staff control (M=4.42; SD=.497) and top management positively influenced financial fraud prevention of the APCSs (M=5.00; SD=.000). The participants strongly agreed, according to the overall mean score, that control efforts had an impact on the financial performance of APCSs in Trans-Nzoia County. (M=4.68; SD=.406).

The results of the above descriptive statistics were supported by the feedback that was gathered during the interview sessions. The three directors who were chosen stated that their companies had policies and procedures in place to make sure company rules were followed. Also they were heard stating that the reconciliation was always documented and approved by the management. Further, the directors mentioned that the APCSs kept record of employees training and achievements for the organization. In addition, employees were urged to report fraud involving APCSs, and appropriate actions were taken to tackle the issue. It was also evident that the directors agreed that APCSs maintained adequate recording and duplicating systems that had efficient staff management and the top management teal positively affected financial fraud preventions of the APCSs. The directors’ remarks were as follows:

Respondent X said:

"…in our company there are policies and procedures that help to ensure management directives are followed. Also there was ease access of information from both internal and external parties".

Also Respondent Y said:

"…in organization, the APCSs keeps records of employees' trainings and achievement and reconciliation always documented and approved by management".

Another remark was from Respondent Z who said:

"…the APCSs maintain adequate recording and duplicating systems with efficient staff control. In addition, the senior management team positively affects the APCSs ability to prevent financial fraud ".

The aforementioned results confirmed Amaka's (2017) claim that internal control evaluated management effectiveness and was crucial to the growth and effectiveness of the organization. Furthermore, the study's findings agreed with those of Nyakundi, Nyamita, and Tinega (2014), who discovered that internal control systems significantly influenced the financial performance of Kenya's public water corporations. They discovered a connection between these systems and a sizable shift in financial performance as well.

Therefore, the research encourages the management of agricultural producer cooperatives societies in Trans-Nzoia County to adopt the appropriate and relevant internal controls in financial management. It is clear that putting internal controls in place can help organizations perform financially efficiently and effectively. On the other hand, lack of internal controls in organizations may result to poor financial performance. Therefore, there is need for the implementation of internal controls that can enhance financial performance in any organization.

Table 2: Descriptive Statistics of Internal Controls on Financial Performance

STATEMENT	N	M	SD
There was increase in the profits	90	4.38	.488
Sales increase experienced by the firm	90	4.93	.251
There is a positive return on investment	90	4.87	.342
There was increase in EPS	90	4.38	.488
There was improved accountability on the financial management	90	4.38	.488
OVERALL MEAN SCORE	**90**	**4.59**	**0.411**

M-Mean; SD-Standard deviation
Source: Research Data (2021)

The descriptive results in Table 2 revealed that the respondents agreed that there was increase in the profits (M=4.38; SD=.488); strongly agreed that there was sales growth experienced by the firm (M=4.93; SD=.251);a positive return on investment (M=4.87; SD=.342);there was increase in share capital (M=4.38; SD=.488) and finally there was improved accountability on the financial management (M=4.38; SD=.488). Participants highly agreed, as evidenced by the participants' overall mean score, that internal control actions had an impact on the financial performance of APCSs in Trans-Nzoia County. (M=4.59; SD=.411).

The director's remarks concurred with the above results. They were heard saying that the internal controls had led to improved sales growth of the cooperative societies. In addition, the directors said that there was improved profitability in the organizations. Moreover, there was increased return on investments and EPS. The following remarks were noted:

Respondent X said:

"…there is more profits and increase of return on investment".

And Respondent Z said:

"… we have experienced increased sales and more profits. Also we have had enhanced accountability measures on the financial performance".

6. Inferential Statistics

Table 3: Coefficients of Internal Controls on Financial Performance

Model	Unstandardized Coefficients		Standardized Coefficients	t	Sig.
	B	Std. Error	Beta		
Constant	-2.725	.212		-12.850	.000
Control Activities	.173	.055	.119	3.141	.002

a. Dependent Variable: Financial Performance

The findings in Table 3 indicate that;

The unstandardized coefficient for the constant (-2.725) suggests that when control activities are held constant, the financial performance is expected to decrease by 2.725 units.

The unstandardized coefficient for control activities (0.173) indicates that a one-unit increase in control activities is associated with a 0.173 increase in financial performance, holding other variables constant. This coefficient provides insight into the direct relationship between control activities and financial performance.

The standardized coefficient for control activities (0.119) suggests that a one-standard deviation increase in control activities is associated with a 0.119 standard deviation increase in financial performance, while controlling for other variables. This coefficient allows for a comparison of the relative importance of control activities compared to other variables in the model.

The t-value for the constant (-12.850) and control activities (3.141) indicates that both coefficients are statistically significant. This means that the observed coefficients are unlikely to have occurred by chance alone. The lower the t-value, the more significant the coefficient. The significance levels for the constant (0.000) and control activities (0.002) are both below the conventional threshold of 0.05. This suggests that both coefficients are statistically significant at the 5% level, providing further evidence of their importance in explaining financial performance.

In conclusion, the table provides information on the coefficients of internal controls on financial performance. The unstandardized and standardized coefficients offer insights into the direct and relative relationships between control activities and financial performance. The t-values and significance levels indicate that both coefficients are statistically significant, suggesting their importance in explaining financial performance.

7. Summary of Findings

The study objective was to assess how internal controls affect financial performance of APCSs in Trans-Nzoia County. According to the study's findings, respondents strongly believed that management always recorded and approved reconciliations, that internal controls were implemented by the organization to boost APCS performance, and that the organization had policies and rules in place to help ensure that executive orders were carried out. Respondents also overwhelmingly agreed that management established control activities to efficiently and effectively carry out the organization's goals and mission; management permits staff to carry out specific tasks and to perform certain transactions within restricted parameters; availability of information from external and internal parties is easily accessible and that the top management team positively affected financial fraud prevention of the APCSs.. Further, the respondents concurred that the APCSs maintained record of employees' trainings and accomplishments for the organization; The APCSs that routinely established internal control systems and created contingency risk plans were less vulnerable to risk, and their staff was effectively under their control. According to the mean score for all respondents, the respondents generally strongly agreed that control actions had effect on the financial performance on APCSs in Trans-Nzoia County.

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