THE EFFECT OF INTERNAL CONTROLS ON FINANCIAL PERFORMANCE OF MICROFINANCE INSTITUTIONS IN KENYA

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ABSTRACT
This paper is on effect of internal controls on financial performance of microfinance institutions in Kenya. Microfinance institutions in Kenya have meticulous responsibility of establishing appropriate internal controls since failure to do so open loopholes for misappropriation of resources. On the other hand excessive internal controls procrastinate growth and development. The study looked at segregation of duties, vouching, authorization and approval of accounting transactions and internal audit functions as specific objectives. Descriptive and diagnostic research designs were used in collection, measurement and analysis of data whilst multiple regression analysis and descriptive statistics to establish the relationship and strength upon which independent variables affect dependent variable. From the population of 53, 21 institutions were sampled using stratified and simple random sampling methods. The study found out segregation of duties, vouching, authorization and approval of accounting transactions and internal audit functions affect financial performance significantly. On segregation of duties the study concluded microfinance institutions should set stages in accounting processes as well as internal check hence recommending proper handling of division of labour, job rotation and job description. Secondly on vouching officers should enquire thoroughly, review support documents and accounts history of the clients hence recommending training of officers and processing at central point. On authorization and approval of accounting transactions the study concluded microfinance institutions should limit the number of officers authorizing payments and bank accounts signatories. Thus the study recommended relevant staff training and adequate provision of policies and procedure manuals. Lastly on internal audit functions the study concluded, in reviewing financial reports auditors must familiarize themselves with relevant international auditing and accounting standards while adhering to professional ethics. Additionally the study has highlighted areas for further research as other institutions besides microfinance institutions especially for comparison.

Key Words: internal controls, financial performance, microfinance institutions, Kenya

INTRODUCTION
Internal control is a process, effected by an entity’s board of directors, management and other personnel, designed to provide reasonable assurance regarding the achievement of a firm’s objectives in the effectiveness and efficiency of operations, reliability of financial and management reporting, compliance with applicable laws, regulations and protect the organization’s reputation (Kaplan, 2008). There are many controls that an MFI can institute to protect it resources against loss to improve performance. A collection of internal controls put in place by the MFI is what forms internal control system (ICS). An internal control is a topic that cuts across a number of disciplines including financial accounting and auditing. It can be traced back to ancient times. In Hellenistic Egypt there was dual administration where one side was involved in collation of taxes while the other supervising them. Sacking of Troy was
one of the examples of weaknesses of internal controls. Internal controls became apparent at the beginning of 21st century following major corporate scandals (PABC 2006).

In Kenya the giant Uchumi supermarket went under in June 2006 due to insolvency and it securities stopped trading at Nairobi stock exchange (N.S.E). It is until the Government of Kenya injected some amount to bail it out of the liquidity trap. The most apparent incident is the fall of two commercial banks in a span of less than five months. Fall of Dubai bank in 14th August, 2015 followed by Imperial bank in 13th October, 2015. The reason cited in the case of Dubai bank was serious liquidity and capital deficiencies that may render inability to meet financial obligations as and when they fall due. In the case of Imperial bank the CBK reported unsafe or unsound business conditions where the appointed Kenya Deposit Insurance Corporation (KDIC) will manage it for 12 months while investigating inappropriate banking practices. Serious ramifications followed when customers could not get back their deposits, numerous jobs were lost and many creditors could not be easily paid. This happened despite both banks being under supervision of the CBK.

Microfinance institutions are financial institutions that provide mode of finance designed to provide low income individuals with the means to become self-sufficient. A microfinance institution issue small loans to those marginalized from normal modes of finance with the intention of helping the poor prosper by allowing them to save or borrow money (Campbell R. Harvey 2012). They earn financial revenue from loans and other financial services in form of interest, fees, penalties and commissions. Financial revenue also includes income from other financial assets, such as investment income. An MFI’s financial activities also generate various expenses, from general operating expenses and the cost of borrowing to provisioning for the potential loss from defaulted loans.

The main aim of microfinance in Kenya was and is to address poverty. From 1980 to 2000, NGO’s and multinational agencies were behind many MFI’s. They were co-financing agencies. The co-financing agencies were concerned with alleviation of poverty and creation of employment as well as increasing income for the poor. They were also concerned with improving social capabilities availability and access to resources and participation in decision making.

Lending by microfinance is either group or individual based or minimalist verses intergraded approach. Group based which take the form of Grameen Model is common. Also unregistered shylocks lend at very high interest rates. Interest rates charged by specialized microfinance institutions are monthly which reflect that they are low but are actually higher than commercial banks. Group guarantee schemes have become inconvenience because each wants to plan his finances and create fear of default among members. Savings of the members become security and sometimes conditions like group registration is a requirement and that the group members must be operating businesses.
STATEMENT OF THE PROBLEM

The efficacy of internal control system on financial performance is paramount in every organization. This is because internal controls ensure prevention and detection of errors and frauds. The firm’s economic assets generate income which abets growth and sustainability. It is imperative for MFI’s to establish water tight controls if at all it is to achieve improved financial performance.

The management of the organization should meet regularly to review the affairs of the firm and direct strategic path of the firm and also ensure continued goal congruence (Reid & Smith, 2000). Internal controls check the governance of MFI’s to achieve profitability (Cha 2009; Cheng 2007) growth and development. Microfinance Institutions are prone to risks that are life threatening to the existence and sustainability. Operational and strategic risks are of non-financial character and result mainly from human error, frauds, system failure, through regulatory environment (COSO 2004) however when they materialize they lead to financial losses for the organization. A number of MFI’s face collapse or near collapse if they are unable to set up internal controls (COSO 2004). Therefore the study explores the effects of internal controls on financial performance.

GENERAL OBJECTIVE

The general objective of the study will be to establish the effect of internal controls on financial performance of MFI’s in Kenya.

SPECIFIC OBJECTIVES

1. To find out the effect of segregation of duties on financial performance of MFI’s in Kenya.
2. To find out the effect of vouching on financial performance of MFI’s in Kenya.
3. To establish the effect of authorization and approvals of accounting transactions on financial performance of MFI’s in Kenya.
4. To establish the effect of internal audit functions on financial performance of MFI’s in Kenya.

LITERATURE REVIEW

Theoretical review

Fundamental theories from corporate governance apply in formulation and implementation of internal controls. They include agency theory which has been expanded into stewardship theory, stakeholder theory, resource dependence theory, management control theory and transaction cost theory. Other relevant theories include business ethics theory, virtue ethics theory, discourse theory and postmodernism ethics theory. The study reviewed agency theory, stewardship theory, management control theory and stakeholders’ theory.
Empirical Literature Review

Segregation of duties

In MFI set up accounting processes should be done to completion by separate individuals. This is so important that the research into internal controls and external auditor’s judgments’ has indicated that the assessment of separation of duties is a dominating factor in an auditors’ evaluation of internal control structure (Ashton, 2004; Ashton and Brown, 1998; Hamilton and Wright, 2002). No single individual should have control over all phases of transaction; ideally the incompatible functional responsibilities of initiating transaction, custody of assets and record keeping should be responsibility of separate individuals. Duties are considered incompatible if a single person can carry out and conceal errors in the course of day to day activities.

Segregation of duties however faces challenges particularly in small MFI’s since it requires adequate staff. Gramling et al. (2010) found that in 2008, a majority of smaller firms with material weaknesses in internal control reported one or more SoD weaknesses. There could also be instances of collusion among staff in the system especially if the number is not big. Theoretical research addressing SoD (Tirole 1996) has used agency theory to focus on collusion. In the accounting process the accountants deployed in various sections are supposed to be objective and independent for the ICS to work.

Volume of work is another consideration which is critical in segregation of duties. The number of transactions handled on daily basis will determine the extent of segregation of duties (COSO 1994). When transactions are much documentation in terms of physical and or electronic records is much. If this is handled by few people they may be overwhelmed by workload increasing the chances of oversight in some documents (Ferrilo, Gilbert and Lynch 1992).

Vouching

Vouching is examination of the particulars contained in a document to justify correctness and flush out errors if any before acting on it to proceed to the next stage. According to COSO (2004) vouching is a technical term, which refers to the inspection of documentary evidence supporting and substantiating a transaction, by an auditor. The officer vouching document should not only look at the details contained but also think about what might be missing from the document (Bonner, et al 2006).

According to Johnson and Kaplan (2001) attaching support documents will enable the officer attending to the document satisfy himself that the process was authentic. It is after this assurance that the accounting document should advance to the next level of processing. All the support documents have reference numbers which should tally with the ones captured in the payment voucher. Dates on the support documents are very important since they reveal when activity took place. It can also reveal whether the activity being handled belong to current financial year or previous.
The officer vouching a document will also find out whether the process conformed to what is provided for in the policies of the MFI. Contravention of the MFI policies especially procurement procedures may not ensure fairness, good quality and economy which is essential and more so can elicit queries from the auditors. For the vouching to produce expected results in deterring errors and fraud (Turner 2007) the officer involved should possess rich work experience and at the same time apply professional skills.

**Authorization and approval of accounting transactions**

The scope and volume of MFI preclude the owners from authorizing every activity or product in the organization forcing them to hire managers to do that work. This work is essentially done by somebody who is hierarchical superior or in a different organization subgroup. Authorization by peers can also work only that it is marred by some influences. The agency theory support this set up as the agents consider their interest prior to equity owners. Authorizer should not be involved in the custody of the duty they are authorizing to ensure independence.

Officers have variant responsibilities depending with a particular MFI and position held along the organization structure (Carmichael 1999). The responsibilities partaken in a particular level define the position occupied by the appropriate officer. MFI’s have given their officers different levels in terms of approving payments and advancing loans (Protiviti 2007). This system is based on the order of seniority of the officers such that senior officers approve cheques bearing bigger amounts relative to junior officers. There is a sealing for every position such that the holder of that particular position cannot approve cheques more than the sealing put (Wright 2002).

This is an important control exercised by the MFI’s across the country. It is destined to ensure objectivity in reviewing payments (COSO 2004). It ensures each of the officer’s check the authenticity of the payment notwithstanding the fact that it has been attended by other signatories. It is hard for one officer to pass payment single handedly (COSO 2002). This control is also boosted by the mandates given to the bank for transacting the accounts. An MFI can give conditionality after appointing signatories as all to sign, some to sign or mandatory signatories. The agency theory, stewardship theory and management control theories are relevant to authorization and approval of accounting transactions and aspects surrounding it.

**Internal audit function**

Audit refer to independent examination of financial statements to see whether they portray a true and fair view of company state of affairs and as to whether books of account and vouchers are kept according to company’s Act. It is a management control that delves other controls to ensure achievement of profitability. For MFI’s that are registered with the NSE auditing by public external auditor is a requirement in law. External auditors report their findings to the shareholders in an AGM while internal auditors advise the management on the areas with weakness in the accounting system. A comprehensive approach of internal audit
looks at a number of areas. Some of these areas explored are operations review, financial review and compliance review.

Operational review is critical review of the operating processes and procedures that mitigate area specific risks (DeMarco, 2000). These reviews examine the use of resources to determine if they are being used in the most effective and efficient manner to fulfill the MFI’s mission and objectives (De Lomba 2000). It is very vital to MFI’s especially when it done from comprehensive approach. This abets accountability in the utilization of resources which in turn boost performance (Protiviti 2007).

Secondly financial review entails accounting and financial transactions to determine if commitments, authorizations, receipt and disbursement of funds are properly and accurately recorded and reported (COSO 2004). This type of review also determines if there are sufficient controls over cash and other assets and that there are adequate processes controls over the acquisition and use of resources.

**RESEARCH METHODOLOGY**

The study is based on the positivism paradigm. The study used descriptive survey and diagnostic research designs to find out the effects of the internal controls on the financial performance of the MFI’s in Kenya. The population comprises of 53 institutions being the members of Association of Microfinance Institutions (AMFI-Kenya, 2012).

According to Fraenkel and Wallen (2000) a simple random sample is one which each member of the population has an equal and independent chance of being selected and proportional sample is where the sample size is a fraction of the whole sample size. Simple random sampling method was used from proportional samples in every category of microfinance institutions. Random sampling method is appropriate for the study since the population is homogeneous with uniform characteristics.

The study used both primary and secondary data as well as qualitative and quantitative information. The primary data gathered from the questionnaires and interview was validated, edited and then coded. Validation was to determine return rate of questionnaires whilst editing helped in formatting information so that it can be recorded. It was classified on the basis of common characteristics and attributes. After the mass of raw data was assembled, it was tabulated in form of statistical tables in order to allow further analysis. The analysis was done using descriptive statistics to establish the relationship between the internal controls and financial performance. Descriptive statistics have been widely used in academic research on governance (Heenetigala, 2011).

The study used multiple regression equation.

The regression equation was $Y = (\beta_0 + \beta_1X_1 + \beta_2X_2 + \beta_3X_3 + \beta_4X_4 + \beta_5X_5 + \beta_6X_6 + \epsilon)$
Where;

i. $Y$ is the Financial performance
ii. $X_1$ is the segregation of duties
iii. $X_2$ is vouching
iv. $X_3$ is authorization and approval of accounting transactions
v. $X_4$ is the internal audit function
vi. $X_5$ is the age of the MFI
vii. $X_6$ is the size of the MFI
viii. $\beta_0$ is the constant (Y-intercept), $\beta_i$ are the regression coefficients of each $X_i$ ($i=1, 2, 3, 4$ and $5$)

**Research Results**

Out of the 21 questionnaires that were issued out, only 20 were duly filled and returned. This gave a response rate of 73%. On whether their MFIs are governed by board of directors, majority 76.9% of the respondents indicated that their MFIs are governed by board of directors while 23.1% indicated other governing bodies. On the academic qualification of the accounting staff, 2.6% had certificate, 33.3% had diploma and 64.1% had degree. On whether their MFIs have accounting unit key performance indicator, 82.1% of the respondents indicated that they have accounting unit key performance indicator while 17.9% indicated no. On how accounting unit key performance indicator are adhered to, 41% indicated regularly, 30.7% indicated occasionally, 23.1% indicated sometimes and 5.2% indicated not at all. On the number of staff in the accounting department, 12.8% of the respondents indicated between 21-40 staff, 71.8% indicated between 41-60 and 15.4% indicated between 61-80 staff. On the number of accounting documents that are rejected daily on average, 79.5% of the respondents indicated that less than 10 accounting documents are rejected while 20.5% indicated more than 10.

<table>
<thead>
<tr>
<th>Table 1: Segregation of Duties</th>
<th>Mean</th>
<th>Std. Dev</th>
</tr>
</thead>
<tbody>
<tr>
<td>Tasks are clearly demarcated</td>
<td>2.28</td>
<td>.559</td>
</tr>
<tr>
<td>There is a system audit trail</td>
<td>2.05</td>
<td>.793</td>
</tr>
<tr>
<td>Job descriptions are completely developed with no overlaps</td>
<td>3.66</td>
<td>.955</td>
</tr>
<tr>
<td>The reporting structure is clearly communicated</td>
<td>4.79</td>
<td>.469</td>
</tr>
<tr>
<td>There is a clear reporting structure</td>
<td>3.51</td>
<td>.756</td>
</tr>
<tr>
<td>I understand clearly how my roles feed into the overall objective of the organization</td>
<td>4.69</td>
<td>.731</td>
</tr>
<tr>
<td>Communication system in MFI is effective</td>
<td>3.30</td>
<td>1.103</td>
</tr>
<tr>
<td>Staffers share responsibilities</td>
<td>3.25</td>
<td>1.185</td>
</tr>
</tbody>
</table>

From the finding, tasks are clearly demarcated had a mean of 2.28 with a standard deviation of 0.559, there is a system audit trail for every transaction had a mean of 2.05 with a standard deviation of 0.793, job descriptions are clearly developed with no overlaps had a mean of 3.66 with a standard deviation of 0.955, the reporting structure is clearly communicated had a mean of 4.79 with a standard deviation of 0.469, there is a clear reporting structure had a
mean of 3.51 with a standard deviation of 0.756, understand clearly how roles feed into the overall objective of the organization had a mean of 4.69 with a standard deviation of 0.731, communication system in MFI is effective had a mean of 3.30 with a standard deviation of 1.103, staffers share responsibilities had a mean of 3.25 with a standard deviation of 1.185.

**Table 2: Vouching**

<table>
<thead>
<tr>
<th></th>
<th>Mean</th>
<th>Std. Dev</th>
</tr>
</thead>
<tbody>
<tr>
<td>Payment vouchers are accompanied by support documents always</td>
<td>2.000</td>
<td>.85840</td>
</tr>
<tr>
<td>Reference numbers of the support documents are captured on the payment vouchers</td>
<td>2.8974</td>
<td>.85208</td>
</tr>
<tr>
<td>The officers involved in the accounting process reject documents in case of errors</td>
<td>3.8205</td>
<td>1.02268</td>
</tr>
<tr>
<td>The officers take time to study client history</td>
<td>4.4872</td>
<td>.50637</td>
</tr>
</tbody>
</table>

From the findings in Table 4.9 above, as to whether the payment vouchers are accompanied by support documents always; the mean was 2.000 with standard deviation of 0.85840. This implies that respondents disagreed on the statement. On whether reference numbers of the support documents are captured on the payment vouchers; the mean was 2.8974 with standard deviation of 0.85208. Respondents were therefore neutral on the statement. On whether the officers involved in the accounting process reject documents in case of errors; the mean was 3.8205 with standard deviation of 1.02268 and this implies that respondents agreed on the statement. Regarding whether the officers take time to study client history; the mean was 4.4872 with standard deviation of 0.50637 and this means that respondents agreed on the statement.

**Table 3: Authorization and Approval of Accounting Transactions**

<table>
<thead>
<tr>
<th></th>
<th>Mean</th>
<th>Std. Dev</th>
</tr>
</thead>
<tbody>
<tr>
<td>Officers bear responsibility according to position held</td>
<td>3.33</td>
<td>1.154</td>
</tr>
<tr>
<td>There is efficiency in signing of accounting documents</td>
<td>3.30</td>
<td>1.103</td>
</tr>
<tr>
<td>Approval of accounting documents is properly controlled</td>
<td>2.23</td>
<td>.484</td>
</tr>
<tr>
<td>There are minimal chances of collusion among signatories</td>
<td>3.51</td>
<td>1.335</td>
</tr>
<tr>
<td>Signature/s of approvers of documents are recognized across the MFI</td>
<td>2.07</td>
<td>.579</td>
</tr>
<tr>
<td>All documents are approved before payments</td>
<td>3.66</td>
<td>1.059</td>
</tr>
</tbody>
</table>

As shown in Table 4.9, officers bear responsibility according to position held had a mean of 3.33 with a standard deviation of 1.154, there is efficiency in signing of accounting documents had a mean of 3.30 with a standard deviation of 1.103, approval of accounting documents is properly controlled had a mean of 2.23 with a standard deviation of 0.484, there are minimal chances of collusion among signatories had a mean of 3.51 with a standard deviation of 1.335, signature/s of approvers of documents are recognized across the MFI had a mean of 2.07 with a standard deviation of 0.579, all documents are approved before payments had a mean of 3.66 with a standard deviation of 1.059.
Table 4: Internal Audit Functions

<table>
<thead>
<tr>
<th>Function</th>
<th>Mean</th>
<th>Std. Deviation</th>
</tr>
</thead>
<tbody>
<tr>
<td>Internal auditors are frequently trained</td>
<td>3.30</td>
<td>1.127</td>
</tr>
<tr>
<td>Internal audit department is influenced by management</td>
<td>4.12</td>
<td>1.151</td>
</tr>
<tr>
<td>Issues raised by internal auditors are addressed</td>
<td>2.41</td>
<td>0.637</td>
</tr>
<tr>
<td>Audit department is well staffed</td>
<td>3.69</td>
<td>1.280</td>
</tr>
<tr>
<td>Audit department is effective in prevention of errors and fraud</td>
<td>3.38</td>
<td>1.041</td>
</tr>
</tbody>
</table>

From the finding, internal auditors are frequently trained had a mean of 3.30 with a standard deviation of 1.127, internal audit department is influenced by management had a mean of 3.52 with a standard deviation of 1.151, issues raised by internal auditors are addressed had a mean of 2.41 with a standard deviation of 0.637, audit department is well staffed had a mean of 3.69 with a standard deviation of 1.280, audit department is effective in prevention of errors and fraud had a mean of 3.38 with a standard deviation of 1.041.

Multiple Regression

The study conducted multiple regression analysis to establish the effect of internal controls on financial performance of MFI’s in Kenya. The results are shown in the subsequent sections.

Table 5: Model Summary

<table>
<thead>
<tr>
<th>Model</th>
<th>R</th>
<th>R Square</th>
<th>Adjusted R Square</th>
<th>Std. Error of the Estimate</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>.477a</td>
<td>.227</td>
<td>.110</td>
<td>3.86227</td>
</tr>
</tbody>
</table>

From the findings in Table 4.12, $R^2$ was 0.227 implying that only 22.7% of the dependent variable (financial performance) was explained by the independent variables while 77.3% of the variations were due to other factors not in the study.

Table 6: ANOVA

<table>
<thead>
<tr>
<th>Model</th>
<th>Sum of Squares</th>
<th>df</th>
<th>Mean Square</th>
<th>F</th>
<th>Sig.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Regression</td>
<td>1478.792</td>
<td>3</td>
<td>295.758</td>
<td>2.768</td>
<td>.034b</td>
</tr>
<tr>
<td>Residual</td>
<td>3525.785</td>
<td>17</td>
<td>106.842</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total</td>
<td>5004.577</td>
<td>38</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

ANOVA statistics of the processed data at 5% level of significance shows that the value of calculated F is 2.768 and the value of F critical at 5% level is 2.62 since F calculated is greater than the F critical (2.768>2.62), this shows that the overall model was significant.

Table 7: Coefficients

<table>
<thead>
<tr>
<th>Model</th>
<th>Unstandardized Coefficients</th>
<th>Standardized Coefficients</th>
<th>Sig.</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>B</td>
<td>Std. Error</td>
<td>Beta</td>
</tr>
<tr>
<td>(Constant)</td>
<td>3.425</td>
<td>10.037</td>
<td>.341</td>
</tr>
<tr>
<td>Segregation of Duties</td>
<td>.123</td>
<td>.236</td>
<td>.097</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Vouching</td>
<td>.114</td>
<td>.145</td>
<td>.054</td>
</tr>
</tbody>
</table>
Authorization and Approval:.018 .190 .018 .095 .025
Internal Audit Function:.045 .211 -.034 .215 .031
Size of the MFI:.053 .074 .117 .712 .048
Age of MFI: 1.486 .570 .414 2.605 .014

From the findings the regression equation is:

\[ Y = 3.425 + 0.123X_1 + 0.114X_2 + 0.018X_3 + 0.045X_4 + 0.053X_5 + 1.486X_6 \]

Where: Y = Financial Performance, X_3 = Authorization and Approval of accounting transactions, X_1 = Segregation of Duties, X_4 = Internal Audit Function, X_2 = Vouching, X_5 = age of the MFI, X_5 is size of MFIs and ε = Error Term.

From the findings in the regression analysis, if the factors (authorization and approval of accounting transactions, segregation of duties, internal audit function, age and size of the MFI) were held constant, performance would be at 3.425. A unit increase in authorization and approval of accounting transactions would lead to an increase in performance by 0.018. A unit increase in segregation of duties would lead to an increase in performance by 0.123. A unit increase in vouching would lead to an increase in performance by 0.114. A unit increase in internal audit function would lead to an increase in performance by 0.045. A unit increase in age of the MFI would lead to an increase in performance by 0.053. A unit increase in size of the MFI would lead to an increase in performance by 1.486.

**SUMMARY OF THE FINDINGS**

**Does segregation of duties affect financial performance of MFI’s in Kenya?**

The study found out that tasks are clearly demarcated, there is a system audit trail for every transaction, job descriptions are clearly developed with no overlaps, the reporting structure is clearly communicated, there is a clear reporting structure, staffers share responsibilities, an officer can properly handle work of another without prior orientation and properly understands work done by other officers in the department.

**Does vouching affect financial performance of MFI’s in Kenya?**

The study established that payment vouchers are accompanied by support documents, reference numbers of the respective support documents are properly captured on the payment vouchers, the officers involved in accounting processes have work experience and professional knowledge, in case there are errors in the document accountants reject the document, the officers consult widely.

**Does authorization and approvals of accounting transactions affect financial performance of MFI’s in Kenya?**

The study also established that officers bear responsibility according to position held, there is efficiency in signing of accounting documents, approval of accounting documents is properly controlled, there are minimal chances of collusion among signatories, signature/s of approvers of documents are recognized across the MFI, all documents are approved before
payments, cheques drawn for payments are unlikely to be dishonored and registration of documents in movement registers is strictly adhered to.

Do an internal audit functions affect financial performance of MFI’s in Kenya?

The study revealed that internal auditors are frequently trained, issues raised by internal auditors are addressed, audit department is well staffed, audit department is effective in prevention of errors and fraud, audit department regularly advise the management, auditors are given appropriate support and audit staffs are competent.

CONCLUSIONS

1. The study concludes that segregation of duties influence financial performance of MFI and this could be through setting up appropriate stages in accounting process considering number of accounting staffers in the institution. Checking the work done by the staffs who have attended to the document prior, before proceeding to the next task ensures the accuracy of the document. The findings are supported by the management control theory.

2. Secondly the study concludes vouching influence financial performance of MFI. The officers peruse accounting documents for the appropriate support documents. This is to confirm authenticity of the transaction. They review the history of the client especially where previous transactions affect current ones.

3. Thirdly the study concludes that authorization and approval of accounting transactions influence financial performance. The findings are supported by agency theory and stewardship theory.

4. Lastly study concludes internal audit functions influence financial performance. The management control theories underpin findings where internal auditors review the policies and procedures that guide activities of the MFI in operation audit. This is underpinned by stewardship theory. Preparation of financial statements should disclose all necessary material information that is of interest to various stakeholders as advocated in stakeholders’ theory.

RECOMMENDATIONS

To achieve improved financial performance by MFI’s the study recommends that;

1. Segregation of duties should be occasionally reviewed to match dynamics in accounting staff. Job rotation should be enhanced to ensure all staff can handle duties in absence of their colleagues. Job description should be modified to include wider range of activities in the accounting department.

2. Vouching should be conducted thoroughly unlike routine checking. In simple routine checking there is discretion information and fictitious entries cannot be discerned. The study recommends sensitization of the exercise to the officers so that they do it thoroughly otherwise they will be held liable for negligence.

3. To ensure that officers appointed from other areas other than finance and accounting are familiar with the accounting documents they are attending to, they should be
subjected to the training for non-accountants. This will give them rudimentary knowledge in accounting and be aware of the things they should look for in accounting document.

4. The internal auditors and accountants should be trained regularly to deal with emerging trends. The study recommends that management of MFIs in Kenya need to develop and retain adequate quality professionals in order to ensure improved internal auditor’s performance, technical, professional skills, readiness to embrace change in auditing standards, proficiency of the internal auditor required knowledge and other competencies needed to perform individual responsibilities.

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