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STRATEGIC MANAGEMENT

THE INFLUENCE OF INTERNAL CONTROLS ON THE PERFORMANCE OF DEPOSIT-TAKING SACCOS IN KIAMBU COUNTY, KENYA

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ABSTRACT

Purpose: SACCOs play a pivotal role in the economy and the financial landscape, particularly in empowering individuals and communities through collective savings and access to credit. This research paper investigated the influence of internal controls on the performance of Deposit-Taking SACCOs in Kiambu County, Kenya.

Problem Statement: Given the increasing number of SACCOs facing deregistration due to poor performance, the study aimed to deepen the understanding of how internal controls affected SACCO performance.

Methodology: A descriptive research design was adopted, focusing on all 13 Deposit-Taking SACCOs registered with SASRA as of December 30, 2022. Data was collected from the management team using semi-structured questionnaires and analyzed through multiple linear regression.

Results: The unstandardized coefficient for internal controls was B = 0.525, with a standard error of 0.092. The standardized coefficient was Beta = 0.555, and the t-value was 5.711, with a significance level of p = 0.000. This p-value indicated a highly significant positive impact on SACCO performance. The significance levels (p-values) confirmed that internal control was critical to enhancing performance outcomes, highly significant at $p < 0.001$. The results revealed a positive and significant effect of internal controls on SACCO performance.

Conclusion: This finding emphasized the necessity for SACCOs to prioritize and strengthen their internal control systems to enhance operational effectiveness and success.

Recommendations: The study recommends that the policymakers and government agents develop models that enhance corporate governance while the regulatory bodies were advised to enforce stringent standards for internal controls and facilitate training programs tailored for SACCO management to enhance internal controls practices.

Keywords: *Internal Controls, Deposit- Taking Saccos, performance*

INTRODUCTION

Organizational performance refers to a firm's ability to achieve its strategic goals effectively through sound management practices, strong governance, and a continuous focus on results (Onyango, 2014; John & Morris, 2011). Performance is influenced by aligning strategic elements such as innovation, management competencies, and inherent organizational structures, which help businesses leverage their strengths for a competitive edge (Kamau, 2018). Effective leadership plays a critical role, as it involves making strategic decisions, implementing robust internal controls, and fostering an environment that encourages high performance (Egessa & Odero, 2020). Identifying and managing these strategic factors enables organizations to optimize resources and achieve sustainable competitive advantages (Berko, 2013).

Deposit-Taking Savings and Credit Cooperative Organizations (DT-SACCOs) are key players in Kenya’s financial sector, providing essential credit and financial services to a large portion of the population. With over 80% of Kenyans relying on cooperatives for income, SACCOs have become vital for economic empowerment, both in urban and rural areas (Karuoya & Waithaka, 2023). Kenya's SACCO sector is ranked among the top globally, particularly in terms of assets, deposits, and membership, reflecting a robust and growing industry. Regulated by the SACCO Societies Regulatory Authority (SASRA), these organizations ensure compliance with licensing requirements, safeguarding members' investments (WOCCU, 2021; Otieno et al., 2015).

Despite this growth, DT-SACCOs face several challenges, including fraud, liquidity problems, and stiff competition from other financial institutions. Issues such as financial mismanagement, poor governance, and non-compliance have led to the revocation of licenses for underperforming SACCOs, causing significant financial losses and reputational damage (Waihenya, 2018; SASRA, 2019). For example, in 2019, SASRA withdrew the licenses of five SACCOs due to their inability to meet regulatory standards, affecting thousands of members and leading to substantial financial setbacks.

Addressing these issues requires the implementation of robust internal controls, which are essential for maintaining financial integrity and operational accountability within SACCOs. Effective internal controls, including governance frameworks and risk management strategies, help mitigate financial mismanagement and fraud, building trust among members. This trust encourages higher deposits and utilization of loan services, which in turn drives profitability and membership growth (SASRA, 2010). Strong internal controls also ensure that loan approval processes are rigorous, maintaining a high-quality loan portfolio and enhancing the organization's reputation.

Overall, the sustainability and success of SACCOs in Kenya depend not only on compliance with regulatory requirements but also on strategic adaptability and sound management practices. In an environment marked by rapid change and intense competition, SACCOs must continuously realign their strategies to leverage their strengths, adapt to new market dynamics, and uphold strong governance practices. The combination of effective leadership, strategic alignment, and robust internal controls will enable SACCOs to overcome challenges, sustain growth, and maintain their critical role in Kenya's economy (Mulei, 2019; Mugendi, 2019).

Statement of the problem

The Kenyan government has implemented policies and laws to support SACCOs, but despite this, many SACCOs still struggle to fulfill their obligations (Mulei, 2019). About 80% of Kenyans derive their livelihood either directly or indirectly from the SACCO sector, (Karuoya & Waithaka 2023). The SACCO industry in Kenya has been recorded the largest in Africa as a continent having a total asset to gross domestic product (GDP) at 5.7% compared to Rwanda which is 3% and Ethiopia 0.7% SASRA (2020).

The number of Kenyans depending on the SACCOS calls for measures to safeguard and protect the members' funds amidst stiff competition and the VUCA business environment. Through the published statistics by SASRA, (2022), key performance parameters like asset base, PAR, and surpluses among others rank SACCOS at different levels, some are doing brilliantly well while others are struggling. Others have even been denied License renewal due to deteriorating performance and non-compliance, others have been put under inquiries for inability to meet members' basic financial services. It has been observed that SACCOs often experience financial under-performance due to ineffective management practices and instances of fraud, (Mbuti, 2014). According to SASRA (2018), factors contributing to the poor performance of SACCOs in Kenya include mismanagement, fraudulent activities, corrupt practices, and the use of creative accounting methods to disguise poor performance raising a question on employees integrity and management competence and quality of internal controls in place to safeguard members' funds.

The SACCO sector in Kenya remains highly competitive, yet it faces emerging challenges related to technological advancements, particularly increased cybersecurity threats. These developments have necessitated the implementation of stronger controls to safeguard members' funds. According to Wamukota et al. (2022), governance scandals have adversely impacted various organizations, including SACCOs, highlighting persistent financial and corporate governance challenges. The withdrawal of licenses from previously authorized SACCOs raises critical concerns regarding the reasons behind these actions and the resulting impact on members who relied on these institutions for savings and financial services.

Based on these issues, the primary aim of this research was to address gaps identified in previous studies by examining the influence of internal controls on the performance of Deposit-Taking SACCOs (DT-SACCOs) in Kiambu County. By exploring the role of internal controls, the study provided valuable insights to enhance the strategic decision-making processes within SACCOs, promoting sustainable growth and contributing to the sector's overall stability. This comprehensive analysis not only aimed to mitigate the risks of SACCO collapse but also to accelerate growth and improve performance, ensuring long-term sustainability for SACCOs in Kiambu County.

THEORETICAL REVIEW

Theoretical review establishes a connection between the researcher and existing literature, demonstrating comprehension of theories relevant to the research topic (Kennedy, 2007). This study was achored on Resource-Based Theory and Agency Theory to provide an understanding of how intrenal control contribute to SACCO's performance.

Resource-Based Theory

Resource-Based Theory (RBT), developed by Edith Penrose (1959) and later enhanced by Wernefelt (1984), emphasizes that an organization's competitiveness is determined by its internal resources and capabilities. It suggests that firms can build effective strategies by leveraging strategic resources that provide a competitive edge, leading to long-term sustainability (Kiswili, 2021; Berko, 2013). In the context of SACCOs, RBT provides a framework for enhancing performance by viewing internal controls as strategic resources. By effectively managing and utilizing these resources, SACCOs can improve their operational efficiency, service offerings, and overall competitiveness against traditional financial institutions (Amina & Mbugua, 2018).

This theory is particularly significant for the study of DT-SACCOs in Kiambu County, as it suggests that by leveraging strategic resources like robust internal controls, these organizations can enhance the quality of their primary assets, such as loan books. Effective monitoring and management of these resources can lead to improved loan portfolios and the development of innovative, competitive products, which in turn attract and retain members. This strategic approach is expected to increase operational efficiency, profitability, and overall performance, ensuring the long-term sustainability of DT-SACCOs within the region.

Agency Theory

Agency theory, introduced by Jensen and Meckling in 1976, explains the dynamics of the principal-agent relationship, focusing on conflicts that arise when one party delegates decision-making to another. The theory introduced the concept of agency costs, which are expenses incurred to monitor and align the interests of agents with those of principals. Over time, scholars such as Eisenhardt (1989) expanded its applicability, emphasizing the importance of governance mechanisms to mitigate agency problems, while Fama (1980s, 1990s) underscored the role of these mechanisms in enhancing organizational performance. Today, agency theory remains a cornerstone in corporate governance, offering insights into aligning managerial actions with shareholder interests, thereby fostering overall organizational efficiency.

In the context of Savings and Credit Cooperative Organizations (SACCOs), agency theory is essential for understanding the relationship between members (principals) and managers (agents). Conflicts of interest can arise when managers prioritize their own interests over those of the members, making effective internal controls and robust board oversight crucial (Mulei, 2019; Kandukuri et al., 2015). By establishing comprehensive risk management practices and monitoring mechanisms, SACCO members can ensure that management actions align with their interests, reducing risks of mismanagement and fraud. This application of agency theory reinforces the cooperative’s mission to serve its members effectively and promotes long-term organizational resilience (Kiilu, 2021).

Empirical Review

Several scholars have extensively researched the role of internal controls and their impact on organizational performance. This chapter examines studies that focus on the relationship between internal controls and performance, highlighting their importance across different sectors. According to the Institute of Internal Auditors (IIA, 2012), internal control refers to a comprehensive system of methods, procedures, and safeguards implemented by an organization to enhance the likelihood of achieving its business objectives. These systems are essential for financial performance, legal compliance, and the overall reliability of a company's financial records (Kiyieka & Muturi, 2018). Effective internal controls not only help in monitoring assets but also maintain the integrity of accounting processes, building members' confidence by preventing fraudulent activities (Umar & Dikko, 2018).

Empirical studies support the positive impact of internal controls on performance. For instance, Umar and Dikko (2018) investigated the effects of internal controls on the performance of commercial banks in Nigeria. Their findings revealed a strong positive relationship between the effectiveness of internal controls and improved bank performance, suggesting that robust control systems are crucial for organizational success. Similarly, Kiyieka and Muturi (2018) conducted a study on the effect of internal controls on the financial performance of deposit-taking Savings and Credit Cooperative Societies (SACCOs) in Kisii County, Kenya. The study established that SACCOs with efficient and effective internal controls demonstrated stronger financial performance compared to those that did not prioritize these systems.

Further research by Frederick and Kyomuhendo (2022) on the internal controls, managerial competence, and financial performance of ABU SACCO also confirmed the positive influence of internal controls on financial outcomes. They emphasized the need for management to strictly adhere to internal control components, such as monitoring, clear communication, and control of activities and environment, to enhance financial performance. This study reiterated that following a structured internal control framework could lead to better financial outcomes, supporting the view that effective internal controls are fundamental to organizational success.

Overall, the literature underscores the critical role of internal controls in ensuring operational efficiency, financial integrity, and sustained organizational growth. By implementing robust control systems, organizations can not only safeguard their assets but also enhance their financial performance, ensuring long-term stability and confidence among stakeholders.

Firm's Performance

Organizational performance is the achievement of an organization's key goals as outlined in its strategic plans (Ghosh & Ansari, 2018). Despite their contributions to socio-economic development, many firms struggle to maintain superior performance due to uncertainties and changes in the business environment (Charles & Ochieng, 2023). Performance can be measured using various parameters, with researchers employing different metrics depending on the organizational context. For example, Frederick and Kyomuhendo (2022) measured financial performance in Ugandan SACCOs using profitability, financial efficiency, and liquidity, finding that effective internal controls and management competence positively impacted performance.

Studies in different sectors have applied varied measures to assess organizational performance. Adamade and Gunu (2017) focused on manufacturing companies in Nigeria, measuring performance in terms of return on invested capital and concluding that strategic factors influenced these returns. Egessa and Odero (2020) examined Deposit-Taking SACCOs in Kenya, using customer satisfaction, membership base, asset base, and deposit base to measure how innovation affects performance. Their study found that innovation had a significant positive effect on SACCO performance, enhancing key aspects like asset and deposit growth.

Ghosh & Ansari (2018) and Charles and Ochieng (2023) further highlight the diversity in performance metrics. Ghosh & Ansari measured SACCO performance in Kenya by considering active accounts, customer deposits, Return on Assets (ROA), and profitability, revealing that good corporate governance improved financial health and customer retention. Charles and Ochieng's research on strategic outsourcing found that aspects like service integration, offshore outsourcing, and multi-sourcing influenced firm efficiency, profitability, competitive advantage, and employee productivity. Together, these studies emphasize that organizational performance can be assessed through a variety of lenses, depending on strategic focus and industry context.

Conceptual Framework

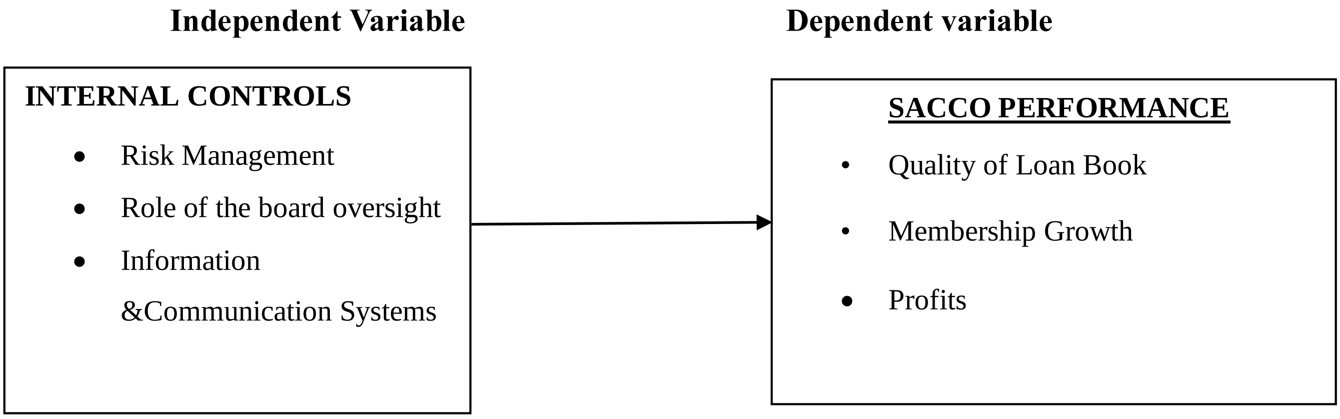

Figure 1: Conceptual Framework

Source: Author (2024)

RESEARCH METHODOLOGY

This study adopted a descriptive research design to gather data on the relationship between independent and dependent variables, providing a detailed understanding of key issues and enabling informed decision-making (Sekaran & Bougie, 2013). The target population comprised 110 senior, middle managers, and lead supervisors from 13 Deposit-Taking SACCOs (DT-SACCOs) in Kiambu County, registered with SASRA as of 30th December 2022. Semi-structured questionnaires, featuring a mix of open-ended and closed-ended questions, were administered through a drop-and-pick-later method. The survey included a Likert scale with five response options ranging from "strongly disagree" to "strongly agree," ideal for measuring attitudes and beliefs (Mugenda & Mugenda, 2013). Data analysis was performed using SPSS, and multiple regression analysis was employed to explore the connections between variables, using a linear regression model to interpret the findings-

$$\mathbf{Y = \beta_0 + \beta X + \varepsilon}$$

Where: - Y= was SACCO performance.

X_1 = Internal Controls.

β_0 = Constant

ε=Error term of the model.

FINDINGS AND DISCUSSIONS

The study analyzed 82 completed questionnaires out of 110 targeted, achieving a 75% response rate deemed adequate by Kothari (2011). Demographically, 56.79% of respondents were female and 43.21% male, with age distribution showing 12.3% aged 18-30, 58.0% aged 31-40, 27.2% aged 41-50, and 2.5% over 50, indicating a predominance in the 31-40 age group. Educational backgrounds varied: 2.5% held a PhD, 19.8% a Master's, 56.8% a Bachelor's, 13.6% a Diploma, and 7.4% in "Other" categories. Experience levels included 3.7% with less than 1 year, 37.8% with 1-5 years, 31.7% with 6-10 years, and 26.8% with over 10 years in the organization. Respondents held diverse roles: 11% in top management, 54% in middle management, and 35% as lead supervisors.

Descriptive Analysis

Descriptive Statistics for Internal Controls

The study conducted a descriptive analysis for internal controls. The findings are as presented in Table 1 below:

Table 1: Descriptive Statistics for Internal Controls

Source: Survey Data, (2024)

	N	NS = Not Sure	SD = Strongly Disagree;	D = Disagree;	A = Agree;	SA = Strongly Agree;	Mean	Std. Deviation
The SACCO employs effective methods to assess the creditworthiness of borrowers	82	12.2	3.7	8.5	51.2	24.4	3.7195	1.23002
The SACCO has robust strategies in place to address operational risks such as fraud and cybersecurity threats	82	4.9	3.7	22	58.5	11	3.6707	0.90342
The board represents the interests and concerns of SACCO members effectively	82	9.8	2.4	22	51.2	14.6	3.5854	1.08811
The board ensures compliance with regulatory requirements and ethical standards.	82	6.1	1.2	13.4	65.9	13.4	3.7927	0.91271
The SACCO ensures the security and confidentiality of member data in its information systems	82	1.2	1.2	4.9	65.9	26.8	4.1585	0.67531
The SACCO provides adequate training and support to staff members to effectively utilize information systems.	82	11	3.7	13.4	53.7	18.3	3.6463	1.15867
Aggregate Score							**3.762183**	**0.994707**

The data analysis reflects members' perceptions of the SACCO's effectiveness across various operational and governance areas, evaluated using a Likert scale. The assessment of borrowers' creditworthiness methods scored a mean of 3.72 (SD = 1.23), indicating general positivity but notable variability in opinions. Strategies for addressing operational risks like fraud and cybersecurity received a mean of 3.67 (SD = 0.90), showing moderate agreement but some uncertainty. The board's effectiveness in representing member interests was rated lower at 3.59 (SD = 1.09), reflecting considerable disagreement and lack of consensus. In contrast, compliance with regulatory requirements was perceived more positively, with a mean of 3.79 (SD = 0.91), while the SACCO's commitment to data security scored the highest at 4.16 (SD = 0.68), indicating strong consensus. Training and support for staff on information systems had a mean score of 3.65 (SD = 1.16), suggesting varied perceptions. Overall, the aggregate mean score of 3.76 (SD = 0.99) points to a generally positive view of the SACCO's operations, though the variability in responses indicates areas of concern, particularly regarding board representation and staff training.

Descriptive Statistics SACCO Performance

The descriptive results are as shown in Table 2:

Table 2: Descriptive Statistics SACCO Performance

	N	NS = Not Sure	SD = Strongly Disagree;	D = Disagree;	A = Agree;	SA = Strongly Agree;	Mean	Std. Deviation
Profitability has increased in consecutive years.	82	1.2	3.7	17.1	47.6	30.5	4.0244	0.86031
The quality of loan book has improved over the years	82	3.7	3.7	22	50	20.7	3.8049	0.93543
Membership has grown in the consecutive years	82	4.9	1.2	6.1	57.3	30.5	4.0732	0.9267
Portfolio At Risk has reduced in consecutive years	82	1.2	4.9	37.8	37.8	18.3	3.6707	0.87566

Source: Survey Data, (2024)

The data presented a generally positive assessment across the surveyed metrics. The data analyzed reflected members' perceptions of key performance indicators of the SACCO, using a Likert scale ranging from Strongly Disagree (SD) to Strongly Agree (SA). The statement regarding profitability increasing in consecutive years received a mean score of 4.02 (SD = 0.86), indicating that most members agreed or strongly agreed with this assessment, although some variability suggested that not all were confident.

The quality of the loan book scored 3.80 (SD = 0.93), showing that members tended to agree that it had improved over the years, but opinions varied, with some members possibly being unsure or disagreeing. Membership growth received a score of 4.07 (SD = 0.93), indicating strong agreement among members about positive trends in membership, with many agreeing or strongly agreeing that growth was evident.

Conversely, the statement regarding the reduction in Portfolio At Risk scored 3.67 (SD = 0.88). While this score indicated general agreement, the variability suggested that not all members were confident in the effectiveness of the SACCO's risk management strategies, with some possibly unsure or disagreeing. Overall, while members recognized improvements in profitability, loan quality, and membership growth, the differing levels of agreement, especially concerning Portfolio At Risk, pointed to opportunities for the SACCO to engage with members and address any concerns.

Regression Analysis

The study performed a regression analysis to assess the effect of internal controls on the performance of DT SACCOs within Kiambu County.

Beta Coefficients of Study Variables

Table 3: Regression Coefficients

Coefficients[a]						
		Unstandardized Coefficients		Standardized Coefficients		
Model		B	Std. Error	Beta	t	Sig.
1	(Constant)	.250	.458		.545	.587
	Internal controls	.525	.092	.555	5.711	.000
a. Dependent Variable: SACCO PERFORMANCE						

Survey Data, (2024)

From the above table, the following regression equation was derived

$Y = 0.25+0.525X_3$

SACCO PERFORMANCE=0.250+0.525 Internal Controls.

The analysis in Table 3 shows that a one-unit increase in internal controls leads to a 0.525-unit increase in SACCO performance, with a constant term of 0.25 representing the baseline performance when other variables are zero. The constant had a standard error of 0.458, a t-value of 0.545, and a significance level of 0.587, indicating it was not statistically significant. In contrast, the unstandardized coefficient for internal controls was 0.525 (standard error = 0.092), with a standardized coefficient (Beta) of 0.555. The t-value was 5.711, and the significance level was $p = 0.000$, reflecting a highly significant positive impact on SACCO performance. The very low p-value ($p < 0.001$) underscores the critical role of internal controls in enhancing performance outcomes.

Content Analysis Results

From the qualitative questions, a key research question was posed to respondents regarding the impact the impact of internal controls on the performance of DT SACCOs in Kiambu County. The data collected demonstrated that effective internal controls were crucial in shaping SACCO performance by ensuring financial accuracy, minimizing fraud, and enhancing operational efficiency. Strong internal controls were found to improve risk management, boost staff morale, and increase member trust, thereby supporting the

SACCO's stability and profitability. Conversely, instances of weak internal controls historically led to financial losses, operational inefficiencies, and diminished member confidence.

Internal controls demonstrated the most pronounced effect on SACCO performance, with a beta coefficient of 0.555 and a significance level of 0.000. This substantial impact highlighted the critical role of effective internal control systems in ensuring financial accuracy, operational efficiency, and risk mitigation. Data indicated that robust internal controls were crucial for enhancing overall SACCO performance, increasing member trust, and supporting stability and profitability. Notably, instances of weak internal controls historically led to financial losses, operational inefficiencies, and diminished member confidence.

CONCLUSION

The study concludes that internal controls have a substantial and positive impact on the performance of Deposit-Taking SACCOs (DT SACCOs) in Kiambu County. Internal controls emerged as a critical factor influencing performance, highlighting the need for SACCOs to prioritize and strengthen these systems to enhance operational effectiveness, ensure long-term success, and support sector growth and continuity. Effective internal controls are essential for safeguarding members' funds from fraud and mismanagement, relying on well-developed and regularly updated policies.

The findings underscore that strong internal controls are foundational to the success of DT SACCOs. The significant positive impact observed suggests that SACCOs must focus on establishing and maintaining comprehensive control systems, which include regular audits, risk assessments, and staff training. These measures help foster a culture of compliance and accountability. By reinforcing internal controls, SACCOs can effectively mitigate risks related to financial mismanagement and operational inefficiencies, thereby strengthening their overall resilience and capacity to serve their members.

RECOMMENDATIONS

The study recommends that DT SACCOs in Kiambu County should focus on strengthening their internal control systems to enhance financial accuracy and operational efficiency, which would significantly improve overall performance. SACCOs should conduct regular audits and risk assessments, establishing a routine schedule to identify and address weaknesses proactively. Empowering the board of directors to oversee these processes is crucial, ensuring that they are actively involved in reviewing audit findings and implementing corrective actions. Additionally, enhancing communication channels within the organization is essential. Clear and open lines of communication between management, staff, and the board will facilitate the timely sharing of information about potential risks and control deficiencies, fostering a culture of transparency and accountability.

The study further recommends implementing comprehensive risk management policies to safeguard members' funds and address potential risks effectively. Regular staff training on these policies, compliance requirements, and fraud prevention strategies will help maintain robust internal controls. Leveraging technology for monitoring and reporting can also improve internal control effectiveness by streamlining processes, reducing human error, and providing real-time insights. Integrating reward systems for staff who uphold internal controls and demonstrate integrity can foster a proactive approach to risk management. For broader impact, policymakers and regulatory bodies should develop models that promote corporate governance and strategic leadership within DT-SACCOs, enforce internal control standards, and facilitate training programs for SACCO management to strengthen governance and accountability.

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