

Impact of Effective Internal Control Implementation on Private commercial Bank's Financial Performance; Special Reference to Central Province of Sri Lanka.

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Abstract

Internal control system is a system design and implemented by the management to safeguard assets, ensuring accuracy and reliability of information and increasing the effectiveness of entity's operations. The need for the internal control system in Banks can't be undermined since the banking sector has a crucial role to play in the economic stability and rapid growth in real economic activities. Nevertheless, effective implementation of internal controls on private bank's financial performance is under studied. Therefore, the study investigates the impact of internal control components on Financial performance of private banks in the Central province of Sri Lanka. Internal controls are measured by the COSO Model of internal controls and five hypotheses were developed using components of internal control (Control environment, Control Activities, Risk Assessment, Information and communication, Monitoring). Financial performance measured based on scales used by previous scholars. The Sample of the study was selected using stratified sampling technique which comprises of 70 executive level employees from Private commercial banks in Central province. The study approach is quantitative and thus deductive approach and data was collected through questionnaire and hypotheses were tested using Multiple regression analysis. As per the multiple regression analysis control environment, risk assessment, information and communication and monitoring have the significant impact while control activities have insignificant impact on the financial performance of private Banks in central province. Based on the finding's researcher concluded that there is a need of much consideration on control environment, risk assessment, information and communication and monitoring which predict the financial performance of private Banks in central province.

Keywords: Internal controls; Financial Performance; Private Banks

1. INTRODUCTION

Internal control system is a vital role in every organization to achieve their management objectives. Internal control system can be defined as a system which has the features of maintaining the assets of a company and ensuring accuracy and reliability of information and reports related to accounting and other procedures and increasing the effectiveness of the operations Gündoğdu (2014). An internal control system which is created by management and implemented by management and employees is a process which is designed to ensure reasonable assurance to achieve specified objectives. In 1992, Committee of Sponsoring Organizations of tread way commission (COSO) developed a model for appraising internal controls. This model has been accepted as the generally accepted framework for internal control. The Company also maintains a system of disclosure controls and measures to ensure that information required to be revealed by the Company is recorded, processed, summarized and reported within the required time periods and accumulated and communicated to the Company's management to allow timely decisions regarding disclosure. Although these procedures are intended to identify and manage risks that could undesirably impact the achievement of the Company's business objectives, they do not provide unconditional assurance against material misstatement, errors, losses or fraud. (Dinesh Kumar, 2012, p. 58).

Banking sector in Sri Lanka plays a major role within the Sri Lankan financial system (Central Bank, 2018, P.345). The main objective of internal control system for Banks is to continuously track the accordance of all banking practices and operations with international auditing standards, banking laws, guidelines and rules to solve problems that may arise where required. In addition to this, with an effective internal control system, inaccurate, fraudulent transactions and irregularities are less to happen in Banks.

Due to the complexity of Banking transactions and many customers engage in banking transactions Banks can create vulnerable transactions of systematic nature. Therefore, there should be a soundness of Bank transactions which contribute towards maintaining stability in financial system in Sri Lanka. If banking sector collapsed the whole economy face to critical problem. The need for the internal control system in the organizations, especially Banks can't be undermined since the Banking sector which has a crucial role to play in the economic instability, slow growth in real economic activities, corruption and risk of fraud. (Olatunji, 2009, p.183).

Sri Lanka CID (Criminal Investigation Division) investigates Rs.40 million frauds at commercial Bank by altering data through fake debit card (News Desk, 2015). Investigation by Central Bank of Sri Lanka found that leak of customer data at HNB due to internal lapses (Economy next, 2017). interim financial released to CSE shows Internal fraud cost of NTB amounting to Rs.365 million during first quarter of operations ended in 31 /3 /2015 (Daily mirror, 2013).

Problem Statement

According to the background of the study its emphasis the importance of internal control in the Bank's Financial performance because banks contribute higher amount to the economic stability of Sri Lanka through banks in Sri Lanka. If Bank Financial performance increases, it effects to the economic growth by enhancing GDP. According to Gunawardhana (2014) shows the increasing of frauds within whole Banking system with the computerization of Bank operations has been increase gradually. The most serious problem hampering the smooth operation in public and private sectors at all the levels has been fraud, errors, defalcations, mismanagement and abuse of Banks. Fraud is really eating deep into the system and that any organization with a weak internal control system, is dangerously exposed to fraud. Control environment its enable to reducing the level fraudulent activities within organizational operation (Ayagre, Gyamerah, & Nartey, 2014) Internal control systems are put in place to ensure safe custody of all assets, detect and safeguard against probable frauds (Magu & Kibati, 2016) Even though every Bank tie with regulations and implement internal control within Bank how these kind of fraudulent activities can be happen which directly effect on Bank performance and it's a question whether there is an impact of internal control on financial performance of private commercial banks.

Most of the prior studies in performance intention were mainly focusing on managerial employees as well as non-managerial employees there are few researchers have found on direct impact of internal control on financial performance (Ayom, 2013; Dineshkumar & Kogulacumar, 2015; Douglas, 2012; Ilias, Abdulatiff, & Mohamed, 2016; Mahadeen, Al-Dmour, Beidat, & Tarhini, 2016; Shanmugam, Haat, & Ali, 2012) with exception to the Dineshkumar and Kogulacumar (2015) research which directly research on that relationship in Sri Lanka for the Tele communication industry above studies were oversea based. Therefor this research is given valuable base for future researchers. And, they are no research conducted to the central province of Sri Lanka regarding this research area. Therefor there is a research gap exist in Sri Lankan context as well as in International context.

When considering about dimensions those affecting to Financial performance researchers do not identified the same dimensions Yemer and Chekol (2017), Ndungu (2013), Mwachiro (2013), Mohomad (2018) identified dimensions of financial performance as Growth in revenue, Shabri, Saad, and Bakar (2016), identified profitability, In here cannot identify consistency of dimensions relating to the financial performance dimensions. It is an important problem observed in examining prior study. Therefore, due to the practical issues of control efficiencies and literature gap exist in relate to the internal control and its impact on financial performance of private commercial banks in Central Province of Sri Lanka lead to the identification of a research problem that is worth to study. The problem statement addressed in the present study: *whether there is an impact of Internal Control on Financial performance of Private commercial banks in Central Province of Sri Lanka?*

2.LITERATURE REVIEW

2.1. Internal controls

Internal control system is important for the smooth running of organizational operations. There are financial and non-financial assets that need to be efficiently and effectively controlled and monitored so that the organization can remain profitable and evergreen (Olufunmilayo & Hannah, 2018). "Internal Controls are processes designed and caused by those charged with governance, management, and other personnel to provide rational assurance about the entity goal achievement. About reliability of the financial reporting, effectiveness and efficiency of operations and compliance with appropriate laws and regulations" (Kinyua, Gakure, Gekara, & Orwa, 2015).

Corporate should be benefited from a better understanding of the interrelated connection among the components of internal control systems, which are integrated into the management process resulting in the maximizing shareholders' value. While all components of an internal control system are vital, a combination between them can lead to managerial excellence and effective governance (Koutoupis & Pappa, 2018). There are many empirical evidences which emphasize the requisite of internal control system in banking system. According to Adenugba and Adeyemi (2011) an insufficient internal control system often causes an inability to detect fraudulent activities and a decrease in the performance of banks. Research conducted by Gündoğdu, (2014) shows that internal control activities of the banks are adapted to the international standards in Turkey and effective control procedures exists in the banking system. In addition, efficient internal control mechanism has great impact on strong and stable outlook of Turkish banking sector.

Olatunji (2009) studied the impact of internal control system in banking sector and according to the findings the ineffective internal control system is the major cause of Bank frauds in Nigeria. It is then determined that the management of every Bank should generate and establish a standard internal control system, strong enough to stand against the tricks of fraud in order to promote continuity of operations and to ensure the liquidity, solvency and going concern concept of the Bank (Olatunji, 2009).

Amudo and Inanga (2009) identify the following six essential components of an effective internal control system; control environment, control activities, risk assessment, information and communications, monitoring, and information technology in their study. The findings of the study revealed that measuring effectiveness of internal control is concerned with the existence and functioning of the six major control components identified by the model. Internal control activities have been much important in Banking practices as the time passes. Furthermore, it is also worth revealing that modern internal control system approach has started to gain importance instead of traditional approaches and methods. It is also clear that the Banks have been trying to improve and put forward distance and central internal control practices through reducing centralized audit and control functions (Gündoğdu, A., 2014). The formation of internal control plays an important in prevention of fraud and irregularities. It is also a foundation for the conclusion that, management and relevant authorities should focus on more strategic ways of internal control establishment as a way to preventing fraud in the public sector (Ademola, I.S, Adedoyin, & Alade, 2015).

2.2. Dimensions of internal control

The COSO framework is built around five main control areas – control environment; risk assessment, information and communication, control activities and monitoring and corrective action. (Inusah & Abdulai, 2015).

Control Environment

The control environment is the one of the five components of the COSO framework and it is composed of the following five principles they are: Integrity and ethical values, Board of director's independency from management and oversight of internal controls, Organization structure, Attracting, develop, and retain quality employees, Management's control philosophy and risk appetitive (Committee of Sponsoring Organizations of the Treadway Commission, 2013).

The heart of effective control is an emphasis on controls categorized as the control environment; management's philosophy and operating style, integrity and ethical values, assignment of authority and responsibility (e.g., accountability), human resource practices (e.g., training, performance appraisal, remuneration and compensation, employee counseling), audit committee, and internal audit (Inusah & Abdulai, 2015). Some of the control environment activities that an organization can undertake include; having an accounting and financial management system, management being committed to the operation of the system, management closely monitoring implementation of internal control systems in organizations, management providing feedback to the junior officers about the operation of the system and having appropriate measures to correct misfeasance in operation of the organization's accounting and finance management system. Further still, an organization's management should act with a great degree of integrity in execution of their roles, uphold ethical values in all management decisions, establish an objective, independent and active audit committee, and ensuring that the board of governors and its committees are independent of management (Kamau, 2014).

For cooperative organizations, the factors related to the control environment include the integrity and ethical values, commitment to competence of employees, management's philosophy and operating style, organizational structure, assignment of authority and responsibility, human resources policies and practices, and the activities of the board of directors or audit committee towards organizational objectives. (Mendoza, 2012). "Control Environment" the results indicate that integrity and ethical values, Code of Conduct and Flowchart are essential elements of the control environment. (Kinyua, Gakure, Gekara, & Orwa, 2015).

Control Activities

The next component of internal control system is control activities. When reviewing empirical studies researcher was able to define control activities as follows. Control activities are the policies and procedures that help ensure that management directives are carried out, for example, that necessary actions are taken to address risks that threaten the achievement of the entity's objectives (Nyakundi, Nyamita, & Tinega, 2014).

Control activities, whether within IT or manual system, have various objectives and are applied at various organizational and functional levels. Generally, control activities that are relevant to an audit may be categorized as policies and procedures that pertain to the following: Performance reviews (Nyakundi, Nyamita, & Tinega, 2014). These control activities include reviews and analyses of actual performance versus budgets, forecasts, and prior period performance; relating different sets of data, operating or financial to one another, together with analyses of the relationships and investigative and corrective actions; comparing internal data with external sources of information; and review of functional or activity performance, such as a Bank's consumer loan manager's review of reports by branch, region, and loan type for loan approvals and collections (Mary, Albert, & Byaruhanga, 2014). Most Bank employees believe that "Control Activities" is the policies and procedures, which are used to ensure that management directives are met. (Karagiorgos, Drogalas, & Dimou, 2012).

Risk Assessment

The third major component of internal control is risk assessment. Risks are the happenings that threaten the achievement of objectives. They finally affect an organization's ability to achieve its mission. Risk assessment is the process of detecting, assessing and determining how to succeed these things. There are both internal and external risks that could prevent the achievement of established objectives at the every level in an organization (Gamage, Lock, & Fernando, 2014). Risk assessment involves the use of systematic procedures to identify and analyze relevant risk and the subsequent management of those risks. Risk assessment incorporates the broader concept of "business risk," not just the risk related to fraud, error or misstatement in financial reporting. Risk assessment should include a strong focus on a cost versus benefit approach to control. (Inusah & Abdulai, 2015).

Some of the risk assessment indicators include; having mechanisms in place to identify and react to changes that can have dramatic effects on the operations; establishing controls for approving decisions regarding financing alternatives and accounting principles, practices and methods, assessing risks according to changes in the operational environment, analyzing the risks that may arise due to changes of new staff and determining the risks that are likely to be brought about by restructuring and establishing whether new services are likely to bring risks to the organization (Bett & Memba, 2017). "Risk Assessment" is considered as a key part of management process which is in place to identify and assess barriers to achieving Bank's objectives. (Karagiorgos, Drogalas, & Dimou, 2012).

Risk management in business it is sometimes referred to as Enterprise Risk Management (ERM), is the process of planning, organizing, leading, and controlling the activities of an organization in order to minimize the effects of risk on an organization's capital and earnings. Enterprise risk management expands the process to include not just risks associated with accidental losses, but also financial, strategic, operational, and other risks (Little, 2013). Risk management is about identifying all internal and external risks in the organization in terms of its significance, likelihood and cause, and establishing plans to prevent/reduce/avoid the occurrence of these risks. Risk significance is a measure of the magnitude of the risk effect if the unfavorable event were to occur. The effect is the ultimate harm that may be done or the opportunity that may be lost that should be quantified if possible. Likelihood is the probability that an unfavorable event would occur if there were no control activities to prevent or reduce the risk from occurring (Dionne, 2013).

Information and Communication

Information and Communication focuses on the nature and quality of information needed for effective control that the systems use to develop such information and reports necessary to communicate it effectively. Information is needed at all levels of organization to assist management in meeting the organization's objectives. (Gamage, Lock, & Fernando, 2014). According to the SLAuS,(2013) an information system encompasses methods and records that: Identify and record all valid transactions, Describe on a timely basis the transactions in sufficient, Measure the value of transactions in a manner that permits recording their proper monetary value in the financial statements, Determine the time period in which transactions occurred to permit recording of transactions in the proper accounting period, Present properly the transactions and related disclosures in the financial statements.

Information is needed at all levels of organization to assist management in meeting the organization's objectives. The information is used by inside parties as well as outside parties. This information should be communicated from top to bottom level that needs it in a form and within a time frame that helps them to carry out their responsibilities. Communication also use by outside parties such as customers, suppliers and regulators. Information about an organization's plans, control environment, risks, control activities, and performance must be communicated up, down, and across an organization. Reliable and relevant information from both internal and external sources must be identified, captured, processed, and communicated to the people who need it in a form and timeframe that are useful.

Monitoring

Monitoring can be defined as a continuing function that aims primarily to provide the management and main stakeholders with early indications of positive or negative progress, in the achievement of objectives. Monitoring helps organizations to assess the quality of performance over time and determine the efficiency of its controls. "Monitoring" most Bank's employees believe that Monitoring procedures are an inherent part of the Bank and are performed on a real-time basis reacting dynamically to changing conditions (Karagiorgos, Drogalas, & Dimou, 2012).

The purpose of monitoring is to determine whether internal control is adequately designed, properly executed, and effective. Internal control is adequately designed and properly executed if all five internal control components (Control Environment, Risk Assessment, Control Activities, Information and Communication, and Monitoring) are present and functioning as designed (Nyakundi, Nyamita, & Tinega, 2014). Monitoring is done to ensure that controls continue to operate effectively. For example, if the timeliness and accuracy of Bank reconciliations are not monitored, personnel are likely to stop preparing them. Monitoring of controls is accomplished through ongoing monitoring activities, separate evaluations, or a combination of the two (SLAuS, 2013).

Monitoring can be defined as a continuing function that aims primarily to provide the management and main stakeholders with early indications of positive or negative progress, in the achievement of objectives. Monitoring helps organizations to assess the quality of performance over time and determine the efficiency of its controls. Effectiveness of the internal control can be achieved through ongoing monitoring at each level of out. Furthermore, monitoring of the major risks should be the part of the daily activities of the all organizations along with the periodic evaluations (Abbas & Iqbal, 2012).

2.3. Financial performance

Financial performance is a measure of company's policies and operations in monetary terms. It is a general measure of a firm's overall financial health over a given period and can be used to compare similar firms across the same industry or to compare industries or sectors in aggregation. There are many ways to Measure Company's financial performance. (Kinyua, Gakure, Gekara, & Orwa, 2015). In the context of organizational financial performance, performance is a measure of the change of the financial state of an organization, or the financial outcomes that results from management decisions and the execution of those decisions by members of the organization. Since the perception of these outcomes is contextual, the measures used to represent performance are selected based upon the circumstances of the organization(s) being observed (Carton, 2004).

Impact of internal controls on financial performance

Positive financial performance in a firm can be achieved by eradicating waste in benefits services processes and systems. The "critical success factor" for a firm is the degree to which it fulfils its set objectives and mission in terms of being efficient, effective and economical. The information obtained from a sound internal control system as reflected from financial statements will provide a report on a firm's financial performance and position that is useful to a wide range of users for assessing the stewardship and making economic decisions (Doyle, Ge, & McVay, 2007).

According to thesis of Douglas conducted on internal control contribution on efficiency and effectiveness in Eco Bank Ghana limited revealed that internal control systems in Eco Bank Ghana Limited and the Banking sector in general. However, the effectiveness of the internal controls could not be described very effective since monitoring is less effective. (Douglus, 2012).

A study regarding "Internal control effectiveness & its relationship with financial performance ". The Results showed that Internal control effectiveness is strongest in private Banks, followed by public Banks and weakest in Islamic Banks, although the difference is not statistically large, but slight variation exists. Moreover, private Banks had a high level of financial performance; public Banks had moderate level of financial performance whereas Islamic Banks were found to have low financial performance. Hence it was concluded that internal control effectiveness has a positive relationship with the financial performance of the Banks (Khan, Shakri, & Chanar, 2015).

Empirical study on Effect of internal control on financial performance in an institution of higher learning in Uganda reveals that there is a significant positive relationship between internal control system (control environment, internal audit, and control activities) with financial performance (liquidity, accountability, and reporting) (Mawanda, 2008).

Another research carried out to find out the impact of internal control and financial performance of private and public organizations in Jaffna district revealed that perceived internal control has significant impact on financial performance. Further study identifies that control environment and information and communication negatively influence on financial performance while risk assessment, control activities and monitoring of the internal control lead to better financial performance (Murleetharan, 2016).

The assessment performed by a public accounting firm in connection with internal control over financial reporting process, provides a major impact upon the reliability of financial statements prepared by these entities and therefore can significantly influence investment decisions. Research results support the conclusion that the more effective internal control over financial is, the lower magnitude of fraudulent financial reporting can be settled (Spatacean, 2012).

Research article by named "A Comparative assessment of Internal Control System in Public and Private Universities in South-West, Nigeria" studied the comparative evaluation of internal control systems in public and private universities of Nigeria. The results of the analysis show that the control systems are not different in public and private universities (Akosile, 2013). Another study was designed to investigate the effect of internal control systems on the financial performance of sugarcane out grower companies in Kenya and all the Finance Managers and heads of internal audit for every out grower company were selected to take part in the study. The study found a positive significant effect of internal control system on the financial performance and concludes that internal control system helps increase performance of Sugarcane out grower companies (Mary, Albert, & Byaruhanga, 2014).

The research by namely "Internal Control in small and Microenterprises in the Vhembe District, Limpopo province, South Africa" investigated the efficiency of control systems in the SMEs, specifically in the Vhembe district in South Africa. According to the result, the efficiency of the control systems practiced by the small business sector was quite low satisfactory control systems. The findings of the research also suggested that small business should be encouraged and promoted to assist growth and expansion that will further enable increased efficiency of the internal control system. (Emmanuel & Agyapong, 2013).

Further research study investigates the effect of internal control systems on cooperative profitability. However, the researcher found that financial losses occurred in the cooperative, caused by inefficient cost control and not due to weak internal controls. Profitability can be improved with a new development plan as well as implementation of effective internal control systems within the cooperative. Good or strong internal control systems would influence the cooperative's profitability as well as help the stability and growth of the cooperative movement in Malaysia. (Shabri, Saad, & Bakar, 2016).

Conducted research study about "Effects of internal control system on the financial performance of remittance companies in modadishu-somalia" The study revealed that control environment, risk assessment and control activity significantly affect the financial performance of remittance companies in Mogadishu. (Mukhongo, 2016).

Empirical study aimed to investigate existence of a relation between the internal control system and financial performance of Telecommunication Company of Golestan province. Findings showed that there was significant and positive relation between internal control system and financial performance of the Telecommunication Company of Golestan province. Thus it can be said that existence of internal control system influences financial performance positively and an internal control system seems to be necessary for effective performance (Shokoohi, Saeidi, & Malekmahmoudi, 2015). According to another thesis its main purpose is to highlight the importance of internal control function, as well as their detailed presentation as imprinted and as experienced in the employees in Banks, to attempt an objective point of view, to draw some conclusions and to arise possible improvements and proposals on internal audit. Also, it aims to highlight the complexity and the nature of the Banking activity. Also, this study investigates the importance of the effectiveness of internal audit and internal control systems in the Greek Bank institutions. The findings of this survey guide us in drawing some conclusions as guidelines for the improvement of internal control and increase its effectiveness on Greek Banks (Paraskevi, 2016).

Hence, Abu-Musa (2010) investigates the existence and adequacy of implemented security controls of computerized accounting information systems in the Saudi Banking sector. The results of study reveal that the vast majority of Saudi Banks have adequate security controls in place. The results also enable Bank managers and practitioners to better secure their computerized accounting information systems and to champion the security of information technology for the success of their Banks.

Further, research conducted to investigate the "Effectiveness of internal control system in Greek Banking sector" within this framework of extremely fluid business environment, the purpose of our study was to underline the importance of a well-organized

internal control system for ensuring the safe and soundness of a credit institution's activity, and by this the stability of the Banking system as a whole. Further study revealed that results point out that all components of internal control is vital in the effectiveness of internal audit and consequently in the business survival and success (Karagiorgos, Drogalas, & Dimou, 2012)

According to another thesis that study focused and look at the influence of accounting information systems (AIS) for effective internal control on firm's performance and found out that when controls are operated efficiently and effectively, there will be improved performance, better accounting information reliability for better decision making for both the internal and external users and the control measures of effectiveness and efficiency of the information reliability will be boasted, effectual and improved operative goals and enhanced performance (Teru, Idoku, & Ndeyati, 2017).

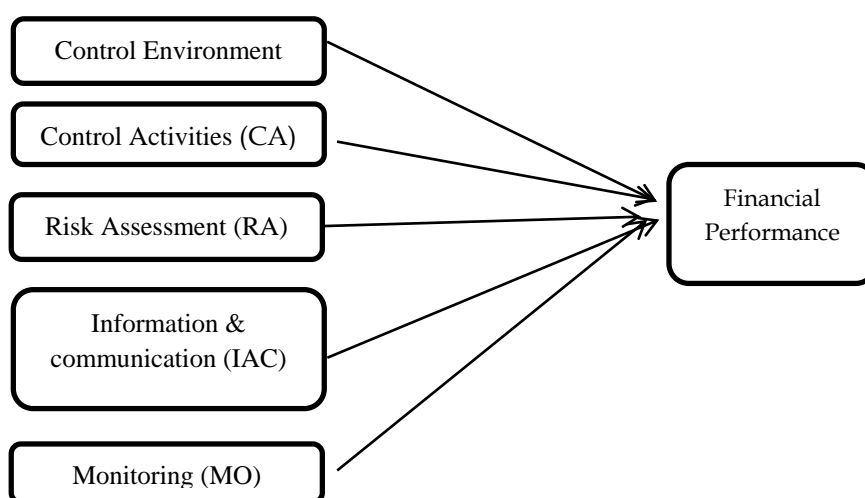
The study sought to determine the effect of internal control systems on financial performance of companies quoted in the Nairobi Securities Exchange (NSE). To achieve the objective of this study, the research specifically looked at the following objectives, control environment, internal audit, risk management, internal control activities and role of corporate governance controls on the financial performance of quoted companies in Kenya. The results and findings concluded that there was significant association between internal control environment and financial performance recommends that internal control environment should be enhanced to further improve the financial performance of companies quoted in Nairobi Securities Exchange. (Kinyua, Gakure, Gekara, & Orwa, 2015).

The overall objective of this study was to establish the effects of internal controls on the financial performance of manufacturing firms in Nairobi Kenya. This was achieved by looking at the effect of control environment, risk assessment, information and communication, control activities and monitoring on the return on asset of manufacturing firms in Kenya. Findings of the study showed that there is a significant relationship between internal controls and financial performance. Manufacturing firms that had invested on effective internal control systems had more improved financial performance as compared to those manufacturing firms that had a weak internal control system. (Njoki, 2015).

The research paper on the topic "Application of Internal Controls in NGOs: Evidence from Zimbabwe" investigated the degree to which NGOs in Zimbabwe implement internal controls in their procedures. The result of the study concluded that strong internal control structures are adopted by the NGOs in Zimbabwe with respect to control environment, Control activities and monitoring. (Ngwenya, 2013).

3. METHODOLOGY

The study is grounded on Committee of Sponsoring Organizations of Tread Way Commission (COSO) Model introduced by COSO committee in 1992 an modified in 2013. Through a comprehensive review of literature (Ayagre, Gyamerah, & Nartey, (2014); Ayom, (2013) ; Douglus, (2012);Dineshkumar & Kogulacumar, (2012); Kumuthinidevi,(2016.);Murleetharan,(2016); Gamage, Lock, & Fernando, (2014) the study identified five major independent variables Control Environment (CE), Control Activities (CA), Risk Assessment (RA), Information & communication (IAC) and Monitoring (MO) that may have effect on Bank's Financial Performance. Conceptual framework of the study is as follows;



Figure; Conceptual Framework of the Study (2019)

Base on the above independent variables five hypotheses were tested. The study collected data from 70 executive level employees Commercial and Sampath Bank which comes under the classification of systematically important private commercial banks which

bear highest turnover an asset base in Private Banks (Central Bank, 2018). This Population was selected because executive level employees have strongly alignment with internal controls, and they are involving in creation an implementation of internal controls. Researchers used solving's equation to decide sample size at 95% confident level and use stratified random sampling technique to select the sample of executive level employees though a population of 85 executive level employees in Private Commercial Banks in Central Province. A structured questionnaire was used in the data collection after considering expert opinion in revising the questionnaire and after a pilot study. The questionnaire was undertaken in English language. All closed ended constructs in the questionnaire comprised with various items on Likert Type five – point scales ranging from 1- strongly disagree, to 5 – strongly agree. Descriptive statistics, correlation analysis and regression analysis were employed in the data analysis.

$$Y = \alpha + \beta_1 X_1 + \beta_2 X_2 + \beta_3 X_3 + \beta_4 X_4 + \beta_5 X_5 + \beta_6 X_6 + e$$

Where Y=Financial Performance, α = Constant, β_1 CE = Control Environment, β_2 CA = Control Activities, β_3 IC = Information & Communication, β_4 RA = Risk Assessment, β_6 M = Monitoring

4.RESULTS & DISCUSSION

The main objective of this study was to empirically examine the impact of internal controls on financial performance of private commercial banks in Central province of Sri Lanka. Data were collected from 70 executive level employees selected from two districts (Kandy and Matale) through a pre-tested structured questionnaire.

4.1. Result of Multicollinearity

Table 4. 1: Result of Multicollinearity

Variable	Tolerance	VIF
Control Environment	0.799	1.251
Control Activities	0.641	1.560
Risk Assessment	0.496	2.017
Information & Communication	0.704	1.421
Monitoring	0.679	1.473

Source: Survey Data (2019)

To test the multicollinearity among independent variables tolerance value and variance inflation factor (VIF) value is calculated; it is generally believed that any VIF that exceeds 5 and a tolerance value lower than 0.10 indicates a potential problem of multicollinearity. According to the results in Table 4.1 the tolerance values are higher than 0.10 in private banks and the VIF values for each relationship falls in between 1.251 and 2.017 in private banks. Thus, there is no evidence for suspecting multicollinearity between the variables.

4.2. Demographic statistics of the sample

The total sample was categorized into seven categories under district, age, position, gender, and educational qualification, civil status, working experience.

Table 4.2: Demographic Statistics of the Sample

District	%	Gender	%	Civil status	%	Education qualification	%
Kandy	67.1	Male	84.3	Married	90	Secondary	1.4
Matale	32.9	Female	15.7	Unmarried	10	Certificate/Diploma	52.9
	100		100		100	Bachelor's degree	34.3
Age		Position		Working experience		Master and Above.	11.4
18-30	15.7	Manager	14.3	0-10	18.6		100
31-40	67.1	Assistant Manger	24.3	10-20	47.1		
41-50	17.1	Officer	61.4	Above 20	34.3		
	100		100		100		

Source: survey data (2019)

According to Table 4.2, out of 70 managerial employees 67.1% managerial employees are from Kandy district and rest of respondents represent the Matale district. When comparing gender distribution in private commercial banks, 84.3% of majority

represents male. Among four age categories most of the respondents of private commercial banks were under 31-40 age group which represents 67.1% and most of respondents were married which represents 90%. When considering this position, 61.4% represents officers in private commercial banks and managers were 14.3% which shows the lowest respondents in regard of position. When considering working experience in banks, 10-20 years range shows the highest respondents of 47.1% in private commercial Banks. Most of the respondents were certificate/diploma holders which represent 52.9% when considering the educational qualifications. Lowest level of respondents was secondary qualification holders in private commercial banks.

4.3. Results of Reliability Analysis

Table 4.3; Results of Reliability Analysis

Internal control	Cronbach's Alpha
Control Environments	0.799
Control Activities	0.826
Risk Assessment	0.838
Communication & information	0.751
Monitoring	0.680
Financial Performance	0.848

Source; Survey data (2019)

Cronbach's Alpha was used to assess the reliability and internal consistency of the data set. According to table 4.3, Results revealed that Cronbach's Alpha coefficient of over 0.68, showing a high internal reliability among the data gathered from the sample.

4.4. Descriptive statistics Results and Correlation analysis result

Table 4.4; Descriptive statistics and results of correlation analysis

Variable	Mean	SD	Skewness	Correlation	FP
CE	4.22	.51363	-.421	Pearson Correlation Sig. (2-tailed)	.648** .000
CA	3.92	.58907	-.303	Pearson Correlation Sig. (2-tailed)	.505** .000
RA	4.00	.57481	-.308	Pearson Correlation Sig. (2-tailed)	.696** .000
IAC	4.18	.47077	-.405	Pearson Correlation Sig. (2-tailed)	.580** .000
MO	3.90	.49432	.302	Pearson Correlation Sig. (2-tailed)	.535** .000
FP	4.29	.51224	-.584		1

**Correlation is significant at the 0.01 level (2-tailed).

Source; Survey data (2019)

Table 4.4 shows the descriptive statistics and result of correlation analysis. Mean values indicate that selected executive level has a favorable mind-set for the internal controls. In this study, since all the skewness values in Private commercial Banks are not exceed -1 or + 1 univariate distribution was normal. Standard deviation (SD) of Private commercial Banks shows values less than 1 which shows small deviations in responses given by respondents. In brief Mean and SD was used to determine the extent of spread of the data.

Further Table 4.4 revealed that all components of internal control system are positively correlated with Financial performance (FP) and there is a significant relationship between overall internal controls (IC) and the organization performance ($p > 0.05$). The Pearson correlation value for Control Environment and Financial performance was 0.648, Control Activities and Financial performance was 0.505, risk Assessment on Financial performance of Private commercial Banks was 0.696, Information and communication on Financial performance of Private commercial Banks was 0.580, Monitoring on Financial performance of Private commercial Banks was 0.535 and all were significant value is 0.000 ($p < 0.01$). These results are similar to the findings of previous studies on impact of internal control on financial performance. (Olufunmilayo & Hannah, 2018; Kinyua, Gakure, Gekara,

& Orwa, 2015; Adenugba and Adeyemi, 2011; Gündoğdu, 2014; Olatunji, 2009; Khan, Shakri and Chanar, 2015; Mawanda, 2008; Murleetharan, 2016; Spatacean, 2012; Shokoohi, Saeidi, & Malekmahmoudi, 2015).

Table 4.5.. Result of regression analysis

Table 4.5; Result of regression analysis

Adjusted R ² =0.699			F=33.121		Sig.=0.000	
Model	Unstandardized Coefficients		Standardized Coefficients		t	Sig.
	B	Std. Error	Beta			
(Constant)	-.363	.391			-.929	.356
CE	.366	.076	.367		4.80	.000
CA	.040	.071	.046		.564	.574
RA	.293	.081	.329		3.61	.001
IAC	.238	.086	.219		2.77	.007
MO	.203	.081	.195		2.48	.015

a. Dependent Variable; FP

Source; survey data (2019)

Table 4.5 presents the result of regression analysis. This provides the idea about up to which extent the model is fitted. Regression model was fitted at sig value of 0.000 (p<0.05). Further, the Adjusted R² =0.699, this means 69.9% of the variation in Financial performance is explained by components of internal control remaining 30.1% of Financial performance of Private commercial Banks is described by other factors which are beyond in the study.

$Y = \alpha + \beta_1CE + \beta_2CA + \beta_3IC + \beta_4RA + \beta_4M$ Where, Y=Financial Performance, α = Constant, β_1CE = Control Environment, β_2CA = Control Activities, β_3IC = Information & Communication, β_4RA = Risk Assessment, β_4M = Monitoring

According to the table 3 four variables out of five are significant at either 0.01 or 0.05 while one variable is not supported. The results revealed that Control Environment (CE), Risk Assessment (RA), Information and communication (IAC) and Monitoring (MO) are statistically significant (p > 0.05). But control Activities is higher than the 0.05 and not statistically significant at either 0.01 or 0.05 on Financial Performance.

The univariate normality was assessed using skewness values. In this study, since all the skewness values in private commercial Banks were not exceed -1 or + 1 assume that the univariate distribution was normal. To check for linearity, researcher used the residual scatter plot. According to the residual plots, the observed residuals are not far above or below the normal line; thus, it can be assumed that the variables had linear relationships with each other.

4. Conclusion & Recommendation

This study found that financial performance is driven by internal control components Control Environment (CE), Risk Assessment (RA), Information and communication (IAC) and Monitoring (MO). Study found that there is a significant positive relationship with five components of internal control and financial performance. From that Control Environment (CE), Risk Assessment (RA), Information and communication and Monitoring (MO) have significant impact on financial performance of private commercial banks in Central Province of Sri Lanka. Researcher suggest maintaining and improve the existing internal controls in private banks to enhance the financial performance of private banks to enhance economic development in Sri Lanka.

Control Environment

Researcher recommended to organization's management to ensure and foster and maintain the highest standards of ethical behavior within the organization and implement awareness programs for employees and management staff to inform policies and procedures as well to sharpen their skills and knowledge with regards to implementation of internal controls.

Risk Assessment

Recommend conveying all employees about risk assessment practically, implement a fraud control plan for the Banks, which addresses relevant risk factors and is updated on a regular basis and undertake a fraud risk assessment (internal and external risks) at least once a year.

Information and Communication

Management should ensure it receives timely, relevant, and reliable reports for decision-making and that all relevant information is communicated to staff, all channels of communication are utilized by Company staff, and that there is quick and free flow of information in time such as introduction of internet based communication that can communicate with each other by being in anywhere in the world.

Monitoring

Further, enhance the existing supervision and conduct on going evaluation during the working hours within the Bank and should evaluate current performance with the expected outcomes and manager should improve the effectiveness of the internal control system in their Bank.

A major limitation of this research is the study is focus only on few private Banks. Also, this study includes conservation nature of the organization and the apathy of staff members towards providing information especially with respect to their internal operation policies and researcher will narrow down the sample to the central province Kandy and Matale district without conducting for whole commercial private Bank outlets in Sri Lanka.

Therefore, the researcher proposed some recommendations for future researchers who interested in this area, for the purpose of making some improvements. Researchers who related to this area are suggested to include more coverage areas or suggested to conduct a survey for the whole Banks, will increase reliability. Further, the number of participants in the survey was quite small. Further research should increase the number of participants and put more time in doing research that could improve the quality of the research. Further researcher proposes to consider moderating variable on internal control and financial performance such as cooperate governance in future researches to enhance the quality of outcome from the research study.

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