INTERNAL CONTROL SYSTEM AS MEDIATOR OF OPERATIONAL RISK MANAGEMENT AND FINANCIAL PERFORMANCE STABILITY

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Abstract: This study aimed at exploring the mediation of higher learning institutions in countries (Tanzania, Kenya, Rwanda, Uganda and Democratic Republic of Congo). A quantitative research study using descriptive correlation design was done to 350 respondents where 308 (90.57%) staff and faculty members participated in filling the questionnaires. Fifty eighty percentage (58%) of the respondents came from the rural places and 42% urban institutions. The data was analyzed using frequency distribution, percentage, the Mean and Standard Deviation. For the Inferential statistics krustkal-wallis test, Mann Whitney test and regression analysis were used. The descriptive statistics findings showed that the institutions that participated in this study had *a fair* internal control system as perceived by the respondents; the level of operational risk management and financial performance and stability were *fairly* perceived as well. The statistics results reveal that the years of operation, size of the firm and location affect financial performance and stability in the selected institutions. Based on Pearson correlation findings, operational risk management had a significant positive relationship with internal control system and its dimensions. All components of internal control system had a positive relationship with financial performance and stability dimensions. Based on the findings, the best path generated by ordinary least square regression (OLS) was on internal control system as mediator of operational risk management and financial performance and stability. Therefore, internal control system had a partial mediating effect on the relationship of operational risk management and financial performance and stability.

Keywords: *internal Control System, operational Risk Management, financial Performance and Stability.*

Introduction

With the increase of global business competition, institutions are intensively striving to achieve their goals. Financial performance and stability issues have been receiving priority attention from policy makers around the world. One main catalyst for this trend was the East Asian financial crisis of the late 1990s. Following that turmoil, the World Bank and the International Monetary Fund (IMF) introduced the financial sector assessment program (FSAP) in the 90's, aimed at assessing regular strength and weaknesses of financial performance and stability systems (Abayomi, 2008).

Several studies that have been conducted on financial performance and stability, operational risks management and insolvency are indicative of the current challenge that organizations are struggling with around the world. It is this need that urges the institution's administrators to give attention mainly on their internal control system, if they are to achieve a conducive financial situation (Komarek, Vilma & Zlatuse, 2013).

According to Schinasi (2011), financial performance and stability can be defined as the ability to maintain the smooth functioning of financial system and to facilitate and support the efficient functioning and performance of the organization. It has been revealed that an institution's financial situation determines the entre operations life span based on the prevailing financial position.

Materials and Methods:

The study utilized a descriptive-correlational design, a quantitative research in which patterns of correlations were analyzed. Specifically, this approach determined whether a significant relationship exist between internal control system and operational risk management.

The mediational effect was examined prior to final data gathering a pilot study was conducted in one of the five institutions considering 100 respondents.

Results:

The study utilized a descriptive-correlational design, a quantitative research in which patterns of correlations were analyzed. Specifically, approach determined whether a significant relationship exist between internal control system and operational risk management. Therefore, the procedures enabled the researcher to make inferences about the relationship between two or more variables considering the moderators (Creswell, 2003).

Prior to final data gathering a pilot study was conducted in one of the five institutions considering 100 respondents.

Discussion:

The grand mean of 3.21 and standard deviation of 0.80 revealed that the respondents perceived a *fair* internal control system in terms of control environment among the institutions of study. This implies that the institutions *sometimes* set the tone of the school in its day to day activities in line with policies, values and management styles.

The Levene's Test for equality in variance was performed further to discover which of urban and rural manifested significant difference in their respondent's perception on financial performance and stability. The three predictors jointly explained 16.3 % of the total variance of the financial performance and stability in terms of liquidity. These results show that there is 83.7% of variance which is not explained by control environment, size of the firm and risk identification. The regression model for prediction is liquidity = 2.459 + .108 control environment + .166 size of the firm + .91 risk identification. Control environment, size of the firm and risk identification positively affect liquidity for every unit increase in control

environment, liquidity increases by .108 (t = 3. 365, p < .000).

Conclusions:

Based on the findings of this study, it could be concluded that internal control system and operational risk management are *fairly* practiced among the five institutions which significantly affects the financial performance and stability. The results are in support to the internal control system theory which says that internal control system and adequate risk operational management systems should not be treated separately, but rather as complimentary. Institutions must therefore, establish a good link between their risk operational management and internal control system in order to survive in this stiff and competitive business operation. There is a significant relationship between risk operational management to financial performance and stability, the predictors to financial performance and stability and risk operational management considering the moderator variable that are size, location and number of years of operation.

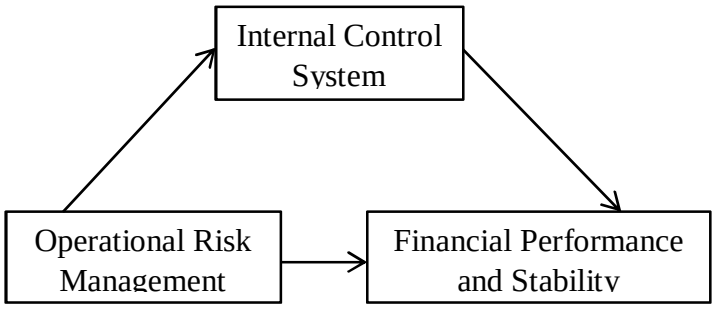
Furthermore, the mediation of internal control system on operational risk management, financial performance and stability revealed the existence of correlations to internal control system, operational risk management and financial performance and stability.

The total effect of operational risk management on financial performance and stability was, *c* = .59 *t* = 22.3176, *p* < .001; that implied that an increase in operational risk management predicted an approximately a 2- point increase in financial performance and stability, therefore it was significantly predictive of the hypothesized mediating variable.

In summary, the indirect effect of operational risk management on financial performance and stability through internal control system was significant. The direct path from operational risk management (c^1) was also significant; therefore, the effects of operational risk management on financial performance and stability were only partially mediated by internal control system. Thus, the hypothesis that, "Internal control system does not mediate between operation risk management and financial and performance stability," was rejected.

Tables and figures:

Path coefficients for operational risk management internal control system financial performance and stability mediation analysis.



Total Effect (c) = .5937 (.000)
Indirect effect (ab) = .1530 (.000)

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