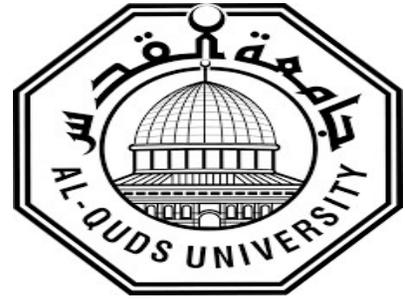


**Deanship of Graduate of Students
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**The Effect of Internal Control Deficiencies on Financial
Performance of Palestinian Companies**

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M.Sc. Thesis

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**The Effect of Internal Control Deficiencies on Financial
Performance of Palestinian Companies**

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Three handwritten signatures in blue ink are displayed on a white background. Each signature is positioned above a horizontal dotted line, which serves as a guide for the signature's placement. The signatures are written in a cursive style.

Jerusalem-Palestine

1445/2024

Dedication

To the mother who held the love of land

To my father who will always be my friend

To the pillars of the heart and the essence of life, To the voices

which keep rejoice in our house, my kids Sama and Majed

Declaration

I certify that this thesis submitted for the degree of Master, is the result of my own research, except otherwise acknowledged, and that this study (or any part of the same) has not been submitted for a higher degree to any other university or institution.

Signature:

A handwritten signature in Arabic script, written in black ink. The signature is stylized and appears to be 'Haya Nabeel Ayaseh'. It is written over a horizontal line that extends to the right.

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Date: 06/01/2024

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Alhamdulillah, Praise to Almighty Allah who blesses me for the success of my thesis. Thanks to my family and friends. I would never have done this alone without the support from them.

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Abstract

The purpose of the study is to investigate the impact of internal control deficiencies, related to the (control environment, control activities, risk assessment, information and communication, and monitoring), on the financial performance of Palestinian companies. This study is considered as exploratory research and quantitative method is used. The questionnaires are distributed to the 405 employees working in the Palestinian companies.

The study findings reveal that respondents perceive a medium level of implementation of the design of internal control. This suggests that there is some degree of structure and control within the organization's internal control framework, but there are deficiencies that hinder its optimal effectiveness. It is crucial for organizations to identify these areas of improvement and take appropriate actions to address them.

Additionally, the study highlights that although the internal control is well designed, it is not properly applied according to the respondents' perception. This means that even though the internal control system is established, respondents perceive its implementation as poor. The results indicate a medium value for the operation of internal control, suggesting that some aspects of internal control are functioning adequately, but there is room for improvement in certain areas. Furthermore, the study reveals that the individuals performing the control lack the necessary authority to carry out their responsibilities effectively. The study also results that, the person performing the control does not possess the necessary authority to perform the control effectively. Results indicate there is an unclear separation between the senior executive management and the board of the director in my company. Results indicate that company does not have definite proper objectives, which means that respondents perceive that their company does not identify proper goals and objectives, or that the company does not communicate its goals and objectives. Results indicate that management does not have specified staff who are in charge of coordinating the different activities in the company to confirm proper communication on internal controls

Based on these findings, the study recommends that organizations prioritize ongoing monitoring and evaluation of their internal control systems. This is essential to ensure that the systems remain relevant and effective in a constantly evolving business environment. By regularly assessing and improving their internal control mechanisms, organizations can enhance their financial performance and mitigate the risks associated with internal control deficiencies.

Keywords: Internal Control Deficiencies, Control Activities, Risk Assessment, Monitoring, Financial Performance, Palestinian companies.

ملخص الدراسة باللغة العربية

هدفت هذه الدراسة التعرف إلى القصور في الرقابة الداخلية (ببيئة الرقابة، أنشطة الرقابة، تقييم المخاطر، والمعلومات والاتصالات، المراقبو والتقييم) على الأداء المالي للشركات الفلسطينية. تعتبر هذه الدراسة بحثا استكشافيا ويتم استخدام الطريقة الكمية، بالإعتماد على الإستبانة كأداة الدراسة الرئيسية ، حيث تم توزيع الإستبانة على 405 موظفين يعملون في الشركات الفلسطينية. توصلت الدراسة إلى أن درجة مستوى متوسط من تنفيذ تصميم الرقابة الداخلية، بالإضافة إلى ذلك ، توصلت الدراسة أنه على الرغم من أن الرقابة الداخلية مصممة بشكل جيد ، إلا أنها لا تطبق بشكل صحيح، وهذا يعني أنه على الرغم من إنشاء نظام الرقابة الداخلية ، فإن عينة الدراسة ترى أن تنفيذه ضعيف. كما وتشير النتائج إلى وجود قيمة متوسطة لتشغيل الرقابة الداخلية ، مما يشير إلى أن بعض جوانب الرقابة الداخلية تعمل بشكل كاف ، ولكن هناك مجال للتحسين في مجالات معينة. علاوة على ذلك ، تكشف الدراسة أن الأفراد الذين يقومون بالرقابة يفتقرون إلى السلطة اللازمة للقيام بمسؤولياتهم بشكل فعال. تشير النتائج أيضا إلى وجود فصل غير واضح بين الإدارة التنفيذية العليا ومجلس الإدارة في الشركات المبحوثة . كما وتشير النتائج إلى أن الشركة ليس لديها أهداف مناسبة محددة ، مما يعني أن المستجيبين يرون أن شركتهم لا تحدد الأهداف والغايات المناسبة ، أو أن الشركة لا تنقل أهدافها وغاياتها. وتشير النتائج أيضا إلى أن الإدارة ليس لديها موظفين محددين مسؤولين عن تنسيق الأنشطة المختلفة في الشركة لتأكيد التواصل المناسب بشأن الضوابط الداخلية

وبناء على هذه النتائج ، توصي الدراسة بأن تعطي المنظمات الأولوية للتقييم والمتابعة المستمرين لنظم الرقابة الداخلية لديها. وهذا أمر ضروري لضمان أن النظم تبقى ذات صلة وفعالة في بيئة الأعمال المتطورة باستمرار. ومن خلال التقييم والتحسين المنتظمين لآليات الرقابة الداخلية ، تستطيع المنظمات تعزيز أدائها المالي والتخفيف من المخاطر المرتبطة بأوجه القصور في الرقابة الداخلية

الكلمات المفتاحية: الرقابة الداخلية ، أنشطة التحكم ، تقييم المخاطر، الرقابة، الأداء المالي ،

الشركات الفلسطينية.

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LIST OF SYMBOLS AND ABBREVIATIONS

PEX = Palestine Exchange

SOX = Sarbanes-Oxley Act

COSO = Committee of Sponsoring Organizations of the Treadway
Commission

KPMG = Klynveld Peat Marwick Goerdeler

IAS = the International Accreditation Service

ICS = Internal Control System

ICP = Internal Control Practices

ROA = Return on Assets

ROE = Return on Equity

SPSS = Statistical Package for the Social Science

Chapter One

1.1. Introduction

The Internal control system serves as a form of assurance for confirming accurate reporting and the attainment of a firm's objectives, particularly in light of the increasing demand for information from internal and external stakeholders. Moreover, security, privacy, and proper management of information are vital aspects for most successful firms (Alawaqleh, 2021)

Internal control is a process that is designed and implemented by the managers and other personnel of a corporation with the objective to achieve reasonable assurance of achieving the goals of the corporate, effectiveness and efficiency of operations, reliance on financial reporting, and compliance with current laws and regulations of the corporate (Eton et al., 2019). The presence of internal control system provides the necessary ground for achieving organizational goals and protecting the interests of all stakeholders. On the other hand, integrated financial reporting and internal controls are prepared by managers and independent auditors and provided to other stakeholders. These integrated reports are very useful for business stakeholders because the presence of an effective internal control structure in the financial reporting process plays a vital role in detecting and preventing the occurrence of financial distortions and fraud. Thus, internal control weaknesses can be expected to reduce the quality of financial information, thus creating a favorable environment for managers to take advantage of, increasing the risk of financial reporting, and providing the conditions for financial reporting to reflect the facts (Hafit,2018).

The well-recognized scandals of corporations such as Enron and WorldCom led to loss of investors' confidence in the financial markets. Likewise, in the Enron and WorldCom case, there was significant effect of internal control deficiencies on financial reporting. Lack of effective and efficient internal control system and environment can expectedly create opportunistic behavior by executive senior management to exercise earning mismanagement, misstatement of financial reporting and even accounting fraud. Thus, the Securities Exchange Commission created the Sarbanes-Oxley Act (SOX) in 2002 in

order to control and governs the financial reporting active of corporations and SOX 302, mandated that the management of corporation`s is in charge of establishing, maintaining, and reporting the effectiveness of the internal control of the business that shows the extent of quality of reported earnings.

The Committee of Sponsoring Organizations of the Treadway Commission (COSO) set a common internal control framework for businesses to evaluate and standardize their internal control systems in order to increase the efficiency and effectiveness of activities and operations, show the reliable financial reporting, and be in consistent with related laws and regulations (COSO, 2013). The COSO framework has five components that are: control environment, risk assessment, control activities, information and communication and monitoring activities. This framework has improved the trust of investors in corporate financial reporting and it acts an essential role in stability of the financial markets (Costello & Wittenberg-Moerman, 2011).

Internal control deficiencies can have significant negative effects on the quality of financial reporting and can create various problems for corporations. When there are weaknesses or deficiencies in internal control, it increases the risk of fraudulent activities and misallocation of resources within the organization (Lenz and Hahn, 2015).

One of the main purposes of internal control is to ensure the reliability and accuracy of financial reporting. When there are deficiencies in internal control, it undermines the integrity of financial statements and can result in unreliable or misleading information being presented to stakeholders, such as investors, creditors, and regulators. Poor internal control can lead to errors, omissions, or even deliberate manipulation of financial data, which can have serious consequences for the organization (Hoang, 2020).

When there are deficiencies in internal control, it can lead to various issues that undermine the integrity of financial statements. These deficiencies can include weaknesses in the control environment, inadequate segregation of duties, lack of proper authorization and approval processes, absence of clear policies and procedures, insufficient monitoring and oversight, and inadequate documentation and record-keeping (Gramling & Schneider, 2018) .Such deficiencies can result in errors, omissions, or intentional manipulation of financial data (Graham & Bedard, 2015). For example, if

there is a lack of segregation of duties, it becomes easier for an individual to perpetrate fraud or manipulate financial records without detection. Inadequate monitoring and oversight can lead to unauthorized transactions going unnoticed, further increasing the risk of fraudulent activities .

The consequences of poor internal control can be significant, it can result in financial statements that are unreliable or misleading, which can erode stakeholders' trust in the organization. Investors may be hesitant to invest in a company with weak internal controls, and creditors may be reluctant to provide loans or credit. Additionally, poor internal control can lead to financial loss, misallocation of resources, and inefficiencies within the organization. It can also damage the organization's reputation and expose it to legal and regulatory risks (Leach et al., 2020).

Bayyoud and Sayyad (2015) who investigated the effect of internal control and risk management on banks in Palestine, they found that banking sector in Palestine has developed due to the developments and reforms of laws associated with internal control and risk management policies and strategies as new requirements and instructions have introduced on the banking institution's activities and operations. However, the study results demonstrated that there are still several internal control deficiencies in these institutions due to the problems associated with independency of internal control and foreign currency fluctuations since the lack of national currency.

1.2. Research Problem

Challenges and limitations in internal control can indeed have adverse effects on the reliability of financial information and the decisions made based on that information. Trust in the reported and disclosed financial information is essential for users to make informed and effective decisions (Rahim, 2018). According to Collins and Kinney (2005), the existence of internal control deficiencies leads to arise of both intentional and unintentional errors into the financial reporting and decreasing the financial performance of the business.

The implementation of effective internal controls is crucial for ensuring the efficiency and effectiveness of operations, the reliability of financial reporting, and compliance with applicable laws and regulations. Agro-processing firms often face risks and vulnerabilities when internal controls are lacking or deficient. This issue is exacerbated by weak management in implementing internal control systems. Research by Ringo (2013) supports this argument, highlighting that despite the presence of internal audits and control systems in local authorities, financial crimes such as fraud, irregularities, liquidity problems, insufficient accountability, delayed financial reporting, asset theft, and noncompliance with rules and regulations persist. These issues result in unfavorable decisions that hinder expected outcomes such as profitability and growth. To maximize financial performance, organizations must implement internal control measures. Additionally, the lack of a systematic procedure to address fraudulent behavior and low compensation further hinder the implementation of internal controls. These challenges have detrimental effects on the financial performance of organizations.

Internal control deficiencies can significantly impact the financial performance of companies. However, there is a lack of research examining this relationship specifically from the perspective of employees of Palestinian companies. Therefore, this study aims to investigate the effect of internal control deficiencies on financial performance as perceived by employees of Palestinian companies."

However, there is scarcity of studies and researches that investigated the effect of the internal control deficiencies on the financial performance of listed companies especially in Palestinian context. Thus, the problem of this study represented by the following major question: **What is the effect of the internal control deficiencies on the financial performance of Palestinian companies?**

1.3. Questions of the Study

Beside on the main question, the researcher developed the following minor questions:

1. What is the effect of control environment deficiencies on the financial performance of Palestinian companies?
2. What is the effect of risk assessment deficiencies on the financial performance of Palestinian companies?
3. What is the effect of information and communication deficiencies on the financial performance of Palestinian companies?
4. What is the effect of control environment deficiencies on the financial performance of Palestinian companies?
5. What is the effect of monitoring deficiencies on the financial performance of Palestinian companies?

1.4. Objectives of the Study

General Objectives:

The purpose of this study is to investigate the effect of internal control deficiencies on the financial performance of Palestinian companies.

Specific Objectives:

1. To estimate the effect of control environment deficiencies on the financial performance of Palestinian companies.
2. To examine the effect of risk assessment deficiencies on the financial performance of Palestinian companies.

3. To measure the effect of information and communication deficiencies on the financial performance of Palestinian companies.
4. To investigate the effect of control environment deficiencies on the financial performance of Palestinian companies.
5. To investigate the effect of monitoring deficiencies on the financial performance of Palestinian companies.

1.5. Importance of the Study

1.5.1 Theoretical importance

Provides valuable insights into the practical implications of internal control deficiencies. Employees are often the ones working directly with internal control processes and systems, and they can offer unique perspectives on how deficiencies impact their daily work, the accuracy of financial reporting, and overall financial performance. Their experiences and observations can shed light on the specific challenges faced by organizations in Palestine and highlight the potential consequences of internal control deficiencies.

Examining the relationship between internal control deficiencies and financial performance within the Palestinian context contributes to the literature on internal control and its impact on organizational outcomes.

Organizations can identify areas for improvement and develop strategies to enhance their internal control systems. This research can help organizations in Palestine better allocate resources, improve decision-making processes, and mitigate risks associated with internal control deficiencies, ultimately leading to improved financial performance.

1.5.2 Practical importance

Organizations can gain insights into specific areas of weakness and identify opportunities for improvement in their internal control systems. This can lead to enhanced financial performance by addressing the root causes of deficiencies and implementing effective controls.

This research can help organizations in Palestine raise awareness and build a culture of internal control. By involving employees in the study and highlighting the impact of internal control deficiencies on financial performance, organizations can foster a greater understanding and commitment to internal control practices

1.6. Assumptions of the study:

H1: There is a negative effect of control activities deficiencies on the financial performance of Palestinian companies.

H2: There is a negative effect of control environment deficiencies on the financial performance of Palestinian companies.

H3: There is a negative effect of risk assessment deficiencies on the financial performance of Palestinian companies

H4: There is a negative effect of monitoring deficiencies on the financial performance of Palestinian companies

H5: There is a negative effect of information and communications deficiencies on the financial performance of Palestinian companies

1.7. Delimitations of the Study

There are some delimitations in this study including temporal, spatial and human delimitations:

The temporal delimitation: the researcher will conduct this thesis at the end of 2022.

Human delimitation: internal control managers and employees, and financial management of Palestinian companies.

Chapter Two

Theoretical framework and literature review

2.1 Introduction

Due to the several financial scandals that hit tremendous businesses in the world such as Enron and WorldCom and the failure of several other companies after the global financial crisis in 2008, there was a necessity to develop the internal control environment and systems to support and recover the trust and confidence of the investors in the financial statements' reliability and validity (Kinyua et al., 2015)

The weaknesses in an internal control system can indeed have several negative effects on the financial performance of businesses, as well as on investor trust and confidence. Empirical studies have provided evidence of these negative impacts. For example, Lenz and Hahn (2015) conducted research that highlights the detrimental effects of internal control weaknesses on financial performance. Their findings suggest that businesses with weak internal controls experience lower profitability, reduced efficiency, and increased financial risks.

Internal control weaknesses also create an environment conducive to fraud. The absence of effective controls and oversight increases the opportunities for fraudulent activities, such as misappropriation of assets, manipulation of financial records, and falsification of financial statements. KPMG's (2016) findings support this assertion, demonstrating a positive correlation between internal control weaknesses and the incidence of fraud cases.

Furthermore, internal control deficiencies increase the likelihood of business failure and bankruptcy. Weak controls can lead to significant financial losses, operational inefficiencies, and a lack of accountability. These factors increase the vulnerability of businesses to financial distress, making them more susceptible to failure and bankruptcy.

Additionally, internal control weaknesses can contribute to the practice of earnings management. In an environment with weak controls, management may be tempted to

manipulate financial results to meet desired targets or to present a more favorable financial position. This can involve practices such as income smoothing, artificial revenue recognition, or the misclassification of expenses. Earnings management can distort the true financial performance of a company and mislead investors and stakeholders.

This chapter covers the literature review and empirical researches and studies that discussed the effect of the internal control deficiencies on the financial performance of Palestinian companies. The researcher at first will introduce the concept of internal control definition. Then, she will present and discuss the major theories that explain the effect of the internal control on the financial performance especially the agency, steward and the positive accounting theories. The second section, will discuss the internal control components through defining these components. Moreover, discussing its nature. The third section will be devoted to the effect of the internal control on the financial performance. The fourth section of the chapter will present and discuss several empirical studies that examined the effect of the internal control on the financial performance in different context

2.2 Internal Control Definition

Internal control refers to the processes, policies, and procedures implemented within an organization to provide reasonable assurance regarding the achievement of its objectives. It involves the systematic management of risks, the safeguarding of assets, the prevention and detection of fraud, and the reliability of financial reporting. According to Saleemi (2008) internal controls are “systems create by the senior executive management of the business to confirm smooth and organized running of regular activities of the business, protecting the assets and the competencies of the organization and creating precise and trustworthy reports”. Appiah (2016) defined internal control as a process accomplished by the board of directors and the senior executive management of the business in providing sensible affirmation concerns the accomplishment of operational, reporting and

compliance goals. It is the approach that a business works and the way that it's staffs' awareness is affected is specified by the control environment”.

2.3 Theoretical framework

There are several theories that can help us to explain the effect of the internal control deficiency on the financial performance of companies. These theories basically are the agency, stewardship, positive accounting, and the attribution theories (Almaliki et al., 2019).

2.3.1 Agency Theory

Agency theory is an economic theory that examines the relationship between principals and agents in situations where one party, known as the principal, delegates decision-making authority to another party, known as the agent, to act on their behalf. The theory explores the potential conflicts of interest that may arise between principals and agents and identifies mechanisms to align their interests and mitigate such conflicts.

In many organizational settings, agency relationships exist when shareholders (principals) hire managers (agents) to run the company. The principal-agent relationship can also be found in various other contexts, such as the relationship between a client and a lawyer, a patient and a doctor, or a government and its officials.

Within the framework of agency theory, internal control deficiencies can have implications for financial performance. Internal control deficiencies can create opportunities for agents to engage in opportunistic behavior, such as unauthorized transactions, misappropriation of funds, or inefficient resource utilization. These actions can result in increased agency costs for principals, as they may need to invest additional resources in monitoring and controlling agent behavior or in rectifying the consequences of agent misconduct. The diversion of resources towards addressing internal control deficiencies can reduce overall financial performance.

2.3.2 Stewardship Theory

According to the Davis, Schoorman and Donaldson (1997) “a steward is the person who ensures that there is an effective and efficient system to protect and safe the interest of the investors and maximizes the wealth of the shareholders. So that, increasing the financial performance of the business. Donaldson and Davis (1991) argued that the stewardship theory concentrates on the management’s ability to create an alignment between the organization or business objectives and their personal objectives.

In light of the Donaldson and Davis (1991) argument that efficient stewardship needs employee empowerment and provision of independence based on trust. This theory argues that in order to maximize the wealth of the shareholders, there should be maximum level of intendance between the business management and the shareholders and investors. The steward ship assumes that there is positive effect of the financial performance and return on creating good reputation and driving investors to increase their investment in the business. Eventually, the stewardship theory suggests that the business management of listed companies act as caretakers of suppliers, shareholders, consumers, creditors and employees of these businesses.

2.3.3 The Positivism Accounting Theory

The positivism accounting theory aims to expect and identify justifications for specific phenomena based on a set of researchers` observations that can be investigated and validated improved through more observations (Otley & Berry, 1994). Positive Accounting Theory seeks to understand and explain accounting practices by examining the economic and political motivations of various stakeholders. It focuses on the relationship between managers and shareholders and aims to predict and explain their choices in accounting methods. The theory assumes that managers are motivated by self-interest and will engage in accounting practices that maximize their own wealth or utility.

This theory states that “all the self-interest and individualism are the main drivers of the personal actions and these actions always act in an opportunistic manner to the extent that the actions will increase their wealth” (Deegan and Unerman, 2006). Thus, this theory assumes that the management will set tools and restriction to limit the actions that are driven by the self-interest. Thus, there is a necessity to create an alignment between the executive management interests and the interests of the investors and shareholders. Thus, there is a necessity to set clear and efficient internal control system in the business that meets the needs of the executive management and shareholders and investors to control and monitor operating activities and costs of the business.

2.4 Importance of Internal Control

Internal control is interesting to confirm the existence of effective and efficient system of business operations, the reliability of the financial reporting and the adherence and compliance with the set laws, polices, procedures and regulation to which the business is subject (Agyei-Mensah, 2016). Internal control helps protect an organization's assets, including physical assets (such as equipment and inventory) and intangible assets (such as intellectual property and customer data). By implementing control measures, such as segregation of duties, access controls, and asset tracking, organizations can minimize the risk of theft, loss, or misuse of assets. (Aikins, 2011).

Adequate and sound effect documentation of policies and procedures are interesting in order to identify the way that the control activities are to be performed and to provide sufficient information for auditors` investigation of the entire competence of control policy over financial management practices (Aikins, 2011). Thus, control activities are crucial in identifying and managing risks to ensure that businesses can effectively and efficiently achieve their goals and objectives. Control activities are the specific policies, procedures, and practices implemented by an organization to mitigate risks and ensure that operations are carried out in a controlled and effective manner (Al Shobaki et al., 2018).

Furthermore, monitoring as one of the components of internal control is interesting to demonstrate the existence of effective and efficient internal controls system and its well-functioning (Amudo & Inanga, 2009). Thus, monitoring specifies whether or not policies and procedures established and carried out by the senior executive management are being performed efficiently by staff (Rae & Subramaniam, 2012).

The existence of effective and efficient internal control is interesting to support the internal auditors and the business ability to detect and prevent fraud and fraudulent practices in the business. Besides, the internal control system supports the shareholders' assurance that the resources are being used effectively in providing the right service at the least cost. Furthermore, the internal control system supports the reliability of the financial performance and supporting accountability among information providers in the business (Jenning et al., 2008).

Internal control is interesting also to provide an independent appraisal of the quality of managerial performance in performing specified tasks, duties and responsibilities for better financial performance through increasing the business revenue (Donald & Delno, 2009).

Ondieki (2013) suggests that having an efficient and effective internal control system positively impacts a business's financial performance. It enables the organization to prevent, detect, and eliminate fraudulent practices, thereby creating an environment conducive to improved financial performance. Additionally, an effective internal control system ensures the protection of business assets and resources, fostering business growth and development. By effectively managing and mitigating various business risks, the internal control system helps minimize their negative impact on financial performance.

Jarvinen and Myllymaki (2016) argued that the existence of weak internal control in the business can increase the potential of the incidence of earnings management and fraud, earnings revisions and financial reports misstatement. Furthermore, Jarvinen and Myllymaki (2016) argued that the weak internal control affects adversely the reliability of the financial reporting and the presentation of valid and quality information for investors

and shareholders, decreasing bond rating, decreasing the level of the business environment and so that decreasing the financial performance of the business

Ge and McVay (2005) revealed that the businesses with at least one internal control weakness have lower financial performance measured by ROA. Furthermore, Kuhn, Ahuja, and Mueller (2013) investigated the effect of the internal control weakness and deficiency on the business operational efficiency and effectiveness. Similarly, in a study of Feng et al. (2015) that aimed to investigate the effect of weakness in the internal control related to inventory weakness on the financial performance, the study results confirmed that this type of weakness affects the inventory turnover of the business and it leads to more inventory impairments.

2.5 COSO Framework

COSO provided five components of the internal control that are: Control environment, risk assessment, control activities, monitoring, communication and information.

2.5.1 Control Activities

The control activities include both the handbook and automatic resources that act an essential role in detecting and preventing or mitigating various risks that can affect negatively the achievement of the business mission and objectives. Thus, the executive management should identify a set of control activities to monitor the business activities and ensure that they achieved efficiently and effectively (Mjaku & Pristina, 2019).

The business performs control activities at the various stages of the processes of the business, at all the levels of the business and over the technology environment (Abiola & Oyewole, 2013). Control activities serve the purpose of detecting and preventing errors, fraud, and other undesirable occurrences within an organization (Oduro & Cromwell, 2018).

According to Aikins (2011) control activities are instruments, procedures and policies introduce in a business in order to ease the accomplishment of the directives given by the business management. These activities also include adequate and appropriate documentation and execution of control activity policy provides information of business financial management practices. Furthermore, some of the interesting control activities in the businesses

are separation of duties, reconciliation of bank statements, providing all the relevant and potential decisions in identifying business risks (Aikins, 2011).

The COSO (Committee of Sponsoring Organizations of the Treadway Commission) framework, in its 2013 update, defines control activities as the specific actions taken by an organization to implement its policies and procedures. The purpose of these control activities is to ensure that management's directives are effectively carried out to mitigate risks and achieve the organization's objectives.

According to COSO (2013) the control activities include “performance reviews such as comparing actual vs. budgets performance, forecasts and prior period performance, information processing that is interesting to examine accuracy, completeness and authorization of transactions, physical controls that are interesting to provide security over both records and other assets, and separation of duties where no one person ought to manage and perform all aspects of a transaction from the beginning to the end”.

2.5.2 Control Environment

It is the set of "standards, processes, and structures that provide the basis for performing internal control across the business" (Chan et al., 2020). The control environment is an interesting measure of the successful and efficient internal regulation. The control environment is the “attitude toward internal control and controls awareness recognized and preserved by the business management and the employees (Pham, 2021). The control environment is the result of philosophy, style, and supportive attitude of the management as well as the competence, ethical values, integrity, and morale of the people of the business or the organization. The organizational structure and the accountability relationships are interesting components of the control environment. Likewise, the internal control environment is perceived as the foundation of other internal control components and activities as it introduces the structures for internal control (Sudsomboon & Ussahawanitchakit, 2009). The existence of effective and efficient control environment is interesting in order to mitigate risks and detect and prevent fraudulent practices and establish sound effect internal control activities (Amudo & Inanga, 2009).

2.5.3 Risk Assessment

Risk assessment or evaluation is a systematic process that involves identifying, analyzing, and evaluating potential risks to an organization. This process considers both external and internal threats and risks that could impact the achievement of organizational objectives (Okonkwo & Ezegeba, 2016). The goal of risk assessment is to provide a comprehensive understanding of the risks and their potential impact, allowing the organization to take appropriate actions to mitigate, reduce, or manage those risks (Wang, 2019)

Theofanis et al., (2011) stated that risk evaluation is the business ability to recognize and analyze the potential threats that impede the accomplishment of the business objectives”. Likewise, Sudsomboon and Ussahawanitchakit (2009) argued that risk evaluation “is the business ability to specify and analyze the potential threats that might affect adversely the financial performance of the organization or the business.

Indeed, senior executive management plays a crucial role in identifying and recognizing potential threats that could hinder the achievement of business objectives and financial performance. By having a clear understanding of these threats, management can take proactive measures to mitigate risks and preserve the sustainability of the business (Cokins, 2009)

Developing efficient risk assessment procedures and policies is essential for effective risk management. This involves establishing a structured and systematic approach to identify, analyze, and evaluate risks across various areas of the business. By implementing robust risk assessment practices, businesses can gain insights into potential vulnerabilities and develop appropriate risk mitigation strategies (Hiles, 2012)

On the other hand, a weak risk assessment process can significantly increase the threats and risks that a business faces on a day-to-day basis. Without a thorough understanding of potential risks, the business may be ill-prepared to address them adequately. This can

lead to a higher likelihood of negative events occurring, such as operational disruptions, financial losses, or reputational damage (Slovic et al., 2013).

When risks are not properly managed, it can have a detrimental impact on the business's ability to achieve better financial performance. The occurrence of significant risks without appropriate mitigation measures can lead to financial losses, decreased profitability, and overall decline in the business's performance. In severe cases, the accumulation of unmanaged risks can lead to the collapse and eventual exit of the business from the market (Douwes & de Kraker, 2014).

2.5.4 Monitoring

Efficient internal control system needs constant monitoring process in order to confirm effective and efficient system performance over time. Monitoring of internal control systems is interesting in order to confirm the existence of high-quality reviews and audits. According to Theofanis et al., (2011) the existence of monitoring activities and system is interesting to support the internal control system's effectiveness and efficiency (Amudo & Inanga, 2009). Thus, monitoring is interesting in order to assist the business to evaluate and assess whether business procedures and policies are efficiently and effectively adopted and implemented in the business by the employees.

Thus, the monitoring activities are interesting in order to assess and evaluate the output of internal restrictions and regulations over time. So that, it is the analysis of the business activities and operations in order to evaluate the service level over time and to investigate if the controls in the business are adequate and efficient. The business executive management ought to emphasize on monitoring activities and efforts on internal control and achievement of business objectives and mission. Likewise, the existence of an efficient and effective monitoring requires the employees to recognize and understand the mission, objectives, responsibilities and risk tolerance levels of the business or the organization (Shoimah, 2015; Ariesa & Berasategu, 2009).

Thus, monitoring in a simple word is constant monitoring activities encompass each of the components of the internal control system and comprise action against irregular, immoral, wasteful, ineffective and useless internal control systems. It can be performed

by often controlling and managing activities such as monitoring of customer complaints and feedback and audits that directed occasionally by internal auditors (Bowrin, 2004).

2.5.5 Information and Communication

Information & Communication is the methods or instruments by which information is spread in the business. It gives the employees the potential to receive an obvious message from top executive management that control responsibilities must be performed seriously.

According to Salameh (2019), communication is an exchange of interesting and meaningful information between the employees or between the employees and the senior executive management in the organization in order to support the decision-making process and planning various actions and activities. Information ought to be communicated to both the employees and the management in the organization who require it in a way and within a timeframe that gives them the opportunity to perform their tasks and responsibilities effectively and efficiently. Furthermore, the communication process may take place between the business and the external environment such as the communication with suppliers, customers, and the legislative and controlling organizations (Rae et al., 2017).

Asiligwa (2017) confirmed that information systems create reports that cover operational, financial and non-financial and information related to the extent of the business compliance and adherence with the set laws, policies and regulations and that make it potential to manage and control the business activities and operations.

Information and communication are the course of establishing, capturing, and appropriately communicating the business financial objectives by the senior executive management to the staff (Theofanis et al., 2011). Researchers argued that information and communication is an interesting component in internal control system since it affects the nature of working relations in different levels of the business (Amudo & Inanga, 2009). Thus, there is necessity for the management to sufficiently and obviously communicate to the employees their duties and responsibilities to support the business financial performance.

COSO (2013) argued that information is interesting for the business to accomplish the responsibilities of the internal control and supporting the realization of the business

objectives and mission. Furthermore, communication takes place either internally or externally and provides the business with the information required to perform daily and routinely activities in the business.

Information gives the employees the opportunity to realize the responsibilities of the internal control and their significance to the accomplishment of the business objectives and mission.

2.6 Correlation Between Internal Control and Financial Performance

Donald & Delno (2009) stated that internal control is “a set of procedures and standards set by a business to confirm appropriate, reliable and effective financial reporting, efficient financial activities and processes, adherence to laws and regulations”.

The internal control is interesting to accomplish the business objectives, and the achieve the financial performance targets, preventing misuse of the business resources and competencies, giving directions to business, acting an essential role in avoiding throwbacks and shocks along the way (Jenning et al., 2008).

Jensen (2003) revealed that there is positive and significant effect of the internal control on improving the business financial performance. Likewise, Fadzil et al. (2005) revealed that there is positive and significant effect of the internal control on achievement of the business goals and objectives. Similarly, Kimutai Ng’etich (2017) found that there is a correlation between the effectiveness and efficiency of the internal control and business success and supporting its financial performance and achievement of the business target revenue objectives as the existence of reliable and sound effect internal control improves the quality of the financial reporting and the quality of the financial statements presentation, protecting the business assets, and ensure business compliance with the laws, regulations, procedures in the business and the industry.

2.6.1 Control Activities and Financial Performance

Control activities are an integral part of an organization's internal control system, and they can have a significant impact on financial performance. Control activities are the policies, procedures, and practices implemented by management to mitigate risks, ensure the reliability of financial information, and safeguard assets (Atu &Adeghe, 2014)

Rosman et al. (2016) investigated the effect of the internal control components basically control environment, control activities, risk assessment, monitoring and budgetary participation on the financial performance effectiveness and efficiency of not profit organizations in Malaysia. The data was taken from a sample of (96) respondents that were selected through using the simple random selection method. The researchers used the multivariate regression analysis that found there is positive and significant effect of the internal control components that are control environment, control activities, risk assessment, monitoring on the listed companies' financial performance.

According to Ejoh and Ejom (2014) who investigated the effect of the internal control activities on the financial performance in Tertiary Institutions in Nigeria. The researchers used the quantitative research design through using survey design. The researchers used the stratified sampling procedure to select the sample members. The findings of the study confirmed that there is insignificant effect of internal control activities on the financial performance of Cross River State College of Education.

Muraleetharan (2013) examined the effect of the control activities on the financial performance of the organizations in Jaffna District, Sri Lanka. The researcher used the quantitative research design through using survey design. The data of the study was taken from a sample of (120) respondents. The study results confirmed that there is positive and significant effect of the control activities on the financial performance of the organization in Jaffna District. Besides, there is positive and significant effect of the control activities on the financial performance. The main implications of this study that organizations should have enough supervision with a clear and modern supply of information. Furthermore, there must be upkeep of adequate recording and duplicating systems and likewise there should be efficient hiring and staffing control with documented directions as to responsibilities and duties of both management and staff.

Magu and Kibati (2016) investigated the effect of internal control components on the financial performance of Kenya Farmers' Association (KFA) Ltd. The researchers used control environment and control activities as proxies of the financial performance. The data of the study was taken from a sample of (78) managers. They used the descriptive and inferential statistics to analyze the obtained data. The study results confirmed that there is inadequate awareness, knowledge and experience about the implementation of an

efficient and effective internal control system. Furthermore, the security system is unable to identify and protect the assets of the business. The study results confirmed that there is positive and significant effect of the internal control on the financial performance. The multivariate regression analysis confirmed that control environment and control activities explain almost (61.3%) of the variability in the financial performance. The researchers suggested that the organizations should involve and invest in employees training in the implementation of the accounting and financial management systems. Besides, there is a necessity to develop and modernize the security system in the institutions to be able to protect the business assets and resources.

Alawattegama (2018), Ejoh and Ejom (2014), Rosman et al. (2016), Muraleetharan (2013), Nyakundi et al. (2014) and Magu and Kibati (2016) confirmed that there are positive and significant control activities component on the financial performance. However, other studies and researches confirmed that there is insignificant effect of the control activities on the financial performance such as Alawattegama (2018) who revealed that there is insignificant effect of the control activities on the financial performance on a sample of (45) banking and finance institutions listed on the Colombo Stock Exchange.

2.6.2 Risk Assessment and Financial Performance

Risk assessment is a critical component of effective risk management and has a direct impact on financial performance. In today's dynamic business environment, organizations face a wide range of risks that can significantly affect their ability to achieve financial objectives and sustain growth. By implementing robust risk assessment processes, businesses can identify, analyze, and evaluate potential risks, allowing them to make informed decisions and take proactive measures to mitigate those risks (Wanjohi, 2013).

The main objective of risk assessment is to identify potential threats and vulnerabilities that could hinder the accomplishment of business objectives and impact financial performance. It involves systematically evaluating the likelihood and potential impact of various risks on the organization. This evaluation provides management with valuable insights into the nature and magnitude of risks, enabling them to prioritize and allocate resources effectively (Mutuku, 2016)

Momanyi and Njiru (2016) examined “the effect of the financial risk management on the financial performance of Deposit taking SACCOs in Nakuru East Sub-County”. The researchers used the quantitative and descriptive research design. The target population was all the fifteen SACCOs in which three employees were selected that consists of (45) respondents. The researchers utilized the survey design in this study. Furthermore, they used the annual reports of listed institutions during the period (2010-2014) to obtain the financial and nonfinancial information of the study. The study results confirmed that there is high level of the adoption and implementation of the financial risk management in the investigated companies. Besides, the study results confirmed that there is a positive and significant effect of the financial risk that includes risk identification, risk monitoring, risk assessment, and risk mitigation on the financial performance.

Ghani and Rosli Mahmood (2015) examined the effect of the risk management practices on the financial performance of the microfinance institutions in Malaysia. The data was taken from a sample of (190) respondents. The study results confirmed that there is positive and significant effect of the risk management practices basically risk identification, risk monitoring and credit risk analysis on the financial performance. However, there is insignificant effect of the risk understanding, risk assessment and risk analysis on the financial performance of the financial institutions. Likewise, Kirogo et al. (2014) investigated the effect of risk assessment on financial performance in insurance institutions in Nakuru town. The researchers used both the descriptive and the inferential statistics to analyze the data of the study. The data was taken from a sample of fifty-two management employees in twenty-seven insurance institutions in Nakuru town. The study results confirmed that there is positive and significant effect of the risk-based auditing through risk assessment on the financial performance of these institutions. The study results confirmed that risk assessment gives the insurance institutions the ability and the potential to identify and detect risks on time and focus on high-risk areas. Thus, promoting better levels of transparency and accountability and improves the financial performance of the insurance institutions. Furthermore, there is positive and significant effect of the risk-based auditing on the financial performance of the investigated insurance institutions. On the other hand, other studies confirmed that there is insignificant effect of the risk management practices and risk assessment on the financial

performance of the businesses such as the findings of Ghani and Rosli Mahmood (2015) and Alawattegama (2018) who demonstrated that there is insignificant effect of the risk assessment on the financial performance of banking institutions and micro finance institutions.

Bett and Memba (2017) examined the effect of the internal control systems on the financial performance of Menengai Oil Company, Kenya. The researchers used the control environment, risk assessment and the information and communication components as proxies of internal control effectiveness. This study followed the quantitative research approach and the correlation design through using survey design. The data was taken from a sample of (189) respondents. The researcher used the descriptive and the inferential statistics in this study. The multivariate regression analysis revealed that there is positive and significant effect of the internal control components on the financial performance. Furthermore, there is positive and significant effect of the control environment, risk assessment and information and communication on the financial performance.

Alawattegama (2018) investigated the effect of the implementation of the enterprise risk management practices on financial performance of banking and finance companies listed in the Colombo Stock Exchange. The researcher used the ERM integrated framework that was suggested by the COSO to evaluate the degree of the adoption and implementation of the ERM practices in the investigated companies. The financial performance was measured by ROA and ROE. The researcher used the multivariate regression analysis. The study results demonstrated that there is positive but insignificant effect of the event identification, risk assessment, risk response and information and communication on financial performance of the business. However, there is negative but insignificant effect of the event identification, control activities and monitoring of ERM functions on financial performance.

Ironkwe and Otti (2016) examined the effect of the accounting information system on the financial performance of banking institutions in Nigeria. The quantitative and the correlation research design and approach were followed in this study. The data was taken from a sample of ninety-one deposit banking institutions. The researchers used the survey design. The researchers used the descriptive and the inferential statistics in this research.

The study results confirmed that there is positive and significant effect of the relevance of accounting information on the financial performance and quality of service delivery of banking institutions in Nigeria. Thus, the accounting information quality in terms of relevance to users affects significantly the financial performance of banking institutions. Likewise, Ali et al. (2016) examined the effect of the AIS on the financial performance of listed companies through moderating the effect of organizational culture. The researchers used the quantitative and the correlation research approach and design through using the survey design. The data was taken from a sample of (273) employees in banking institutions in Jordan. The researcher used the multivariate regression analysis to analyze the obtained data. The study results confirmed that there is positive and significant effect of the service, information and system quality on the AIS success and effectiveness. Thus, this affects positively the financial performance of the investigated organizations and businesses. Likewise, Abubakar (2014) investigated the effect of marketing communication on the financial performance of banking institutions through analyzing the First Bank of Nigeria PLC as a case study. The researchers used t- test and the multivariate regression analysis to analyze the obtained data and information. The findings of the study confirmed that there is positive and significant effect of marketing information on financial performance of the bank measured by return on assets (ROA). Nyakundi et al. (2014) examined the effect of internal control systems on financial performance among SMEs in Kisumu city, Kenya. The researchers used the quantitative research design through using survey design. Furthermore, the used the annual reports and the websites of listed companies to obtain the financial and nonfinancial data of the study. The researchers used both the descriptive and the inferential statistics to analyze the obtained data. The study results confirmed that there is positive and significant effect of the control activities on the financial performance. Furthermore, the entire internal control components affect significantly financial performance of SMEs.

2.7 Types of Internal Control Deficiency

2.7.1 Segregation of duties: is a fundamental principle of internal control that aims to prevent fraud and errors by ensuring that no single individual has complete control over a transaction from beginning to end. When there is a deficiency in the segregation of duties, it means that incompatible functions or responsibilities are assigned to the same person or that there is insufficient oversight and review of critical processes (Lin Pizzini, Vargus and Bardhan, 2011). A deficiency in segregation of duties can occur when an organization lacks the necessary resources or personnel to effectively separate duties. This may result in individuals having access to and control over multiple stages of a transaction, increasing the risk of errors, fraud, or misappropriation of assets. Additionally, inadequate oversight and review processes can further compound the deficiency by failing to detect and address any irregularities or deviations from established controls (Gramling and Schneider, 2018).

2.7.2 Lack of Documentation and Policies: Internal control deficiencies may arise when there is a lack of documented policies and procedures. Without clear guidelines, employees may not know how to perform tasks correctly or consistently, increasing the risk of errors or inconsistencies in financial reporting. An internal control deficiency related to lack of documentation and policies occurs when an organization fails to establish clear and comprehensive guidelines for employees to follow in their day-to-day activities. This deficiency can have a significant impact on financial performance and the reliability of financial reporting (Norman, Rose and Rose, 2010).

When policies and procedures are not properly documented, employees may not have a clear understanding of how to carry out their tasks correctly and consistently. This lack of guidance can lead to errors, omissions, or inconsistencies in financial transactions and reporting. For example, without documented guidelines on expense reimbursement, employees may submit claims that do not comply with company policies or fail to provide adequate supporting documentation (Bedard, Hoitash, Hoitash and Westermann, 2012).

2.7.3 Inadequate Authorization and Approval Processes: Deficiencies in authorization and approval processes can lead to unauthorized transactions or inappropriate access to sensitive information. This may occur when there are weak controls over the approval of financial transactions, such as purchases, expenses, or changes to key financial data. Inadequate authorization and approval processes can give rise to internal control deficiencies that increase the risk of unauthorized transactions and inappropriate access to sensitive information (Hammersley et al., 2008). These deficiencies commonly occur when there are weak controls in place for approving financial transactions, including purchases, expenses, or changes to key financial data. When authorization and approval processes are insufficient, it becomes easier for unauthorized individuals to initiate or execute transactions without proper scrutiny or oversight. This opens the door to potential fraud, misappropriation of assets, or errors that can negatively impact financial performance (Bizarro et al., 2011).

2.7.4 Inadequate Physical Controls: Physical controls involve measures to protect physical assets, such as cash, inventory, or equipment, from theft or damage. Deficiencies in physical controls can include weak security measures, lack of proper access controls, or inadequate monitoring of assets. Insufficient physical controls within an organization can give rise to internal control deficiencies that compromise the protection of physical assets, such as cash, inventory, or equipment (Ogneva et al., 2007). These deficiencies often manifest in weak security measures, inadequate access controls, or insufficient monitoring of assets. Weak security measures refer to vulnerabilities in the physical infrastructure and safeguards that are intended to protect assets from theft, damage, or unauthorized access. For example, if a building lacks proper locks, alarms, or surveillance systems, it becomes easier for unauthorized individuals to gain access to valuable assets. Inadequate security measures can also include ineffective measures to prevent and detect theft, such as the absence of security personnel or insufficient security training for employees (Ge and McVay, 2005).

2.8 Literature Review

Anh, Thi, Quang & Thi (2020) investigated the determinants of the internal control efficiency and effectiveness in cement manufacturing companies listed in Vietnam. The data was taken from a sample of (210) managers and employees. the study confirmed that there is positive and significant effect of the internal control components and the efficiency and effectiveness of the internal control in the investigated companies. The researcher argued that these businesses have to invest in development of the internal control system.

Thuneibat, Rehaily & Basodan (2019) examined the reality of the adoption and implementation of the internal control in listed companies in Saudi. Besides, the researchers used four proxies of financial performance that are (ROA, ROE, EPS, and profit margin). The study results confirmed that there is high level of the implementation of internal control components in the listed companies. Besides, there is positive and significant effect of internal control components on the ROA and ROE. However, there is positive but insignificant effect of the internal control components on EPS and profit margin.

Kyale and Mutua (2018) examined the effect of the internal control effectiveness on the financial performance of financial institutions in Nairobi County. The data was taken from a sample of (115) financial institutions. The study results confirmed that there is positive and significant effect of the internal control components that are the internal audit and control activities on the financial performance of listed companies in this study. However, the main limitation of this study that the researchers used the questionnaire to measure the financial performance rather than using the actual figures of the financial performance and profitability from the annual reports of listed companies. However, there is insignificant effect of the quality of information and communication on financial performance.

Kaunda and Aura (2017) examined the effect of the internal control components on the fraud detection among (21) Kenyan commercial banks. The study results revealed that there is negative and significant effect of the financial governance control on the fraud detection and prevention. However, there is negative but insignificant effect of the financial governance controls on the fraud detection and prevention.

Collins (2017) investigated the effect of the internal control on the financial performance of commercial banks in South Africa through using a case study Absa Group Limited. The data was taken from a sample of (80) top level managers in the company. The study results confirmed that there is positive and significant effect of internal control on financial performance in the group.

Kioko and Wambugu (2017) investigated the effect of the internal control effectiveness and efficiency on the firm value of the listed companies in New York Stock Exchange (NYS). The researchers used the quantitative and correlation research design. The data was taken from a sample of (14) listed companies. The study results confirmed that there was positive and significant effect of internal control components basically control activities and risk assessment on the firm value. However, there is insignificant effect of monitoring and communication and information components on the firm value. However, the main limitation of this study that it was performed on a small sample of listed companies. Thus, this sample may not be representative for the entire population.

Hamadi & Juma (2016) investigated the effect of the internal control effectiveness and efficiency of the internal control in preventing fraud in financing administration among investment businesses in Kenya. The study results confirmed that the weakness of the internal control system increases the potential of the fraudulent practices in the businesses and the internal control weakness leads to decreasing financial performance. Furthermore, the study results revealed that the inadequate control activities support fraud in the business.

Louz (2016) examined the effect of the internal control on the financial performance of Hellenic Open University in Greece. The data was taken from a sample of (130) respondents. The study results confirmed that the risk assessment and control environment are the most interesting components of internal control that affect financial performance.

Kinyua (2015) investigated the effect of the internal control environment on the financial performance of listed companies in Kenya. The study results demonstrated that there was positive effect of internal control environment on financial performance. This result is in alignment with Mawanda (2008) who found that there was positive and significant effect of internal control components on the financial performance as the existence of efficient

internal control system increases the financial performance of the investigated businesses. Furthermore, Kamau, (2014) examined the correlation between the effectiveness and efficiency of the internal control environment and the financial performance of manufacturing companies in Kenya. The study results demonstrated that most of the listed companies have control environment as an interesting function of the internal control system in their businesses. Furthermore, there was positive and significant effect of the control environment on the financial performance of the manufacturing companies in Kenya. Besides, the study revealed that all these businesses involve in training and development of employees to implement the financial and accounting management systems.

In another study performed by Kinyua (2015) who examined the efficiency and effectiveness of the internal control implementation and its effect on financial performance. The study results confirmed that there was positive and significant effect of the implementation of efficient internal control system and financial performance of a business. Thus, the main reason for the deterioration of the financial performance of businesses is the internal control weaknesses and deficiencies. The researcher suggested based on the study findings that the organizations should develop and update their internal control system and to have adequate size of employees who are able to perform the internal control effectively and efficiently.

Ndiwa (2014) investigated the effect of the internal control components on the financial performance in tertiary training institutions in Kenya. The researcher used the case study in this study through analyzing the effect of the internal control weakness on the financial performance in the African Institute of Research and Development Studies. The study results demonstrated that there is a direct and significant effect of internal control on the financial performance of the institution as the internal control weakness decreased the financial performance of the institute.

Mwakimasinde, Odhiambo and Byaruhanga (2014) examined the effect of the internal control on the financial performance in the sugarcane out grower companies in Kenya. The study results confirmed that there is positive and significant effect of internal control on financial performance in sugarcane out grower companies. The major implication of

this study that the investigated companies should involve in development of the internal control system.

Anecho (2013) examined the effect of the internal control, accountability, operational efficiency on financial performance of (45) financial institutions out of (115) financial institutions that work in Egyptian financial sector. The study results confirmed that there is positive and significant effect of the corporate governance instruments and mechanisms on the financial performance of these institutions. However, the study findings documented that there was insignificant effect of the internal control on the financial performance. Malik (2010) examined the effect of the internal control components on the insurance institutions' firm value in New York. The data was taken from a sample of (67) insurance institutions. The study results confirmed that there is positive and significant effect of internal control system on the firm value of the insurance institutions as the existence of effective and well proper established internal control system enhances the financial performance of the insurance institutions.

Njoroge (2017) investigated the effect of the risk assessment as an interesting component of internal control on the financial performance of pharmaceutical companies in Kenya throughout the period 2013-2015. The data was taken from the annual reports of the companies. The study results confirmed that there is positive and significant effect of the risk assessment on the financial performance of the pharmaceutical companies in Kenya.

2.9 Conclusion

Internal control is a system that the senior executive management establishes and creates to confirm smooth and organized running of regular activities of the business, protecting the assets and the competencies of the organization and creating precise and trustworthy reports. According to COSO framework (2013) internal control is “A process accomplished by the board of directors and the senior executive management of the business in providing sensible affirmation concerns the accomplishment of operational, reporting and compliance goals. It is the approach that a business works and the way that it's staffs' awareness is affected is specified by the control environment”.

According to the IAS internal control involves business plan, separation of duties and responsibilities, document control, protection and rationale use of business assets and competencies, employees' competence, control of accounting and arithmetic, collecting and storage of records, authorization and approvals, supervision, duty rotation and vocation, practicality of cost, routine and automatic checking. The researcher presented and discussed several theories that can act an essential role in explaining the effect of the internal control deficiency on the financial performance of companies. These theories basically are the agency, stewardship, positive accounting, and the attribution theories.

The previous empirical studies have confirmed that the internal control is interesting to confirm the existence of effective and efficient system of business operations, reliability of the business financial reporting and the adherence and compliance with the set laws, polices, procedures and regulation to which the business is subject. Thus, the existence of efficient and effective internal control supports the financial performance of the business and it supports the potential of the business to avert, detect, and remove fraudulent practices.

COSO provided five components of the internal control that are: Control environment, risk assessment, control activities, monitoring, communication and information. The control activities include both the handbook and automatic resources that act an essential role in detecting and preventing or mitigating various risks that can affect negatively the achievement of the business mission and objectives. Whereas, the control environment is the set of "standards, processes, and structures that provide the basis for performing internal control across the business. However, risk assessment or evaluation of risk takes

into consideration the evaluation of both the external and internal threats and risks and basically introduces a prompt threatening system to specify remote risks or risks with least prospect, and take indispensable activities to reduce and decrease such risks. Whereas, monitoring is the efficient internal control system needs constant monitoring process in order to confirm effective and efficient system performance over time. Monitoring of internal control systems is interesting in order to confirm the existence of high-quality reviews and audits. Eventually, information & communication is the “Methods or instruments by which information is spread in the business. It gives the employees the potential to receive an obvious message from top executive management that control responsibilities must be performed seriously.

The weakness of the internal control system affects negatively the financial performance of businesses as documented by several empirical studies. Furthermore, it affects negatively the trust and confidence of the investors and the shareholders in the reliability of the financial statement’s representation, increasing the incidence of fraud and increasing the likelihood of the business failure and bankruptcy and increasing the exercise of the earnings management in the listed businesses.

A substantial deficiency is one or a mixture of deficits that may lead to the likelihood that the controls of a business will not discover or inhibit a substantial fault in the balance or disclosure of an account. Internal control weakness would influence the listed companies disclosing an unqualified conclusion on internal control over financial report, and unqualified conclusion have critical significances for businesses for instance poor lending decision.

In the assessment the internal control, internal auditors usually evaluate internal control deficiency from pervasive control and internal control deficiency CD from process specific controls. The first type that is the pervasive controls are control that influences several processes in the business. Such as the control over management predominate is one of the pervasive controls. “Management override” is a concept used to describe the ability and the power of management to influence accounting entries by intervening the controls to disclose a fraudulent financial statement. If there are no controls over management overrule, the senior executive management may purposefully misstate the nature and timing of a transaction in order to affect the amount of revenues or expenses.

So that, affecting several accounts. Thus, management overrule control is a pervasive control and it has a high effect on the business from several processes.

Chapter Three

Methodology

This chapter presents the procedures and the methodology used to conduct this research. It also explains the research design, target population, sample size and type, validity, and reliability of the questionnaire, and statistical methods.

3.1 Study Design

This study focuses on the impact of internal control deficiencies (design of internal control, operation of internal control, control environment, control activities, risk assessment, information and communication, and monitoring) on Financial Performance of Palestinian companies in. The study uses a quantitative approach to reach the findings; a structured questionnaire was used as the data collection tool to gather information from the employees and internal control managers and financial management of Palestinian companies. The Secondary data was obtained from published and unpublished articles.

3.2 Study Instrument

A structured questionnaire was distributed to the employees working in the Palestinian companies. The questionnaire includes the personal information and the dimensions of study variables including Internal Control Deficiency dimensions (design of internal control, operation of internal control, control environment, control activities, risk assessment, information and communication, and monitoring deficiencies) and financial performance.

The variables are scaled using a 5 Likert scale from 5= strongly agree, to 1= strongly disagree. The questionnaire was distributed to the employees and internal control managers and financial management. It was made to achieve the study objectives, answer the study questions, and test research hypotheses.

The questionnaire used by the scholar to collect data takes the following methods to be performed: questionnaire design, the validity of the questionnaire, and the reliability of the questionnaire, as discussed in this section:

3.2.1 Questionnaire Design

The questionnaire was used in this study to collect data after modification by editing some of the wording used to make it clearer and more relevant to participants. It included three parts including demographic data, the dimensions of study variables including; internal control deficiency (design of internal control, operation of internal control, control environment, control activities, risk assessment, information and communication, monitoring deficiencies), and financial performance.

First part: the demographic information about the respondents consisted of four variables including: (job title, legal form of the company, frequency of internal control systems revision, and sector of the company).

Second part: covered the research's two main variables:

Internal Control Deficiency, which consisted of seven dimensions. These dimensions are based on (Leonard, 2022; Tesfaye, 2019) study.

The financial performance consisted of five items. These items were based on (Mawanda, 2008; Abdi, 2015).

3.2.2 Validity of Questionnaire

The questionnaire was developed, approved, and edited to reach the final form which was distributed to the target respondents. The questionnaire was sent to evaluators (appendix (3)) and the supervisor to evaluate each dimension and its consistency to validate the consistency of all the paragraphs in the questions. The first draft of the questionnaire was structured into (47) forty-seven items total.

Table 1: Questionnaire items

| Study Variables | (Number of Items) |
|---|-------------------|
| Internal Control Deficiency steps: | 39 |
| 1) design | 5 |
| 2) Operations | 3 |
| 3) Environment | 7 |
| 4) Activities | 7 |
| 5) Risk assessment | 6 |
| 6) Information and communication | 6 |
| 7) Monitoring | 5 |
| Financial performance | 5 |
| Total | 44 |

3.2.3 Reliability of Questionnaire

The study employed Cronbach's α coefficient as a measure of scale reliability, with a reference value of 0.7 (Hair et al., 1995; Tavakol & Dennick, 2011). All variables yielded excellent results, with α values surpassing 0.829.(Table 2).

To assess the convergent and divergent validity of the scales, we conducted an explanatory factor analysis. During this analysis, we eliminated items that contributed minimally to the model's explanatory power ($R^2 > 0.5$). Convergent validity was determined by examining the factor loadings of the indicators, following the guidelines of Hair Jr. et al. (2016) and Sekaran & Bougie (2010, p. 290), which suggests a loading value greater than 0.50. All loading values for the latent constructs exceeded this threshold ($\beta > 0.599$), table 2 shows the results of explanatory factor analysis and Cronbach's α coefficient, indicating that the latent variables effectively account for the observed variables.

In terms of discriminant validity, the factor correlation matrix, table 3, Factor Correlation Matrix, illustrates that the correlation between any pairs of independent variables (design, Operations, Environment, Activities, Risk assessment, Information and communication,

Monitoring) does not exceed 0.7, which indicates that independent variables illustrate discriminant validity according to Gaskin and Lim (2016), Furthermore, the correlation between each pair of scales did not surpass 0.8, demonstrating adequate discriminant validity.

Table 2: Cronbach’s α , factor loading,

| Variable | Cronbach’s Alpha |
|-------------------------------|-------------------------|
| Design | .894 |
| Operations | .829 |
| Environment | .957 |
| Activities | .966 |
| Risk assessment | .923 |
| Information and communication | .947 |
| Monitoring | .924 |
| Financial performance | .890 |

3.3 Population and Sample

The study population consisted of employees and internal control managers and financial management of listed corporations at PEX. The sample is the part of the population that is chosen according to scientific rules and methods so that the population is properly represented. The researcher selected a non-probability sample of the original study population .The sample size of this study is identified according to Krejcie and Morgan (1970).

The sample size (n)

$$(n) = \frac{Z^2 P(1-P)}{d^2}$$

Where:

n : Sample size required,

z : Z statistic for a level of confidence required,

P : Expected prevalence or proportion (If the expected prevalence is 20%, then $P= 0.2$),
and

d : Precision (If the precision is 5%, then $d = 0.05$).

$$\text{The sample size} = \frac{0.95^2 * 0.5(1-0.5)}{0.05^2}$$

$$= 60\%$$

Collected sample size = 310, Number of distributed questionnaires = 450, Number of recovered questionnaires = 405

3.3.1 Unit of analysis

The unit of analysis consists of employees working in listed companies in Palestine with the following job titles: director of the internal control department, internal audit manager, compliance department manager, risk department manager, anti-money laundering manager.

3.3.2 Statistical Approaches

The primary data were analyzed by using the Statistical Package for Social Sciences (SPSS V26.0).

- Descriptive tests: Frequency to describe the demographic variables, mean and standard deviation to answer the study questions.
- Simple linear regressions to test the impact of Internal Control Deficiency on financial performance.

Chapter Four

Findings

4.1 Introduction

In this chapter, the focus is on analyzing the results of the study and testing the hypotheses by answering the study questions. The analysis is based on the most prominent results obtained from the questionnaire. The variables of the study are identified and analyzed using statistical software, SPSS (Statistical Package for the Social Sciences), to obtain the study results.

The chapter starts by examining the responses of the study sample participants in relation to the study's main axes, which are aligned with the study questions. This analysis aims to provide insights into the participants' perspectives and opinions on the study topic.

4.2 Descriptive statistics

Table 4 illustrates the sample demographics characteristics.

Table 3: Descriptive statistics of participant characteristics

| Item | Percentage (%) | Frequency |
|--|----------------|-----------|
| job title | | |
| Director of the Internal Control Department | 31.9 | 133 |
| Internal audit manager | 42.9 | 29 |
| Compliance Department Manager | 9.4 | 31 |
| Risk Department Manager | 10.0 | 18 |
| Anti-money laundering manager | 18 | 58 |
| Legal form of the company | | |
| Partnership | 9.4 | 29 |
| corporate listed in the Palestine exchange | 68.7 | 213 |
| corporate not listed in the Palestine exchange | 3.5 | 11 |

| | | |
|---|------|-----|
| limited liability company | 18.4 | 57 |
| How frequently does, your company review its internal control systems? | | |
| Every Five years | 18.1 | 56 |
| Annually | 21.9 | 68 |
| Semiannually | 26.8 | 83 |
| When need arise | 33.2 | 103 |
| Sector of the company | | |
| Constructions | 18.7 | 58 |
| Manufacturing | 39.7 | 123 |
| commerce | 41.6 | 129 |

According to the data presents in table, 133 (31.9%) of participant were Director of the Internal Control Department, 213(68.7%) were corporate listed in the Palestine exchange, regarding Sector of the company, 129(41.6%) were commerce, 123(39.7%) were Manufacturing

4.3 Results of the study

This section reviews the analysis of the data to identify the most prominent results that were reached by analyzing its items and testing the relationships between the study variables represented by the independent variables, which are Internal Control Deficiency (Internal Control Deficiency, Financial Performance, design of Internal control, Operation of Internal control, Control Environment, Control Activities, Risk Assessment, Information and Communication, Monitoring deficiencies) and dependent variable Financial Performance.

4.3.1 Results of the study questions

In this section, we will answer the study questions. This study will create three categories to classify the means (low, medium, and high). Since the highest value is 7, the lowest value is 1, the interval length will be as follow:

$$\frac{\text{max}V - \text{Min}V}{\text{number of intervals}} = \frac{5 - 1}{3} = \frac{4}{3} = 1.33$$

Therefore, if the mean is between 1 and 2.33, it will be considered as low, if the mean is between 2.34 and 3.67, it will be considered as medium, and if the mean is above 3.67, it will be considered as high.

Table 4: the study population's means and standard deviation of design of internal control.

| | Item | Mean | Std. Deviation | | Rank |
|---------|--|--------|----------------|--------|------|
| design1 | Existing controls are not properly designed. Thus, the financial reporting risks may not be addressed. | 3.64 | 1.014 | Medium | 1 |
| design2 | Control is missing in my company | 3.35 | .949 | Medium | 2 |
| design3 | The control is well designed but not properly applied. | 3.64 | 1.011 | Medium | 1 |
| design4 | Duties are not clearly defined among the employees. | 3.22 | .899 | Medium | 4 |
| design5 | Job description for the employees is clear and obvious. | 3.30 | .916 | Medium | 3 |
| Design | | 3.4284 | .80337 | Medium | |

Table 4 illustrates mean, standard deviation, and rank for Design of internal control items. Results indicate that respondents perceive a medium implementation of the Design of internal control (M= 3.4284, SD= 80337). Item 3 (“The control is well designed but not properly applied.”) has the highest mean (M= 3.64, SD= 1.011), which means that although the internal control is established, respondents perceive the implementation of the internal control as poor. On the other hand, item 4 (“Duties are not clearly defined among the employees.”) has the lowest mean (M= 3.22, SD= .899). Which means that respondents perceive that their duties and tasks are well-defined.

Table 5: the study population's means and standard deviation of Operation of Internal control.

| | item | Mean | Std. Deviation | | Rank |
|------------|--|--------|----------------|--------|------|
| Operation1 | . Current controls are not operated as designed | 3.36 | .962 | Medium | 3 |
| Operation2 | The person performing the control does not possess the necessary authority to perform the control effectively. | 3.73 | 1.032 | High | 1 |
| Operation3 | The person performing the control does not possess the necessary competence to perform the control effectively | 3.61 | .988 | Medium | 2 |
| Operation | | 3.5677 | .85830 | Medium | |

Table 5 illustrates the mean, standard deviation, and rank the for Operation of Internal control. Results indicate that respondents illustrate a medium value on this dimension (M=3.5677, SD=.85830). Item2 (“The person performing the control does not possess the necessary authority to perform the control effectively”) has the highest mean (M=3.73, SD=1.032), which means that respondents perceive that the person who implements the

control, should have more authority to implement it. Lack of authority can be a great barrier to implementing operations control. On the other hand, item 1 (“Current controls are not operated as designed”) has the lowest mean (M=3.36, SD=.962). Which means that respondents perceive that current operation controls are operating as it is supposed to be.

Table 6: The study population's means and standard deviation of Control Environment.

| | Item | Mean | Std. Deviation | | Rank |
|--------------|--|------|----------------|--------|------|
| Environment1 | There is ineffective internal auditing in the company | 3.28 | 1.185 | Medium | 3 |
| Environment2 | Staff of internal control do not understand their responsibilities very well | 3.28 | 1.069 | Medium | 3 |
| Environment3 | Employees does not commit to the policies and procedures of the comp. | 3.36 | 1.214 | Medium | 1 |
| Environment4 | improper actions are carried out to correct errors in operations of the finance management system | 3.29 | 1.228 | Medium | 2 |
| Environment5 | Management shows low level of integrity in accomplishment of its roles | 3.19 | 1.131 | Medium | 4 |
| Environment6 | Ethical values are ignored in the decisions of the management | 3.15 | 1.171 | Medium | 5 |
| Environment7 | There is an unclear separation between the senior executive management and the board of the director in my company | 2.94 | 1.213 | Medium | 6 |

| | | | | |
|-------------|--------|---------|--------|--|
| Environment | 3.2134 | 1.04807 | Medium | |
|-------------|--------|---------|--------|--|

Table 6 illustrates the mean, standard deviation, and rank for Control Environment items. Results indicate that respondents illustrate medium values on this construct (M=3.2134, SD=1.04807). Item3 (“Employee does not commit to the policies and procedures of the company”) has the highest mean (M=3.36, SD=1.214). Which means that respondents perceive that policies and procedures are not well enforced among employees. On the other hand, item 7 (“There is an unclear separation between the senior executive management and the board of the director in my company”) has the lowest mean (M=2.94, SD=1.213). Which means that respondents perceive those authorities and responsibilities of the senior management is clear.

Table 7: the study population's means and standard deviation of Control Activities.

| | item | Mean | Std. Deviation | | rank |
|-------------|--|------|----------------|--------|------|
| Activities1 | Insufficient number staffing (number of employees in internal control department) | 2.39 | 1.179 | Medium | 3 |
| Activities2 | Improper measures are adopted to correct errors in operation of the accounting management system in the company. | 2.32 | 1.184 | Low | 6 |
| Activities3 | My company has inadequate procedures to register it's assets and properties | 2.38 | 1.063 | Medium | 4 |
| Activities4 | The management has improper employment policy | 2.43 | 1.097 | Medium | 2 |
| Activities5 | Actions of control is not performed to identify weaknesses | 2.38 | 1.119 | Medium | 4 |
| Activities6 | My company has a poor-designed chart of account | 2.37 | 1.116 | Medium | 5 |

| | | | | | |
|--------------------|--|--------|---------|--------|---|
| Activities7 | My company has inefficient security system to identify and safeguard assets and properties | 2.44 | 1.138 | Medium | 1 |
| Control Activities | | 2.3857 | 1.02814 | Medium | |

Table 7 illustrates the mean, standard deviation, and rank for Control Activities. Results indicate that respondents illustrate medium on this construct (M=2.3857, SD=1.02814). Item7 ("My company has an inefficient security system to identify and safeguard assets and properties.") has the highest mean (M=2.44, SD=1.138), which means that respondents believe that implementing security systems to protect assets are not enough, or the systems are not well applied. On the other hand, item 2("Improper measures are adopted to correct errors in the operation of the accounting management system in the company.") has the lowest mean (M=2.32, SD=1.184). Which means that respondents believe that accounting information systems are working properly, and when faulty, are corrected in the right manner.

Table 8: the study population's means and standard deviation of Risk Assessment.

| | N | Mean | Std. Deviation | | rank |
|------------------|---|------|----------------|--------|------|
| Risk_Assessment1 | Inadequate strategies of fraud detection | 3.00 | 1.026 | medium | 3 |
| Risk_Assessment2 | My company rarely carries out documents verification that decrease risk | 3.05 | 1.028 | medium | 2 |
| Risk_Assessment3 | My company does not have definite proper objectives | 3.07 | .986 | medium | 1 |
| Risk_Assessment4 | My company has an unclear standard for specification of which risks to the company are most significant and critical. | 2.97 | 1.045 | medium | 4 |

| | | | | | |
|------------------|--|--------|--------|--------|---|
| Risk_Assessment5 | The company strategic plans do not match its objectives. | 3.00 | .980 | medium | 3 |
| Risk_Assessment6 | The company does not have alternative plans for any unexpected changes that might influence the company's activities | 3.05 | 1.034 | medium | 2 |
| Risk Assessment | | 3.0226 | .86464 | medium | |

Table 8 illustrates the mean, standard deviation, and rank for Risk Assessment items. Results indicate that respondents illustrate a medium perception of Risk Assessment (M=3.0226, SD=.86464). item3 (“My company does not have definite proper objectives.”) has the highest mean (M=3.07, SD=.986), which means that respondents perceive that their company does not identify proper goals and objectives, or that the company does not communicate its goals and objectives. On the other hand, item 4 (“My company has an unclear standard for specification of which risks to the company are most significant and critical.”) has the lowest mean (M=2.97, SD=1.045), which means that respondents perceive their company has clear standards to identify risk.

Table 9: The study population's means and standard deviation of Information and Communication.

| | item | Mean | Std. Deviation | | rank |
|------------|---|------|----------------|--------|------|
| Info_Comm1 | My management does not have specified staff who are in charge of coordinating the different activities in the company to confirm proper communication on internal controls. | 3.12 | 1.149 | medium | 1 |
| Info_Comm2 | There is unclear awareness of the significance of internal controls, including the segregation of duties | 3.02 | 1.156 | medium | 2 |

| | | | | | |
|-------------------------------|---|--------|--------|--------|---|
| Info_Comm3 | The information is not recorded and disclosed to all stakeholders' timeliness. | 2.86 | 1.114 | medium | 4 |
| Info_Comm4 | There is a lack of consistency between the preparation, development and review of the information and strategic plans | 2.85 | 1.127 | medium | 5 |
| Info_Comm5 | The management does not pass the information to its employees clearly and smoothly | 2.89 | 1.191 | medium | 3 |
| Info_Comm6 | The company does not communicate with external parties that might influence the internal control function. | 3.02 | 1.164 | medium | 2 |
| Information and Communication | | 2.9651 | .98949 | medium | |

Table 9 illustrates the mean, standard deviation, and rank for Information and Communication items. Results indicate that respondents illustrate a medium perception of Information and Communication in their companies (M=2.9651, SD=.98949). Item1 (“My management does not have specified staff who are in charge of coordinating the different activities in the company to confirm proper communication on internal controls.”) has the highest mean (M=3.12, SD=1.149). Which means that internal controls may be designed properly, but lack of communication may cause it to be ignored, bypassed, or unknown. On the other hand, item 4 (“There is a lack of consistency between the preparation, development and review of the information and strategic plans.”) has the lowest mean (M=2.85, SD=1.127).

Table 10: the study population's means and standard deviation of monitoring deficiencies.

| | item | Mean | Std. Deviation | | rank |
|-------------|--|--------|----------------|--------|------|
| Monitoring1 | There is no clear process investigation of controls activities on constant basis. | 3.10 | 1.031 | medium | 1 |
| Monitoring2 | Irregular internal control implementation reviews | 2.97 | 1.001 | medium | 3 |
| Monitoring3 | Management has not assigned responsibilities for the timely review of audit reports | 2.87 | 1.061 | medium | 5 |
| Monitoring4 | There are improper mechanisms put in place to monitor the quality of internal control structure in the company over time | 2.96 | 1.034 | medium | 4 |
| Monitoring5 | The company has no box for complaints from clients which are handled seriously | 2.99 | .912 | medium | 2 |
| Monitoring | | 2.9761 | .91266 | medium | |

Table 10 illustrates the mean, standard deviation, and rank for Monitoring deficiencies items. Results indicate that respondents perceive medium Monitoring deficiencies from their companies (M= 2.9761, SD= .91266). Item 1 (“There is no clear process investigation of controls activities on a constant basis.”) has the highest mean (M= 3.10, SD= 1.031). Which means that a clear and specified process should be established to monitor and investigate activities. On the other hand, item 3 (“Management has not assigned responsibilities for the timely review of audit reports.”) has the lowest mean (M= 2.87, SD= 1.061).

Table 11: the study population's n means and standard deviation of Internal Control Deficiency

| | item | Mean | Std. Deviation | | rank |
|-----------------------------|-------------------------------|--------|----------------|--------|------|
| 1 | Design | 3.4284 | .80337 | medium | 2 |
| 2 | Operation | 3.5677 | .85830 | medium | 1 |
| 3 | Environment | 3.2134 | 1.0480 | medium | 4 |
| 4 | Control Activities | 2.3857 | 1.02814 | medium | 3 |
| 5 | Risk Assessment | 3.0226 | .86464 | medium | 5 |
| 6 | Information and Communication | 2.9651 | .98949 | medium | 7 |
| 7 | Monitoring | 2.9761 | .91266 | medium | 6 |
| Internal Control Deficiency | | 3.0217 | .74473 | medium | |

Table 11 illustrates the mean, standard deviation, and rank for Internal Control Deficiency items. Results indicate that respondents perceive a medium Internal Control Deficiency made by their company (M=3.0217, SD=.74473). Item2 (“operations.”) has the highest mean (M=3.5677, SD=.85830). Which means that respondents believe that the main cause of internal control deficiencies comes from the operations. On the other hand, item 7 (“Information and Communication”) has the lowest mean (M=3.162, SD=1.9968).

Table 12: the study population's means and standard deviation of Financial Performance.

| | item | Mean | Std. Deviation | | rank |
|-----------------|--|------|----------------|--------|------|
| Financial_perf1 | The fees charged by our institution are appropriate to cover the running costs | 3.07 | 1.9968 | medium | 3 |

| | | | | | |
|-----------------------|---|--------|--------|--------|---|
| Financial_perf2 | Problems of outstanding cheques are solved in time to reconcile the company balance of an account and book balance of the customer. | 3.05 | .972 | medium | 4 |
| Financial_perf3 | Financial performance is the measurement of the results of a firm's Policies and operations in monetary terms. | 3.17 | 1.023 | | 1 |
| Financial_perf4 | Our company has enough cash to meet its obligations effectively (as and when they fall due) | 3.13 | 1.004 | medium | 2 |
| Financial_perf5 | Our company's asset base has greatly increased over time | 3.13 | 1.002 | | 2 |
| Financial performance | | 3.1103 | .83458 | medium | |

Table 12 illustrates the mean, standard deviation, and rank for financial performance items. Results indicate that respondents perceive that their company's financial performance is medium (M= 3.1103, SD= .83458). Item 3 (“Financial performance is the measurement of the results of a firm’s Policies and operations in monetary terms.”) has the highest mean (M= 3.17, SD= 1.023). On the other hand, item 2 (“Problems of outstanding cheese are solved in time to reconcile the Bank balance of an account and book balance of the customer.”) has the lowest mean (M= 3.05, SD= .972). which means that respondents perceive that their companies suffer from outstanding cheque problems.

4.4 Testing hypotheses

In this section, we show the results of the research hypotheses. According to Strijker et al., (2020), if R^2 is greater than .25, it has a high explanation power. It has a medium explanation power if the value of R^2 is between .12 and .25. Where values between .02 and .12 is indicate a low explanation power.

The main hypothesis proposes: There is a negative effect of internal control deficiencies on the financial performance of listed companies in Palestine. To test the main

hypothesis, the study used simple linear regression. Tables 14, 15 and 16 illustrate the results.

Table 13: results of model summary analysis for the main hypothesis

| Model | R | R Square | Adjusted R Square | Std. Error of the Estimate |
|-------|-------------------|----------|-------------------|----------------------------|
| 1 | .665 ^a | .442 | .440 | .62450 |

a. Predictors: (Constant), Internal_Control_Deficiency

Table 14: results of ANOVA analysis for the main hypothesis

| Model | Sum of Squares | df | Mean Square | F | Sig. |
|------------|----------------|-----|-------------|---------|-------------------|
| Regression | 95.107 | 1 | 95.107 | 243.866 | .000 ^b |
| Residual | 120.120 | 308 | .390 | | |
| Total | 215.227 | 309 | | | |

a. Dependent Variable: Financial performance

b. Predictors: (Constant), Internal_Control_Deficiency

Table 15: Results of the analysis of the coefficients for the main hypothesis

| Model | Unstandardized B | Coefficients Std. Error | Standardized Coefficients Beta | t | Sig. |
|-----------------------------|------------------|-------------------------|--------------------------------|---------|------|
| (Constant) | 5.361 | .148 | | 36.117 | .000 |
| Internal_Control_Deficiency | -.745 | .048 | -.665 | -15.616 | .000 |

a. Dependent Variable: Financial performance

Table 14 shows the explanation factor (R^2) of internal control deficiency. The internal control deficiency has a high explanatory power in explaining financial performance ($R^2=0.440$, $p=0.000$). Which means that 44.0% of the variance in financial performance is explained by internal control deficiency. Moreover, internal control deficiency has a negative significant effect on financial performance ($B=-0.665$, $Sig=0.000$) which means that when internal control deficiency increases by one standard unit, financial performance decreases by .665 standard unit. Therefore, we reject H_01 and accept the alternative hypotheses which indicate that there is a significant negative impact of internal control deficiency on financial performance.

Testing sub hypotheses

1. $H_{a1.1}$: There is a negative effect of control design deficiency on the financial performance of listed companies in Palestine.

Table 16: results of model summary analysis for the first sub-hypothesis

| Model | R | R Square | Adjusted R Square | Std. Error of the Estimate |
|-------|------|----------|-------------------|----------------------------|
| 1 | .440 | .194 | .191 | .75056 |

Predictors: (Constant), Design

Table 17: results of ANOVA analysis for the first sub hypothesis

| Model | Sum of Squares | df | Mean Square | F | Sig. |
|------------|----------------|-----|-------------|--------|-------------------|
| Regression | 41.716 | 1 | 41.716 | 74.050 | .000 ^b |
| Residual | 173.511 | 308 | .563 | | |
| Total | 215.227 | 309 | | | |

Dependent Variable: Financial performance

Predictors: (Constant), Design

Table 18: Results of the analysis of the coefficients for first sub-hypothesis

| Model | Unstandardized B | Coefficients Std. Error | Standardized Coefficients Beta | t | Sig. |
|-----------------------------|------------------|-------------------------|--------------------------------|--------|------|
| (Constant) | 4.678 | .187 | | 25.000 | .000 |
| Internal_Control_Deficiency | -.457 | .053 | -.440 | -8.605 | .000 |

Dependent Variable: Financial performance

Table 17 shows the explanation factor (R^2) of control design deficiency. The control design deficiency has a medium explanatory power in explaining financial performance ($R^2= 0.191$, $p= 0.000$) which means that 19.1% of the variance in financial performance is explained by control design. Moreover, control design has a negative significant effect on financial performance ($B= -0.440$, $Sig= 0.000$) which means that when control design increases by one standard unit, financial performance decreases by .44 standard unit. Therefore, we reject $H_{o1.1}$ and accept the alternative hypotheses which indicate that there is a significant negative impact of control design on financial performance.

2. $H_{a1.2}$: There is a negative effect of Operation deficiency on the financial performance of listed companies in Palestine.

Table 19: results of model summary analysis second sub-hypothesis

| Model | R | R Square | Adjusted R Square | Std. Error of the Estimate |
|-------|------|----------|-------------------|----------------------------|
| 1 | .351 | .123 | .120 | .78276 |

Predictors: (Constant), Operation

Table 20: results of ANOVA analysis for the second sub-hypothesis

| Model | Sum of Squares | df | Mean Square | F | Sig. |
|------------|----------------|-----|-------------|--------|-------------------|
| Regression | 26.511 | 1 | 26.511 | 43.268 | .000 ^b |
| Residual | 43.268 | 308 | .613 | | |
| Total | 215.227 | 309 | | | |

Dependent Variable: Financial performance

Predictors: (Constant), Operation

Table 21: Results of the analysis of the coefficients for the second sub-hypothesis

| Model | Unstandardized B | Coefficients Std. Error | Standardized Coefficients Beta | t | Sig. |
|----------------------|------------------|-------------------------|--------------------------------|---------|------|
| (Constant) | 4.328 | .190 | | 22.735 | .000 |
| Operation deficiency | -.341- | .052 | -.351- | -6.578- | .000 |

Dependent Variable: Financial performance

Table 20 shows the explanation factor (R^2) of operation deficiency. The operation deficiency has a high explanatory power in explaining financial performance ($R^2= 0.12$, $p= 0.000$) which means that 12% of the variance in financial performance is explained by internal operation deficiency. Moreover, operation deficiency has a negative significant effect on financial performance ($B= -0.315$, $Sig= 0.000$) which means that when operation deficiency increases by one standard unit, financial performance decreases by .315 standard unit. Therefore, we reject $H_{o1.2}$ and accept the alternative hypotheses which indicate that there is a significant negative impact of operation deficiency on financial performance.

- Ha1.3: There is a negative effect of control environment deficiency on the financial performance of listed companies in Palestine.

Table 22: results of model summary analysis for the third sub-hypothesis

| Model | R | R Square | Adjusted R Square | Std. Error of the Estimate |
|-------|------|----------|-------------------|----------------------------|
| 1 | .596 | .355 | .353 | .67135 |

Predictors: (Constant), Environment

Table 23: results of ANOVA analysis for the third sub-hypothesis

| Model | Sum of Squares | df | Mean Square | F | Sig. |
|------------|----------------|-----|-------------|---------|-------------------|
| Regression | 76.407 | 1 | 169.524 | 138.820 | .000 ^b |
| Residual | 138.820 | 308 | .451 | | |
| Total | 215.227 | 309 | | | |

Dependent Variable: Financial performance

Predictors: (Constant), Environment

Table 24: Results of the analysis of the coefficients for the third sub-hypothesis

| Model | Unstandardized B | Coefficients Std. Error | Standardized Coefficients Beta | t | Sig. |
|---------------------|------------------|-------------------------|--------------------------------|---------|------|
| (Constant) | 4.635 | .123 | | 37.637 | .000 |
| control environment | -.474 | .036 | -.596 | -13.020 | .000 |

Dependent Variable: Financial performance

Table 23 shows the explanation factor (R^2) of the control environment deficiency. the control environment deficiency has a high explanatory power in explaining financial performance ($R^2= 0.353$, $p= 0.000$) which means that 35.3% of the variance in financial performance is explained by the control environment. Moreover, the control environment has a negative significant effect on financial performance ($B= -0.596$, $Sig= 0.000$) which means that when control environment deficiency increases by one standard unit, financial performance decreases by .596 standard unit. Therefore, we reject $H_{01.3}$ and accept the alternative hypotheses which indicate that there is a significant negative impact of control environment deficiency on financial performance.

4. Ha1.4: There is a negative effect of control activities deficiency on the financial performance of listed companies in Palestine.

Table 25: results of model summary analysis for the fourth sub-hypothesis

| Model | R | R Square | Adjusted R Square | Std. Error of the Estimate |
|-------|------|----------|-------------------|----------------------------|
| 1 | .516 | .266 | .264 | .71604 |

Predictors: (Constant), Activities

Table 26: results of ANOVA analysis for the fourth sub-hypothesis

| Model | Sum of Squares | df | Mean Square | F | Sig. |
|------------|----------------|-----|-------------|---------|-------------------|
| Regression | 57.311 | 1 | 57.311 | 111.779 | .000 ^b |
| Residual | 157.916 | 308 | .390 | | |
| Total | 215.227 | 309 | | | |

Dependent Variable: Financial performance

Predictors: (Constant), Activities

Table 27: Results of the analysis of the coefficients for the fourth sub-hypothesis

| Model | Unstandardized B | Coefficients Std. Error | Standardized Coefficients Beta | t | Sig. |
|--------------------|------------------|-------------------------|--------------------------------|---------|------|
| (Constant) | 4.110 | .103 | | 39.939 | .000 |
| control activities | -.419 | .040 | -.516 | -10.573 | .000 |

Dependent Variable: Financial performance

Table 26 shows the explanation factor (R^2) of the control activities deficiency. The control activities deficiency has a high explanatory power in explaining financial performance ($R^2 = 0.264$, $p = 0.000$) which means that 26.4% of the variance in financial performance is explained by control activities deficiency. moreover, control activities deficiency has a negative significant effect on financial performance ($B = -0.516$, $Sig = 0.000$) which means that when control activities deficiency increases by one standard unit, financial performance decreases by .516 standard unit. Therefore, we reject $H_{01.4}$

and accept the alternative hypotheses which indicate that there is a significant negative impact of control activities deficiency on financial performance.

5. Ha1.5: There is a negative effect of risk assessment deficiency on the financial performance of listed companies in Palestine.

Table 28: results of model summary analysis for the fifth sub-hypothesis

| Model | R | R Square | Adjusted R Square | Std. Error of the Estimate |
|-------|------|----------|-------------------|----------------------------|
| 1 | .521 | .271 | .269 | .71375 |

Predictors: (Constant), Risk Assessment

Table 29: results of ANOVA analysis for the fifth sub-hypothesis

| Model | Sum of Squares | df | Mean Square | F | Sig. |
|------------|----------------|-----|-------------|---------|-------------------|
| Regression | 58.322 | 1 | 58.322 | 114.483 | .000 ^b |
| Residual | 156.905 | 308 | .509 | | |
| Total | 215.227 | 309 | | | |

Dependent Variable: Financial performance

Predictors: (Constant), Risk Assessment

Table 30: Results of the analysis of the coefficients for the fifth sub-hypothesis

| Model | Unstandardized B | Coefficients Std. Error | Standardized Coefficients Beta | t | Sig. |
|----------------------------|------------------|-------------------------|--------------------------------|----------|------|
| (Constant) | 5.361 | .148 | | 36.117 | .000 |
| risk assessment deficiency | -.745- | .048 | -.665- | -15.616- | .000 |

Table 29 shows the explanation factor (R^2) of risk assessment deficiency. the risk assessment deficiency has a high explanatory power in explaining financial performance ($R^2= 0.269$, $p= 0.000$) which means that 26.9% of the variance in financial performance is explained by risk assessment deficiency. moreover, risk assessment deficiency has a negative significant effect on financial performance ($B= -0.665$, $Sig= 0.000$) which means that when risk assessment deficiency increases by one standard unit, financial performance decreases by .665 standard unit. Therefore, we reject $H_{0.1.5}$ and accept the

alternative hypotheses which indicate that there is a significant negative impact of risk assessment deficiency on financial performance.

6. Ha1.6: There is a negative effect of information and communication deficiency on the financial performance of listed companies in Palestine.

Table 31: results of model summary analysis for the sixth sub-hypothesis

| Model | R | R Square | Adjusted R Square | Std. Error of the Estimate |
|-------|------|----------|-------------------|----------------------------|
| 1 | .591 | .349 | .347 | .67457 |

Predictors: (Constant), Information and Communication

Table 32: results of ANOVA analysis for the sixth sub-hypothesis

| Model | Sum of Squares | df | Mean Square | F | Sig. |
|------------|----------------|-----|-------------|---------|-------------------|
| Regression | 75.071 | 1 | 75.071 | 164.974 | .000 ^b |
| Residual | 140.156 | 308 | .455 | | |
| Total | 215.227 | 309 | | | |

Dependent Variable: Financial performance

Predictors: (Constant), Information and Communication

Table 33: Results of the analysis of the coefficients for the sixth sub-hypothesis

| Model | Unstandardized B | Coefficients Std. Error | Standardized Coefficients Beta | t | Sig. |
|-------------------------------|------------------|-------------------------|--------------------------------|---------|------|
| (Constant) | 4.587 | .121 | | 37.847 | .000 |
| information and communication | -.498 | .039 | -.591 | -12.844 | .000 |

Dependent Variable: Financial performance

Table 32 shows the explanation factor (R^2) of information and communication deficiency. The information and communication deficiency has a high explanatory power in explaining financial performance ($R^2 = 0.347$, $p = 0.000$) which means that 34.7% of

the variance in financial performance is explained by information and communication deficiency. moreover, information and communication deficiency have a negative significant effect on financial performance ($B = -0.591$, $Sig = 0.000$) which means that when information and communication deficiency increases by one standard unit, financial performance decreases by .591 standard unit. Therefore, we reject $H_{0.1.6}$ and accept the alternative hypotheses which indicate that there is a significant negative impact of information and communication deficiency on financial performance.

7. $H_{a1.7}$: There is a negative effect of monitoring deficiency on the financial performance of listed companies in Palestine.

Table 34: results of model summary analysis for the seventh sub-hypothesis

| Model | R | R Square | Adjusted R Square | Std. Error of the Estimate |
|-------|------|----------|-------------------|----------------------------|
| 1 | .514 | .264 | .261 | .71730 |

Predictors: (Constant), Monitoring

Table 35: results of ANOVA analysis for the seventh sub-hypothesis

| Model | Sum of Squares | Df | Mean Square | F | Sig. |
|------------|----------------|-----|-------------|---------|-------------------|
| Regression | 56.756 | 1 | 56.756 | 110.309 | .000 ^b |
| Residual | 158.471 | 308 | .515 | | |
| Total | 215.227 | 309 | | | |

Predictors: (Constant), Monitoring

Dependent Variable: Financial performance

Table 36: Results of the analysis of the coefficients for the seventh sub-hypothesis

| Model | Unstandardized B | Coefficients Std. Error | Standardized Coefficients Beta | t | Sig. |
|-----------------------|------------------|-------------------------|--------------------------------|----------|------|
| (Constant) | 4.508 | .139 | | 32.393 | .000 |
| monitoring deficiency | -.470- | .045 | -.514- | -10.503- | .000 |

Dependent Variable: Financial performance

Tables 35 and 36 show the explanation factor (R^2) of monitoring deficiency. The monitoring deficiency has a high explanatory power in explaining financial performance ($R^2 = 0.261$, $p = 0.000$) which means that 26.1% of the variance in financial performance is explained by monitoring deficiency. Moreover, monitoring deficiency has a negative significant effect on financial performance ($B = -0.514$, $Sig = 0.000$) which means that when monitoring deficiency increases by one standard unit, financial performance decreases by .514 standard unit. Therefore, we reject $H_{0.1.7}$ and accept the alternative hypotheses which indicate that there is a significant negative impact of monitoring deficiency on financial performance.

Considering all the independent variables we can express the relationship between the dependent variable and the dependent variables as follows:

$$\text{Financial performance} = A_0 + -.440 * [\text{control design deficiency}] + -.351 * [\text{Operation deficiency}] + -.596 * [\text{control environment deficiency}] + -.516 * [\text{control activities deficiency}] + -.665 * [\text{risk assessment deficiency}] + -.591 * [\text{information and communication deficiency}] + -.514 * [\text{monitoring deficiency}] + \varepsilon$$

Chapter Five

Results and recommendations

5.1 Introduction

Internal control deficiencies can have significant implications for an organization's financial performance. These deficiencies can undermine the reliability and accuracy of financial reporting, leading to misstatements and errors in financial statements. As a result, investors may lose confidence in the company's financial information, leading to a decline in stock prices and difficulty in attracting capital. Moreover, internal control deficiencies increase the risk of fraud, asset misappropriation, and operational inefficiencies, which can directly impact an organization's profitability and overall financial health. Additionally, regulatory non-compliance and legal consequences may arise due to inadequate internal controls, resulting in financial penalties and reputational damage. Therefore, it is crucial for organizations to prioritize and continuously assess their internal control systems to mitigate these risks and safeguard their financial performance, ensuring transparency, accuracy, and accountability in their financial reporting processes. By doing so, companies can enhance investor trust, minimize financial losses, and maintain a competitive edge in the marketplace.

5.2 Results

The purpose of the study is to investigate the effect of internal control deficiency (control environment, Control Activities, Risk Assessment, Information and Communication, Monitoring deficiencies) on the financial performance of Palestinian companies. The questionnaire is the main appropriate tool for the field study to obtain information and data that is being filled in by the respondent. The population of the study consists of the employees and internal control managers and financial management of Palestinian companies. The study results that:

1. Respondents perceive a medium implementation of the Design of internal control, a medium level of implementation implies that there is some degree of structure and control within the organization's internal control framework. However, there may be gaps or deficiencies that prevent it from reaching an optimal level of effectiveness. It is important for organizations to identify these areas of improvement and take appropriate actions to address them. It indicates that there is a certain degree of structure and control within the organization's internal control framework. However, it also suggests that there may be gaps or deficiencies that hinder its optimal effectiveness.
2. The study result that the control is well designed but not properly applied, which means that although the internal control is established, respondents perceive the implementation of the internal control as poor, the organization has established a sound internal control framework on paper or in theory. However, the respondents' perception suggests that the implementation of this internal control framework is lacking or ineffective.
3. Results indicate that respondents illustrate a medium value for Operation of Internal control. This indicates that while some aspects of internal control are functioning adequately, there may be room for improvement in certain areas, it suggests that some aspects of the internal control system are functioning adequately. However, there may still be areas where improvements can be made to enhance the overall effectiveness of the internal control operations.

4. A medium value implies that there is a certain level of functionality and implementation of internal control processes within the organization. It indicates that some control activities and monitoring mechanisms are in place, but there may be gaps or deficiencies in certain areas that need attention.
5. The study also results that, the person performing the control does not possess the necessary authority to perform the control effectively, which means that respondents perceive that the person who implements the control, should have more authority to implement it. Lack of authority can be a great barrier to implementing operations control.
6. The study Results indicate that respondents illustrate medium values on Control Environment items, this suggests that while there is some degree of control environment in place, there may be areas where improvement is needed to strengthen the overall control culture, The control environment sets the tone for the organization and influences the behavior and attitudes towards internal control. It encompasses factors such as management's commitment to internal control, ethical values, integrity, accountability, and the overall control consciousness within the organization
7. Results indicate there is an unclear separation between the senior executive management and the board of the director in my company, which means that respondents perceive that policies and procedures are not well enforced among employees, this can lead to challenges in enforcing policies and procedures among employees.
8. Results indicate that respondents illustrate medium on Control Activities, which means that respondents believe that implementing security systems to protect assets are not enough, or the systems are not well applied, it suggests that respondents believe there is room for improvement in implementing control measures to protect assets within the organization. It indicates that either the existing security systems are not considered sufficient, or they are not being effectively applied.
9. Results indicate that respondents illustrate a medium perception of Risk Assessment, this indicates that the organization recognizes the importance of

- assessing and managing risks but may not have fully developed or implemented a comprehensive risk assessment process
10. Results indicate that company does not have definite proper objectives, which means that respondents perceive that their company does not identify proper goals and objectives, or that the company does not communicate its goals and objectives
 11. Results indicate that respondents illustrate a medium perception of Information and Communication in their companies, this suggests that while there may be some established processes and practices in place, there is room for improvement in certain areas related to information sharing and communication.
 12. Results indicate that management does not have specified staff who are in charge of coordinating the different activities in the company to confirm proper communication on internal controls. Which means that internal controls may be designed properly, but lack of communication may cause it to be ignored, bypassed, or unknown.
 13. Results indicate that respondents perceive medium Monitoring deficiencies from their companies, which means the organization has implemented some monitoring processes but may not have a comprehensive and robust system in place to consistently assess and evaluate the effectiveness of internal controls.
 14. Results indicate that respondents illustrate that there is no clear process investigation of controls activities on a constant basis, which means that a clear and specified process should be established to monitor and investigate activities.
 15. Results indicate that respondents perceive a medium Internal Control Deficiency made by their company, this suggests that there are identifiable weaknesses or gaps in the organization's internal control system that need to be addressed to ensure effective risk management and safeguarding of assets.
 16. Results indicate that respondents perceive that their company's financial performance is medium. This indicate that the company is achieving satisfactory results, but there may be room for improvement in certain areas to enhance financial stability, profitability, and overall success.

17. The study result that there is a significant negative impact of control design on financial performance.
18. The study result that there is a significant negative impact of operation deficiency on financial performance.
19. The study result that there is a significant negative impact of control environment deficiency on financial performance, A control environment deficiency refers to weaknesses or gaps in the overall control culture, including factors such as management commitment, ethical values, accountability, and communication.
20. The study's result indicating a significant negative impact of control activities deficiency on financial performance highlights the critical role that control activities play in safeguarding assets, mitigating risks, and ensuring efficient operations within an organization. Control activities refer to the specific policies, procedures, and practices implemented to achieve control objectives
21. The study's result indicating a significant negative impact of risk assessment deficiency on financial performance emphasizes the importance of robust risk assessment processes within an organization. Risk assessment is a systematic process of identifying, analyzing, and evaluating risks to determine their potential impact and likelihood.
22. The study's result indicating a significant negative impact of information and communication deficiency on financial performance highlights the crucial role that effective information and communication systems play within an organization. Information and communication deficiencies refer to weaknesses in the processes, systems, and practices related to the timely and accurate flow of information.

5.2 Recommendations

1. Organizations should prioritize ongoing monitoring and evaluation of their internal control systems to ensure that they remain relevant and effective in a constantly evolving business environment. This includes regular reviews of control procedures, periodic risk assessments, and continuous training and communication to promote a strong control culture throughout the organization.
2. Organizations should invest in training and education programs to ensure that employees have the necessary knowledge and skills to effectively execute internal control procedures. This can help foster a strong control culture and ensure that employees understand the importance of adhering to control measures.
3. Organizations should emphasize the importance of competence and ongoing training for employees. By providing adequate training and development opportunities, employees can enhance their knowledge and skills related to control procedures, risk management, and compliance requirements. This helps to create a workforce that is equipped to understand and implement effective internal controls.
4. Organizations should establish a systematic and consistent approach to assess and evaluate risks. This involves gathering relevant information, analyzing potential impacts and likelihoods, and determining appropriate risk responses. This process should be periodically reviewed and updated to ensure its effectiveness and relevance.
5. Organizations should consider the use of technology and digital tools to facilitate information sharing and communication. This can include implementing collaborative platforms, intranets, or communication software that enable real-time sharing of information and effective collaboration among employees.
6. organizations should establish a reporting and feedback mechanism to communicate monitoring results and findings to relevant stakeholders. This can include providing management with timely and comprehensive reports, highlighting areas of concern, and recommending corrective actions to address identified deficiencies.

7. Organizations should prioritize and address the most critical control deficiencies. This may involve implementing new control procedures, enhancing existing controls, or redesigning processes to mitigate risks effectively.

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Appendix

Questionnaire

Dear sister and brother:

I note that this questionnaire aims to identify your opinion for the questions asked to obtain data related to a study entitled "**The Impact of the Internal Control Deficiency on The Financial Performance of the Palestinian listed companies**". It will be used as research supplementary master's degree in accounting from AL- Quds University.

Kindly answer the questions carefully, since the validity of the results of this research depends primarily on the accuracy of your choice, note that there is no correct or wrong answer. We would like to point out that the information provided would be treated confidentially, and will be used for research purposes only.

Guidelines:

1. Please read the question carefully and put "√" towards the choice expresses your opinion.
2. Please fill the questionnaire without leaving any item unanswered.

Best regards

Write or tick (✓) the appropriate response to each of the question

1. Your job title

- Director of the Internal Control Department
- Internal audit manager
- Compliance Department Manager
- Risk Department Manager
- Anti-money laundering manager

2. Legal form of the company

- partnership
- corporate listed in Palestine exchange
- corporate not listed in Palestine exchange
- limited liability company

3. How frequent does, your company review its internal control systems?

- Every Five years
- Annually
- Semiannually
- When need arise

4. Sector of the company

- constructions
- manufacturing
- commerce

- Please state the presence of internal control statements in the section below
- The design of Internal control over financial reporting

| No. | Statement | yes | No | Not Applicable |
|-----|--|-----|----|----------------|
| 1. | Existing controls are not properly designed. Thus, the financial reporting risks may not be addressed. | | | |
| 2. | Control is missing in my company | | | |
| 3. | The control is well designed but not properly applied. | | | |
| 4. | Duties are not clearly defined among the employees. | | | |
| 5. | Job description for the employees is clear and obvious. | | | |

- Operation of Internal control over financial reporting

| No. | Statement | yes | no | Not Applicable |
|-----|--|-----|----|----------------|
| 1. | Current controls are not operated as designed | | | |
| 2. | The person performing the control does not possess the necessary authority to perform the control effectively. | | | |
| 3. | The person performing the control does not possess the necessary competence to perform the control effectively | | | |

• **Control Environment over financial reporting**

| No. | Statement | yes | no | Not Applicable |
|-----|---|-----|----|----------------|
| 1. | There is ineffective internal auditing in the company | | | |
| 2. | Staff of internal control do not understand their responsibilities very well | | | |
| 3. | Employees does not commit to the policies and procedures of the comp. | | | |
| 4. | improper actions are carried out to correct errors in operations of the finance management system | | | |
| 5. | Management shows low level of integrity in accomplishment of its roles | | | |
| 6. | Ethical values are ignored in the decisions of the management | | | |
| 7. | There is an unclear separation between the senior executive management and the board of the director in my bank | | | |

• **Control Activities over financial reporting**

| No. | Statement | yes | no | Not Applicable |
|-----|---|-----|----|----------------|
| 1. | Insufficient number staffing (number of employees in internal control | | | |

| No. | Statement | yes | no | Not Applicable |
|-----|--|-----|----|-------------------|
| | department) | | | |
| 2. | Improper measures are adopted to correct errors in operation of the accounting management system in the company. | | | |
| 3. | My company has inadequate procedures to register it`s assets and properties | | | |
| 4. | The management has improper employment policy | | | |
| 5. | Actions of control is not performed to identify weaknesses | | | |
| 6. | My company has a poor-designed chart of account | | | |
| 7. | My company has inefficient security system to identify and safeguard assets and properties | | | |

• **Risk Assessment over financial reporting**

| No. | Statement | Yes | No | Not Applicable |
|-----|---|-----|----|-------------------|
| 1. | Inadequate strategies of fraud detection | | | |
| 2. | My company rarely carries out documents verification that decrease risk | | | |
| 3. | My company does not have definite proper objectives | | | |
| 4. | My company has an unclear standard for specification of which risks to the company are most significant and | | | |

| No. | Statement | Yes | No | Not Applicable |
|-----|---|-----|----|----------------|
| | critical | | | |
| 5. | The company strategic plans do not match its objectives. | | | |
| 6. | The company does not have alternative plans for any unexpected changes that might influence the bank`s activities | | | |

• **Information and Communication over financial reporting**

| No. | Statement | Yes | No | Not Applicable |
|-----|---|-----|----|----------------|
| 1. | My management does not have specified staff who are in charge of coordinating the different activities in the company to confirm proper communication on internal controls. | | | |
| 2. | There is unclear awareness of the significance of internal controls, including the segregation of duties | | | |
| 3. | The information is not recorded and disclosed to all stakeholders` timeliness. | | | |
| 4. | There is a lack of consistency between the preparation, development and review of the information and strategic plans | | | |
| 5. | The management does not pass the information to its employees clearly and smoothly | | | |
| 6. | The company does not communicate with | | | |

| No. | Statement | Yes | No | Not Applicable |
|-----|--|-----|----|----------------|
| | external parties that might influence the internal control function. | | | |

- **Monitoring deficiencies over financial reporting**

| No. | Statement | Yes | No | Not Applicable |
|-----|--|-----|----|----------------|
| 1. | There is no clear process investigation of controls activities on constant basis. | | | |
| 2. | Irregular internal control implementation reviews | | | |
| 3. | Management has not assigned responsibilities for the timely review of audit reports | | | |
| 4. | There are improper mechanisms put in place to monitor the quality of internal control structure in the company over time | | | |
| 5. | The company has no box for complaints from clients which are handled seriously | | | |

- **Financial Performance**

| No. | Statement | Yes | No | Not Applicable |
|-----|---|-----|----|----------------|
| 1. | The fees charged by our institution are appropriate to cover the running costs | | | |
| 2. | Problems of outstanding cheques are solved in time to reconcile the company balance of an account and book balance of the customer. | | | |
| 3. | Financial performance is the measurement of | | | |

| No. | Statement | Yes | No | Not Applicable |
|------------|--|------------|-----------|---------------------------|
| | the results of a firm's Policies and operations in monetary terms. | | | |
| 4. | Our company has enough cash to meet its obligations effectively (as and when they fall due | | | |
| 5. | Our company's asset base has greatly increased over time | | | |