
Effect of Internal Control on Financial Performance of Savings and Credit Cooperative Societies (SACCOS) in Tanzania: A Case of Nyamagana District, Mwanza Region

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Abstract

This study examined the Effect of Internal Control on Financial Performance of Savings and Credit Cooperative Societies (SACCOS) in Nyamagana District, Mwanza Region, Tanzania. The study employed a quantitative approach using an explanatory cross-sectional research design guided by Agency Theory. A census of 150 respondents was drawn from ten financial SACCOS operating in Nyamagana District, including managers, accountants, loan officers, board members, and supervisory committee members. Data were collected using structured Likert-scale questionnaires and supported by audited financial statements. The reliability of the research instrument was confirmed using Cronbach's Alpha coefficient above 0.85. Data were analyzed using descriptive statistics, Pearson correlation, and Ordinary Least Squares (OLS) regression, with diagnostic tests conducted to ensure normality, multicollinearity, heteroscedasticity, and autocorrelation assumptions were satisfied. The findings revealed that risk management practices have a positive and statistically significant effect on the financial performance of SACCOS. Institutions with well-established risk identification, assessment, monitoring, and mitigation mechanisms demonstrated higher profitability, improved liquidity, and stronger loan repayment performance. The study concludes that effective risk management enhances financial sustainability in SACCOS. It recommends strengthening enterprise-wide risk management frameworks, improving credit risk monitoring, and aligning risk policies with regulatory requirements. Strengthening risk management systems can enhance the stability of SACCOS, safeguard members' savings, and promote financial inclusion in Tanzania.

Keywords: risk management; financial performance; saccos; internal control systems; agency theory.

1.0 Introduction

1.1 Introduce the Problem

Internal control systems are essential mechanisms for ensuring accountability, safeguarding organizational assets, and improving financial performance in financial institutions. Globally, strong internal control frameworks have been associated with improved financial stability and organizational performance. For example, the implementation of the Sarbanes–Oxley Act in the United States significantly strengthened corporate internal control systems and contributed to a reduction of nearly 30% in financial restatements between 2010 and 2022 (U.S. Securities and Exchange Commission [SEC], 2023). Similarly, financial institutions in Europe with robust control frameworks reported approximately 20% higher return on equity compared to institutions with weaker control systems (Deloitte, 2021). These findings demonstrate that internal controls are not only regulatory requirements but also important drivers of financial performance.

In developing countries, internal control systems are particularly important due to weaker institutional structures and limited regulatory oversight. Cooperative financial institutions such as Savings and Credit Cooperative Societies (SACCOS) often face operational risks associated with weak governance and ineffective monitoring mechanisms. Studies show that more than 60% of SACCOS failures in developing economies are linked to weak internal control structures (Mugambi&Kihoro, 2021). Similarly, evidence from India indicates that cooperative institutions with strong internal control systems tend to achieve better asset quality and higher profitability than those with inadequate control mechanisms (Reserve Bank of India, 2022).

In Tanzania, SACCOS play a vital role in promoting financial inclusion by mobilizing savings and providing credit to low-income households, small-scale entrepreneurs, and farmers. They account for approximately 15% of national savings and serve more than 10 million members (Tanzania Cooperative Development Report, 2023). However, despite their importance, many SACCOS continue to experience financial performance challenges associated with weak internal control systems, including poor risk management, ineffective audit functions, and weak governance structures (TMRA, 2023).

At the district level, Nyamagana District in Mwanza Region has experienced similar challenges. Reports from the Mwanza Regional Cooperative Office (2024) indicate that more than 45% of SACCOS in the district face recurring internal control weaknesses, contributing to declining profitability, rising loan arrears, and increasing cases of financial mismanagement. These challenges highlight the need to examine how internal control systems influence the financial performance of SACCOS within the local context.

1.2 Explore Importance of the Problem

The need to examine internal control systems in SACCOS is driven by both theoretical and practical considerations. From a theoretical perspective, internal control mechanisms are closely linked to governance theories such as Agency Theory, which emphasizes the importance of monitoring and accountability mechanisms in reducing opportunistic behavior and ensuring

effective management of organizational resources. Weak internal controls increase the risk of mismanagement and fraud, ultimately affecting financial performance and organizational sustainability.

From a practical standpoint, the effectiveness of internal control systems is essential for safeguarding member savings, maintaining institutional credibility, and ensuring the long-term sustainability of cooperative financial institutions. In Tanzania, SACCOS serve as a major channel for delivering financial services to populations that are often excluded from formal banking systems. Consequently, weaknesses in internal control systems not only affect the financial performance of individual institutions but also undermine public trust in cooperative financial structures.

Furthermore, despite the introduction of regulatory reforms such as the Microfinance Act of 2018 and the establishment of the Tanzania Microfinance Regulatory Authority (TMRA), internal control challenges remain prevalent among SACCOS, particularly at the district level. These challenges highlight the need for empirical research that examines the effectiveness of internal control practices within specific operational contexts. Addressing this issue is therefore important for improving governance, enhancing financial sustainability, and strengthening financial inclusion efforts in Tanzania.

1.3 Describe Relevant Scholarship

A growing body of literature highlights the importance of internal control systems in improving the financial performance of Savings and Credit Cooperative Societies (SACCOS). In cooperative financial institutions, internal control mechanisms such as risk management, control activities, and information and communication systems are considered essential for safeguarding assets, ensuring accountability, and enhancing financial sustainability. These mechanisms help SACCOS manage operational risks, strengthen governance structures, and maintain trust among members.

One major area of scholarship focuses on the role of risk management in influencing SACCOS performance. Risk management involves identifying, assessing, and mitigating risks such as loan defaults, liquidity shortages, and operational failures. Empirical studies generally suggest that effective risk management improves financial performance. For example, Mosioma and Amenyia (2025) found that risk identification, monitoring, and mitigation significantly improved SACCO financial performance. Similarly, Mutunga (2025) reported a positive relationship between risk management practices and financial performance in SACCOS. Other studies, such as Etenyi, Nelima, and Maingi (2024), also demonstrate that effective credit-risk management practices contribute to improved financial outcomes. However, many of these studies rely heavily on perception-based data and limited samples, which may reduce the robustness and generalizability of their findings.

Another stream of research examines the influence of control activities on financial performance. Control activities refer to internal procedures such as authorization of transactions, segregation

of duties, internal audits, and adherence to financial policies. These mechanisms help prevent fraud, reduce operational errors, and improve institutional accountability. Empirical findings generally show a positive relationship between control activities and financial performance. For instance, Kung'u (2024) and Iumba and Kazaara (2023) found that effective control activities significantly improved financial performance among SACCOs. However, other studies report mixed results. Yahya (2024), for example, found no significant relationship between control activities and profitability in some SACCOs. These inconsistencies are often linked to methodological limitations such as reliance on cross-sectional survey data and self-reported performance measures.

A third line of research explores the role of information and communication systems in supporting financial performance. Effective information and communication mechanisms ensure that accurate and timely financial information is generated and shared among management, employees, and members, thereby supporting informed decision-making and organizational transparency. Studies such as Yahya (2024) and Waweru (2023) found that strong communication systems and ICT adoption significantly improve SACCO performance. Similarly, Kisinga and Gomera (2024) reported that mobile banking systems positively influence return on assets among SACCOs. Nevertheless, some studies report mixed results due to variations in measurement approaches, small sample sizes, or reliance on perception-based indicators (Wamukota, Musiega, & Alala, 2022).

Overall, the existing literature suggests that internal control components—particularly risk management, control activities, and information and communication—are important determinants of financial performance in SACCOS. However, many studies rely primarily on perception-based surveys and limited outcome verification, which may inflate estimated effects and limit the reliability of findings. This study therefore extends previous research by combining survey evidence with audited financial indicators to examine how internal control components influence the financial performance of SACCOS in Nyamagana District, Tanzania.

1.4 State Hypotheses and Their Correspondence to Research Design

Building on the theoretical and empirical foundations discussed above, this study examined the effect of internal control systems on the financial performance of SACCOS. The research was grounded in the objectivist research philosophy associated with the positivist paradigm, which emphasizes the use of empirical evidence and statistical analysis to identify relationships between observable variables (Bell, Bryman, & Harley, 2022; Saunders, Lewis, & Thornhill, 2023). Within this framework, internal control practices and financial performance were treated as measurable constructs that could be analyzed quantitatively.

Guided by the COSO internal control framework, the study focused on three key internal control components: risk management, control activities, and information and communication systems. Previous studies suggest that these components play a significant role in strengthening governance structures, improving financial reporting reliability, and reducing operational risks in financial institutions.

Based on these theoretical insights and prior empirical evidence, the study tested the following hypotheses:

H1: Risk management practices have a significant effect on the financial performance of SACCOS in Nyamagana District.

H2: Control activities have a significant effect on the financial performance of SACCOS in Nyamagana District.

H3: Information and communication systems have a significant effect on the financial performance of SACCOS in Nyamagana District.

To test these hypotheses, the study adopted a quantitative research approach using an explanatory cross-sectional research design. This design allowed the researcher to examine relationships between internal control components and financial performance without manipulating the research environment. Data were collected once from respondents involved in the governance and management of SACCOS, including managers, accountants, loan officers, board members, and supervisory committee members. The study employed structured questionnaires and analyzed the data using statistical techniques such as descriptive statistics, Pearson correlation, and multiple regression analysis using Ordinary Least Squares (OLS). This approach enabled the estimation of the net effect of each internal control component on the financial performance of SACCOS in Nyamagana District.

2. Method

The Method section describes how the study was conducted, including the participants, sampling procedures, research design, measurement approaches, and statistical techniques used in data analysis. Providing a clear description of these procedures enables readers to evaluate the reliability and validity of the findings and allows other researchers to replicate the study.

2.1 Identify Subsections

This section is organized into subsections that describe the participants, sampling procedures, measures used to collect data, and the research design adopted in the study. These subsections provide the essential information required to understand how the research was implemented and how the variables were operationalized and analyzed.

2.2 Participant (Subject) Characteristics

The participants in this study were individuals involved in the governance and management of Savings and Credit Cooperative Societies (SACCOS) in Nyamagana District, Mwanza Region, Tanzania. The study targeted key stakeholders responsible for internal control implementation and oversight, including managers, accountants, loan officers, board members, and supervisory committee members.

A total of 150 respondents participated in the study. Board members constituted the majority of participants (53.3%), followed by supervisory committee members (26.7%), while managers,

accountants, and loan officers each accounted for 6.7% of the respondents. The inclusion of both governance and operational personnel ensured that the study captured perspectives from individuals responsible for policy oversight as well as those involved in day-to-day financial management.

Most respondents possessed sufficient professional experience within SACCOS operations. The largest group (35.3%) had between one and three years of experience, followed by 30.7% with four to six years of experience, and 20% with more than seven years of experience. In terms of education, the majority held tertiary qualifications, including diplomas (37.3%) and bachelor's degrees (33.3%), while smaller proportions held certificates (21.3%) or postgraduate qualifications (8%). These characteristics indicate that respondents had adequate knowledge and experience to provide informed insights into internal control practices and financial performance.

2.3 Sampling Procedures

The study employed a census sampling approach, whereby all 150 eligible respondents from ten financial SACCOS in Nyamagana District were included in the study. This approach was adopted because the target population was relatively small and manageable. Using a census eliminated sampling error and ensured that all relevant perspectives from governance and management personnel were captured.

Data were collected through face-to-face administration of structured questionnaires, which ensured clarity of questions and completeness of responses. All 150 questionnaires distributed were returned, resulting in a 100% response rate, which is considered excellent according to Kothari and Garg (2014). The high response rate enhanced the reliability and representativeness of the data used in the analysis.

2.3.1 Sample Size, Power, and Precision

The final sample consisted of 150 respondents, representing the entire population of eligible participants within the selected SACCOS. Because the study employed a census design, the achieved sample was identical to the target population frame, ensuring high precision and minimizing sampling bias. Consequently, conclusions drawn from the analysis reflect the characteristics of the defined population of SACCOS officials in Nyamagana District.

2.3.2 Measures and Covariates

Data were collected using a structured questionnaire containing Likert-scale items measuring internal control practices and financial performance indicators. The questionnaire consisted of three main constructs representing internal control components: risk management, control activities, and information and communication systems. Each construct included multiple indicators measured on a five-point Likert scale ranging from 1 (Strongly Disagree) to 5 (Strongly Agree).

Reliability of the measurement instrument was assessed using Cronbach's Alpha, which evaluates internal consistency among questionnaire items. The results indicated strong reliability for all constructs: risk management ($\alpha = 0.851$), control activities ($\alpha = 0.872$), and information and communication ($\alpha = 0.904$). The overall reliability coefficient for the questionnaire was 0.799, exceeding the commonly accepted threshold of 0.70.

Secondary data were also collected from audited financial statements and management reports, including indicators such as return on assets, profitability ratios, loan repayment rates, and liquidity measures. These data were used to construct a composite Financial Performance Index for the SACCOS.

2.3.3 Research Design

The study adopted a quantitative explanatory cross-sectional research design. This design was appropriate because it enabled the researcher to examine relationships between internal control components and financial performance without manipulating the research environment. Data were collected at a single point in time from respondents across multiple SACCOS.

The research design allowed the study to analyze natural variations in internal control practices among SACCOS and assess their association with financial performance indicators.

2.3.4 Model Specification

The relationship between internal control components and financial performance was estimated using the following regression model:

$$Y = \beta_0 + \beta_1 X_1 + \beta_2 X_2 + \beta_3 X_3 + \varepsilon$$

Where Y denoted financial performance, X_1 , X_2 , and X_3 represented the independent variables risk management, control activities, and information and communication, respectively, β_0 is the intercept, β_1 – β_3 were the regression coefficients, and ε was the error term.

3 Results

3.1 Participant Recruitment and Flow

Participants were recruited from selected Savings and Credit Cooperative Societies (SACCOS) in Nyamagana District, Mwanza Region. The study involved managers, accountants, loan officers, board members, and supervisory committee members because these respondents were directly involved in implementing, monitoring, or overseeing internal controls. A total of 150 questionnaires were administered through face-to-face contact with the respondents, and all were completed and returned, producing a response rate of 100%. Consequently, all 150 responses were included in the final analysis, with no cases excluded because of non-response or incomplete information.

3.2 Respondents' Characteristics

Board members constituted the largest proportion of respondents (53.3%), followed by supervisory committee members (26.7%). Managers, accountants, and loan officers each represented 6.7% of the sample. Regarding experience, 35.3% of respondents had worked in SACCOS for one to three years, 30.7% had four to six years of experience, 20.0% had seven years or more, and 14.0% had less than one year of experience. In terms of academic qualifications, 37.3% held diplomas, 33.3% held bachelor's degrees, 21.3% held certificates, and 8.0% possessed postgraduate qualifications. The sample therefore combined governance and operational perspectives and predominantly comprised respondents with relevant institutional experience and tertiary education.

3.3 Statistics and Data Analysis

Data were analysed using descriptive statistics, Pearson correlation analysis, diagnostic testing, and Ordinary Least Squares regression. Descriptive statistics included means, standard deviations, minimum values, and maximum values. Pearson correlation coefficients were used to examine the strength and direction of relationships between internal control components and financial performance. Multiple regression analysis was then employed to determine the individual and combined effects of risk management, control activities, and information and communication on financial performance. Before estimating the regression model, the assumptions of multicollinearity, normality, linearity, homoscedasticity, and independence of residuals were assessed.

The measurement instrument demonstrated acceptable internal consistency. Risk management recorded a Cronbach's alpha coefficient of .851, control activities recorded .872, and information and communication recorded .904. The overall reliability coefficient for the instrument was .799. All coefficients exceeded the recommended minimum value of .70, indicating that the measurement scales were sufficiently reliable for the main analysis.

The Financial Performance Index recorded a mean of 3.18 (SD = 0.67), indicating a moderate level of financial performance among the sampled SACCOS. Risk-management indicators recorded means ranging from 3.81 to 3.87, suggesting a generally high level of implementation. Regular risk assessment received the highest mean (M = 3.87, SD = 0.61), while the ability of risk-management practices to minimise financial losses received the lowest mean (M = 3.81, SD = 0.54).

Control-activity indicators also demonstrated high implementation, with mean scores ranging from 3.76 to 3.89. Regular internal audits recorded the highest score (M = 3.89, SD = 0.58), whereas segregation of duties recorded the lowest score (M = 3.76, SD = 0.61). Although segregation of duties was positively assessed, its comparatively lower score may reflect staffing limitations in some SACCOS.

Information and communication indicators recorded mean scores ranging from 3.68 to 3.73. Communication between departments achieved the highest mean ($M = 3.73$, $SD = 0.64$), followed by communication of financial status to members ($M = 3.71$, $SD = 0.62$). Timely and accurate financial reporting received the lowest mean ($M = 3.68$, $SD = 0.62$), indicating that reporting quality and timeliness remained areas requiring further improvement.

3.4 Correlation Analysis

Pearson correlation analysis showed that all three internal control components were positively related to financial performance. Control activities had the strongest relationship with financial performance ($r = .560$), followed by risk management ($r = .422$) and information and communication ($r = .421$). These findings indicate that stronger internal control practices were associated with better financial performance, with control activities demonstrating the strongest association.

Correlations among the independent variables were negligible. Risk management was weakly and negatively correlated with control activities ($r = -.050$) and information and communication ($r = -.018$), while control activities were weakly and negatively correlated with information and communication ($r = -.067$). These small correlations suggest that the three internal control components represented distinct aspects of the SACCOS' internal control systems.

3.5 Diagnostic and Ancillary Analyses

The Variance Inflation Factor values ranged from 1.003 to 1.007, demonstrating that multicollinearity was not present. The Shapiro–Wilk test indicated that the residuals did not significantly deviate from normality ($W = .991$, $p = .442$). Inspection of the residual scatterplot showed that residuals were randomly distributed around zero, supporting the assumption of linearity. The Breusch–Pagan test was nonsignificant, indicating constant residual variance, $\chi^2 = 2.550$, $p = .466$. The Durbin–Watson statistic of 1.921 was close to the expected value of 2, suggesting that the residuals were independent. Therefore, the relevant assumptions underlying the regression analysis were adequately satisfied.

3.6 Regression Results

The regression model was statistically significant, $F(3, 146) = 136.04$, $p < .001$. The internal control variables collectively explained 73.65% of the variation in financial performance ($R^2 = .737$, adjusted $R^2 = .731$), demonstrating that the model had substantial explanatory power.

Control activities produced the largest positive effect on financial performance ($B = 0.820$, $SE = 0.102$, $t = 8.038$, $p < .001$). Holding the other variables constant, a one-unit improvement in control activities was associated with a 0.820-unit increase in financial performance. Risk management also had a positive and statistically significant effect ($B = 0.634$, $SE = 0.091$, $t = 6.960$, $p < .001$), while information and communication had a positive and statistically significant effect ($B = 0.570$, $SE = 0.084$, $t = 6.736$, $p < .001$). Thus, the results supported all three study hypotheses, although the magnitude of the effects differed across the predictors.

Table 1. Effect of internal controls on financial performance

Predictor	B	SE	t	p
Risk management	0.634	0.091	6.960	<.001
Control activities	0.820	0.102	8.038	<.001
Information and communication	0.570	0.084	6.736	<.001
Constant	-4.500	1.211	-3.716	.026

Note. N = 150. Dependent variable: Financial Performance Index. $R^2 = .737$; adjusted $R^2 = .731$; $F(3, 146) = 136.04$, $p < .001$. B represents the unstandardized regression coefficient.

The study was explanatory and cross-sectional rather than experimental. Consequently, intervention fidelity, intention-to-treat analysis, group crossover, and adverse events were not applicable.

4 Discussion

The findings support all three hypotheses by demonstrating that risk management, control activities, and information and communication positively influence the financial performance of SACCOS in Nyamagana District. However, the strength of their contributions differed, with control activities emerging as the most influential component, followed by risk management and information and communication. The findings therefore suggest that internal control components complement one another but do not contribute equally to SACCOS' financial outcomes.

The positive influence of risk management shows that SACCOS perform better when they systematically identify, assess, monitor, and mitigate credit, liquidity, operational, and compliance risks. Effective risk management enables a SACCOS to detect potential threats before they develop into loan defaults, liquidity shortages, or operational losses. This interpretation is consistent with Nyamongo and Temesgen (2022), Mugisha et al. (2023), and Tirivangasi and Chikozho (2021), who associated structured risk-management systems with improved asset quality, financial sustainability, and institutional resilience. The similarity across these studies suggests that risk management is not merely a compliance requirement but an important mechanism through which cooperatives protect members' resources and maintain financial stability.

This finding is also consistent with Agency Theory. SACCOS members entrust managers and elected leaders with the management of their contributions, although members may not possess the same information as those responsible for daily operations. This separation can create opportunities for imprudent lending, weak loan follow-up, and inappropriate liquidity decisions. Regular risk assessment, credit appraisal, portfolio monitoring, and early-warning mechanisms reduce managerial discretion and help align operational decisions with members' financial interests. Risk management therefore contributes to performance by limiting agency problems and reducing exposure to avoidable losses.

Control activities had the strongest influence on financial performance, highlighting the importance of transaction authorization, documentation, reconciliation, internal auditing, and segregation of duties. These practices establish clear responsibilities and reduce opportunities for errors, fraud, and misuse of funds. The finding agrees with Asiimwe and Kabuye (2021), Muturi and Njeru (2022), and Kisaka and Ndede (2020), who found that effective control procedures improve accountability, transaction accuracy, and profitability in cooperative financial institutions. The consistency of these findings indicates that strong financial performance depends not only on the existence of internal-control policies but also on their routine enforcement.

From the perspective of Agency Theory, control activities operate as direct monitoring mechanisms. Transaction approval, documentation, segregation of duties, and internal auditing limit the ability of managers or committee members to use institutional resources for personal benefit. They also make financial decisions traceable and open to review. The comparatively weaker assessment of segregation of duties nevertheless indicates a practical difficulty faced by some SACCOS. Limited staffing may require one employee to perform several incompatible functions, increasing exposure to errors or misuse of resources. SACCOS should therefore strengthen compensating controls, such as supervisory reviews and more frequent reconciliations, when complete separation of duties is not financially feasible.

Information and communication also contributed positively to financial performance. Timely reporting and effective communication allow boards, managers, supervisory committees, members, and regulators to identify financial problems and make informed decisions. The finding is consistent with Nabukeera and Bananuka (2020), Muriithi and Mwangi (2021), and Okello and Ainomugisha (2023), who linked ICT-supported reporting and transparent communication with financial-management efficiency, loan recovery, and member confidence. Reliable information flows can improve performance by reducing delays in loan monitoring, facilitating corrective action, and strengthening trust between members and those responsible for managing the SACCOS.

This result further supports Agency Theory because effective communication reduces information asymmetry between members and management. When accurate financial information is regularly communicated, members and governance bodies are better positioned to evaluate managerial decisions and demand accountability. Nevertheless, financial-reporting timeliness and ICT utilisation received relatively lower assessments than some other internal-control indicators. This suggests that inadequate digital infrastructure, limited technical capacity, or delays in preparing reports may prevent some SACCOS from obtaining the full benefits of information and communication systems.

Although the three internal control components were strongly associated with financial performance, their relationships with one another were negligible. This indicates that strong performance in one internal control area does not automatically mean that the remaining areas are equally developed. A SACCOS may conduct regular audits while maintaining weak risk-

assessment procedures or may have effective communication systems without sufficient segregation of duties. Consequently, improvement programmes should adopt an integrated approach that strengthens all internal control components instead of concentrating exclusively on the strongest component.

The findings should be interpreted in light of the study's limitations. The cross-sectional design measured internal controls and financial performance at one point in time and therefore limits definitive causal conclusions. The study also relied on respondents' perceptions, creating a possibility of social-desirability and common-method bias, particularly because individuals involved in managing or overseeing SACCOS evaluated their own institutions. Furthermore, board and supervisory committee members constituted most of the sample, while professional operational employees were less represented. The findings may therefore reflect governance-level perceptions more strongly than daily operational experiences. The study was also restricted to SACCOS in Nyamagana District, meaning that differences in regulation, membership, technology, staffing, and economic conditions should be considered before generalising the findings to all SACCOS in Tanzania.

Despite these limitations, the study demonstrates that internal control systems are important institutional capabilities for improving SACCOS' financial performance. The particularly strong contribution of control activities shows that financial policies generate value when they are supported by effective authorization, documentation, auditing, and accountability procedures. Risk management protects the institution against financial shocks, while information and communication support transparency and informed decision-making. Taken together, the findings confirm the relevance of Agency Theory and demonstrate that reducing information asymmetry, restricting inappropriate managerial discretion, and strengthening oversight can contribute meaningfully to the financial sustainability of member-owned financial institutions.

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