

**IMPACT OF INTERNAL CONTROL SYSTEM ON FINANCIAL
PERFORMANCE OF SMALL AND MEDIUM SCALE
ENTERPRISES IN COLOMBO DISTRICT**

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ABSTRACT

The objective of this study is to find the internal control system practices among small and medium scale enterprises in Colombo district. Further, it finding out the impact of internal control system on financial performance of small and medium scale organization in Colombo district. The SME sector has become a crucial segment and a major section of private sector in developing countries. Therefore, for the developing countries, it is important to accelerate the growth of small and medium enterprises in order to gain sustainable development. However poor practices of internal control system leads to failure of the business, poor financial activities, lower attainment of the entity's goal objective and failed to protect organization asset. Therefore this research aim to explore internal control system practices in Colombo district and evaluate whether internal control system have an impact to the financial performance of the business.

Internal controls system was looked at from the perspective of control culture, risk assessment, administration activity, accounting information and communication, and monitoring and evaluation. Primary data was collected from owners of SMEs in Colombo district. There, one hundred owners were selected as sample and questionnaire were issued to them to collect the primary data. Collected data for the study was presented in the form of tables and chart and analyzed using the software Statistical Package of Social Science, version 19.0. The data analysis included the Univariate analysis (descriptive) and Bivariate analysis.

According to the analysis, the finding showed internal control system of SMS is at moderate level (2.84) and also financial performance is at moderate level. However majority of respondent have lower level of internal control practice, and financial performance in Colombo district. There is moderate positive but significant relationship between internal control system and financial performance. As well as the dimensions of internal control system are at moderate level while control culture are major among them. There are moderate but significant relationship between each dimension of internal control system and financial performance (ANPM, AROA and AROI) of SME.

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