

# **The Journal of ARSYM**

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The Journal of ARSYM (JARSYM) is a refereed journal published bi-annually by the Faculty of Business Studies & Finance, Wayamba University of Sri Lanka. The JARSYM aims to disseminate high-quality research findings on various timely topics generated by undergraduate and postgraduate researchers at the Wayamba University of Sri Lanka. Furthermore, it opens up avenues for the undergraduates involved in the industry to share their inventions, state-of-the-art discoveries, and novel ideas. The main philosophy behind the JARSYM is to enhance the research culture within the faculty, thereby within the Wayamba University of Sri Lanka. All research articles submitted are double-blind reviewed before publishing. Views expressed in the research articles are not the views of the Faculty of Business Studies and Finance, Wayamba University of Sri Lanka, or the Editorial Board.

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**Cover Page by:**

Dr. R.M.T.N. Rathnayake  
Lecturer  
Department of Accountancy  
Wayamba University of Sri Lanka

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The Journal of ARSYM (JARSYM) is a refereed bi-annual journal committed to publishing undergraduate research papers of the Faculty of Business Studies and Finance, Wayamba University of Sri Lanka. The JARSYM publishes theoretical and empirical papers spanning all the major research fields in business studies and finance. The JARSYM aims to facilitate and encourage undergraduates by providing a platform to impart and share knowledge in the form of high-quality and unique research papers.

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# Mediating Effect of Internal Control System on the Relationship Between E-accounting and the Financial Performance: Evidence from SME in Colombo District

Munasinghe, M.A.D.P.M.<sup>1</sup>, Jameel, A.L.M.<sup>2</sup>

<sup>1,2</sup>Department of Accountancy & Finance, Faculty of Management Studies, Rajarata University of Sri Lanka

<sup>1</sup>piumi.m1996.pm@gmail.com, <sup>2</sup>mjameel95@gmail.com

## ABSTRACT

The advent of the information technology era radically altered the way accounting processes assist efficient decision-making, forcing businesses to adapt to the new changes to remain competitive. Internal control systems and the effects of financial performance are critical for the success of SMEs. E-accounting must be adopted by SMEs to achieve effectiveness in the internal control system and financial performance. This paper examines the mediator effects of the Internal Control System on the relationship between E-accounting characteristics and the financial performance of SMEs in the Colombo District. E-accounting is classified into four categories: information quality, cost reduction, quick decision making, and ease of use of the software. The research was carried out by conducting a review of existing studies on the topic and related issues. The theories covered are the Technology Acceptance Model (TAM) Theory, Contingency Theory and Stewardship Theory. The primary data was gathered from a sample of 240 respondents such as financial managers, accountants and internal auditors who worked at SMEs in the Colombo district through questionnaires. The Primary data was collected based on a structured questionnaire using the Likert Scale. The hypotheses of the study were tested using the reliability and validity test, descriptive analysis, correlation analysis, multiple regression analysis, and mediating analyses. The study finds a significant positive relationship between information quality, cost reduction, quick decision making, and ease of use of the software on financial performance. Whereas a significant positive relationship between information quality, cost reduction, quick decision making, and ease to use of the software on the Internal Control System. The results of this study indicate that Internal Control was shown to significantly positively mediate the effect of E-accounting on financial performance. Therefore, the study improves the existing literature on the title and will help increase the knowledge of students and scholars who are interested in this area.

**Keywords:** *E-accounting Characteristics, Internal Control System, Financial Performance, Small & Medium Scale Enterprises*

## 1. INTRODUCTION

Accounting plays a critical part in an organization because every company must keep track of financial information. It operates in a rapidly changing environment, and the procedures, policies, standards, rules, and framework of

accounting are often changed. Nowadays, businesses are complex due to the high volume of transactions, competitiveness and global markets. The accounting field also needs to improve to bear the number of transactions of the firm and adopt innovative techniques (Huang & Liu, 2005). According to Huang and Liu (2005), the emergence of Information Technology has enhanced the improvement of the accounting field. Accounting integrated with IT to meet the growing need for accurate and up-to-date information. Business entities must keep track of their financial data in order to link it to their operations (Hla & Teru, 2015). In comparison to manual accounting, e-accounting produces more accurate results and produces more dependable information that is easier to deal with and has a lower risk of error. Furthermore, it encourages quick decision-making, which increases financial performance in SMEs (Nicolau & Bhattacharya, 2006). However, earlier studies highlighted that SMEs face many obstacles which hamper their growth. The lack of a proper information system is the primary factor in SMEs failures (Amoako, 2013; Dabor et al., 2016; Kapurubandara & Lawson, 2009). In Sri Lanka, most SMEs have not succeeded because of the inadequate accounting system and poor accounting practices (Rathnasiri, 2015). The findings demonstrate that SMEs are not using the most up-to-date e-accounting to generate strategic information (Ismail et al., 2003). Internal control is responsible for monitoring accounting data and ensuring that it is relevant and ensures better SMEs Financial Performance. E-accounting is a basic component derived from technologies in general but the main issue is whether applying E-accounting contributes to Financial Performance results. Throughout the literature, several studies have examined the impact of mediating effects of the Internal Control System on the relationship between E-accounting and the performance of SMEs (Soudani, 2013; Alfartoosi & Jusoh, 2020; Alfartoosi et al, 2021; Oden, 2019). Oden, (2019) noted that E-accounting implementation and success have been comprehensively researched but the contemporary literature shows slight evidence of the mediating effect of the Internal Control System relationship between E-accounting and Financial Performance measures. So, in this research author attempts to do a kind of examination based on SMEs in the Colombo district to fill this knowledge gap.

Therefore, the problem statement of this study can also be referred to answer the following;

- How Does the Internal Control System mediate the relationship between E-accounting and the Financial Performance of SMEs in the Colombo District?

In this background, the overall objective of this study is to identify the mediating effect of the Internal Control System on the relationship between E-accounting and Financial Performance. In this connection, the following specific objectives will be focused:

- 1) To examine the relationship between the E-accounting and the Financial Performance of SMEs in the Colombo District.



- 2) To examine the relationship between the E-accounting and the Internal Control System of SMEs in the Colombo District.
- 3) To examine the relationship between the Internal Control System and the Financial Performance of SMEs in the Colombo District.

## **2. LITERATURE REVIEW**

### **2.1. Information Quality and Finance Performance**

Bouwens and Abernethy (2000) stated that the competitiveness of firms can be damaged by incomplete and inaccurate data, as input control and employee competencies are important to the data quality of AIS. Further, the data of inferior quality may cause an opposing effect on decision making and consequently affect firm performance. Information is input for AIS, which is processed to produce information that is needed to make decisions. The quality and effectiveness of E-accounting rely on the input quality, output quality and process. Emeka-Nwokeji (2012) noted that when adapting for e-accounting, one needs to consider the quality of the system and the data quality utilized for the organization's decision-making process. Furthermore, an Information system improvement project requires quality data. Data quality is a critical factor, which is relevant directly to a perceived decrease in time and effort for decision-making and it is significant to provide the quality assurance of the supplied data for enhancing Financial Performance.

### **2.2. Cost Reduction and Finance Performance**

Neogy (2014) pointed out that Cost Reduction is another factor in judging the efficiency of the Accounting Systems of the selected companies. Accounting Systems can lead to cost-effectiveness because efficient Accounting Software helps identify excess costs, and that excess cost can be reduced by the management. They concluded that cost-effectiveness can be measured with the help of operating ratio, and its results give the use of a computerized Accounting Information System allows selected mobile telecommunication companies to perform accounting functions more effectively and efficiently, as the use of computerized Accounting Information System results in significant cost Reduction. Choudhari (2018) noted that the importance of cost reduction techniques on organizational performance in a highly competitive environment is examined in this study. To ensure more profit growth by producing quality goods and services with available resources on the ground, an organization must reduce costs to an acceptable level in terms of control and reduction of wastage and loss. From the findings of this research, it was evident that cost reduction has a positive impact on organizational performance.

### **2.3. Ease to Use and Finance Performance**

Landauer (1996) pointed out that increasing ease of use in the workplace raises several responses from employees, such as "Workers who enjoy their work do it better, stay longer in the face of temptation, and contribute ideas and enthusiasm to the evolution of enhanced productivity". Similarly, Chenhall (2003), noted that the appropriate design of an Accounting Information System supports business strategies in a way that increases organizational performance.

Organizational performance is a function of financial performance management and Accounting Information Systems. The quality of software, which is easy to use and understandable, would be beneficial to its users.

#### **2.4. Fast Decision Making and Finance Performance**

According to Franklin and Krieger (2011), decision-making is an important component in organizational management; decision-making development is viewed as the organization's brain and nerve centre. It defines decision-making as the process of defining the nature of a need, problem, or opportunity, generating alternative solutions, evaluating them, and finally selecting among the available alternatives

#### **2.5. Mediating Effects of ICS on the Relationship between E-accounting Characteristics and Financial Performance**

Soudani (2013) investigated focusing on measuring the Implementation of E-accounting Systems on Financial Performance in the services industry in the United Arab Emirates. The population of the study consisted of all listed companies that have been operating in the United Arab Emirates Stock Market. The researcher constructed the questionnaire to target financial managers, accountants, and internal auditors who worked at these organizations. The study found that there isn't a direct influence between the Internal Control System and financial performance. However, the perceived e-accounting system has a significant impact on Financial Performance through the effects of the internal control system. In addition, the implementation of e-accounting systems on financial performance is highlighted due to the reliability of financial reporting, timely feedback on the achievement of operational goals, and the facilitation of the company's transactions.

Mehdi, Mahmoud and Ebadollah (2015) examined the effect of implementing an Accounting Information System on the efficiency, profitability and productivity of SMEs in Iran. The study employed a descriptive survey research design. Findings from the study revealed that efficient implementation of Accounting Information Systems in SMEs listed on the Tehran Stock Exchange is positively associated with performance, productivity, and profitability. Oden (2021) examined the effect of electronic accounting on an organization's corporate performance. The researcher used both primary and secondary data collection methods for information gathering. Primary data were collected through questionnaire administration, oral interviews, and personal observations. Secondary data were collected through periodicals and journals, textbooks, lecture notebooks, and the Internet. The researcher found that electronic accounting has a significant effect on the accounts receivables of an organization, and electronic accounting has an impact on an organisation's financial reporting.

The researchers note that there are limited published studies (Soudani, 2013; Alfartoosi & Jusoh, 2020; Alfartoosi et al., 2021; Oden, 2019) in the area of the mediating effect of Internal Control System relationship between E-accounting and Financial Performance in Sri Lanka. As well, extant literature reveals mixed results related to research topics. To the researchers' knowledge, there exists a

notable lack of published studies, and results were inconsistent. The theoretical contribution of this study is its theoretical contribution by bridging the above-mentioned gap by providing a wider perspective of the concept. It contributes to the extant local literature and fills the gaps observed.

### 3. METHODOLOGY

#### 3.1 Conceptual Framework

The conceptual framework (Figure 1) for the study has been developed by considering and examining the mediating effects of the internal control system on the relationship between e-accounting and the financial performance of SMEs in the Colombo District.

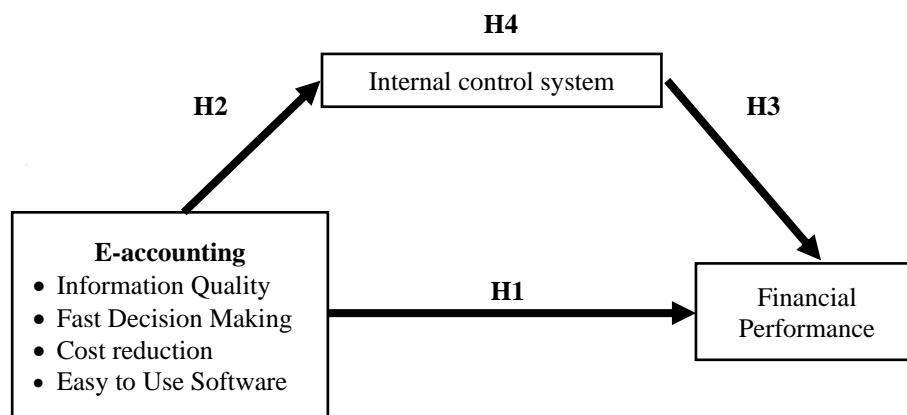


Figure 1: Conceptual Framework

#### 3.2. Population and sample

Assenga, Aly, and Hussainey (2018) stated that the overview of a population from data gathered using any sample is based on probability. To simplify the research findings to the population, it is essential to decide on enough sample size. Sri Lanka has a little over 3,000 SMEs with a turnover of less than Rs.750million (Perera and Samarakoon, 2021). This research selects only SMEs in the Colombo district. A total of 325 SMEs in the Colombo district in the Western Province of Sri Lanka (Perera and Samarakoon, 2021). In the study, the researcher selected a sample of 240 SMEs from the total population by using the simple random sample method. The population of the study consists of employees who employ accounts-related activities (accountants, financial managers and internal auditors) and use e-accounting in carrying out their job responsibilities in SMEs in the Colombo district. So, the unit of analysis of this study is an employee who engages in accounting-related activities by using e-accounting of SMEs in the Colombo district.

#### 3.3. Methods of Data Collection

This study uses primary data to collect data for the study. The questionnaire was developed based on existing literature and previous quantitative studies. It mostly used online surveys and mobile surveys, in particular, which have a very small cost per respondent and paper surveys are also used. A pilot study was

followed for a questionnaire using professionals and academics. Then, the developed questionnaire was given to employees who engaged in accounts-related activities (accountants, financial managers, and internal auditors) and used e-accounting in carrying out their job responsibilities in SMEs in the Colombo district. The questionnaire includes open-ended questions that provide multiple choices. The questionnaire has two sessions, which include general information about the company profile and the evaluation of the mediating effects of the Internal Control System on the relationship between E-accounting characteristics and financial performance. The last part is about the Financial Performance. It uses a Likert scale measure with five categories.

## 4. RESULTS

### 4.1. Validity and reliability

The validity and reliability tests were conducted to ensure the error-free and valid instruments for the study. A factor analysis was used to validate the study variables. Before the analysis, the Kaiser-Meyer-Olkin Measure of Sampling Adequacy and Bartlett's Test of Sphericity were tested. The KMO should be greater than 0.5, and Bartlett's Test of Sphericity should be significant. Table 01 given below shows that the KMO is 0.847 and Bartlett's Test of Sphericity, which is significant at  $p < 0.000$ . Hence, the data used for the study were adequate for further analysis.

**Table 1: KMO and Bartlett's Test results for the independent variable**

<b>KMO and Bartlett's Test (Independent Variable)</b>		
Kaiser-Meyer-Olkin Measure of Sampling Adequacy.		0.847
Bartlett's Test of Sphericity	Approx. Chi-Square	608.305
	df	6
	Sig.	0.000

Source: survey data 2022

According to Table 2, data analysis results in KMO and Bartlett's test value being more than 0.8. As indicated, the sampling is adequate. The dependent variable (FP) KMO coefficient for this dataset fell at a meritorious level of 0.864 (between 0.8-0.9), exceeding the recommended value of 0.6 Kaiser (1970), indicating that the sample is adequate.

**Table 2: KMO and Bartlett's Test results for the dependent variable**

<b>KMO and Bartlett's Test (Dependent variable)</b>		
Kaiser-Meyer-Olkin Measure of Sampling Adequacy.		0.864
Bartlett's Test of Sphericity	Approx. Chi-Square	357.540
	df	15
	Sig.	0.000

Source: survey data 2022

Cronbach's alpha test was conducted in order to confirm the internal consistency of the variables used for the study. Accordingly, in Table 3 Cronbach's alpha values exceed the 0.70 level, showing a high consistency level among the dimensions and the constructs.

**Table 3: Reliability Analysis of E-Accounting**

Variable / Dimensions	No. of Statements	Cronbach's Alpha
E-Accounting	20	0.905
Information Quality	5	0.726
Cost Reduction	5	0.701
Fast Decision Making	5	0.730
Easy to Use	5	0.759
Financial Performance	6	0.758
Internal Control System	9	0.864

Source: survey data 2022

#### 4.2. Descriptive Analysis

Descriptive statistics describe the behaviour of the data. If the data points are close to the mean, indicating that the responses are fairly uniform, the standard deviation will be small. Table 4 shows descriptive statistics of data.

**Table 4: Descriptive Statistics**

	N	Minimum	Maximum	Mean	Std. Deviation
Information Quality	240	1.40	5.00	4.517	0.435
Cost Reduction	240	1.20	5.00	4.387	0.455
Fast Decision Making	240	1.00	5.00	4.444	0.437
Easy to Use	240	1.20	5.00	4.420	0.462
Internal Control System	240	1.11	5.00	4.473	0.450
Financial Performance	240	1.50	5.00	4.460	0.421
Valid N (listwise)	240				

Source: survey data 2022

#### 4.3. Correlation Analysis

Table 5 shows the relationship among the main study variables. Survey data emphasise that analysis, Pearson correlation values indicate that all the independent variables except the variable, the presence of E-Accounting, have a positive relationship with the dependent variable because of their positive Pearson correlation values. According to this analysis, every Pearson correlation value is positive, and every P value is less than 0.01. Therefore, every hypothesis is accepted according to the correlation result. Overall, due to the positive correlation between E-accounting, Financial Performance and Internal Control System. In the analysis, every Pearson correlation value is positive and also every P value is less than 0.01; therefore, every hypothesis is accepted according to the correlation result.

**Table 5: Pearson Correlations among Independent, Dependent and Mediating Variables**

	Information Quality	Cost Reduction	Fast Decision Making	Ease of Use	Internal Control System	Financial Performance	E-accounting
Information Quality	1**						
Cost Reduction	0.705**	1**					
Fast Decision Making	0.636**	0.727**	1**				
Ease of Use	0.669**	0.765**	0.715**	1**			
Internal Control System	0.747**	0.788**	0.741**	0.764*	1**		
Financial Performance	0.680**	0.720**	0.719**	0.745*	0.831**	1**	
E-accounting	0.851**	0.908**	0.871**	0.896*	0.862**	0.812**	1**

Source: survey data 2022

### 4.3. Regression Analysis

#### 4.3.1 Impact of E-accounting on Financial Performance (Step - 1)

##### 4.3.1.1 E-accounting Dimensions on Financial Performance

**Table 6: Model Summary of Regression Model**

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	0.814 <sup>a</sup>	0.663	0.657	0.246

a. Predictors: (Constant), Ease of Use, Information Quality, Fast Decision Making, Cost Reduction

Source: survey data 2022

**Table 7: Coefficients of Regression Model**

Model	Unstandardized Coefficients		Standardized Coefficients	t	Sig.
	B	Std. Error	Beta		
(Constant)	0.612	0.183		3.340	0.001
1 Information Quality	0.194	0.055	0.200	3.546	0.000
Cost Reduction	0.145	0.063	0.157	2.314	0.022
Fast Decision Making	0.250	0.058	0.259	4.329	0.000
Ease of Use	0.278	0.059	0.305	4.741	0.000

Table 6 shows the model summary of simple regression that Adjusted R Square is 0.657 as the correlation coefficient between E-accounting and Finance

Performance. It says that there was a strong positive correlation between ease of use, information quality, fast Decision-making, and cost reduction on financial performance.

Table 7, the significant level is 0.000, which is less than 0.05, showing that this model fits a regression model.

#### 4.3.1.2 E-accounting on Financial Performance

**Table 8: Model Summary of Regression Model**

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	0.812 <sup>a</sup>	0.660	0.659	0.246

a. Predictors: (Constant), Electronic Accounting

Table 8 shows the model summary of simple regression that Adjusted R Square is 0.659 as the correlation coefficient between E-accounting and Finance Performance. It says that there was a strong positive correlation between E-accounting and Finance Performance.

**Table 9: Coefficients of Regression Model**

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	0.613	0.180		3.413	0.001
	E-accounting	0.866	0.040	0.812	21.495	0.000

a. Dependent Variable: Financial Performance

Table 9 indicates that the significant level is 0.000 which is less than 0.05 gives evidence that this model fits a regression model.

#### 4.3.2 Impact of E-accounting on Internal Control System (Step – 2)

##### 4.3.2.1 E-accounting (Independent variable Dimensions) on Internal Control System

**Table 10: Model Summary of Regression Model**

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	0.863 <sup>a</sup>	0.744	0.740	0.229

a. Predictors: (Constant), Easy of Use, Information Quality, Fast Decision Making, Cost Reduction

According to Table 10, the model summary of simple regression shows that Adjusted R Square is 0.740 as the correlation coefficient between ease of Use, Information Quality, Fast decision-making, Cost Reduction and Internal Control System. It says that there is a strong positive correlation between all independent dimensions of the Internal Control System.

According to Table 11, the significant level is 0.000, which is less than 0.05 gives evidence that this model fits a regression model.

**Table 11: Coefficients of Regression Model**

Model	Unstandardized Coefficients		Standardized Coefficients	t	Sig.
	B	Std. Error	Beta		
(Constant)	0.098	0.171		0.573	0.567
Information Quality	0.280	0.051	0.271	5.507	0.000
1 Cost Reduction	0.271	0.058	0.274	4.642	0.000
Fast Decision Making	0.215	0.054	0.209	4.004	0.000
Ease to Use	0.218	0.055	0.224	3.981	0.000

a. Dependent Variable: Internal Control System

Source: survey data 2022

#### 4.3.2.2 E-accounting on Internal Control System

**Table 12: Model Summary of Regression Model**

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	0.862 <sup>a</sup>	0.743	0.742	0.228

a. Predictors: (Constant), E-accounting

(Source: survey data 2022)

According to Table 12, the model summary of simple regression shows that Adjusted R Square is 0.742 as the correlation coefficient between E-accounting. It says that there is a strong positive correlation between E-accounting and Internal Control Systems.

**Table 13: Coefficients of Regression Model**

Model	Unstandardized Coefficients		Standardized Coefficients	t	Sig.
	B	Std. Error	Beta		
1 (Constant)	0.105	0.167		0.629	0.530
E-accounting	0.983	0.037	0.862	26.233	0.000

a. Dependent Variable: Internal Control System

Source: survey data 2022

Table 13, the significant level is 0.000 which is less than 0.05 gives evidence that this model fits a regression model.

#### 4.3.3 Impact of Internal Control System on Finance Performance (Step – 3)

**Table 14: Model Summary of Regression Model**

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	0.831 <sup>a</sup>	0.691	0.689	0.234

a. Predictors: (Constant), Internal Control System

Source: survey data 2022



According to Table 14, the model summary of simple regression shows that Adjusted R Square is 0.689 as the correlation coefficient between the Internal Control System. It says a strong positive correlation exists between the Internal Control System (mediating variable) and Finance Performance.

**Table 15: Coefficients of Regression Model**

Model	Unstandardized Coefficients		Standardized Coefficients	t	Sig.
	B	Std. Error	Beta		
1 (Constant)	0.986	0.151		6.512	0.000
Internal Control System	0.777	0.034	0.831	23.048	0.000

a. Dependent Variable: Financial Performance  
(Source: survey data 2022)

Table 15, the significant level is 0.000, which is less than 0.05 gives evidence that this model fits a regression model.

#### 4.4. Multiple Regression Analysis

Multiple linear regression is an extension of simple linear regression in which there is a single dependent (response) variable (Y) and independent (predictor) variables. In multiple linear regressions, the dependent variable is quantitative while the independent variables may be quantitative or indicator (0,1) variables. The usual purpose of multiple regression analysis is to create a regression equation for predicting the dependent variable from a group of independent variables (Elliott & Woodward, 2016).

##### 4.4.1. Impact of E-accounting and Internal Control System on Financial Performance (Step – 4)

**Table 16: Model Summary of Regression Model**

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	0.852 <sup>a</sup>	0.727	0.724	0.221

a. Predictors: (Constant), Internal Control System, Electronic Accounting  
Source: survey data 2022

According to Table 16, the model summary of simple regression shows that adjusted R Square is 0.724 as the correlation coefficient between E-accounting and Internal Control System with Financial Performance. It says that was a strong positive correlation between E-accounting and Internal Control System on Financial Performance.

Table 17 shows that the  $\beta$  coefficient of E-accounting is 0.399. It is statically significant at 95% of confidence. Because the p-value is 0.000 and less than the selected Alpha value ( $p < 0.05$ ). The  $\beta$  coefficient shows that for every unit of increase in E-accounting, there is an increase in Financial Performance of 0.399 units.

**Table 17: Coefficients of Regression Model**

Model	Unstandardized Coefficients		Standardized Coefficients	t	Sig.
	B	Std. Error	Beta		
(Constant)	0.563	0.162		3.484	0.001
1 Electronic Accounting	0.399	0.071	0.374	5.580	0.000
Internal Control System	0.475	0.063	0.509	7.591	0.000

a. Dependent Variable: Financial Performance

Source: survey data 2022

The  $\beta$  coefficient for the Internal Control System is 0.475. It is statistically significant at 95% of confidence. Because p-value is 0.000 and less than the selected Alpha value ( $p < 0.05$ ). The  $\beta$  coefficient shows that for every unit of increase in the Internal Control System, there is an increase in Financial Performance of 0.475 units.

#### 4.5. Mediation Analysis

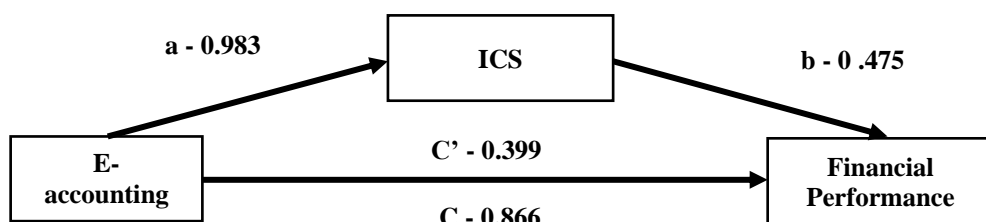
With regard to the mediating effects of the Internal Control System on the relationship between E-accounting and the Financial Performance of SMEs in the Colombo District, Baron and Kenney's (1986) criteria for mediation was used. The results of the mediation analysis by (Baron & Kenny, 1986) regression approach were reported in the following table.

**Table 18: Summary of Regression Models**

Details	Model 1	Model 2	Model 3	Model 4
R	0.812	0.862	0.831	0.852
R Square	0.660	0.743	0.691	0.727
Adjusted R Square	0.659	0.742	0.689	0.724
ANOVA – Sig.	0.000	0.000	0.000	0.000
Constant	0.613	0.105	0.986	0.563
E accounting	0.866	0.983		0.399
Internal Control System			0.777	0.475

Source: survey data 2022

To identify the mediating role of Internal Control System, four models were taken into consideration. According to the above-derived results, it can be concluded that Internal Control System plays a partial mediating role in the connection between E-accounting and Financial Performance from SMEs in Colombo District.



**Figure 2: Coefficient Path**

This model can be conceptualized as a causal model where E-accounting on Financial Performance is mediated by Internal Control System as shown in Figure 2.

Here,

- a - Regression weight on E-accounting Characteristics when predicting Internal Control System.
- b and c' - The regression weights on Internal Control System and E-accounting Characteristics respectively, when both are used together to Financial Performance.
- c - Regression weight on E-accounting Characteristics when predicting Financial Performance.

From these findings, three conditions have been satisfied that are necessary for mediation.

Direct effect - Impact can be measured as the reduction in the regression weight for E-accounting on Financial Performance

$$c - c' = 0.866 - 0.399 = 0.467$$

Indirect Effect - Impact can be calculated as the product of the indirect paths from E-accounting to Financial Performance through the Internal Control System

$$a * b = 0.983 * 0.475 = 0.467$$

Total Impact - equal to the direct impact plus the indirect impact

$$c = c' + a * b$$

$$0.866 = 0.399 + 0.983 * 0.475$$

$$0.866 = 0.399 + 0.467$$

$$0.866 = 0.866$$

**Table 18: Summary of Hypotheses Testing**

Hypotheses	Correlation		Decision	Regression		Decision
	r	p		$\beta$	P	
H1:	0.812**	0.000	Supported	0.866	0.000	Supported
H2:	0.862**	0.000	Supported	0.983	0.000	Supported
H3:	0.831**	0.000	Supported	0.777	0.000	Supported
Hypotheses	Decision Criteria					Decision
H4:	By using the notation of mediation analysis: c- c' = a*b					Accepted
	Here, the difference in the equation is equal to zero as per the decision criteria					
	0.866 - 0.399 = 0.983*0.475					
	0.467 = 0.467					

Source: survey data 2022

Regression analysis was conducted to find the beta value of a, b, c and c'. And the model fits were shown in the appendices.

As the difference is equal to zero as per the decision criteria, it could be concluded that the Internal Control System plays a mediating role. And this study accepted the formulated hypothesis, too. Therefore, the researcher interprets the mediating effects of the Internal Control System on the relationship between E-accounting Characteristics and Financial Performance.

As per the literature, the researcher has mentioned ten hypotheses for all the relationships among the three variables.

## **5. DISCUSSION**

Based on the results presented in Table 4, The findings also show the mediating effects of the Internal Control System on the relationship between E-accounting and the Financial Performance of SMEs in the Colombo District. Through this study, four hypotheses are tested. The findings confirmed the study's four hypotheses. The findings are consistent with the evidence and ideas presented in the review of the literature. Furthermore, this research will shed light on the viability of accounting software in improving the quality of work in SMEs. Through this study, e-accounting has a significant positive impact on Financial Performance and an Internal Control System. Also, there is a significant positive relationship between Internal Control Systems and Financial Performance. In contrast, the current study provides a finer understanding of the positive effect mediating the influence of the Internal Control System on the relationship between E-accounting and the Financial Performance of SMEs in the Colombo District.

## **6. CONCLUSION**

The study was carried out to find out the mediating effects of the Internal Control System on the relationship between E-accounting and the Financial Performance of SMEs in the Colombo District. Through this study, hypotheses are tested. E-accounting has a significant positive impact on Financial Performance and an Internal Control System. Also, significant positive relationship between Internal Control Systems and Financial Performance. In contrast, the current study provides a finer understanding of the positive effect mediating the influence of the Internal Control System on the relationship between E-accounting and the Financial Performance of SMEs in the Colombo District. Existing literature offers evidence of the Effect of E-accounting characteristics and Financial Performance, though it is important to highlight that an in-depth study is required to examine factors that may influence this relationship. Deploying the support of the technology acceptance model (TAM) theory, Contingency Theory and stewardship theory, along with the support from empirical literature, anecdotal evidence and rational arguments, a set of four (4) hypotheses have been developed. The hypotheses are tested based on the collected data from 240 respondents who answered the questionnaire sent through e-mail. The respondents are employees working in SMEs and familiar with accounting

packages in the Colombo district. The collected data is analyzed using multiple regression analysis to test the hypotheses and achieve the objectives. All the dependent, mediating and independent variables chosen for the study have Cronbach's alpha value above 0.7, indicating all variables have high internal consistency and are acceptable. Pearson's coefficient of correlation is used to examine the variables' causal relationship. The descriptive data analysis also confirmed that the majority of respondents believed that the independent variables and dependent variables used in this study had a positive effect on the dependent variable. The following part of this chapter concludes the findings of the study. This study helps the management of businesses to identify the importance of e-accounting and, the necessity to face the ever-changing competitive environment, and how they can contribute to increasing the FP and productivity of their businesses. Therefore, the study improves the existing literature on the title and will help increase the knowledge of students and scholars who are interested in this topic. Furthermore, the study is important to exit and potential SMEs in deciding whether to implement or improve e-accounting. Also, Employees in accounting-related activities may better understand the importance of using accounting software to increase their job effectiveness and business performance. Further, potential investors of SMEs may tend to use accounting software for their business activities.

## **6. LIMITATION AND RESEARCH FUTURE DIRECTION**

In view of the limitations constrained in this study, suggestions can be provided for subsequent studies in the future. So, this study only involved the SMEs in the Colombo District. Furthermore, future research should include other agencies from various industries and compare their performance in e-accounting. The study will generate a result that is more reliable if the research is based on island-wide SMEs. However, according to the time frame, the sample size has been limited to only 240 SMEs in only one geographical area of the Colombo district. It recommends taking a larger sample to confirm the current findings of this research and improve the validity of the study. In addition, the author uses the random sampling method to select the sample, but there are several effective sampling methods other than the random sample method. In this study, only using the survey method of a questionnaire to collect data is also a limitation. In future studies, researchers may employ personal detailed interviews, observations, controlled experiments and focus group discussions to gather more useful data as behavioural finance biases come up with irrational thinking. Moreover, the base research for the topic is very few in Sri Lanka, so the existing knowledge is at a lower level. As the current study aimed to identify the mediating effects of E-accounting on the Financial Performance of SMEs in the Colombo District, only a few factors were highlighted in this study. Some other factors that may influence the impact of e-accounting on the effectiveness of Financial Performance by the system must also be considered in any future study. Also, many factors, such as accounting software security risks, can impact the relationship between e-accounts and internal control systems and, thus, SME

financial performance. As a result, future research should look into the security risks of using E-accounting in SMEs.

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