Management Controls and Small Scale Enterprise’s (SSEs) Profitability in Ogun State, Nigeria

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Abstract: The attainment or otherwise of the primary objective of business, which is profitability, is dependent on the effectiveness of controls inherent in its processes. The most susceptible to the misuse of resources due to lack of controls are the small scale enterprises (SSE). This leads to the death of seven out of every ten SSE established in their first two years. This study examined the effect of management controls of SSEs on their profitability. The use ordinary least square regression was employed in testing the research hypothesis formulated. Survey data was collected through the use of questionnaires. The study observed that internal control system has a positive significant effect on the financial performance of SSEs. The study therefore concludes that the establishment of controls such as preventive, corrective and detective controls forestalls organizations profit from leaks.

Key Words: Management Control, Small Scale Enterprise, Primary Business Objective

1.0 Introduction
The attainment or otherwise of the primary objective of business, which is profitability, is dependent on the effectiveness of controls inherent in its processes. This implies that big and small organizations, profit oriented and non-profit oriented organizations, corporate and informal organizations, schools and religious organization and any institutions that intends to actualize organizational objective(s) must institute an effective means of safeguarding her assets, curbing employee’s excesses and a feedback mechanism that provides reasonable assurance of the resourceful utilization of organizations resources. The described process can simply be called management control or internal controls. According to Treba 2003; Brennan & Soloman, 2008 internal control serves as veritable tool to drive and realize organizational missions and
objectives. In continuance Mawanda (2008), asserts that the establishment and implementation of controls within organizational processes consistently leads to improved financial performance.

However, due to poor reporting structure, absence of organizational hierarchy, neglect of instituted corporate governance codes, employee permissiveness without adequate checks, consistent prevalence of inaccuracy, inability to separate business purse from owners purse and general sloppiness in a business makes SSEs most susceptible to the misuse of resources, thus the lack of management controls becomes obvious and mostly leads to the death of such organization. More specifically, statistics from Small Business Advocacy (2011) states that seven out of 10 new employer firms survive at least the first 2 years, half at least 5 years, a third at least 10 years, and a quarter stay in business 15 years or more various reasons could be adjudged for the death of such small businesses although not mentioned by the institute, this study posits that chief amongst these reasons is control inadequacy. However, several excuses to validate the lack of internal control amongst SSEs such as smallness of the business, fewer hands to manage the business and increase in the running cost of business have been put forward in defense of non-implementation of a functional management control system amongst SSEs (Putra, 2009). Hence, this study seeks to investigate the role of internal control on the financial performance of small scale enterprises in Ogun state Nigeria.

2.0 Literature Review
Management controls are those procedures, policies, rules and regulations established by an enterprise to ensure the efficient utilization of scarce resources on a daily basis. According to The Committee of Sponsoring Organization (COSO, 2013) management control is defined as a process effected by an entity’s board of directors, management and other personnel, designed to provide reasonable assurance regarding the achievement of objectives in the following categories: i. Effectiveness and efficiency of operations. ii. Reliability of financial reporting iii. Compliance with applicable laws and regulations. According to Millichamp, (2002), internal control system is the total system of controls, financial and otherwise, recognized by the management in order to carry on the business of the enterprise in a logical and efficient manner, ensure loyalty to management policies, safeguard the asset and secure as far as possible the completeness and accuracy of the records. Similarly, Izedonmi, (2002) defined internal control as those procedures, rules and regulations established within an enterprise to ensure the efficient utilization of scarce resources of the organization and to prevent and detect potential danger among other things.

2.1 Taxonomy of Internal Control
The sum of all management control activities can be categorized under three main heading: preventive, detective and corrective controls. The categorization has been used in this study to examine the effective and efficient use of organizations resources so as to result in profit amongst SSEs. They are hereby discussed:

1. Preventive Controls: Preventive controls are controls that are used to discourage errors and irregularities from happening.
They are also used to ensure that the departmental objectives are being met. Examples of preventive controls are; Segregation of duties, Approval, authorization and verification, Security of assets amongst others.

2. Detective Controls: Detective controls are controls that used to discover errors or irregularities after they have occurred. It also monitors the activities in order to identify instances where the procedures where not followed. Examples; Performance review of budget/ forecast to determine extent of variation and financial reconciliation activities amongst others.

3. Corrective Controls: Corrective controls are controls that help to restore the system back to its normal state. For example; an organization may suggest a full restoration of a system from backup tapes after incidence of deliberate fire outbreak (arson).

2.2 Small Scale Enterprises
According to Small and Medium Enterprises Development Agency of Nigeria (SMEDAN), small enterprises can be defined as those businesses that have a work force of 10 and do not exceed 49 employees and their total asset are above five million naira (N5m) but does not exceed fifty million naira (N50m). Small scale enterprises are at the heart of stimulating economic development and improving the overall economic climate of the country. This makes such businesses indispensable in the economic development equation (Thomas & Norman, 2006).

The benefits of having functional clusters of small scale businesses are numerous to mention. They include but not limited to the following: They improve the economic climate of any country by adding to the GDP. They incur lower overhead cost thereby making entry into business easy for any prospective trader. Lower cost will result in lower prices for consumers. Small scale businesses build better and personal relationships with customers, suppliers and employees. They are inventive and innovative, thus, they introduce newer products that uniquely meet the needs of customers. They are more efficient and enduring during times of economic crisis. They constitute an effective way of expanding the manufacturing sector and a formidable approach to country-wide industrialization. They are an effective avenue of increasing the quality of life of the masses by providing opportunities for small investments, labor engagement and sustained supply-chain (Keskin, Senturk, Sungur, & Kiris, 2010).

2.3 Management Control and Financial Performance of SSEs
The implementation of an internal control systems as well as internal audit practice is expected to improve financial performance (Jensen, 2003). Thus, this study examined the body of literature to ascertain the impact of preventive, detective and corrective controls on the financial performance of SSEs. Whittington and Pany (2001) in their book principle of auditing and other assurance services affirms that various control practices put in place by an organization significantly impacts on the organizations performance positively.

3.0 Research Methodology
The population of the study is the owners and managers of small scale
businesses in Ogun State. We investigated management control issue using detective, preventive and corrective controls as the taxonomy. The study adopted a survey research design to elicit the opinions of owner-managers in Ogun state based on closed ended structured questionnaire on the taxonomy of control as described in the literature review section of this study. The study utilized the judgmental sampling technique in the administration of the questionnaire.

Three research hypotheses were formulated and stated in their null form:

H01 Establishing preventive control measures have no significant effect on the financial performance of small scale enterprises
H02 Instituting corrective control actions have no significant effect on the financial performance of small scale enterprises
H03 Introducing detective control processes have no significant effect on the financial performance of small scale enterprises

Percentage analysis and weighted mean were used for the descriptive statistics while regression statistics were used for inferential analysis, at 1% significant level. The study utilized statistical software named Statistical Package for Social Science in analyzing the data. The regression model for the study is:

$$FP = \beta_0 + \beta_1X_1 + \beta_2X_2 + \beta_3X_3 + \epsilon$$

Where:
FP - Financial performance, \( \beta_0 \) – Constant, X1- Preventive control, X2- Corrective control, X3- Detective control, \( \epsilon \) - Error Term

3.1 Analysis and Discussion

<table>
<thead>
<tr>
<th>S/N</th>
<th>Regression Analysis Model Summary</th>
<th>R</th>
<th>R-Square</th>
<th>Adjusted R-square</th>
<th>F-Value</th>
<th>Std. Error of the Estimate</th>
</tr>
</thead>
<tbody>
<tr>
<td>1.</td>
<td>Preventive Control</td>
<td>.347</td>
<td>.120</td>
<td>.110</td>
<td>12.179</td>
<td>.36275</td>
</tr>
<tr>
<td>2.</td>
<td>Detective Control</td>
<td>.333*</td>
<td>.111</td>
<td>.101</td>
<td>11.068</td>
<td>.36476</td>
</tr>
<tr>
<td>3.</td>
<td>Corrective Control</td>
<td>.339*</td>
<td>.115</td>
<td>.105</td>
<td>11.559</td>
<td>.36387</td>
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</table>

1. Preventive Control: The model summary shows that there exist a relationship between preventive control measure and the financial performance of SSEs as explained by \( r \) of .347. However, the R-square reveals that there are more factors that influence the outcome of firm’s profitability but only 12% of those factors are explained by establishing preventive control measures as captured in this study. The results from the table denote that the model is statistically significant with a significance level at 0.001, with an F- value of 12.179. Hence, this study posits that we accept the alternate hypothesis and reject the null hypothesis.

2. Detective Control: The model summary shows that there exist a relationship between introducing detective control processes and the financial performance of SSEs as explained by \( r \) of .333. However, the R-square reveals that there are more factors that influence the outcome of firm’s profitability amongst SSEs but only 11% of those factors are explained by introducing detective control
processes as captured in this study. The results from the table denote that the model is statistically significant with a significance level at 0.001, with an F-value of 11.068. Hence, this study posits that we accept the alternate hypothesis and reject the null hypothesis. This implies that the reinforcement of proactive detective processes would forestall “immaterial” leaks from the profit which in the long-run can ground an organisation.

3. Corrective Control: The model summary shows that there exist a relationship between Instituting corrective control actions and the financial performance of SSEs as explained by $r$ of .339. However, the R-square reveals that there are more factors that influence the outcome of firm’s profitability but only 11.5% of those factors are explained by Instituting corrective control actions as captured in this study. The results from the table denote that the model is statistically significant with a significance level at 0.001, with an F-value of 11.559. Hence, this study posits that we accept the alternate hypothesis and reject the null hypothesis. This implies that as various SSEs institute tougher corrective actions it would impact on the organisations going concern positively.

4.0 Conclusion

The absence of an effective internal control system opens up an organization to potential threat of fraudulent activities, in order to prevent the occurrence of fraud, which will lead to loss of financial and non-financial asset of a business, it is essential that an effective internal control system be implemented because this has a positive effect on financial performance. The findings of the study suggested that internal control especially preventive control, detective control and corrective control are significant areas, where owners or managers of small scale enterprises, should give great attention to in order to improve their financial status.

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