

INTERNAL CONTROL FOR SUSTAINABLE DEVELOPMENT OF SMALL SCALE ENTERPRISES IN LAGOS STATE: A STUDY OF SELECTED LOCAL GOVERNMENTS

Segun Idowu Adeniyi¹, Busari Ganiyu Adeniran²

¹Segun Idowu Adeniyi, Nnamdi Azikiwe University, Awka, Nigeria, Faculty of Management Sciences, princeadeidowu@gmail.com

²Busari Ganiyu Adeniran, Nnamdi Azikiwe University, Awka, Nigeria, Faculty of Management Sciences

Abstract: The study examines the influence of internal control system on small scale enterprises sustainable development. The specific objective is to determine the influence of organizational structure and recruitment of personnel in small scale enterprises on their net profit margin. The study adopted survey design. Questionnaires were employed for gathering primary data and secondary data was obtained from the books of account. The researcher employed the purposive sampling technique in selecting participants for the study. Linear regression technique was employed as the basic statistical tool for data analyses in this study, with the aid of SPSS 20.0 software. We discovered significant relationship between organizational structures and recruitment of personnel in small scale enterprises and net profit margin. We recommend that there should be no fusion of personality between the owner of the business and the business. This will encourage the business owner to have good organization structure. Once there is separation of duties among the personnel, it will induce efficient and effective internal control in the organization.

Keywords: Internal control, sustainable development, organization structure, net profit margin.

JEL Classification: M21, G21

INTRODUCTION

According to Solomon (2004), entrepreneur start - up small scale business for survival purpose. This intent spur the entrepreneur to design strategies for the survival of the business. Many scholars agreed that small scale enterprises serve as an engine room for economic growth of Nigeria economy. Coleman and Cohn, 2001; Gunu, 2004; and Aremu, 2010; asserted that small scale enterprises have contributed greatly to job creation, revenue mobilization and poverty alleviation.

Federal government of Nigeria recognized the vital roles played by small scale enterprise for the economic development of the economy. Government provide an enabling environment, like establishment of micro finance banks, establishment of agencies and programme to provide consultancy services , for their business to survive.

Mutezo (2005) opines that majority of entrepreneurs are concerned with their turnover and profit made from the business. They place emphasis on sales rather than putting internal control mechanism on ground – eventually leading to business failure. Aremu,(2010) noted that small scale business is characterized by high rate of failure that could be reduced if the businesses were properly managed. Many literatures attribute the main reasons for their failure ass lack of effective internal control. Campbell and Hartcher (2006) affirmed that for any business to operate effectively, personnel in the business should ensure adequate internal financial controls are maintained.

However, many scholars are silent about the influence of organization structure, segregation of duties and employment of personnel on small scale enterprises sustainable development.

When there is no proper organization structure, it may be difficult to separate duties among the personnel and it is likely to increase the risk of fraud in the organization. This may be due to informal means of recruiting their staffs. Therefore, when the organization is not properly structured, it may have adverse effect on the implementation of adequate internal control system.

However, despite the importance of small scale enterprises, there is limited empirical research on the influence of organization structure, segregation of duties and employment on small scale enterprises sustainable development in Lagos State. Hence, this study stands to fill the gap.

The main objective of the study is to examine the influence of internal control system on small scale enterprises sustainable development. The specific objective is to determine the influence of organizational structure and recruitment of personnel in small scale enterprises on their net profit margin.

The research question to be answered by the study is; to what extent does organizational structure and recruitment of personnel influence net profit margin of small scale enterprises in Lagos State? Therefore, the study will be guided by a hypothesis that there is no significant relationship between organizational structures, recruitment of personnel and net profit margin of small scale enterprises in Lagos State.

1. OBJECTIVE OF THE STUDY

The main objective of the study is to examine the influence of strategic cost reduction techniques used by banks on their financial performance. The specific objective is; to ascertain the influence of downsizing of staff and reduction of staff salary on bank profitability.

The study will be guided by this hypothesis:

Ho: downsizing of staff and reduction of staff salary does not significantly leads to increase in return on asset.

1.1 Scope of the study

The study will cover internal control measure taken by small scale enterprise for sustainable development. Our focus will be Lagos Island

Local government Area, Lagos Mainland Local Government Area, Apapa Local Government Area and Oshodi - Isolo Local Government Area of Lagos State. These four local governments were selected because they serve as commercial nerve centre of Lagos State.

2. LITERATURE REVIEW

2.1 Conceptual framework

Internal control

Nweke, Ekwueme and Okoye (1997) describe internal control as a measure established by management with a view to carrying the corporate activities of the organization in an orderly manner, safeguarding the company's assets and securing the completeness and accuracy of the records. Song (2008) define internal control as a way of assisting the business to provide an efficient and effective management of company assets. Therefore, internal control is a mechanism designed by management to guide business properties and harmonize its resources with the sole aim of achieving organization goals.

Statement of Auditing Standards No. 115, Communicating Internal Control Related Matters Identified in an Audit, defines internal control as 'a process, effected by those charged with governance, management, and other personnel, designed to provide reasonable assurance about the achievement of the entity's objectives with regard to the reliability of financial reporting, effectiveness and efficiency of operations, and compliance with applicable laws and regulations. Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (2013) affirms that the key objective of internal control is the effectiveness and efficiency of the organization. This encompasses financial performance and operational goals, and safeguarding assets against loss.

Campbell and Hartcher (2003) opine that many small business enterprises are known for having weak internal control. Jackson and Stent (2007) posit that majority of small scale enterprises do weigh the cost of implementing internal controls against the expected benefit to be derived from proper implementation of internal controls.

Sustainable Development

Stark (1982) describe sustainable development as a development that “meets the need of present generation without compromising the needs of future generations’.

Sustainable Development is a process of change in which the exploitation of resources, the direction of investment, the orientation of technological Development, and institutional change are all in harmony and enhance both current and future potential to meet human needs and aspirations.

2.2 Empirical review

Ifekwem and Adedamola (2016) investigate the survival strategies and sustainability of SMEs using selected small businesses in the Oshodi-Isolo Local Government Area, Lagos State. The study discovered that maintaining small but committed and motivated employees is critical in guaranteeing the survival of the SMEs in a volatile economy

Lyndon, Lisa and Juan-Pierré (2012) studied internal financial controls and informal businesses sustainability in the Cape Town Central Business District of South Africa. The study makes it clear that informal businesses do not regard internal control as an integral part of management for the business to survive. A similar study by Oseifuah and Gyekye (2013) agreed with the findings of Lyndon, Lisa and Juan-Pierré (2012). In the study Oseifuah and Gyekye sought to establish the effectiveness of internal controls in SMEs in South Africa. The study found that there is inadequate internal control measure among small scale enterprises. Nyakundi et al (2014) study on management practices in Nigerian private companies indicates that Nigerian firms use some financial control techniques occasionally. Similarly, Siwangaza et al, (2014) examine the degree of fit between size and structural variables in small and medium enterprises also recommend increase in the use of control measures to achieve high economic performance in these enterprises.

A study by Njaramba and Ngugi (2014) in Kenya which sought to establish the influence of internal control on growth of small business by analyzing the relationship between human

resource practices, entrepreneurial skills, managerial skills as internal control factors on the growth of small and medium enterprise in the errand services businesses in Nairobi. It was established that entrepreneurship skills, managerial skills, human resource practice and technology as internal control factors have a positive correlation with growth of errand service providers in Nairobi.

Concluding the review of empirical studies, we found that there is no empirical evidence on the influence of organizational structure and personnel recruitment as internal control mechanism on small scale sustainable development in Lagos State, this form the thrust of this study.

3. METHODS AND DESIGN

The study adopted survey design. Questionnaires were employed for gathering primary data. The use of questionnaires promises a wider coverage since it helps researchers to approach respondents more easily than other methods (Amadahe, 2002). This ensured a holistic and an in-depth examination into the internal among small scale enterprises in selected local government area in Lagos State. Secondary data was obtained from their books of account.

The population of the study comprises of small scale enterprises owners in the selected areas. The small scale business are categorized into; clothing and textile, food and beverage stores, general merchants, foot wears, cosmetics and house hold appliances. The justification for these business owners as participants for the study was based on its role in economic development of the selected local government area.

The researcher employed the purposive sampling technique in selecting participants for the study. This sampling technique was used for convenience sake. This sampling technique was used because the researcher wishes to focus on owners of small scale enterprises that are knowledgeable about organization structure and keep their financial records up to date. 240 participants were judgmentally selected as a sample size from the population. Five Likert Scale was used for the structured questionnaire. The score was assigned to Likert

scale as follows: Very Correct (5), Correct (4), I am not sure (3), at times (2), and Not Correct (1). Internal control will be measured by; organization structure and recruitment of personnel while Sustainable development will be measured by net profit margin.

The reliability and validity of the instrument for the study was determined by using the test re- test technique. Moreover, the instrument was scrutinized and properly validated for its face contents by five experts from accountancy department and business administration department of Lagos State University.

3.1 Model Specification

In order to test the above hypothesis, the relationship between the dependent variable (Npm) and the explanatory (independent) variables (MgtSr and Rpl) was estimated in the following models specified

$$Npm = f (MgtSr + Rpl) \quad (1)$$

The model to be used to confirm this proposition is presented below:

$$Npm = \beta_0 + \beta_1 MgtSr + \beta_2 Rpl + eit \quad (2)$$

Where:

Npm = Net profit margin

MgtSr = Management structure

Rpl = Recruitment of personnel

$\beta_0, \beta_1, \beta_2$ = Regression Coefficients,

eit = Error term.

4. DATA ANALYSIS, RESULTS AND DISCUSSIONS

Linear regression technique was employed as the basic statistical tool for data analyses in this study, with the aid of SPSS 20.0 software.

Tab. 1: The sample size of 240 selected from the population was tabulated below

S/N	Respondents type of Business	Total
1	clothing and textile	40
2	food and beverage stores	40
3	general merchants	40
4	foot wears	40
5	Cosmetics	40
6	house hold appliances	40
Total		240

Source: Field survey, 2017

Two hundred and forty copies of questionnaires were purposively administered by the researcher. One hundred and Ninety four copies

were successfully retrieved from respondents. This represents 80.8% of the number of questionnaire administered.

Tab. 2: Administration of questionnaire details was tabulated below

S/N	Administration of questionnaire	Number of copies	Percentage (%)
1	Copies administered	240	100
2	Copies returned	194	80.8
3	Wrongly filed/unreturned copies	46	19.2

Source: Field survey, 2017

5. RESULTS AND DISCUSSIONS

Analysis of response

Research question: To what extent does organization structure and recruitment

of personnel influence net profit margin of small scale enterprises in Lagos State

Tab. 3: The effect of organization structure and recruitment of personnel on net profit margin of small scale enterprises

Organization structure		Very correct	Correct	I am not sure	At times	Not correct	Total	Mean score	Remark
1	The business is controlled mainly by the family.	130	40	14	06	04	194	4.47	Accept
2	The chairman of the firm is the director and human resources manager	140	30	15	08	01	194	4.55	Accept
3	The firm accountant also perform the duty of audit manger	160	20	09	05	00	194	4.73	Accept
4	The head of marketing/sales department control purchasing activities of the firm	170	15	05	02	02	194	4.80	Accept
5	The head of marketing/ sales department is a blood relation of the firm accountant	120	30	14	20	10	194	4.19	Accept
6	The chairman of the firm is a close relation of the firm accountant.	145	25	14	08	02	194	4.56	Accept
Recruitment of personnel									
7	The chairman of the firm recruit personnel for the firm	154	25	05	05	05	194	4.28	Accept
8	Recruitment of personnel are done within the kinsmen to strengthen family tie	160	20	10	04	00	194	4.73	Accept
9	The recruitments are done through our religion denomination of the chairman.	100	50	25	11	08	194	4.31	Accept
10	Employment of staff is based on recommendation of respected personality within the family and religious circle.	150	30	10	04	00	194	4.68	Accept
11	The firm do not engage consulting firm for staff recruitment because of their consultancy fees.	160	25	04	01	00	194	4.71	Accept
12	The firm do not advertise their job vacancies	165	20	09	00	00	194	4.80	Accept
Profit margin									
13	Managers collect kickbacks from the firm suppliers. This leads to increase in price of goods purchased	120	40	15	15	04	194	4.32	Accept
14	There is outright cash thefts by employee	145	35	10	04	00	194	4.65	Accept
15	The employee use false invoice to create a false payment obligation for the firm	130	40	15	05	04	194	4.48	Accept
16	The marketing manager sometimes ordering un – needed inventory because of personal gain	130	50	10	04	00	194	4.58	Accept
17	Unauthorized disbursement of fund for family activities	110	60	14	09	01	194	4.39	Accept
18	The accountant does under state turnover by not capturing all revenue that accrues to the firm.	140	30	10	10	04	194	4.51	Accept

Source: field survey, 2017

Table 3a shows the opinion of different respondents as well as their mean score on organization structure, recruitment of employee and its influence on firm profitability. From the table above, it shows that majority of the respondents agreed that small scale enterprises are family oriented in term of their

structure. However, from the responds to questions on organization structure of small scale enterprises, there is over lapping of duties by employee. For example, question 3 and 4 shows that accountant does the work of auditor and marketing/ sales manager also perform the work of purchasing manager. This is supported

by 4.73 and 4.80 mean scores which are accepted. Moreover response to question 6 shows that the chairman, who owns the organization, entrust the account of the firm to their relations. This is the clear evidence of 4.56 mean score, which is accepted.

With respect to questions, 7 to 12, on how small scale enterprises employ their employees, it was discovered that, personnel are employed based on family ties, religion affiliation of the proprietor, recommendation from respected personalities without engaging consulting firms for the recruitment. These were supported by the mean scores; 4.28, 4.73, 4.31, 4.68, 4.71 and 4.80 which are accepted.

The issues concerning net profit of small scale enterprises was addressed in question 13 to 18. From the response of the respondents, majority of the respondents agreed that organization structure and the means of recruiting employee in small scale enterprises have negative impact on their net profit. There always are cases of outright cash theft by employee. This opinion is supported by 4.32 mean score of the response

and it is accepted. Managers collect kickbacks from the firm suppliers and this act leads to increase in price of goods purchased. This is supported by mean score of 4.65, which is accepted. Unauthorized disbursement of fund for family activities and under state turnover by accountant because he is to examine the books of account that he prepare is well pronounced among small scale enterprises. This is supported by the response mean score of 4.39 and 4.51 which are accepted.

Our decision is that, organization structure and personnel recruitment process among small scale enterprises have negative effect on the net profit of the business.

Testing of hypothesis

The hypothesis formulated for the study is tested with the use of regression analysis. If the regression is less than the critical value, the null hypothesis (Ho) will be accepted and the alternative hypothesis (Hi) will be rejected and vice versa.

Tab 3b: The model summary

Model Summaryb							
Model	R	R Square	Adjusted R Square	Std. Error of the Estimate	Sig. F	Durbin-Watson	
1	.710	.504	.173	3.38206	1.523b	1.674	
a. Predictors: (Constant),, recruitment of personnel, management structure							
b. Dependent Variable: Net profit Margin							

Source: Authors own study 2017

In the first table (3) entitled the model summary, the value of R value = .710; however R² = .504 shows that 50.4% of the dependent variable (Net profit Margin) has been explained by the independent variables; recruitment of personnel (Rpl) and management structure (MgtSr). However, the unexplained variation is 0.496 which is about 49.6%; thus we can understand

that the model is providing a good fit to the data since the unexplained variation is 0.496. This clearly shows that the regression line fits the data and Durbin Watson (Dw) suggests that the model is serially correlated since 1.674 lies between 1.635 to 1.679.

Tab 4: ANOVA and the significance of the model

ANOVA ^b						
Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	34.833	2	17.417	1.523	.350 ^b
	Residual	34.315	3	11.438		
	Total	69.148	5			
a. Predictors: (Constant), recruitment of personnel, management structure						
b. Dependent Net profit Margin						

Source: Authors own study, 2017

ANOVA results (specifically f-ratio) test the overall significance of the model. The f-ratio (1.523) shows that the variables (Rpl and MgtSr) are the major determinants in explaining net profit margin.. It can be observed that the independent variables do not have a significant effect on the dependent variable based on the f-ratio suggesting that; overall, the model in the study is significantly good enough in explaining the variation on the dependent variable. The independent variables are statistically not significant because its significance value is 0.350, that is $P > 0.05$. So the alternate hypothesis is rejected while null hypothesis is accepted. Therefore, there is no significant relationship between organizational structures and recruitment of personnel in small scale enterprises and net profit margin.

6. CONCLUSION AND RECOMMENDATION

Small scale enterprises have been acknowledged as an engine room to economic development of Nigeria. Therefore, both the federal government of Nigeria and State governments in the country have been creating an enabling environment for its sustainability. Despite the efforts to promote sustainable development among small scale business enterprises, there is high incidence of business failure among them. It was discovered that business owners have responsibility for their business sustainable development in Nigeria. One of the key ingredients for its sustainable development is by maintaining efficient and effective internal control procedures in their organization.

This study investigates the influence of internal control mechanism on small scale enterprises

sustainable development. It was discovered that many small scale enterprises have difficulty in maintaining effective internal control measures of their informality in their management method and procedures. In many of the organization structure, the relations of the owner of the business are put in the key positions. The belief is that relations will always see to the success of the business. There is no separation of duties among staff, and most cases, the staffs are relations of the owner of the business or they are member of the same religion.

We found out that recruitment of personnel among small scale business owner deviate from modern recruitment procedures. Employment of staff is based on recommendation from a reliable and respected person. Most times, it is based on kinship, which is usually restricted to the nuclear family, and not extended family. There means of recruiting staff is not expensive and less stressful.

We recommend that small business owners should see their business as an entity that can stand on its own and they should stand on their own as an entity. There should be no fusion of personality between the owner of the business and the business. This will encourage the business owner to have good organization structure. Once there is separation of duties among the personnel, it will induce efficient and effective internal control in the organization.

Though, the modern procedures of recruiting staffs may be expensive for small scale enterprises owner; they should ensure that qualified staff are employed. This can be done through engaging small scale consulting firm for their recruitment. Relations that are engaged as staff do work contrary to the objectives of the

organization because of greediness and too much familiarity.

REFERENCES

Amadahe, F. K. (2002). *Fundamentals of educational research methods*. Mimeograph. Cape Coast: University of Cape Coast.

Aremu, M. A. (2010). Small and Medium Scale Enterprises As A Means of Employment Generation and Capacity Building In Nigeria, A Paper Presented at the International Conference on Management and Enterprise Development on "Intellectuals and New Strategies for Sustainability Development of the Third World" Held at Conference Center, University of Ibadan, Ibadan, Nigeria, October 5th - 8th.

Campbell, S., & Hartcher, J. A. (2003). Internal Controls for Small Business. Available from: <http://www.whistleblowing.com.au/information/documents/InternalControls.pdf>.

Campbell S., & Hartcher, J. (2006). Internal controls for small business. *CPA Australia*. 3-17, September.

Coleman, S., & Cohn, R. (2001). Small firms' use of financial leverage: Evidence from the 1993 national survey of small business finances. *Journal of Business and Entrepreneurship*. 12(3).

Committee of Sponsoring Organizations of the Treadway Committee (COSO). (1992). Internal control integrated framework. Executive Summary.

Gunu, U. (2004). Small scale enterprises in Nigeria: Their start up, characteristics, sources of finance and importance. *Ilorin Journal of Business and Social Sciences*. 9(1 & 2), 36 – 43.

Lyndon Y., Lisa S., & Juan-Pierré, B. (2012). South African informal businesses sustainability in the Cape Town Central Business District: The power of internal financial control. *African Journal of Business Management*. 6(45).

Mutezo, A. (2009). *Obstacles in the access to SMME finance: an empirical perspective on Tshwane*. Published Master's Thesis, Johannesburg: University of South Africa.

Njaramba, E. A. N., & Ngugi, J. K. (2014). The influence of internal controls on growth of small and medium enterprise in the errand services businesses in Nairobi County.

International Journal of Current Business and Social Sciences. 1(1).

Nweke, M. M, Ekwueme, C. M., & Okoye, P. V. C. (1997). *Modern Auditing*. snaap press Ltd., Enugu.

Nyakundi, D. O., Nyamita, M. O., & Tinega, T. M. (2014). Effect of internal control systems on financial performance of small and medium scale business enterprises in Kisumu City, Kenya. *International Journal of Social Sciences and Entrepreneurship*. 1(11).

Oseifuah, E. K., & Gyekye, A. B. (2013). Internal control in small and micro enterprises in the Vhembe District, Limpopo Province, South Africa. *European Scientific Journal*. 9(4).

Solomon, G. (2004). *Entrepreneurship and impact of entrepreneurial orientation training on SMMEs in the South African context: A longitudinal Approach (Magister Commerce)*. Unpublished Master's Thesis. Cape Town: University of the Western Cape.

Song, W. (2008). The Hygiene Factor of Growth for Small and Medium sized Enterprises. An Internal Control Perspective. *African Journal of Business Management*.

S tark, O. (1982). On modeling the informal sector. *World development*. 10(5), 413-5.