

Small and medium enterprises in mauritius



Basically businesses are regarded as small based on different features.

Different countries define SME differently. For example the definition of SMEs in European Union (Eu) is based on Turnover or balance sheet total and headcount.

The Small and Medium Industries Development Organization (SMIDO) which was established under the SMIDO 1993 as a parastatal body, was the prime support institution for Small and Medium Enterprises (SMEs) in Mauritius. It aims was to foster growth and development of SMEs”. Small Medium Enterprise is defined as:

“ Manufacturing enterprises which uses production equipment with an aggregate CIF value not exceeding ten million rupees. “ Manufacturing means the transformation, conversion of raw materials, repair, packing and assembly of semi-finished parts into finished goods. Production Equipment means machinery and equipment used in the process of manufacturing”.

As per SMEDA act of 2009, the SME definition comprises of enterprise of all economic sectors. There is no differentiation between services and manufacturing sectors. Therefore, turnover criteria are used across sectors.

“ A Small Enterprise is defined as an enterprise which has an annual turnover of not more than 10 million MUR “.

“ A Medium Enterprise is defined as an enterprise which has an annual turnover of more than 10 million MUR but not more than 50 million MUR”.

No differences are made between service and manufacturing sector.

According to the Organization for Economic Cooperation and Development
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(OECD), some countries refer to the number of employee as criteria for SME's and some other use a combination of the number of employees, invested capital, sales and industry type. Basically there is no universally agreed definition of Small & Medium Enterprises as it is based on the number of employees, on business or turnover and assets. However, according to the exposure draft for SME'S of IASB, SMEs is an enterprise that do not has public accountability and publish general purpose financial statement for external users.

The bottom line mission of SMEDA is to assist Mauritius start, build and grow businesses. It also seeks to develop an entrepreneurial culture in Mauritius where a large proportion of the population is willing to start a business.

2. 1. 2 The importance of SMES in Mauritius

According to Beyene (2002) Small and Medium Scale Enterprises (SMEs) are universally acknowledged as effective instruments for employment generation and economic growth . Padachi (xxx) who analyzed the importance attached to accounting services among small to Medium sized Mauritian Manufacturing firms states that: " SME'S are the backbone of an economy as they are the major contributor and plays an important role as efficient providers of intermediate goods and services to large firms".

Big businesses and small businesses have a big difference in the role played by the owner and manager. In small business, the owner and the manager are often the same person (Vos E and Roulston C (2008)) . In this respect they are acknowledged as owner-manager. Basically most SMEs in Mauritius are private limited company. However there are some firms that are

organized as sole proprietorship. It was also found that majority of the firms are family-owned and the owner- managers takes all the responsibility of the business.

Lal K and Peedoly A S (2006) who carried a survey to locate Mauritian SMEs in the present context of global competition and to identify the extent to which they have adopted ICTs as a tool to meet the challenges suggested that:

“ The general picture of Mauritian SMEs that emerges from the above findings is that the overwhelming majority are ill-equipped both literally and figuratively to cope with the challenges of globalization. The gradual demise of some of the economic pillars of the country in recent years triggered by contemporaneous ideological, economic and political realities of globalization and their accompanying effects on the unemployment rates are presenting at the one same time both a challenge and an opportunity for the SME sector.”

2. 2 Accounting information System and its implication

2. 2. 1 What is an accounting information system?

Accounting information system collects and processes transaction data and communicate financial information to decision makers. Weygandt J (2010).

Besides Moscove A Et al(1999), there are many ways where accounting itself is an information system. It distributes information to those in need of it.

However Moscove A et al (1999) point out that many people think of computers when they hear the word information system. He suggests that

information system may not necessary be a computerized system. It can still exist with or without a computer. However it may use computers to process a paper-based information. Furthermore, the data may also be captured in order to input electronically, processed by computer, and output to a computer screen.

Accounting information system plays a vital role in a company . In these modern times accounting information are almost processed by a computer rather than on paper. According to Smith (2008), most companies involved accountants to maintain their accounting system but today with the introduction of computers and several types of accounting software the number of accountant to maintain accounts in Small Medium Enterprise has reduced . Owners of SME'S invest some amount of money for installing computer technology and accounting software. As a result, expenses made on paper work and extra staff is eliminated.

Son et al. (2006) conducted a prominent survey in Vietnam on users' perceptions and uses of financial reports of small and medium companies found that the user's accounting expertise was one of the main factors affecting the information use of the owner or director. Due to lack of accounting expertise they are not able to use or understand the information." There was a negative perception among users about the reliability of financial information provided by small medium enterprise. Reliability and timeliness were found to be the most desirable characteristic affecting the utility of information.

2. 2. 2 Implication of accounting information systems for SME'S

The Accounting information has two primary informational components: financial accounting and managerial (management) accounting

Management accounting is concerned with providing information about an organization to managers to help them in managing the business . Basically the activities that are involved are decision-making, planning and control. Therefore it is the collection, analysis, dissemination and interpretation of information for managers of an organization that will assist in the making of decision and planning based on those decision and finally to control so as to ensure the accomplishment of planning. (Atrill and Mclaney) . It generates monthly or weekly reports for the internal users of the company. It tends to focus on products, department and activities. Furthermore it helps management with the organization's acquisition, processing, distribution and selling activities.

Financial accounting collects and summarizes financial data to prepare financial report for the firm's management, investors, lenders, suppliers, tax authorities and other stakeholders. These external users rarely have access to the internal information of the company. Therefore they have to rely only on the general report presented by the company. Although it is prepare for external use, managers also use it for evaluating organization's performance. Furthermore, financial statements are prepared to comply with tax regulation and are also useful for loan negotiations.

Isa et al. (2007) examine financial and management accounting practices in small and medium enterprise in Malaysia. The results showed that majorities of company prepare financial and management accounting reports such as profit and loss, balance sheet and cash flow statement on a regular basis. The use of computerized system was predominant among the firm. The management accounting reports include budget and different types of budget such as variance analysis, production cost statement, cost volume profit analysis and benchmarking report.

2.3 General sources of accounting information for SMEs

The financial statement of SMEs comprises of income statement, balance sheet, the directors report and disclosure of accounting policies. There are only some SMEs whose financial statements are audited giving rise to the audit report. In Mauritius, financial reporting which is governed by company act 2001 does not require smaller incorporated company to have statutory audit. Consequently when preparing financial statement, international financial reporting are followed. According to company act 2001 small companies (turnover Palmer Kristine N (1994) carried a survey on the financial information used by small independent Retailer owner-manager. She found that daily records of sales and other transactions were mostly kept which little of them uses computerized accounting system. Cash method of record keeping was used. A checkbook and a profit and loss statement were to be their financial statement. The financial information that was prepared did not give them the appropriate information . It was simply prepared for tax purposes. She further stipulated that information that was gathered was not written down on paper or recorded in any

accounting system. It was found to be only in their minds. In this respect, financial guidance is needed by the owner-manager to identify the information they need to make a good decision by changing their methods of gathering information to a sophisticated accounting system.

Basically the owners of small enterprise used external accountant or bookkeepers primarily to produce financial statement, to provide tax or VAT information or to run the accounting system (Sian S and Robert C (2009)). Accountant additionally provides services such as production of annual report and routine tax work and management accounts. (Chittenden et al. 1990). Garvin C Reid (xxx) suggests that annual account contained historical data that do not promote monitoring and control in the company although it is important for statutory requirement for tax purposes. Collis and Jarvis (2002) who conducted a survey in UK on financial information and management of small private company where sources and utility of financial information used were indentified, suggested that the most useful general sources of information were periodic management accounts, cash flow information and bank statement which are also form of cash flow information. It was also found that the most widely used information is monthly/quarterly management accounts and cash flow information in various forms. This shows that much attention are placed on controlling cash as previous research (Jarvis et al. 1996) indicates that cash flow management is important to help small firm for their survival.

John and Healeas (2000) stipulated that the statutory account was not useful for decision-making and management accounts and cash flow forecast were preferably used. Collis and Jarvis (2002) found when the company received <https://assignbuster.com/small-and-medium-enterprises-in-mauritius-essay-samples/>

statutory accounts, at the same time they get additional information such as verbal explanation or analysis of accounts. Furthermore, detailed profit and loss and some management advice were also provided to a lesser extent.

Sian S and Robert C (2009) and John and Healeas (2000) also found that few SME'S owners-manager has difficulty do understand the contents of statutory accounts. Besides, as accountant often prepare financial statement, they advise small enterprises on internal, management planning, decision making control and future strategy.(Chittenden et al. 1990, Deakins et al. 2001.)

According to the final report of Expert Group conducted by the European Commission and expert also suggest that

“ Normally statutory accounts of small enterprises are not considered to be particularly useful for managing the enterprise, but the majority of directors receive management advice or further analysis at the same time”.

Recently, Isa et al. (2007) conducted a survey on financial and management accounting practices among small and medium enterprise in Malaysia. The findings revealed that all owners- managers of the sample prepared balance sheet and profit and loss. In addition to the main financial statement; cash flow statement, fixed assets records, tax returns and inventory analysis were prepared. As far as the frequency of report generation is concerned, it was found that a greater extent of the owner-managers prepared this report on a monthly basis. Furthermore owner- manager prepare management accounting reports which comprised of budget, production cost and cost volume profit analysis.

Pinson L (2007) points out all of the general records in small business that is used to track the day to day transaction. Some of them are:

Cash in Bank

Revenue and expense Journal

Invoices and sales receipt

Petty cash record

Inventory records

Fixed asset log

Accounts receivable and payable

Payroll record

Customer records

Business checkbook

2. 4 External users of financial statement

The International Accounting standard board (IASB) identifies seven main users of financial statement . They are

Investors

Lenders

Suppliers

Employees

Customers

Government

Public

The intergovernmental working group of expert on International Standards of Accounting and Reporting (ISAR) issued a publication on Accounting and financial reporting Guidelines for SMEs where they identified six principal users of financial statement namely: management, lenders and others creditors, Government , Taxation authority, their agencies and credit agencies.

According to the Final report of the Expert group 2008, the main users of financial statement is business owners/investors, management , government and its agencies, Banks and their creditors, customer or suppliers and employees

“ The objective of financial statements of a small or medium-sized entity is to provide information about the financial position, performance and cash flows of the entity that is useful for economic decision-making by a broad range of users who are not in a position to demand reports tailored to meet their particular information needs. Examples of external users include owners who are not involved in managing the business, existing and potential creditors, and credit rating agencies.” (Exposure draft of a proposed IFRS for Small and Medium-sized Entities, February 2007).

Amir and farooq (2010) conduct a prominent survey in Sweden on whether SMEs in Sweden are inclined to the adoption of IFRS for SMEs and how do they prepare for its implementation. They interviewed (Henrik) the chief financial controller regarding the users of financial statement:

“ When asked if tax authorities need financial statements for the calculation of taxes, Henry said that tax authorities surely need financial statements in order to calculate the taxes. He added that there is a possibility that by the end of this year a threshold will be defined for the companies which will not require hiring the services of an auditor. After the implementation of this threshold, the tax authorities would need to take extra consideration of the financial statements of such companies which fall below this defined threshold. According to Anonym, there has been much discussions regarding this issue that whether tax reports can be based on the financial statements. There should be complete information symmetry because the accountants and auditors might know much more than personnel in tax department. In this way, the tax department does not want to rely on financial statements which are made in accordance to specific accounting standards, and they want to use their own rules for the calculation of tax purposes.”

Banks is considered as one of the crucial source for small enterprise (Chittenden et al. 1990; Storey 1994). Collis and Jarvis (2000) identified that the main non-statutory recipients of the statutory financial statements as major lenders, the Inland Revenue and management. Most of the company used it to provide information to the bank. Berry and Warring (1995) stipulated that a set of expanded financial statement are demanded for any loan application by the bank. This findings is similar to that of Collis and <https://assignbuster.com/small-and-medium-enterprises-in-mauritius-essay-samples/>

Jarvis (2000) where it was suggest that majority of the company use statutory accounts to provide information to the bank

The extent to which managers use financial information

A financial report is a report which is published by an enterprise to provide accounting information to reflect the financial position on a particular date and its operating results and cash flow for an accounting period to the users of financial report. It includes accounting statements and notes and other information that shall be disclosed in the financial reports. Sian S and Robert C (2009) state that, the bank statement and annual reports were the most essential information resources for the owner- managers. It was further stipulated that most owner-manager rarely use financial statement and if so only to compare income with past periods. Collis and Jarvis (2000) also suggest that the most useful purpose of the annual account that owner-manager consider is that, it helps to determine directors remuneration and dividend. It was also useful for comparing performance with previous period and also for loan and finance purposes. Directors, who sent their accounts to the bank, consider the statutory accounts are advantageous for management purposes and would opt for a voluntary audit.

In contrast, Barker and Noonan (1996) highlight that financial statement was primarily useful for owners or directors. However, the preparation of financial statement in high standards is not beneficial to the owners or directors but to the bank instead. The financial statement was of great importance in cash management decision if the information is not available until at least three or six months after the year end. Abdel K. Halabi et al. (2010) conduct a survey of owners to examine what financial information small firm owner's record <https://assignbuster.com/small-and-medium-enterprises-in-mauritius-essay-samples/>

and the system they use to collect, process and report that information. It affirms that accounting reports were not produced for use in the business because it was beyond the understandability of the owner-manager but rather for taxation purposes. Taxation returns and accounting reports utilized similar information but look different. Some owners use these accounting reports only for analyzing information for decision-making.

Furthermore, Abdel K. Halabi et al. (2010) also studied whether financial information was used in the evaluations of the firm's performance. It was found that there were both positive and negative responses. The positive one suggests that the information was recorded up to date and each quarter they have an idea of the firm's performance. It was argued that the value achieved from the recording of financial information is based on the financial skill and their relationship with the accountant. Moreover, some owners used a computerized system such as an "off-the-shelf accounting packages to record financial information. With such system, comparison across time period was advantageous. Basically, the owners trusted everything that was generated from a computer thus allowing the production of timely reports. This study (2010) states

"Financial management skills are critical to the survival of small firms. Despite this the majority of owners of small firms do not (as yet) need to comply with any specific accounting standards and must only report financial information for taxation purposes. Financial information and accounting reports can inform owners of the consequences of their firm's operations and the impacts of their past decision making. It can be used to help owners

grow and develop their firm and thus, strengthen the economic and social contribution small firms can make.”

Longenecker et al. (2006) state that managers must have accurate, meaningful and timely information to make good decision. This is particularly true of financial information about firms operations. Sometimes owner-manager tends to believe that they have less need of financial statement because they are involved in personal involvement in day to day operation.

“ An accounting system structures the flow of financial information to provide a complete picture of a firm’s financial activities . Conceivably a few very small firms may not require formal financial statement. Most however, need at least monthly financial statement which should be computer generated. The benefits of using a computer in developing financial information are so great and the costs so low that it makes absolutely no sense to do otherwise . An accounting system for small business should offer financial statement for use by management , bankers and prospective creditors.”

Amir and farooq (2010) questioned X (chief financial controller) and Y(chartered accountant of company z) concerning their opinion regarding the view that small business managers are less dependent upon formal financial statements.

X states:” In one-man owned firm the owner knows what his business is about, what he makes and sells, so he does not have to rely on any kind of formal financial statements. In a way, it can be associated with the size of the firm, the more employees a firm has got the more management it needs,
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and the financial statements is required in order to keep a check and balance. According to Y, small business managers are less dependent on financial statements because in these businesses there are businessmen who do not know much about book-keeping and financial information. The only thing they know is how to earn money, and they can do it without the use of any kind of financial information. Thus, involvement can make the managers understand much more than just getting the idea from financial statements.”

Owners or Managers believed that financial statement are very important for capital making decision. (Holmes s (1988)). Nandan R (2010) stated since SME's have independent ownership where owners or managers provide majority of capital required for the operation of the enterprise. Holmes and Nicholls (1989) point out that small business owner or manager rarely does have access to all information that is considered important for all aspects of the business. This were due to the four external factors such as business size , the amount of time under current management , the industrial sector and the education level of the owner or manager.

2. 6 Financial awareness among managers

Sian S and Robert C (2009) highlights that many owner-managers turned to accountants to provide accounting service, such as the preparation of accounts or the provision of tax or vat information because of lack of financial awareness among them. Deakins et al (2001) found that owners-managers have different approaches concerning business planning. Basically planning was important to those firms under growing growth and periods of rapid changes.

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However, Collis and Jarvis (2002), argued that due to the fact that the accountant, employees or director are qualified, the company have considerable financial expertise which is available internally to assist in the analysis of financial information. It was also found that some firms had a computerized or partly computerized system. There information technology is used for their assistance.

Son et al. (2006) also argued that accounting expertise was seen as the biggest threats to the use of financial information by the directors. In fact the directors do not understand the information because of its low quality. This result in low awareness of cost-benefit consideration of reporting task. The external users were concerned with the reliability of financial information provided by the small enterprise basically an owner-manager should be fully aware about the product or services on which their business is based. The owner-manager may not be skillful in business management skills particularly when starting the business. The financial management may be expected to be simple and cash flow-based. As the owners concentrate in the running of the business, this may leave very little time for the owner-manager to learn about the worthiness of using more financial management tools for the accomplishment of their goal rather than the basic itself.

Padachi states that:

“ In fact, when account is taken of the limited resources that are usually available to SMEs, the typical lack of expertise in financial management of their owner-managers, and the likely consequences of making poor decisions, the need for government support is undeniable.”

Abdelrahim R and Alsaddie A (2008) who analyzed small business performance in Syria, confirmed in a wide ranging questionnaire that managers training are positively related to successful business performance. When small firm's managers has adequate training , it has a huge impact on business performance and as a result are likely to grow successfully. It was further found that managers who received training in marketing's skills had better business performance in terms of turnover and profitability than that received in other business fields such as accounting. However, it was stipulated that there is a lack of awareness among small business managers in training of marketing.

The study states:

“ Lack of awareness among small business managers of the potential benefits of training in general and marketing in particular on their business performance. Lack of managerial training does not necessarily lead to failure, but with a high degree of certainty, as evidenced by the results, overall business performance will improve.”