

The role of internal control and risk management on going concern of MSMEs

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Abstract

Micro, Small, and Medium Enterprises (MSMEs) become the most important pillar of the Indonesian economy. However, MSMEs face more risks in business continuity due to a lack of resources, especially in developing countries. MSMEs are better able to carry out internal control and risk management to survive in a volatile market. As a risk management tool, internal control does contribute to the sustainability of MSMEs. The purpose of the study is to test and analyze internal control and risk management for ongoing concerns of MSMEs. This research is quantitative research. The population of this study is MSME business actors in Magelang Regency. The sampling technique uses convenience sampling with the number of samples used in this research being 135 MSMEs in Magelang Regency. Hypothesis testing uses the SEM-PLS analysis tool. The results of this study show that internal control and risk management are not significant in achieving MSMEs' business continuity. This study expands the literature by providing empirical evidence on the role of internal control and risk management in the growth of going concern of MSMEs.

Keywords

Internal control, Risk management, Going concern, MSMEs

Introduction

The going concern is the achievement of the target for the business sustainability of an entity or Micro, Small, and Medium Enterprises (MSMEs). All companies, both large and small, need to pay attention to business continuity, to ensure that the company will continue to operate in the future. There are several external and internal factors that ensure business continuity including government policies, market and marketing, economic conditions, business partnerships, business management, and family factors. The factors of business management are internal control and risk management.

Since the COVID pandemic until post-COVID-19, almost all businesses have experienced problems in maintaining business continuity, especially MSMEs. In the Indonesian economy, MSMEs are the most important business pillar and support. MSMEs are one of the important parts of the Indonesian economy. The roles of MSMEs include: 1)

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helping the economy of the community around the business location, 2) creating employment opportunities, 3) increasing state revenue through taxes and from exports, and 4) the small and medium enterprises as a forum in implementing and creating innovation. The number of MSMEs is not small, it reaches 64,2 million and it will make a great contribution to GDP of 61,07% or worth 8.573,89 trillion rupiah. This contribution can absorb 97% of the total existing workforce and collect up to 60,4% of the total investment. The success of the industrial and trade sectors has given great enthusiasm for creating a national economic structure.

MSMEs are one of the leading sectors in Magelang Regency besides agriculture and tourism which are always driven by growth and development. Magelang Regency has various types of MSMEs that are developing. Those are the industries of food processing, tofu, batik, furniture, and various other types of industries. The total number of MSMEs in Magelang Regency reaches 24.000, which consists of industries of food and non-food. Economic growth in Magelang has experienced ups and downs in the amount of production of goods and services which is produced by economic activities in all sectors and can be known from measurements with the Gross Regional Domestic Product (GDP) Instrument. More than 109.000 MSMEs in Magelang Regency have made a great contribution to moving the wheels of the economy [1].

The large number of MSMEs causes business competition so that improvements are made continuously, and this cannot be separated from the risks that may occur. Business competition and high uncertainty are some of the risks that can happen in all businesses, which are external factors for MSMEs that are not small. This is where risk management plays an important role [2]. Poor risk management will have a more severe risk impact [3]. MSMEs must continue to make improvements so that their businesses do not go bankrupt and continue to sustain their business. One of the concepts in management accounting to review risk management is continuous improvement, so that effective risk management is created [2,4]. The existence of risk management will make entities more aware of the risks faced. Risk management in MSMEs can be based on project or traditional risk management, which is expected to help reduce losses that are received [5][6]. In the era of progress supported by information technology, internal control and risk management are important aspects that support the ongoing concern of MSMEs.

Good governance shows that every level of the organization in all its operations must be an important part, then an effective risk management and internal control system will be needed [7]. Internal control is a tool used to direct, monitor, and measure SME resources, which plays an important role in the prevention and detection of fraud as well as physical protection. Besides that, it also leads to high operational efficiency of the business. The existence of a strong internal control system to monitor and run the business makes the prospect of bankruptcy will be reduced [7].

Internal control will have a good influence on the Environmental, Social, and Governance (ESG) rating, which will later affect the company's sustainability. It happens

because a good internal control system will improve operational efficiency and effectiveness, reliable reporting, and compliance with relevant laws and regulations. It is ensured by the integrity of all forms of information, and adequate internal control can help the long-term growth of companies with a high level of trust [8].

Research on the survival of MSMEs has been researched, stating that the implementation of risk management can affect the company's value that will help the company maintain business continuity [9,10]. Implementation of risk management impacts the efficiency of cost investment, which can increase business agility [11]. The implementation will support the achievement of the SDGs target in achieving the environmental pillar, which is one of the indicators of ongoing concern. Management needs to evaluate internal processes and controls to evaluate ongoing-concern so that it is sufficient to overcome the risks caused by the new economic environment, which varies greatly by industry because the COVID-19 crisis is a unique and unprecedented event [12].

The formulation of this research problem is whether internal control and risk management affect the survival of MSMEs. This study aims to answer whether internal control and risk management can affect the sustainability of Magelang MSMEs. There is still little research on business sustainability, especially in Magelang Regency. These are implications of the results of this study: first, it can be used as evaluation material for the existence and survival of businesses in maintaining global competition, transparency, and accountability in determining the choice of external auditors of companies. Second, the implications of policies and practices in business risk management provide a verifiable explanation for MSMEs to ensure business sustainability. Third, it is used for MSME decision-making, especially in developing countries like Indonesia.

Method

The type of research is qualitative research. This study uses primary data obtained through filling in direct respondents. The population of this study is MSME actors in Magelang Regency. The research sample used convenience sampling with a sample that used as many as 135 MSMEs in Magelang Regency. The questionnaire uses a Likert scale of 1 to 5, which means 1: Strongly disagree; 2: Disagree; 3: Neutral 4: Agree; 5: Strongly agree. Hypothesis testing uses the SEM-PLS analysis tool [13].

Results and Discussion

Validity and reliability tests

Based on Table 1 shows that the AVE value for all variables is greater than 0,5, so it can be said that all valid indicators converge in forming their respective variables. In addition, Cronbach's Alpha, Rho A, and Composite Reliability/CR values have greater values than 0,7 for all variables so that the overall construction has high reliability. It

concluded that all variables and items used in this study meet the validity and reliability of the measurement of variables.

Table 1. Validity and reliability tests

	Cronbach's Alpha	rho_A	Composite Reliability	Average Variance Extracted (AVE)
Internal Control	0.918	0.923	0.931	0.575
Risk Management	0.892	0.909	0.914	0.575
Going concern of MSMEs	0.882	0.885	0.916	0.687

Source: primary data processed, 2024

Table 2. Nilai R Square

	R Square	R Square Adjusted
Going concern of MSMEs	0.314	0.304

Source: primary data processed, 2024

Table 2 shows the value of the determinant coefficient of 0.314, meaning that internal control and risk management have an influence going concern by 31% while the remaining 69% is explained by variants from other variables outside this research model.

Model conformance test

The model conformance test uses the statistical indicators of Standardized Root Mean Square Residual (SRMR), Normed Fit Index (NFI) and RMS theta. To get a suitable model, the indicator must meet a value, namely SRMS < 0.08; NFI > 0.90; RMS_theta close to zero. The results are shown in **Table 3**.

Table 3. Model conformance test

	Saturated Model	Estimated Model
SRMR	0.086	0.086
d_ ULS	2.042	2.042
d_ G	0.966	0.966
Chi-Square	674.992	674.992
NFI	0.725	0.725
rms Theta	0.178	

Source : Created by author in 2024

Based on the test results, it was obtained that the SRMS value of 0.086 should be less than 0.08. An NFI value of 0.725 is less than 0.900. The RMS theta value was generated at 0.178, close to the value of 0. Of the three indicators, the model formed has met the conformity criteria so that the model can be used and is good at describing the relationship between variables.

Model formation

The formation of the SEM model has a significant influence between variables if the p-value of T-Statistic is less than the significance level of 5%. The relationship can be seen in **Table 4**

Table 4. Hypothesis Test

Variable	t statistic	p value
Internal Control	0.05	0.264
Risk Management	0.05	0.328

Source : Created by author in 2024

In Figure 1, it is obtained that the relationship between the variables of Internal control and risk management has a p-value of 0.264 and 0.328 greater than the significance level of 0.05 so that it is not significant, so hypothesis 1 and hypothesis 2 are declared rejected.

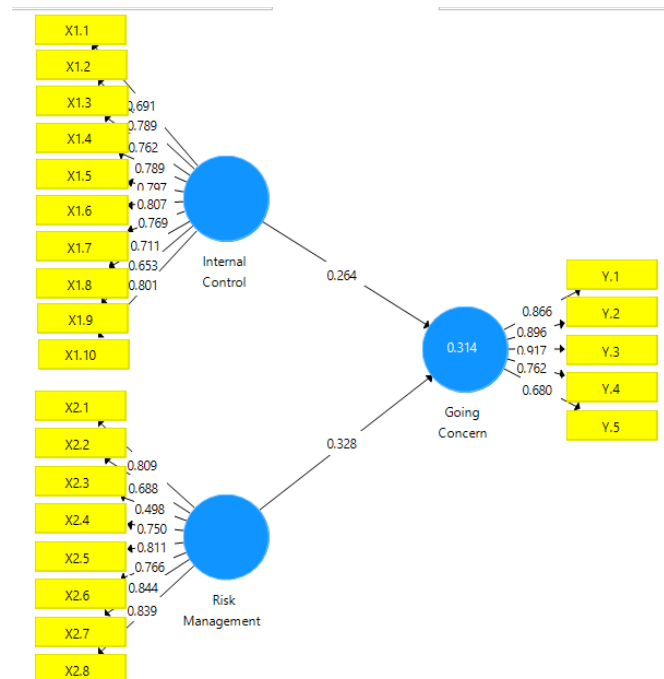


Figure 1. Research Model

Internal control affects the business continuity of MSMEs

Based on the results of the hypothesis test, it shows that the hypothesis is not accepted. Internal control does not affect the going concern of MSMEs. This is because MSMEs have not understood internal control and have not carried out internal control in their business [14]. MSMEs in managing their businesses are more managed dominantly by owners. Business owners in the MSME business are very dominant in management, control and supervision, so that everything is done by the owner, there is no separation of duties. Management carried out by people who are not different can result in fraud or other mistakes, [15] this slows down the increase in business. In accounting standards, a good business must have a separation of businesses. In addition, in the management of MSMEs, there is a lack of effective communication between MSME owners and all employees, lack of information disclosure or transparency; lack of trust from all employees; MSMEs are less able to handle customer complaints properly to maintain output quality; financial transactions are carried out only by the owner; supervision and monitoring are only carried out by the owner, so it is less effective.

So far, MSMEs have not implemented ideal internal control because it is not easy and requires a lot of money, although it is still needed. MSMEs also have a limited number of employees. The large number of employees, the implementation of each of these control components is carried out adequately [16]. For smaller MSMEs, of course, it is a challenge in itself, because to implement it is certainly not easy and there are other considerations both in terms of cost and implementation.

This study does not support the research [17];[18]; and [19], showing that the internal control structure has a positive and significant effect on business success. The internal control system can be an effort to continue the business. With a good control system, business continuity will continue and compete with the many risks and competitors that arise. Business continuity is carried out by management regarding future assumptions, by having economic benefits that flow to the entity. According to [20] that entities in achieving their goals must have adequate internal control, which is very important to ensure the sustainability of the company's main operating activities in the long term. It was found that 50% of MSMEs in Malaysia experienced bankruptcy caused by misuse of company assets, misuse of company funds, misreporting, and illegal investments, as internal controls [21].

Risk management affects the business continuity of MSMEs

Based on the results of the hypothesis test, it shows that the second hypothesis is not accepted, namely risk management cannot improve the business continuity of MSMEs. So far, MSMEs have only focused on daily operational issues rather than strategic risk management, namely business continuity is more determined by access to funding and operational capabilities than the implementation of formal risk management. MSMEs that have risk management are only limited to a simple risk management system so that it is only a formality without real implementation.

MSMEs prioritize other aspects, such as marketing or product development, compared to risk management. Not all MSME actors are aware of the importance of risk management in maintaining going concern. In addition, risk management and strategy management in their business are rarely carried out by most MSMEs. MSMEs also have limited resources and funds [6].

Research [22] shows that risk management has seven stages, but the last two stages still cannot be implemented because it takes time to implement risk management for several periods. The results of this study do not support the research [2] that risk management can maintain business continuity. Research [23] explains that risk management supports the achievement of SDGs targets in achieving environmental pillars where the environment is one of the indicators in the continuity of a business.

Conclusion

Business continuity is the achievement of the target for the going concern of MSMEs. All entities, both large and small, need to pay attention to business continuity, to ensure

that the company will continue to operate in the future. MSMEs, which are the breadwinners of Indonesia's economic income, have an important role in their existence. Therefore, the sustainability of MSMEs is a very important concern for all stakeholders, especially the government. This study found that internal control and risk management have no effect on the sustainability of MSME businesses. MSME actors play a dominant role in having access to control, monitor, and supervise. MSMEs do not have adequate planning and do not have a vision and mission. Besides that, most of the goals of MSMEs are only to meet operational costs and meet the needs of family life, not to develop a business. This research is still researching the sustainability of MSME businesses in terms of internal control and risk management. The limitation of this study is that the variables used, the results do not support the theory, while the sample is still around Magelang, not yet with the MSME cluster so that for future research, a wider number of samples can be used and carried out per MSME cluster. Further research may consider other variables.

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