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## IMPACT OF ACCOUNTING AND AUDIT SERVICE FOR SMALL AND MEDIUM SCALE ENTERPRISES' PERFORMANCE

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### Abstract

*Small businesses are important to the Nigerian economy. As a developing economy, the investment of vast wealth and resources in small businesses and the auditing of their business are very crucial to the financial growth and prosperity of the economy. The aim of this study is to determine the impact of accounting and audit service on Small and Medium scale Enterprise in Ogun State using a sample of small businesses and audit firms. Data used for this study were obtained from primary source through the administration of one hundred questionnaires (150) to small and medium scale operator out of which One hundred and twenty (120) questionnaires were recovered. The respondents were selected using random sampling technique. The study employed Chi square and ordinary Probit Regression analysis in investigate the impact of accounting and audit services on small and medium scale enterprises in ijobu ode local government areas. The study recommended that Small and medium scale enterprises should be encouraged to adopt sound accounting system and the cost of installing and operating such systems should be minimized. And also, accounting systems should bear relevance to the size and needs of small and medium scale enterprises and Accountants involved in the audit of small and medium scale enterprises should adopt methodologies that adequately capture the accounting and reporting needs of the enterprises and comment on their peculiarities, if necessary, in the audit report.*

**Keywords:** Accounting and Audit Services, SMEs, Probit Regression Analysis, Nigeria

### 1. INTRODUCTION

Small scale businesses are of great importance to the survival of an economy. They are to an extent an index of development and the wellbeing of the masses. Administrative management is very vital for the survival of any business. It is even more so with small businesses since the normal organizational structures are not very visible in small businesses. Management of personnel, use of accounting information and financing options are areas that must be taken seriously for effective management and survival of small businesses. The small scale business entrepreneurs find it extremely difficult to carry on business for certain number of factors ranging from lack of adequate capital to lack of management expertise. In order to solve these problems, both the Federal and the State Governments decided to come to the aid of the small scale business entrepreneurs by way of providing loans to them at very low rates of interest and also providing the management with consultancy

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services on several occasions. Despite these incentives, there were still frequent business failures among small scale enterprises in Nigeria.

In the recent past, a lot of innovative policies have been initiated and implemented by the Federal Government. The first was the policy of channeling 10 percent of banks' profits before tax into equity investment in small and medium industries. The bankers' committee launched the approved operational guidelines for Small and Medium Industries Equity Investment Scheme (SMIEIS) on August 1, 2001 under the scheme, banks are required to invest 10 percent of their profit before tax in small and medium scale industries of their choice in a partnership effort aimed at improving the flow of funds to revitalize the real sector of the economy (CBN, 2002).

Despite these efforts, most small scale enterprises in Nigeria still fail mostly because of inadequate administrative management expertise. Some small scale enterprises could not boast of adequate accounting standard that is capable of providing information on the activities and decision process of the enterprise. Without proper knowledge of accounting, one will find it difficult to provide adequate administrative management that will ensure the survival of small scale enterprises in Nigeria. Baridam (2004) is of the view that a small scale business is one which possesses at least two of the following characteristics: (a) management, usually the managers are also the owners, (b) capital is supplied and the ownership is held by an individual or small group; (c) the area of operation is mainly local, (d) the relative size of the firm within its industry must be small when compared with the biggest units in its field. Aborode (2005) defines small scale enterprises as an enterprise with a labor size of 11 - 100 workers or a total cost of not more than N50 million, including working capital but excluding cost of land. Nwoye (2004) observes it as enterprises employing between 1 - 35 people. They utilize by-products or intermediate products from larger firms. They also utilize local raw materials. The importance of small scale enterprises can be seen in the vital role, which they play in the development of the economy.

The relevance of accounting information and the operation of a business organization and society can be established by looking at the ways accounting information has helped small scale firms to improve on their performance. The role of accounting information on the improvement of the performance of small scale firms are: (i) as a tool for control. It was probably the control aspect of book-keeping which helps to guard against the petty dishonesty and incompetence commonly displayed by employees of small scale enterprises. Business organizations normally have numerous assets, for example, cash, stock of goods, furniture, buildings, machinery, etc. It is imperative in all that a proper accounting system should be installed to ensure that each and every item is accounted for with a view to reducing opportunities for theft and misappropriation and to ensure economic expenses as the employees knowing that every item has been accounted for, will be careful in handling all business properties; (ii) Assistance in credit dealings.

Most of today's businesses are conducted on credit basis. A trader, more often than not finds himself with two alternatives either to extend credit facilities to his customers; (iii) Assisting in taxation matters. The government charges taxes of various types e.g. sales tax, local tax, custom duty, excise duty, etc., to be able to calculate and pay the correct amount of tax due, an entrepreneur must know his exact sales figure hence the need for accurate accounts. Absence of proper accounts can easily lead to over taxation, a situation which can be very unpleasant; and (iv) Assistance in determination of profit. The ultimate objective of all business undertakings is to make profit. It would be difficult to ascertain whether a business is making profit or loss without the help of complete up-to-date accounts.

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An accounting and auditing service system is an orderly, efficient scheme for providing accurate financial information and controls. Regulatory requirements and internal administration policies are key considerations in the design of an effective accounting system. Thus accounting and auditing service systems show the books, records, voucher, and files and related supporting data resulting from the application of the accounting process. It involves the design of documents and transactions flow through an organization. The uniqueness of small and medium scale businesses call for careful consideration in the design of accounting systems. Small and medium scale enterprises are a vast majority of businesses found in variety of primary and intermediate production of the economy. These establishments have tremendous impact on the state and well-being of the nation in employment generation, as sources of national outputs and revenues, providing feedstock for large corporations. They may lack the sophistication to apply the detailed accounting processes, yet the value of accounting and auditing service systems to these businesses is quite profound.

Accounting and auditing services are essential for the running or operation of a small business inasmuch as financial and human resources are involved. The salon or stationary store operator must keep accounting records of his/her business if the business is to succeed amidst competitors. In order to control his or her operations the small business owner needs to have a good understanding of financial statements and the basic fundamentals of accounting record keeping. This is very vital for the effective running of the business. The financial statement and the accounting records kept are interdependent because the financial statement is usually generated from accounting records. The financial statements of a company or business enterprise include the Balance Sheet, the Income Statement (Profit and Loss Account) and the Cash Flow Statement.

However, other financial statements according to Izedonmi (2000) include Note to the Account, Statement of Accounting Policies, Value Added Statement and Directors' Report. In auditing small businesses, the essential financial statements can be the balance sheet, income statement (Profit and Loss account) or cash flow statement. Ayozie (1990) a financial statement is the summary of the transactions of a business entity for a given period of time. The income statement is traditionally called the trading and profit and loss account. This is a financial statement that shows or reports the success (profit) or failure (loss) of a business during a period. The profit and loss account shows the results of the flow of activity and transactions and is designed to report the profit performance of a business for a specified period of time. The period could be one month, a quarter or a year. But most income statements are one year. The income statements report the revenues, i.e. gross sales and expenses made by the business over a period. No business can achieve its goals without cash.

Accounting to Glautier and Underdown (2001), cash is the lifeblood of a business. Glautier viewed that a healthy cash flow statement (measured as cash inflows minus cash outflows) is fundamental to a business's ability to survive and prosper. The cash flow statement is a financial statement that shows the inflows and outflows of cash for a particular period of time. The cash flow statement provides an insight into how the cash generated by a business were spent and the level of the liquidity of the business entity. According to Campbell (2009), "small business accounting covers issues and tools relating to accounting and bookkeeping for a small business". Small business accounting includes cash flow and related finance issues; tax record keeping; accounting software; billing and invoicing applications. Small businesses like large ones have financial goals. Their business operations have to be looked through by a professional accountant to best advise them on how to reach their financial goals. A small enterprise can

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improve its business operations internally and externally by engaging the services of a professional accountant that may include the auditor to audit the business. The audits can be financial audit, private audit, management audit and so on depending on the aspect of the business its owner deems necessary to be examined.

A financial audit is a thorough analysis of a firm's past and current financial position designed to verify and evaluate the effectiveness of its financial operations. It can help management detect circumstances that could lead to financial problems in the future. A management audit is much broader in scope than a financial audit. A management audit aims at detecting potential managerial problems in the small enterprise that threaten its existence. Frequently a small business manager is so closely involved in the firm's operation that he never recognizes its primary problem areas. Given its broad scope and inherent benefits, a management audit can best be suitable for small scale businesses.

A small business management audit is useful to an auditor in performing consulting services for small businesses. It offers pertinent suggestions for improving managerial and business performance if properly used. There are vital questions designed to assist the small business owner or manager in sincerely and honestly evaluating strengths and weaknesses and defining opportunities and potential difficulties in his business. Another aspect of the audit of a small business is strategic planning. Planning is very necessary for a small business. The small business operator should know the kind of business that is operated and have a written description of his target market. Knowing where the production or service is aimed facilitates the creation of a unified "theme" for any business (Campbell, 2009). The potential opportunities for increased sales and profits for the business should be identified. New products, new markets, or new locations could generate more business for the small business if management has the capacity to reach them.

Small scale enterprises play a vital role in the economic development of any country. In Nigeria, the management of these enterprises has been constrained by lack of knowledge of accounting and audit services by the stakeholders. There has been controversy over the years between accounting, audit services and business enterprises in determining the success of a small scale enterprise. Accounting and audit services are both critical influences to the success of small scale enterprise because they are part of the successive factors that can influence, affect and impact on a small scale enterprise.

According to Okoh and Uzoka (2012). They observed that most small scale enterprises in Nigeria still fail mostly because of adequate administrative management expertise. Some small scale enterprises could not boast of adequate accounting standard that is capable of providing information on the activities and decision process of the enterprise. Without proper knowledge of accounting, one will find it difficult to provide adequate administrative management that will ensure the survival of small scale enterprises in Nigeria. Some of the causes of failure have been traced to lack of knowledge of proper accounting system. The place of sound accounting and audit services in any business, irrespective of its scale, cannot be overemphasized even if they would have. Hence, the existence of single entries in their books and in some cases incomplete records (Onaolapo, 2011). Audits of small and medium scale enterprises have proven to be among the most worrisome for professional accountants because of the inadequacy of the internal controls. Except for statutory demands, small and medium scale enterprises hardly give serious thoughts to the process of sound accounting, yet the inadequacy and ineffectiveness of accounting processes have been responsible for untimely collapse of a host of them (Mukaila and Adeyemi,

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2011). The general objective of this study is to examine the impact of using accounting and audit service for business decision making.

## 2. LITERATURE REVIEW

This contains all the literature review on the impact of accounting and audit service on Small and Medium Scale Enterprise. This will be divided into three categories which are Conceptual Framework, Theoretical Background and the Empirical Background of the subject matter. In recent years, as part of the economic reforms in Nigeria, there has been a switch of emphasis from the grandiose capital intensive, large-scale industrial projects to small/medium scale enterprises with immense potentials for developing domestic capacity for rapid substantial industrial development (Dasanayaka, 2009). Determining the scale of operations and structure of small or medium scale enterprises is crucial. Among the notable indicators are independent management (independent of any other party, except from the owners) mostly dominated by the sole proprietorships, partnerships and private limited company. But Nigerians favor “one-man” business for lack of trust. Most small/medium scale enterprises are located in the interiors of the nation. Flexibility of administration is another important feature of small/medium scale enterprise.

This has greatly enhanced their productivity and profitability because administrative bottlenecks are totally absent. Adaptability to customers’ needs enhances competitiveness. (Olatunji, 2000; Aroma and Adeyemi, 2011) Other considerations include organizational manpower, limit on capital investment, annual turnover, management structure, as well as the assessment of size of particular enterprises. (Olatunji, 1995; Safiriyu, 2012) explains the relativity of such descriptions. Section 351 (1) of CAMA 1990 describes the small company as “a private company having a share capital; the amount of its turnover for the year in question should be a maximum of #2 million, or such amount as may be fixed by the commission; the net assets value is not more than #1 million; none of its members is alien, government or a government corporation; the directors should hold at least 5% of its equity shares capital. The National Economic Reconstruction fund (1989) defined small scale enterprises are those with fixed asset other than land but inclusive of the cost new investment not exceeding #10 million. The Central Bank of Nigeria (2004), defined a small scale enterprises “as one whose capital investment does not exceeding N5 million (including land and working capital) or whose turnover is not more than #25 million annually. In the bid to increase its share of world’s industrial production (about 25%) by the year 2000 and (about 40%) by the year 2010 as recent world industrial production statistics show, developing economies are increasingly focusing small and medium scale businesses (Okafor, 1999; Akwaese, 1987) the united Nations industrial development organization (UNIDO, 1980). It has been discovered that lots of small and medium scale enterprises shut down before they can achieve their goals a result of poor management arising from inadequate weak and undependable accounting and financial information. (Olatunji, 2000; Safiriyu, 2012).

As observed by Wood (1979), many small businesses can have all the information they want by merely keeping a cash book and having some form of records, not necessarily in double entry system. (Vickery and Mendes, 1973; Olaoye, 2012). This is an aberration and requires a conversion to double entry system for meaningful reporting (Adebisi and Azeez, 1999; Olatunji, 1995; Onaolapo, et al. 2011). The mechanics of the conversion involve the preparation of a statement of affairs and estimation certain data for the updates of full set of ledgers and henceforth a complete double entry system is installed. (Pickles and Lafferty, 1974). The challenge is amplified by the audit requirements for small companies (Millichamp, 1984) observed that in most small companies accounting and financial management are

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carried out by just one person, making segregation of duties impracticable or irrelevant. Controls may have to depend on the close involvement of the owners in the management of the business and to extent of their integrity. This calls for an adaptation of accounting systems to need of these businesses (Abeygunasekera and Fonseka, 2013).

## **2.1 Theoretical Framework**

### **2.1.1 Agency Theory**

Agency relationship could be defined as a contract among the organization owner(s) and its top management work with the organization as agents to perform some service on behalf of owners who delegate some decision making authorities to managers. These authorities could be misused by managers to meet their own personal interests. Therefore, the existence of the audit committees and the external and internal auditors will help the organization in enhancing their performance, and also will ensure that the management carries out its plans according to procedures (Adams, 1994). Peurseem and Pumphrey (2005) considered internal auditors as agents and monitors for a variety of the internal audit users that include the board, audit committee and senior management. Agency problems could occur when the board or its audit committee is inefficient, and hence, the senior management is likely to be a powerful influence over the internal audit. This complex web creates an inherent dilemma for the internal audit: how can it carry out their monitoring role over management if it is ineffective itself? Internal auditors often are employed by senior management, but at the same time, they are also agents of the board and audit committee who trust in the internal auditors' ability to evaluate senior management's works.

However, internal auditors may have varying motives to act against the board of directors' interests and its audit committee and these motives include financial rewards from managers, personal relationships with them, and the power of senior management in shaping the future position of internal auditors and their salaries. In such a work environment, internal auditors as agents may have an incentive to be bias of information flows, which leads to new concerns of the board and audit committee about their trust on the internal auditors' objectivity, and preventing such threats of objectivity becomes necessary for the board and its audit committee. Internal auditors as agents must perform audit processes at the professional level requiring education and professional certifications, experience, and other competencies needed to perform their responsibilities perfectly. Having internal auditors with such requirements and the existence of training programs for internal auditors, would increase the confidence level of the board and audit committee in the internal auditor competence.

### **2.1.2 Institutional Theory**

Institutional theory explains how organizational structures and practices are shaped through changes induced by normative pressures, including both external and internal sources such as laws and regulations, or by the professions (Zucker, 1987; Mihret et al., 2010). Similarly, Arena and Azzone (2007) identified the following external forces that impact both individuals and organizations:

- i. laws and regulations (coercive isomorphism);
- ii, choices of other organizations (mimetic isomorphism); and
- iii. consultation or professional bodies (normative isomorphism).

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Several previous studies in internal audit have adopted an institutional theory (Al-Twajjry *et al.*, 2003; Arena & Azzone, 2006; Arena & Azzone, 2007; Mihret *et al.*, 2010). Al-Twajjry *et al.* (2003) adopted the isomorphic perspective to investigate internal audit in Saudi Arabia, and the institutional theory is employed to explain their findings regarding the establishments of internal audit and the role of the government in promoting their development. Similarly, Arena and Azzone (2006) focused, on the coercive isomorphism, to investigate the development of internal audit in six Italian companies as a multiple case study. Their findings confirmed that the adoption and development of internal audit were impacted by the coercive, mimetic and normative pressures. More recently a study by Arena and Azzone (2007), based on survey involving 364 Italian companies, found that the isomorphic pressures have a significant impact on the companies' support of internal auditing.

### 2.1.3 Communication Theory

In accordance with the needs of the IIA as the professional body that takes care of internal auditing, several studies such as by Davidson (1991), Quinn and Hargie (2004) and Golen (2008), confirm the importance of and the need for effective communication skills in all organization functions. Studies done by Lewis and Graham (1988) and Smith (2005) suggested some ways to improve these communication skills. Previous studies by Hahn (2008) and Golen (2008) discussed communication barriers and how they can be overcome. At the same time, several previous studies have dedicated their work to communication in organizations. These studies evidenced that, effective communication and interpersonal relationships between managers and staff have a strong contribution to improve profitability, and productivity; and it leads to higher quality of services and products, and reduction in costs (Clampitt & Downs, 1993). According to both IIA Standards and previous studies, the study of effective communication in internal auditing is necessary, and hence this study should consider the communication theory for its achievement. Davidson (1991) confirms that, all auditors can benefit from knowledge of current communication concepts, and even those who believe they are good communicators need to work consciously on assessing, improving, and applying their skills. Davidson's communication theory is based on three basic truths about communication. These are:

- i. It is impossible not to communicate;
- ii. Communication is a multilevel phenomenon,
- iii. Message sent does not always equal message received.

Hahn (2008) confirmed that much information is as bad as little information because it reduces the receiver's ability to concentrate effectively on the most significant messages. In such an environment, internal audit users may have new concerns about their trust for internal auditors' performance. Thus, effective communication becomes necessary as a solution to this problem. To overcome such communication problems, Hahn (2008) recommends parties of the communication process to focus and offer only the necessary information by easy ways - provide meaning to the information rather than just pass on the message, and keep the information clear and simple to understand and finally ask for feedback. The existence of effective communication between internal auditors themselves, internal auditors and auditee internal auditors and organization members, without any doubt, is needed to strengthen the internal audit effectiveness. As has been pointed out earlier, agency theory can explain and cover the importance of having an effective communication between organization members and internal auditors as agents to them. However, the importance of effective communication in this study extends to include the relationship between internal auditors and auditees,

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which can be explained under the communication theory. In this study, effective communication is one of the main factors for the effectiveness, which is measured by examining the relationship with auditees.

#### **2.1.4 Linking Theories of the Study**

Research in auditing has traditionally been conducted under the framework of agency theory (Pilcher et al., 2011). However, Mihret et al. (2010) argued that the neoclassical economic theories including agency theory were the main reason for limited research in internal auditing. They criticized the assumption that organizational phenomena are only driven by maximizing the self-interest of individuals, and they confirmed that the behavior of individuals cannot be abstracted from the social settings. Thus, they suggested institutional theory. The use of more than theory in combination enables considering social and behavioral aspects and the economic dimensions. Several previous studies have adopted both agency and institutional theories (Yamak & Suer, 2005; Christopher et al., 2009; Yaqi et al., 2012). In this study, while agency theory is mainly employed to understand economic motives that make internal auditors seek in achieving their personal interests even if they were against the organization members' interests or organizational interests, institutional theory informs about the level of compliance with ISPPA, and its impact on the companies' support of internal audit. Moreover, communication theory is used to explain the importance of effective communication between internal auditors and auditees.

#### **2.2 Empirical Framework**

The critical role of computers in modern business prompts enterprises to take special measures in order to protect their information systems and ensure their accurate and safe function. The combination of automated and non-automated procedures with the aim to protect information systems is called auditing. Information systems audit includes the methods, the policies and the procedures that provide information assurance and security, assets safeguard, data integrity maintenance, and compliance with law and regulations. Moreover, these procedures manage to mitigate risks concerned with the use of information technology by organizations, and to minimize the damage caused from computer errors electronic crime and security breaches.

Rezaee and Reinstein, (1998) studied the impact of informational technology on auditing activities. Their study was centered on the key issues of SAS No. 80 that offer auditor's guidance to obtain sufficient evidence so that they evaluate their clients' information systems. Rezaee and Reinstein (1998) argued that information technology contributed to the simplification of information entry into the transactions and the overall processes. Also, according to Rezaee and Reinstein, (1998) due to information technology, the evaluation of the related controls and results became more critical. To accumulate sufficient evidence and therefore make informed decisions, answers must be given to certain questions, such as where to look for that evidence, what auditing processes to take into consideration and how to evaluate these processes. Through the report published in 2000, the Public Oversight Board expressed concerns about the ability of auditors to properly assess the risks arising from rapid changes in information systems.

The POB encouraged auditors to expand their knowledge of information systems, hoping to help themselves with the development of more effective audit approaches. Furthermore, the POB recognized the need to attract and keep qualified technical IT specialists for the audit function and confirmed that more and more auditors would find out that it is necessary to fully understand the risks associated with new and advanced information systems as well as the controls that are needed to address those risks.

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Hermanson, *et al.* (2002) conducted a survey to examine internal auditors' activities related to information technology, in U.S.A. companies. The evidence gathered from more than 100 directors of internal auditing showed that internal auditors focus primarily on "traditional risks and audits, such as safeguarding of IT asset, data integrity and security, while giving little attention to other risks such as those related to systems development and acquisition. According to the results, many factors affect the internal auditors' performance of IT evaluation, including the nature of the audit target, the prevalence of specific information\ systems audit specialists on the internal audit staff and the availability of new information systems.

Rishel and Ivancevich, (2003) claimed that the basic responsibilities of internal auditors had to do with risk management issues and control especially during the pre-implementation and monitoring phases of informational technology projects. Through their study, they argued that internal auditors should pay attention to system configuration and IT implementations to ensure that adequate controls are performed. Additionally, internal auditors should communicate with the IT department to assure that not only new systems but also modifications to existing systems are well documented, as proper documentation is essential to internal audit in terms of evaluation of risks and controls. In the same period, Meredith and Akers (2003) conducted a survey to investigate whether consulting affects the independence of the internal audit function. They surveyed 241 chief executive officers (CEOs) and examined their opinions on internal audit's involvement in systems development, and particularly they examined whether such involvement sets in danger the independence of internal auditors and if auditors should act as consultants for systems development projects. The results revealed that what interests CEOs more is the maintenance of internal audit function's independence even if the internal auditors act as consultants. Respondents were unconcerned about internal audit's involvement in the planning and design phases and did not support its involvement in the development, implementation and maintenance phases. The results of the comparison of perceptions between CEOs and chief audit executives (CAEs) revealed that there are significant differences between these two categories regarding their expectations. CEOs considered independence to be the most important matter, while CAEs emphasized the need for internal auditors to act as consultants.

Hadden *et al.* (2003) investigated the IT qualifications and activities of audit committees, internal and external auditors with regard to IT risk management. The results of the study suggested that audit committees appear to offer limited supervision of IT-related risks, while they do believe that they should take a more active role in this field. As for internal auditors, the results revealed that their involvement in information technology oversight was rated as "above average", while the respective involvement of the external auditors was rated as "moderate". One year later, Hunton *et al.* (2004) carried out a research in order to examine, understand and assess the extent to which financial auditors and information systems auditors are able to identify the audit risks associated with ERP systems. The results revealed that financial auditors are less interested in ERP risks compared to information systems audit specialists, while the second ones dispute financial auditors' ability to identify risks associated with ERP systems, something which could have negative effects on audit quality. The threats of computerized accounting information systems (CAIS) in Saudi companies were examined by Abu-Musa (2006).

### 3. METHODOLOGY

The study employed descriptive survey and qualitative research design approach, in order to examine the impact of accounting and audit services on small and medium scale enterprises. The study used questionnaires to elicit information from the target group.

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### 3.1 Model Specification

The model adopted for this study is based on the components of accounting and audit services following the work of Olutunji (2013) and Samson, et. al. (2012). The later work on the impact of accounting system on the performance of SMEs in Nigeria while the former worked on the demand and supply of accounting and audit services to Small and Scales business in Nigeria. Hence, the components of accounting practices are: qualified personnel (QP) and record keeping (RK) while, the components of audit service reviewed in the literature are: audit fees (AFE), fear of taxes (FT) and government interference which was proxied by audit fears (AUF). The model used for the study is described as small and medium scale performance being a function of accounting and audit services. The model used for this study is specified as:

$$SMEsP = f(\text{Accounting Services, Audit Services}) \dots \dots \dots \text{Equation (i)}$$

$$SMEsP = \beta_0 + \beta_1QP + \beta_2RK + \beta_3AFE + \beta_4FT + \beta_5AUF + \xi \dots \dots \dots \text{Equation (ii)}$$

Where:

SMEsP= Small and Medium Scale performance

QP= Qualified Personnel

RK= Recording Keeping

AFE= Audit Fees

FT= Fear of Taxes

AUF= Audit Fear

$\xi$ = Error Term

Where  $\beta_0$  is the constant and  $\beta_1 \dots \dots \dots \beta_5$  are the parameters of the variables to be estimated and  $\xi$  is the error term that is normally distributed with a mean of zero and a constant variance.

### 3.2 Sample and Sampling Techniques

The researcher randomly select five major areas in Ijebu ode metropolis and they are: Ijegun, Choice; Lagos Garage; Oke Aje and Ita OsunThe justification of this area was based on the definition of SMEs adopted for the study. The study adopted the definition put forward by Amoako (2012) as the basis for the study. He defined Small scale business as enterprises that employ less than 10 persons while medium scale business as enterprises that employ less than 50 persons. Based on this criterion, One hundred and fifty (150) SMEs Operators were the sample used for this study covering five major markets in Ijebu Ode Local Government Areas of Ogun State. A stratified sampling technique was used by classifying SMEs into various strata based on types of businesses and they are: poultry, fishing, retail trade, service and agro-allied. Random and accidental sampling techniques was also employed in the study in choosing the respondents used in the study.

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### 3.3 Research Instrument

The study used self-structured questionnaire and records to elicit information from the respondents about the defined problem so that the data, after analysis and interpretation would result in a further appreciation of the problem. The questionnaire had two sections “A” and “B”. Section “A” contained questions on demographic characteristics of the respondents; while section “B” contained items which specifically measured the research questions in the study. In this part, the respondent were required to answer “Strongly Agreed”, “Agreed”, “Strongly Disagreed” and “Disagreed” to a number of questions. Closed and open ended types of questionnaires were raised in the study

### 3.4 Method of Data Analysis

The method of data analysis was based on the nature of data used for the study. Factor analysis as used to investigate the importance of accounting and audit practices on small and medium scale enterprises, binary probit regression analysis was used to investigate the impact of accounting and audit services on small and medium scale enterprises and the justification of this statistical tools was based on the fact that the dependent variables (small and medium scale performance) used in the study is a binary choice responses i.e (poor and excellent performance). Descriptive statistics such as simple percentage was also to analyze the demographic questions and questions related to accounting and audit practices raised in the study while, Chi-square estimation techniques was also used to determine the relationship between poor audit services and SMEs failure. Stata 11 software statistical package was used to achieve the objectives of the study.

### 3.5 Sources of Data

Primary source of data collection were majorly employed in the study, examples of such are: questionnaires, interview and observations. Secondary source includes Journals, Newspapers and publications.

## 4.0 RESULTS AND FINDINGS

This section focuses on data presentation, analysis and interpretation. Inferential Statistics such as the simple percentage were used to analyze the demographic questions of the respondents and also some questions related to the impact of accounting and audit practices on small and medium scale enterprises performance. Factor analysis was used to investigate the importance of accounting and audit service on small and medium scale enterprises, binary probit regression analysis was also used to examine the effect of accounting and audit on performance of small and medium enterprises while spearman rank correlation was also used to examine the relationship between poor audit services and SME’s failure, using Ijebu Ode as a case study. Pre estimation test such as reliability test such as Cronbach alpha was also used to validate the instrument of data collection used of the study.

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**Table 1: Questionnaires Distribution Analysis**

Questionnaire	Respondents	Percentage
Returned	120	80
Not Returned	30	20
Total	150	100

**Source:** Field Survey, (2017)

Table 1 shows that out of 150 copies of questionnaires distributed to various small and medium scale operators covering five major market areas such as Ijebu, Choice, Lagos Garage, Oke Aje and Ita Osun in Ijebu Ode metropolis, it was revealed that 120 respondents which form about 80 percent of the total copies of questionnaire distributed were duly returned while 30 respondents which form about 20 percent of the total copies of questionnaires distributed were not returned by the respondents.

## 4.2 Pre-estimation Test

### Table 2 Reliability test

The Cronbach alpha is used to test the reliability for the data collected for the study:

Average interitem covariance	Number of items in the scale	Scale reliability coefficient
.2018616	6	0.7890

Source: Author's Computation, (2017)

The alpha coefficient for the three items is 0.7890, suggesting that the items have relatively high internal consistency. It is equally to note that a reliability coefficient of 0.70 or higher is considered acceptable

## 4.3: Demographic Analysis

### Table 3: Gender Distribution of Respondents

Options	No. of Respondent	Percentage
Male	45	37.5
Female	75	62.5
Total	120	100

**Source:** Field Survey, (2017)

The table above shows that 37.5% representing about 45 respondents were male sampled for the study, while 62.5% representing about 75 respondents were female respondents sampled for the study.

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This result indicated that the number of female small and medium scale operators is higher than that of male in Ijebu ode metropolis.

**Table 4: Marital Status of Respondents**

Options	No. of Respondent	Percentage
Single	23	19
Married	59	49
Divorced	21	18
Widow	17	14
Total	120	100

**Source:** Field Survey, (2017)

In the above table, it is seen that majority of the respondent are married and this represent about 49% of the total respondent, 19% respondents of the sampled respondents were single, 18% respondents are divorced, while 14% of the sampled respondents which form about 17 respondents out of the total 120 respondents are widow. This shows that a larger percentage of respondent sampled in the study which comprises of SMEs operators in Ijebu ode metropolis are married.

**Table 5: Age Distribution of Respondents**

Options	No. of Respondent	Percentage
18- 25	16	13
26- 35	45	38
36- 45	33	28
46 and above	26	21
Total	120	100

**Source:** Field Survey, (2017)

The table 5 above shows the age distribution of the sampled respondents. The table revealed that 13% representing 16 respondents fall within between (18-25) year, 38% representing 45 respondents falls within the age of (26–35) year, 28% representing 33 respondents falls within the age (36-45) years, while 21% of the total respondent falls within the age bracket of (46 years and above). This shows that a larger percentage of respondent sampled in the study which consists SMEs operators in Ijebu ode metropolis falls within the age bracket (36-45). This result indicated that the sampled respondents are vast in their level of exposure to small and medium businesses as a whole.

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**Table 6: Educational Background of the Respondents**

Options	No. of Respondent	Percentage
Primary school	18	15
Secondary school	40	33
Tertiary school	50	42
Postgraduate school	12	10
Total	120	100

**Source:** Field Survey, (2017)

The above table shows that 15% representing 18 respondent reported that primary school was their highest educational qualification, 33% representing 40 respondents reported that secondary school was their highest educational qualification, 42% representing 50 respondents also reported that tertiary school was their highest educational qualification, while 10% of the total respondent only had postgraduate school as their highest educational qualification. This table revealed that majority of the sampled respondents consisting of SMEs operators in Ijebu ode metropolis are graduates of various tertiary institutions. This therefore implies that the majority of the responses from the sample respondent were accurate and reliable as they were educated and they understood the implications as well as the importance of accounting and audit practices.

#### 4.4 Questions Relation to Accounting and Audit Practices on Small and Medium Scale Enterprises

**Table 7: Distribution of responses as to whether good financial reporting enhances small and medium scale enterprises performance**

Options	No. of Respondent	Percentage
Strongly Agree	42	35
Agree	59	49
Disagree	14	12
Strongly Disagree	5	4
Total	120	100

**Source:** Field Survey, (2017)

The table above shows that the distribution of responses as to good financial reporting enhances small and medium scale enterprises performance. It was revealed that 35% of the sampled population strongly agrees to the statement, 49% of the total respondents also agree to the statements while 12% of the sampled respondents disagree to the statement and also 5% of the sampled respondents strongly disagree to the statement. This table showed that majority of the sampled respondents which form about

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84% of the sampled respondents indicated that good financial reporting enhances small and medium scale enterprises performance.

**Table 8: Distribution of responses as to whether audit problems of small and medium scale enterprises affects credibility of accounting practices**

Options	No. of Respondent	Percentage
Strongly Agree	29	24
Agree	31	26
Disagree	28	23
Strongly Disagree	32	27
Total	120	100

**Source:** Field Survey, (2017)

The table above shows that the distribution of responses as to whether audit problems of small and medium scale enterprises affects credibility of accounting practices. It was revealed that 24% of the sampled population strongly agree to the statement, 26% of the total respondents also agree to the statements while, 23% of the sampled respondents disagree to the statement and also 27% of the sampled respondents strongly disagree to the statement. The table revealed that 50% of the sampled respondent agree to the statements while 50% of the sampled respondents also disagree to the statements and this indicated that there is equal percentage of responses as to whether audit problems of small and medium scale enterprises affects the credibility of accounting practices. This study is indifferent based on the opinion of the sampled respondents.

**Table 9: Distribution of responses as to whether excessive cost of implementing accounting systems prevent adoption of accounting system**

Options	No. of Respondent	Percentage
Strongly Agree	52	43
Agree	49	41
Disagree	6	5
Strongly Disagree	13	11
Total	120	100

**Source:** Field Survey, (2017)

The table above shows that the distribution of responses as to whether excessive cost of implementing accounting systems prevent adoption of accounting system. It was revealed that 43% of the sampled population strongly agrees to the statement, 41% of the total respondents also agree to the statements while 5% of the sampled respondents disagree to the statement and also 11% of the sampled

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respondents strongly disagree to the statement. This table showed that majority of the sampled respondents which form about 84% of the sampled respondents indicated that excessive cost of implementing accounting systems prevent adoption of accounting system

**Table 10: Distribution of responses as to whether sound accounting records and audit practices by small and medium scale enterprises facilitates effective decision making**

Options	No. of Respondent	Percentage
Strongly Agree	58	48
Agree	62	52
Disagree	0	6
Strongly Disagree	0	13
Total	120	100

**Source:** Field Survey, (2017)

The table above shows that the distribution of responses as to whether sound accounting records by small and medium scale enterprises facilitates effective decision making The table revealed that 48% of the sampled population strongly agree to the statement and also 52% of the total respondents also agree to the statements that sound accounting records by small and medium scale enterprises facilitates effective decision making. This table showed that all the sampled respondents which form about 100% reported that sound accounting records by small and medium scale enterprises facilitate effective decision making.

## 4.5 Hypothesis Testing

### 4.5.1 Factor Analysis

**Table 11: Determine the importance of accounting on small and medium scale enterprises.**

Variables	Factor Loading	Rank	Mean	Rank
Accuracy	0.332	3	4.23	3
Reliable	0.467	1	5.14	1
Timely	0.863	2	8.53	2
Relevant	0.887	4	9.91	4
Consistent	0.686	6	8.11	6
Clear	0.513	5	7.65	5

Source: Author's Computation, (2017)

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The table 11 above shows top six importance of accounting on small and medium scale enterprises on the basis of factor loading and arithmetic mean. On the basis of factor loadings, ranking of top six variables is in such manner: Reliability is first; Timeliness is second; Accuracy is third; Relevant is fourth; clearly is fifth while, Consistent is sixth. On the other hand, on the basis of arithmetic mean, Reliability is first; Timeliness is second; Accuracy is third; Relevant is fourth; clearly is fifth while, Consistent is sixth. Based on the result above, the factor loading and arithmetic mean ranking were the same.

**Table 12: Determine the importance of audit services on small and medium scale enterprises.**

Variables	Factor Loading	Rank	Mean	Rank
Business objectives	0.412	1	5.23	3
Risk of misstatement	0.517	3	6.14	2
Fraud prevention	0.993	2	7.23	1
Cost of capital	0.786	4	8.01	4

Source: Author's Computation, (2017)

The table 12 above shows top four importance of audit services on small and medium scale enterprises on the basis of factor loading and arithmetic mean. On the basis of factor loadings, ranking of top four variables is in such manner: a business objective is first; fraud prevention is second; risk of misstatement is third while cost of capital is fourth. On the other hand, on the basis of arithmetic mean: fraud prevention is first; risk of misstatement is second; business of objectives is third while, cost of capital is fourth. Based on the following, there are little differences on the ranking basis; the result revealed that the two basis factor loading and arithmetic mean ranking were not the same. Based on the result shown in table 11 and table 12 above, It was discovered that the importance of accounting on small and medium scale enterprises are accuracy, timeliness, reliability, relevance, clearly and consistent while, the importance of audit services on small and medium scale enterprises are fraud prevention, risk of misstatement, business objectives and cost of capital.

#### 4.5.2 Binary Probit Regression

**Table 13: Summary Statistics of Result**

Variables	Coefficients	dy/dx	Prob Value	Prob- F	Cut1
QP	1.1693	0.0667	0.023	0.0871	1.0346
RK	1.68833	0.034	0.039		
AF	-0.06125	0.02415	0.008		
FT	-0.1368	0.05595	0.082		
AUF	-0.3431	0.1352	0.008		
CONSTANT	1.3047		0.026		

Source: Author's Computation, (2017)

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#### 4.6 Presentation of Result

$$\text{SMEs P} = 1.3047 + 1.1693\text{QP} - 1.68833\text{RK} - 0.06125\text{AF} - 0.1368\text{FT} - 0.3431\text{AUF}$$

#### 4.7 Interpretation of Result

The Prob>chi2 shows a value of 0.000, indicating that the model is statistically significant at 1%, 5% and 10%. The coefficient of qualified personnel (QP) is significant at 10 percent in explaining the variation in small and medium scale performance in Ijebu ode metropolis, the result shows that there is a positive relationship between qualified personnel (QP) and small and medium scale performance, giving a value of 1.1693. The marginal effect shows that if there is an increase in qualified personnel involved in accounting practices by small and medium scale enterprises, the probability that it will influence small and medium scale enterprises performance in Ijebu ode metropolis is 0.06 percent.

The coefficient of record keeping (RK) is significant at 5 percent in explaining the variation in small and medium scale performance in Ijebu ode metropolis, the result shows that there is a positive relationship between record keeping and performance of small and medium scale, giving a value of 1.68833, This implies that it is more likely to report a higher category of small and medium scale performance (excellent performance) using the threshold i.e (cut analysis) since the value of the coefficient is greater than /cut1. The marginal effect shows that an increase in record keeping will increase the probability of influencing the performance of small and medium scale enterprises in Ijebu ode metropolis by 0.034 percent.

The coefficient of audit fees (AFE) is significant at 1 percent in explaining the variation in the performance of small and medium scale enterprises in Ijebu ode metropolis, the result also shows that there is a negative relationship between audit fees (AFE) and performance of small and medium scale businesses, giving a value of -0.06125 and this is likely to report a lower category of small and medium scale performance (poor performance) as it cannot extend to (excellent performance) using the threshold i.e (cut analysis) since the value of the coefficient is lesser than /cut1. The marginal effect signals that an increase in audit fees will necessarily decrease the probability of influencing the performance of small and medium scale businesses in Ijebu ode metropolis by 0.02415 percent.

The coefficient of fear of taxes (FT) is significant at 10 percent in explaining the variation in the performance of small and medium scale enterprises in Ijebu ode metropolis, the result shows that there is a negative relationship between fear of taxes and performance of small and medium scale enterprises, giving a value of -0.1368 and this is likely to report a lower category of small and medium scale performance (poor performance) as it cannot extend to (excellent performance) using the threshold i.e (cut analysis) since the value of the coefficient is lesser than /cut1. The marginal effect shows that an increase in fear of taxes will necessarily decrease the probability of influencing the performance financing of small and medium scale businesses in Ijebu ode metropolis by 0.05595 percent.

The coefficient of government interference proxied by audit fears (AUF) is also significant at 1 percent in explaining the variation in the performance of small and medium scale enterprises in Ijebu ode metropolis, the result shows that there is a negative relationship between audit fears and performance of small and medium scale enterprises, giving a value of -0.3413. This implies that the coefficient of audit fears (AUF) is likely to report a lower category of small and medium scale performance (poor performance) as it cannot extend to (excellent performance) using the threshold

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i.e(cut analysis) since the value of the coefficient is lesser than /cut1. The marginal effect shows that an increase in audit fears will necessarily decreases the probability of enhancing the performance of small and medium scale enterprises in Ijebu ode metropolis by 0.1352.

#### 4.5.3 Chi-Square Statistics

**Table 14: Examine the relationships between poor audits services and SMEs failure**

Chi Square Calculated	Prob. Value	Observation
6.234	0.0000	120

*Source:* Author's Computation, (2017)

Degree of Freedom =  $(r-1)(c-1)$

Degree of Freedom =  $(4-1)(2-1)$

Degree of Freedom =  $(3)(1)$

Degree of Freedom = 3

Using 5% level of significance

Chi-Tabulated = 7.815

The table above revealed that calculated chi square is 6.234 while, the chi-tabulated is 7.815. The result from hypothesis shows that the chi-square calculated of 6.234 is lesser than the chi-tabulated of 7.815 at 5% level of significance. Thus, the null hypothesis which states that there is no significant relationship between SME's failure and audit services should not be rejected. This therefore implies that poor audit failure does not leads to SMEs failure.

The study discovered that there are significant importance of accounting and audit services on small and medium scale enterprises, this therefore implies that the null hypothesis which states that there are not significant importance of accounting and audit services on small and medium scale enterprises should not accepted, the study also revealed that there are significant effect of accounting and audit services on small and medium scale performance which also implies that the null hypothesis should be rejected while the third hypothesis which states that there is no significant relationship between SME's failure and audit services should not be rejected which implies that poor audit failure does not leads to SMEs failure.

## 5. CONCLUSION AND RECOMMENDATION

The study concludes that the number of female small and medium scale operators is higher than that of male in Ijebu ode metropolis, the largest percentage of respondent sampled in the study which comprises of SMEs operators in Ijebu ode metropolis are married and also the largest percentage of respondent sampled in the study which consists SMEs operators in Ijebu ode metropolis falls within the age bracket (36-45) which implies that they are vast in their level of exposure to small and medium businesses as a whole. The study also concludes that majority of the sampled respondents consisting of SMEs operators in Ijebu ode metropolis are graduates of various tertiary institutions, majority of the sampled respondents which form about 84% of the sampled respondents indicated that good financial

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reporting enhances small and medium scale enterprises performance, and also that 50% of the sampled respondent agree to the statements while 50% of the sampled respondents also disagree to the statements and this indicated that there is equal percentage of responses as to whether audit problems of small and medium scale enterprises affects the credibility of accounting practices. This study is indifferent based on the opinion of the sampled respondents.

The study further revealed that majority of the sampled respondents which form about 84% of the sampled respondents indicated that excessive cost of implementing accounting systems prevent adoption of accounting system and also that all the sampled respondents which form about 100% reported that sound accounting records by small and medium scale enterprises facilitates effective decision making. The study also concludes that the top six importance of accounting on small and medium scale enterprises are timeliness, accuracy, relevant, clearly, consistent and reliability on the basis of factor loading while reliability, timeliness, accuracy, relevant, clearly and consistent is sixth on the basis of arithmetic mean, while the importance of audit services on small and medium scale enterprises are business objectives, fraud prevention, risk of misstatement and cost of capital is fourth on the basis of factor loading while fraud prevention, risk of misstatement, business of objectives and cost of capital on the basis of arithmetic mean ranking.

The study also concludes that increase in qualified personnel involved and adequate record keeping has the probability of influencing small and medium scale enterprises performance in Ijebu ode metropolis while increase in audit fees (AFE), government interference (audit fear) and fear of taxes will decrease the probability of influencing the performance of small and medium scale businesses in Ijebu ode metropolis and also the study concludes that poor audit failure does not leads to SMEs failure.

Based on the following conclusions, the study recommends the following:

- (i). Small and medium scale enterprises should be encouraged to adopt sound accounting system and the cost of installing and operating such systems should be minimized.
- (ii). Accounting systems should bear relevance to the size and needs of small and medium scale enterprises and Accountants involved in the audit of small and medium scale enterprises should adopt methodologies that adequately capture the accounting and reporting needs of the enterprises and comment on their peculiarities, if necessary, in the audit report.
- (iii). Adherence to internal controls as laid down by management (even if guidance is obtained from professional accountants) is crucial to maintaining integrity of records. The roles of the professional accountant as consultants/part-time accountants are of immense value to entrepreneurs on how best to manage their business organizations for great results.
- (iv). Regulatory bodies, educational and financial institutions as well as other stake holders should organize periodic training on proper records keeping to SME owners/managers as well as regulate consultancy fee for easy access to consultancy services.
- (v). Small businesses should as a matter of urgency evolve suitable culture appropriate for their demand of professional services of accountants and auditors. This will adequately promote the financial performance of their businesses.

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(vi). Operators of small scale businesses should painstakingly correct their perception of accounting and audit services. This is a major factor that has limited the effectiveness and efficiency of auditors in Nigeria.

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