

Auditing and Sustainability Prospect of Micro, Small and Medium Enterprises in Nigeria

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Abstract

Auditing of Micro, small and medium enterprises (MSMEs) have witnessed a change with the advent of Companies and Allied Matters Act (CAMA) 2020 that has withdrawn the statutory requirement of appointing external auditors. This study thus examined the influence of auditing on sustainability of MSMEs and the impact of the audit exemption legislation on sustainability of MSMEs. A quasi-experimental research design was adopted that used the cross-sectional survey setting to sample 99 respondents using a structured questionnaire that depicted the views of owner-managers, company accountant/auditors, customers and external providers of finance in areas that related to the objective of the study. Statistical tools in Descriptive and Inferential analysis of mean, standard deviation and regression analysis were used to analyse the research questions and hypothesis. The outcome of the study showed that auditing indeed has a significant influence on the sustainability of MSMEs, $R^2=50.2$ ($P<0.05$); as it relates to MSMEs being able to effectively and efficiently manage their finances, among others. The researcher recommended that there should be subsequent amendments to the CAMA 2020 that would stipulate alternative safeguards and measures to enable users of financial statements of MSMEs have adequate confidence in relying on their financial information. Voluntary audit should be encouraged since MSMEs is the growth engine of every economy, any means of ensuring their survival should be employed.

Keywords: Sustainability, MSMEs, Auditing, CAMA-2020, Financial

INTRODUCTION

Corporate business world in Nigeria have witnessed a prominent change with the advent of the Companies and Allied Matters Act, 1990 (CAP C20, LFN 2004) ('CAMA') repeal and re-enactment as CAMA 2020 ("the Act"). CAMA 2020 innovations sought to help lessen the compliance burden of small and medium enterprises (SMEs) among others; but include new provisions that would help businesses in the corporate world (Obayomi, 2020). A key highlight in CAMA 2020 is Section 402(1) which provided that small companies (in accordance with Section 394) were exempted from appointing auditors, that is, micro, small, and medium enterprises (MSMEs) are no longer statutorily in compulsion to audit their financial statements. MSMEs were required by CAMA 1990 to audit their accounts and appoint auditors. Small companies have also been exempted from statutory audit in many countries, such as Singapore, the United States, the United Kingdom and several other European countries (Haron, Ismail, Ganesan & Hamzah, 2016). Exemption of small companies from audit has been traced to the fact that the owners of MSMEs at times serve in capacity of both managers and directors, little value is added from audit and also the prerequisite of a strong internal control is often lacking (Collis, 2010; Kamarudin, Abidin, & Smith, 2012 as cited in Haron, *et al.*, 2016).

MSMEs play a major role both in national and global economies contributing to development, job creation and export among others hence it is said that the MSMEs sector is the growth engine of any economy. MSMEs in Nigeria are relatively easy to start-up and in an equivalent way have a high

tendency to close-down (Ogunsanmi, Omorogbe & Uchehara, 2019). Therefore, sustainability of MSMEs is of utmost importance, as it is becoming central to the conduct of business (Akpata, 2018). Sustainability as it relates to small and medium sized enterprises (SMEs) involve the balance on one side between financial, human and material resources, and then the social and economic environment it operates on the other (Adriana & Laurentiu, 2019). The most pressing problem of MSMEs have been deduced to be obtaining finance among other pressing issues; The National Bureau of Statistics (NBS) accounts that less than 5% of SMEs have access to funds for working capital and funding expansion (PwC MSME Survey, 2020).

Legislation on audit exemption requires companies to no longer present audited statements, this will hence likely have an adverse effect on credit availability and also, affect audit firms whose main clients are small companies (Haron, *et al.*, 2016). The need for audit has been as a result of meeting the requirements of trustees, shareholders, directors, funders or regulators; group level decisions that audits should be undertaken by all businesses in the group; perceptions that audits add credibility to a company and improve its reputation; perceptions that audits represent good financial practice; and inertia (i.e., companies with a history of always undergoing audits) (BEIS Research Paper, 2017). Given these perceived shortcoming and benefits of adopting auditing practice in MSMEs, there is therefore the need to feel the 'rhythm of those in the rocking boat'. This study therefore evaluated the willingness of MSMEs to carry out audit; and determine the influence of auditing on sustainability of MSMEs.

This study report is segmented into four sections. Following the introduction is literature review where basic concepts are reviewed and the theoretical foundation for the study is discussed. Section three is the study methodology and results of the hypothesis tested are discussed; while section four summarises the findings, conclusion and recommendations.

LITERATURE REVIEW

Auditing

Auditing and Audit are used interchangeably depending on the context of usage. Auditing is a systematic process that involves the review and examination of an organisation or individual records or operations, after which evidence is gathered for an expression of opinion in form of report as to the truth and fairness, assurance or attestation of the process carried out. Auditing is usually guided by rules and standards that define the whole process to be taken.

Costello (2003) poist auditing to be a process which is systematic that involves obtaining and evaluating evidence as to assertions about economic actions and ascertaining the degree of correspondence of events between these assertions and any established criteria and then communicate the results to interested users. The Explanatory Foreword to the Auditing Standards and Guidelines issued by the Institute of Chartered Accountants in England and Wales (ICAEW) defines an audit in the following terms: "An audit is the independent examination of and expression of opinion on the financial statements of an enterprise by an appointed auditor in pursuance of that appointment and in compliance with any relevant statutory obligation" (Ghatalia, 2001 pp. 3). The Report of the Committee on Basic Auditing Concepts of the American Accounting Association (AAA) defines auditing, "as a systematic process of objectively obtaining and evaluating evidence regarding assertions about economic actions and events to ascertain the degree of correspondence between those assertions and established criteria and communicating the results to interested users" (Hooks, 1973 pp. 6). According to the definition given by the International Federation of Accountants (IFAC), "An audit is the independent examination of financial information of any entity, whether profit-oriented or not and irrespective of its size, or legal form when such an examination is conducted to express an opinion thereon" (Kangal, nd).

However, Owolabi, Jayeoba and Ajibade (2016) cited Flint (1988), that audit is a social phenomenon serving no purpose or value having only practical usefulness with an existence wholly Unitarian and Wang (2004) also explained financial audit to be the process of self-identity, self-measurement and self-edit on management's financial accountability.

It can be seen from the definitions provided above that auditing is an examination, review or process which is always done by an independent party and carried out to express an opinion on either financial record, assertions, events, etc.; as to the true and fairness, assurance or attestation.

Though Owolabi *et al.*, (2016) showed the work of Flint which was opined that auditing is just a social phenomenon with no real value; this is preposterous, as auditing has been seen by majority to provide assurance. Auditing is an independent examination or review of financial records to express an opinion to its true and fairness in line with rules and regulations as regards statutory audit; however in line with non-audit services it is a review that provides assurance and attestations that confirms events or processes and this is done with clients need serving as guideline for the process.

Audit Exemption and Voluntary Audit

Audit exemption and deregularization of audit for SMEs is an apparent issue and often discussed in the auditing industry. Many developed countries like the UK, Australia and New Zealand have addressed the issue by exempting audit for them while some other countries have deregulated audits for SMEs such as Singapore and European Union Countries (Haron, *et al.*, citing Kamarudin, Abidin, & Smith, 2012). In Nigeria, the Companies and Allied Matters Act 2020 introduced exemption from audit for Micro, Small and Medium enterprises (MSMEs). In general, audit exemption is given to SMEs due to several reasons such as SME's lack of internal control system, arising from a limited number of staff and the owners are usually also the managers and in some cases, the shareholders and the directors are the same person, thus would make auditing meaningless. Audit fees SMEs are expected to pay pose financial drain for the small companies, with no benefits being directed back to such companies. This position was reiterated in a study conducted by Chung and Narasimhan (2001). Small companies are in support of the elimination of mandatory audits, as an audit exemption would lessen the workload of directors and staff involved in preparing for annual audits. However, auditors believe that SMEs actually derive substantial benefits from audited accounts such as detection of fraud and improved decision making as have been discovered by authors (Haron *et al.*, as citing Collis, 2010; Kamarudin, Abidin, & Smith, 2012; Salleh, Che Rose, Kumar, & Jaafar, 2008)

Biswas, Honey and Catherine (2011) referring to the study of Seow (2001), states that users of audited financial statements identify and make use of the benefits of assurance that auditing brings, hence the demand for voluntary audit, even if it is not required by law. Auditors also offer other essential and useful services. Biswas *et al.*, citing Carey *et al.*, (2000) indicated that the demand for voluntary audits is positively related with the level of the firm's debts. That is, as the debt size of the firm increases, there is more willingness of getting an audit; auditing also help to control stakeholders' conflict of interests. In addition, the willingness to obtain voluntary audits tend to increase as the size of the firm increases reasonably, that is, as a firm grows, the number of transactions also increases with higher probabilities of inaccuracies and this leads for obtaining voluntary audit.

Samson, Mary, Clement and Sule (2012) which studied the gap between the supply of audit services by professional accountants and demand for the services by small businesses in Nigeria, reiterated that factors causing gaps internally and externally include the perception, and inexperience of owners, owners' fear of audit, regulations of auditing business enterprises in Nigeria and audit fees. These gaps have constituted prominent setbacks in auditing small scale businesses in Nigeria. The study concluded that small scale businesses do not demand for accounting and audit services in Nigeria, although the part of accounting and auditing services is central to the welfare of small business entities. Regrettably, engagement of an auditor for quality audits and having the very best internal controls can be very

expensive, for small businesses. Consequently, the wrong perception and the inexperience of small business owners, operators and managers on the audit of a business constitute a negative impact on auditors in providing accounting and audit services to small scale business in Nigeria and the fear of audits is also a major characteristic of small business owners that inhibits possible audits of small businesses.

Olasupo, Sorunke and Olawuyi (2016) expressed that the position of auditing in any organisation, regardless of its size cannot be overstressed. However, Audit of Small and Medium Enterprises (SMEs) have proven to be among the most worrisome for professional accountants due to inadequacy of the internal controls citing Olatunji (2013); and if not for statutory demand, small and medium enterprise hardly consider the course of sound accounting system, risk assessment and auditing which cause for their imminent and untimely failure. The absence of this standard accounting system and detailed financial records has been a major barrier to Statutory Auditing of many SMEs, and thus, negatively affect performance as they find it hard to persuade stakeholders (creditors, supplier, tax authorities etc.), that there has been steady review by an independent expert into the affairs of the firms.

Concept of MSMEs' Sustainability

Sustainability is a broad concept that researchers and policymakers apply in many industries including business, community development, public services, and non-profit organisations (Gázquez-Abad, Huertas-García, Vázquez-Gómez, & Romeo, 2015 as cited in Adoukonou, 2019).

Sustainability was first defined with an environmental approach appearing in the Brundtlan Commission's report that was adopted by the United Nations General Assembly in 1987, which proposed practical means to reverse environmental problems. This report also known as 'our common future' defines what is understood by sustainable development, as "the development that meets current needs without compromising the ability of future generations to meet their own needs"(Brundtland, 1987 pp. 41). However, "sustainability" is a complex and multidimensional concept with multiple interpretations; as sustainability is recognised as companies been fully conscious of the effect of their activities on the substantial and inconsequential state of both the direct and indirect environment which not only deals with exploring opportunities and threats in the market, but also analyzing willfully the social, environmental, and economic impact that the developed business activity is having on the environment (Sarango-Lalangui, Álvarez-García & Río-Rama, 2018).

In business, sustainability refers to doing business without negatively impacting the environment, community, or society as a whole. Sustainability in business generally addresses two main categories: the effect business has on the environment and society. The goal of a sustainable business strategy is to make a positive impact on at least one of those areas. When companies fail to assume responsibility, the opposite can happen, leading to issues like environmental degradation, inequality, and social injustice. Sustainable businesses consider a wide array of environmental, economic, and social factors when making businesses decisions. These organisations monitor the impact of their operations to ensure that their short-term profits do not turn into long-term liabilities (Spiliakos, 2018).

A sustainable business has four criteria: it integrates principles of sustainability into each of its business decisions, supplies environmentally friendly products or services, greener than traditional competition and it has made an enduring commitment to environmental principles in the business operations. In line with the definition on sustainable development by the World Council for Economic Development (WCED), for MSMEs to foster sustainable best practices, the whole organization are required to be involved; there have to be stakeholders' engagement; environmental management systems, proper reporting and disclosure systems and analysis of the lifecycle of products; thereby, being able to attract and retain investors easily, be innovative and adaptive to environment and experience less financial and reputation risk (Ogunsanmi, Omorogbe & Uchehara, 2019).

Theoretical Review

This study is founded on the basis of lending credibility theory and theory of inspired confidence

Lending credibility theory

This theory is derived from public perception and suggests that the principal function of audit is to add credibility to the financial statements, thus, the selling point of the auditor is to apply his technical competence to verify a financial statement so that the users of accounts can rely on the audited accounts. In this view, the service that the auditors are providing to the clients is credibility. Chesoli (2019), citing Hayes, Dassen, Schilder and Wallage (2005) identified that through audit function, fair presentation of firm's value is enhanced. The Institute of Chartered Accountants (2009, cited in Shumba (2015) also supported this theory by stating that the fundamental purpose of audit is the provision and promotion of investor's confidence and trust in financial information. However, Chesoli citing Porter (1990) reiterated that investor's investment decisions are not based on audited financial information. Although, audited financials are seen to have essentials that increase the users' confidence in the records provided by management (in the financial statement). Users' are perceived to gain benefits from the increased credibility, in that, audited financial statements boosts their confidence in an organisation's financial records and management's stewardship. This credibility gained would have an effect on decisions by stakeholders and also help shareholders put trust in management; thereby, a reduction in the 'information asymmetry' between stakeholders and management (Chesoli, 2019; Shumba, 2015; Okpala, 2015 as cited in Olufemi, 2019; Ittonen, 2010; mbaknol.com).

Theory of inspired confidence (Theory of rational expectations)

This theory was propounded by Limperg in the late 1920s and relates to the need and provision of audit services that came about by Limperg in 1932 series of essays. Audit services is seen to be demanded in direct relation to the involvement of third parties (interested parties) desire for accountability from management in return for their investments which could have been achieved through the issued periodic financial reports, however, due to possible bias from management in information provided which is void of monitoring by outside parties, prompted the need for audit to assure the reliability of information provided. With regards to the provision or supply of audit assurance, Limperg (1932) as cited in Olufemi (2019), asserted that public expectations as regards the auditor's functions are as a result of society's belief of expertise and independent opinion that will be provided in examination; that is, confidence is rested by the society on the auditor to give an independent opinion and the auditor is to maintain an appropriate business conduct and independence from the firm being audited. This is vital, in order to gratify commitment to review business procedures and make available a credible opinion on the financial reports (Chesoli, 2019; Olufemi, 2019; Ittonen, 2010; & mbaknol.com).

The above theories are relevant to the study as the theory of inspired confidence and lending credibility theory are important as to the sustainability of MSMEs. Auditing of MSMEs will help provide confidence of customers, suppliers, employees of MSMEs, which translate into loyalty and accountability resulting in growth. The lending credibility theory ensures reliability on the provision in the audited accounts to provide a basis for external financing which could lead of into ensuring the sustainability of MSMEs. Thus, null hypothesis tested is, H_0 : Auditing practice has no significant influence on MSMEs sustainability.

THE STUDY METHOD

A Quasi-Experimental research design applying a cross-sectional survey research setting was adopted for this study. This design assisted in capturing the influence of auditing on sustainability of MSMEs. Data was collected from 99 respondents which were owners as well as the managers, company accountants

who were also auditors, customers and external providers of finance as they relates to MSMEs around the Lagos metropolis through the use of a questionnaire examining the willingness of audit practices, impact of audit exemption on sustainability and the influence of auditing on sustainability of MSMEs. A 99% response rate was achieved.

Result and discussion

Data gathered were analyzed descriptively with means, and standard deviation; while inferential statistics tool used was the regression analysis and hypothesis tested to ascertain the influence of auditing on sustainability of MSMEs. From the 5-point Likert scale used in ascertaining respondent’s opinion, means were determined (see Appendix 1). The mean scores was interpreted as: means greater than or equal to 3.0 implies agreed ($\bar{x} \geq 3.0 \Rightarrow agreed$), while means less than 3.0 implied disagreed ($\bar{x} < 3.0 \Rightarrow disagreed$).The standard deviation measured response variation from the mean. Large standard deviation represents wide variation in responses while smaller standard deviation meant similar respondent views on issues.

The descriptive result for responses on the willingness of MSMEs to carrying out audit, it has a summation means score of 3.86 which means that majority of respondents agreed that audit is essential ad willing to carry out auditing practice; while opinions on the possible influence of auditing on sustainability of MSMEs, it had a total means score of 4.17 which signified that a large number of respondents agreed that auditing influences sustainability (see Appendix 1).

Result from Test of Hypothesis

The result from the test of hypothesis- H_0 : Auditing practice has no significant influence on sustainability of MSMEs, is shown o Table 1a-c.

Model Specification

$$Y = a + f(X_i) + e$$

$$MS = a + \beta(AP) + e$$

Where $a = Constant$,

$Y = MSMEs' sustainability (MS)$,

$X_i = Auditing practice (AP)$

$f = beta (\beta) value, and$

$e = error term.$

Table 1a: Model Summary: Result on influence of auditing on Sustainability

Model	R	R ²	Adjusted R ²	Standard Error of the Estimate
1	.639 ^a	.502	.479	1.855

Table 1b: ANOVA^b: Result on Analysis of Variance of Auditing and Sustainability

Model		Sum of Squares	Df	Mean Square	F	Sig.
1	Regression	5.108	1	5.108	4.147	.042 ^a
	Residual	71.602	98	.731		
	Total	76.710	99			

a. Predictors: (Constant), AP

b. Dependent Variable: MS

a. Predictors: (Constant), AP

Table 1c: Coefficients^a: Result on Influence of Auditing practice and Sustainability of MSMEs

Model		Unstandardized Coefficients		Standardized Coefficients	T	Sig.
		B	Std. Error	Beta		
1	(Constant)	4.111	.321		12.824	.000
	Auditing	1.030	.279	.539	.384	.042

a. Dependent Variable: MS

The model summary of the regression analysis shows the influence of auditing on sustainability of MSMEs as shown in Table 1a. The result showed a correlation of 0.639, which implies a positive and strong relationship between auditing and sustainability of MSMEs. The R² of the model (0.502; p < 0.05) shows that about 50% variations in sustainability of MSMEs is explained by auditing practice.

The analysis of variance from the regression model is summarized in Table 1b. The sum of square of the regression is 5.108; residual sum of the squares is 71.602. The F-statistic shows a poor goodness of fit of the model though it is significant and positive in explaining the influence of auditing practice on MSMEs sustainability.

Table 1c presents the coefficients of the analysis. Auditing has positive influence on sustainability of MSMEs. This is evident from the coefficient of the independent variable (auditing) 1.030 which is positive. The significant value of the coefficient (0.041) is less than, P < 0.05, and therefore implies that auditing has positive and significant influence on MSMEs.

The result of the regression analysis summarized in Table 1b showed the probability value of auditing as 0.042 which is less than 5% significance level. As a result of this, the null hypothesis is rejected and concluded that auditing has significant influence on sustainability of MSMEs.

Conclusion

Sequel to the findings espoused in this research on Micro, Small and Medium Enterprises (MSMEs), and need to undergo audit, sustainability is shown to be influenced by auditing practice, although MSMEs may not have carried out audit since they were no longer required by law. The evidences from this study have shown that, auditing is significant to MSMEs sustainability and also have significant value in MSMEs. Respondents showed willingness to carry out audit.

Auditing is important to the sustainability of MSMEs. The advent of audit exemption in CAMA 2020 stands in variation with the desires of the respondents. The law would reduce voluntary compliance and associated benefits. BEIS Research Paper, (2017) supports that the perceived benefits of compliance is higher than actual benefits.

Recommendations

In other to achieve sustainability through the practice of auditing, it is recommended that:

There should be subsequent amendments to the CAMA 2020 that would stipulate alternative safeguards and measures to enable users of financial statements of SMEs have adequate confidence in relying on MSMEs financial information.

Voluntary audit is to be encouraged with regards to the matter of the assurance that audit brings to MSMEs. This is crucial because when the size of MSMEs grows, there is a tendency of increase in the probability of inaccuracies which brings about the need for voluntary audit as posed in Biswas, Honey and Catherine, (2011) study. Auditors should recommend non-audit services for MSMEs, as that would be beneficial to their operations.

A further study on tax authority's requirement of audited accounts as it relates to the compliance by MSMEs, still remains an issue as audited financial statement is required for tax assessment. But with this law of MSMEs non-compulsion to audit, and exemption from audit, would create another great issue for the tax authority in tax administration. Hence, this study strongly recommends that MSMEs should be encouraged to carry out audit practices.

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APPENDIX

1. Analysis of willingness MSMEs to carry out Audit

Table 1: Analysis of Auditing Practices of MSMEs

S/No	Items	Mean	SD	VHE (%)	HE (%)	AE (%)	LE (%)	VLE (%)
1.	Audit of financial records is done in MSMEs	3.89	1.08	35	33	22	6	4
2	Audit is carried out due to statutory legislation like CAMA, FIRS	3.82	1.06	31	35	22	9	3
3	Audit is carried out on advice by accountants	4.03	0.94	39	32	22	7	
4	Major customers, suppliers or trade creditors require audited accounts	3.92	1.05	38	27	26	7	2
5	Audit is carried out based on directors and shareholders preference	3.94	1.01	36	32	24	6	2
6	Audit is carried out based on providers of finance preference	3.97	0.97	37	31	25	6	1
7	Audit is carried out as a Corporate Social Responsibility	3.57	1.17	26	29	27	12	6
8	Audit is carried out to build image of the company	3.65	1.12	27	30	29	9	5
9	Audit will not be carried out if not required	3.95	1.15	45	20	24	7	4
	Total	3.86						

Source: Author's Computation (2021) using SPSS 20.0

2. Analysis of influence of Auditing on Sustainability of MSMEs

Table 2: Analysis of Auditing on Sustainability of MSMEs

S/No	Items	Mean	Std De	VHE (%)	HE (%)	AE (%)	LE (%)	VLE (%)
1.	Audit helps to effectively and effectively manage finances of MSMEs.	4.23	0.85	43	42	12	1	2
2.	Audit helps to provide special benefits and opportunities to MSMEs who undergo audit	4.13	0.87	40	37	20	2	1
3.	Audit helps to ensure control (internal) and monitor operations of MSMEs	4.13	0.78	36	43	19	2	
4.	Audit helps to ensure compliance of MSMEs on statutory and industrial requirements	4.20	0.79	39	45	14	1	1
	Total	4.17						

Source: Author's Computation (2021) using SPSS 20.0