

**DETERMINANTS INFLUENCING THE ADOPTION OF ACCOUNTING
PRACTICES BY SMALL AND MEDIUM ENTERPRISES IN NAIROBI, KENYA**

PAULINE WANGUI NJIRAINI

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DECLARATION

This research project is my own work and it has not been submitted to any other university or institution for an award.

Signature:.....Date:.....

Pauline Njiraini

Reg. No: D61/75385/2009

Supervisor's Declaration

This work has been submitted with my approval as university supervisor

Supervisor

Signature:.....Date:.....

Dr. Kennedy Okiro

Senior Lecturer, School of Economics

University of Nairobi

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LIST OF ABBREVIATIONS AND ACRONYMS

GoK	Government of Kenya
ICT	Information Communication Technology
IFAC	International Federation of Accountants
IFRS	International Financial Reporting Standards
SMEs	Small and Medium Enterprises

ABSTRACT

Already burgeoning literature on small and medium enterprises indicates the essential role they play in economic development in countries that are both developed and developing. Accounting plays a significant role as a determinant of success or failure of business enterprises especially SMEs. Accounting practices avail information to both the owners and managers of SMEs and thus they are indispensable to firms that seek a growth trajectory and improved performance goal. Firms have competing needs for their resources and professional accounting services have to equally compete for the scarce resources of the firm. Never the less, examined literature indicates that some influencers may have a direct role of determining whether a firm uses accounting services or not. The main objective of this research was to investigate the determinants influencing the adoption of accounting practices by various SMES operating in Nairobi, Kenya. The study used a descriptive research design. The targeted population included all SMEs operating in Nairobi County that are licensed. Simple random sampling was used to pick out the sample size of 85. Data collection in this study was done through use of a questionnaire. The findings show knowledge competence, competition, legislation and firm size influenced the use of accounting services. SMEs need to hire qualified accountants to address the challenges that SMEs face such as stiff competition. This will enhance proper book keeping and in addition encourage the adherence to legal requirements of maintain proper books of accounts and this will also promote the growth of SMEs.

CHAPTER ONE

INTRODUCTION

1.1 Background of the study

Small and medium enterprises (SMEs) are more of the backbones of economies in countries around the world and this has seen a growing emphasis on the need to ensure they are successful. Already burgeoning literature on small and medium enterprises indicates the essential role they play in economic development in countries that are both developed and developing (Muneer, Ahmad, & Ali, 2017). SMEs need critical accounting services to enable them accomplish their economic role and ensure they continue to grow and achieve sustainability in their performance.

Accounting plays a significant role as a determinant of success or failure of business enterprises especially SMEs. Accounting practices avail information to both the owners and managers of SMEs and thus they are indispensable to firms that seek a growth trajectory and improved performance goal (Uddin et al., 2017). The accountant is an essential source of advisory services and support SMEs in financial management, assurance services, statutory advice, business advice, and emergency advice to improve their growth and performance. The accounting services that SMEs need include taxation, auditing, financial reporting, business consulting, and assurance services; these are essential services sought by a majority of SMEs today (Husin & Ibrahim, 2015).

The International Federation of Accountants (IFAC) supports the opinion that simplified and appropriate guidance is required for SMEs. Moreover, the accounting body is of the

view that user demands are quite different when compared to those of listed firms and this factor has to be considered when developing accounting rules and regulations for SMEs. Additionally, IFAC observes that International Financial Reporting Standards might be too complex for SMEs and might often result in it being too costly when compared with the derived benefits for use of International Financial Reporting Standards (IFRSs) (Sjögrén, Syrjä, & Puumalainen, 2014). This has seen the development of International Financial Reporting Standards specifically to cater for SMEs whose adoption and use continues to receive less scholarly interest.

1.1.1 Accounting Practices

Accounting practices are varied and wide and are not just limited to the traditional financial accounting, or book keeping services. They include other accounting related systems that enable auditing, taxation, business advisory, management accounting, cost accounting, accounting information systems, and assurance services. A firm needs to incarnate a majority of these practices in its operations if it desires to have a growth trajectory and improved performance (Ali, 2017). Harun, Ishak, Sofri, Siti, & Yuvaraj (2010) note that the critical accounting services required by a majority of firms which are SMEs to make them more competitive include financial reporting, auditing, taxation, strategic planning and accounting for management services. Such services influence the success of SMEs and put them on a growth trajectory when implemented properly.

The management of SMEs needs to recognize the effect and possible outcomes of a rapidly changing environment around accounting practices such as taxation regulations, prudent financial management requirements, need for reliable and accurate financial information.

SMEs require help to enable them use financial tools such as budgeting, cost analysis, taxation, financial ratios, breakeven point, management accounting, auditing and other assurance services. This is mainly because of a lack of solid financial backgrounds among a majority of SME managers and owners (Harun et al., 2010). The SMEs will thus have a plethora of factors that influence the decisions on using or adopting accounting practices. The lack of accounting knowledge is top among the top reasons that determine their decision to use accounting services.

1.1.2 Small and Medium Enterprises

SMEs have received wide definitions with each author giving a definition based on the context of use. In the Micro and Small Enterprises Act of 2002, they are defined as enterprises whose maximum turnover per year is Ksh 500,000 (\$5,000) and whose total employees are 10 to 49 in number (GoK, 2015). Although not covered by the act, medium enterprises are those having a turnover of between \$ 50,000 and US\$8M and have employees numbering between 50-99 people.

Nyathi, Nyoni, and Bonga (2018) observe that the reason behind this is largely due to the impossibility of capturing all the characteristics of what constitutes an SME. It is also complex to fully distinguish the enterprises that operate in various sectors of the industry or country. The definition of SMEs has thus been grounded on the amount of capital base, personnel, turnover, share of market, infrastructure of the firm among other attributes. The European Commission (2016) defined SMEs as enterprises having an annual turnover of EUR 50 million or less and employ 250 people or less and whose balance sheet annually is EUR 43 million or less.

Chelimo and Sophia (2014) describe SMEs to be entities employing a maximum of 10 people and refer to them as micro, those having more than 10 but less than 50 are classified as being small and entities whose employees number between 50 and 250 as medium enterprises. Other scholars have used the size of the firm's assets to define SMEs. The emphasis on small and micro reveals that they are not regarded as being huge with big financial and asset resources. They are regarded as operating on the scale between big corporations and sole proprietorship of miniature business venture. Never the less, there is growing recognition that such enterprises need to properly adopt good accounting practices into their operations to ensure their growth and sustainability.

1.1.3 Small and Medium Enterprises accounting practices

There is burgeoning application and use of accounting data and information in SMEs, with new methods and systems coming up that allow assembly and evaluation of accounting information in a manner that supports management decision making. Accounting practices in SMEs ensure the collection of information, verification of the information; accuracy, relevancy, and reliability of information that enables SMEs make economic and non-economic decisions. Lack of proper and adequate accounting data and information is believed to be a major reason behind closure of many SMEs around the world (Nyathi et al., 2018).

Poor accounting practices directly and negatively affect SME growth and sustainability. Decisions in a firm must be backed by solid financial information for them to be effective. However, majority of business owners, particularly small and medium enterprise owners continue to operate their enterprises without sound accounting or financial judgment. They

often make essential decisions on credit and investments with little analysis of accounting and financial information (Udhin et al., 2017). Already, literature is highlighting the variables that drive firms to be involved in the use of accounting practices. Accounting practices in SMEs largely depend on the age and size of the business, taxation requirements; need to support shareholders, and the knowledge and skills of owners and managers. These variables however remain inconclusive and are dependent on the industry in which the firm operates. Other variables have also been fronted as barriers to accounting information use in SMEs include high costs of hiring qualified accountants which has seen a majority of SMEs entirely abandon the financial domain of their enterprises (Maseko & Manyani, 2011).

1.1.4 Determinants of use of accounting services

Firms have competing needs for their resources and professional accounting services have to equally compete for the scarce resources of the firm. Never the less, examined literature indicates that some influencers may have a direct role of determining whether a firm uses accounting services or not. Njeri (2016) found that competence, knowledge and firm size had a direct influencing role in use of accounting services by firm. In their study in Tanzania, Waweru, Ntui and Mangena (2011) found that significant factors that determined use of accounting services included company size, the number of non-executive directors, internal financing and number of employees. Studies have shown the existence of a strong relationship between the accounting methods chosen and income strategy in organizations (Waweru et al., 2011).

According to Padachi (2012) notes that firm size, age of business, legal structure, family involvement and level of education all determine whether a firm will use accounting services or not. Firms which have well-structured internal accounting systems also benefit from the services that such internal departments offer to the larger firm and are more likely to witness improve performance and increased efficiency levels. It is therefore crucial that firms seeking a growth trajectory or seeking an improvement of their business operations need to incorporate better or more improved accounting practices into their operations.

1.2 Research Problem

Research provides evidence that a majority of SMEs do not operate for more than one year and often collapse just a few months of beginning operations (Karadag, 2015; Maduekwe & Kamala, 2016). Poor or a complete lack of using proper accounting methods, practices and services is one of the major causes of collapse of SMEs. This is largely due to the ignorance by such SMEs to incorporate proper accounting services into their operations, choosing instead to do their accounting in a lackadaisical manner. SMEs operating in Kenya rarely use professional accounting services. This is demonstrated by the Okwena, Okioma and Onsongo(2010) who found in their study that SMEs had poor book keeping practices which had a negative effect on their financial performance. Further, small business failure inevitably is a result of poor or careless financial management.

Due to the environmental challenges that SMEs face, SMEs require the assistance of a professional who will be able, for instance, identify competitive forces through the use of accounting numbers. That way, a drop in profitability as shown by a profit and loss account would be a likely indicator of new entrants to the already competitive market (Kipsang,

2017). While extant literature shows that use of good accounting services is essential for the growth and survival of SMEs, this sector continues to receive growing attention in recent times.

Globally, research in this area continues to be reported. Al Smirat (2013) examined accounting in south Jordanian SMEs and established that most of them used basic and simple accounting systems. The study recommended good accounting practices as a remedy to improving firm performance. The study did not disclose why such SMEs preferred use of simple accounting practices or factors that led to such a practice. Owusu, Assabil, & Asare (2015) studied book keeping practices effect on Ghanian SMEs performance. In Nigeria, Adekunle and Adejare (2014) investigated book keeping and the effect it has on performance of SMEs. The study establishes the existence of a positive association between performance and proper book keeping. In South Africa, Sibanda and Manda (2016) study found that most SMEs did not keep proper books f account.

In Kenya, in particular, just a handful of studies have been reported on this subject matter, thus documenting the need for more research in this area. Mutua (2015) study found that most SMEs were not keeping proper books of accounts, but did not disclose the reason for such failure. Chelimo and Sophia (2014) reported similar findings on their study of accounting practices in selected SMEs in Kenya.

Accounting practices are not limited to just book keeping, they include, taxation, auditing, management accounting, financial reporting, cost accounting among others. Existing studies have been biased towards book keeping and this study addresses the subject matter in a wholesome way. SMEs do not just need book keeping but they also need to incorporate

other accounting practices into their operations. The studies report the absence of use of proper accounting services but do not adequately explain the underlying reasons for such an absence. The studies also focus more on book keeping practices as the major accounting practice that is examined. There exists a gap of which determinants influence SMEs to use adopt and use accounting services and the current study makes a contribution by providing new empirical evidence on the subject matter.

1.3 Research Objective

The main objective of this research was to investigate the determinants influencing the adoption of accounting practices by various SMES operating in Nairobi, Kenya.

1.4 Value of the study

The findings of the study are beneficial to a number of groups:

To SMEs, the study furnishes them with new evidence on impediments that they need to overcome in the quest to adopt proper accounting practices. This enables them use proper accounting services in their operations. To policy makers, the study informs them on the need to frame better policies and regulations to encourage SMEs to adopt and use professional accounting services. This study enriches the extant empirical evidence on the subject matter and provides ground for more scholarly investigations.

Stakeholders and policy makers are equipped with knowledge to enable them come up with guidelines and policies that promotes the development of accounting services. Government gets more information that assists it to better manage the SME sector through encouraging adoption and use of various accounting services. The findings from this study assist SMEs

by encouraging them overcome the challenges of using accounting services as a way of improving their performance. Finally, this study builds the existing theoretical framework on accounting services and avails new empirical evidence to scholars who have an interest in this area.

CHAPTER TWO

LITERATURE REVIEW

2.1 Introduction

This chapter reviews literature that is related to the study. Theories which support the study, main variables, the conceptual framework and the research gap is presented.

2.2 Theoretical Framework

2.2.1 Resource Based View Theory

This theory was proposed by Wernerfelt (1995). According to the theory, firms are entities that are a collection of various types of resources where the amount of value that is derivable from a particular resource depends largely on the ease of availability of other resources. Firms often have a long list of available resources or resources that they need to put together. According to this theory, not all the resources that are available to a firm carry equal importance or are capable of becoming a source of competitive advantage. It is therefore essential that firms concentrate on resources that give them a competitive advantage in a particular sector or industry.

According to Barney (1991), the need to create a competitive advantage must adhere to four critical conditions which are rareness, value, imitability and non-substitutability. Grant (1991) contends that the amount of reliability, transparency, and transferability are crucial factors. On the other hand, Collis and Montgomery (1995) propose that resources must possess five essential characteristics for them to give a firm competitive advantage.

These are appropriability, durability, competitive superiority, substitutability and imitability. Amit and Schoemaker (1993) further widen the scope by proposing eight characteristics of complete resources which are low tradability, complementarity, scarcity, appropriability, low substitutability, inimitability, level of durability and degree of overlap with industry strategic factors.

A majority of SMEs operate under immense pressure where financial, time, and expert resources are constraints. This means they will tend to control how they use their resources which influences which accounting services that they decide to use. The chosen type of accounting service thus depends on the available resources. When an SME's resources constraint it against seeking professional accounting services such as auditing, management accounting, tax advice, assurance among other services, they may opt to not use the services at all. This means an SME that intended to use a particular service finds itself constrained due to a lack of enough resources to pursue this agenda. As such, the available resources of an organization are therefore crucial in influencing the type of accounting service that a particular SME seeks.

2.2.2 Competition Theory- Porter Five Forces Framework

Porter (1980) put forward the five forces which are crucial in shaping the level and type of competition in a firm. These are threats of new entrants, competition, the amount of bargaining power from buyers and suppliers, the level of threats and availability of substitutes. The amount of barriers that impede entry into an industry are major competition forces that guide and shape how firms perform in a given economy (Porter. 1980).

Bain (1956) pioneered studies on entry barriers and came up with four key type of barriers which are economies of scale, absolute costs, capital requirements, and differentiation of products. Based on the economic theory, the barriers to entry in any given industry can create disadvantages on new entrants relative to existing industry players. The barriers to entry are therefore designed to increase the difficulty for anyone to join the industry and if they so wish to join, to know that they start at the back of the line because existing players are already miles ahead.

2.2.3 Positive Accounting Theory

This theory is a useful predictor in identifying the determinants that lead to accounting services and the benefits of using accounting services (Watts & Zimmerman, 1990). To predict means that the use of accounting services can influence financial reporting by firms (Basu, 1997). To explain means revealing the key factors that can trigger conservative accounting such as regulation, tax, contracting and litigation and the impact that this has on the financial statements quality. The theory therefore supports the hypothesis, that the underlying reasons among them legal and financial requirements have a direct influence on accounting services use by organizations.

2.3 Determinants of use of accounting services

The inadequacy of qualified staff and knowledge is a major impediment to SMEs in their quest to carry out accounting functions. They do not have requisite knowledge and skills to perform key functions of accounting (Everaert et al., 2006). A majority of SME owners and managers do not have adequate professional skills and knowledge on accounting and as such are often unable to adopt and use accounting services in their firms (Kamyabi &

Devi, 2011). Apart from human resources, government support and commitment by top management have also been fronted as major determinants of use of accounting services in SMEs.

2.3.1 Human Resource

The type of available human resource is an essential determinant of use of accounting services. A positive link exists between human resource and use of accounting services (Alshbiel & Al-Awaqleh, 2011). Studies have indicated that accounting personnel quality is a major factor that determines use of accounting services. A strong association also exists between available human resource and the intention to use accounting services, notably, computerized accounting information systems (Ahmad et al., 2013). A lack of skilled personnel can be a major impediment for small business not to use accounting services (Gibson et al., 2000).

2.3.2 Commitment by Management

The level of commitment by management is very essential because without it, the use of accounting services will not be successful. This is due to the importance of top management in ensuring that resources are available to enable implantation of accounting services. When there are low levels of top management commitment and support, then use of accounting services may be impended (Komala, 2012). Existing studies show that commitment by an organization's top management can improve the effectiveness of accounting services adoption and use. Additionally, management has an effect on accounting services implementation (Rahayu, 2012). Lutfi, Idris and Mohammed (2016) study found that commitment by top management has a direct significant effect on

accounting services usage. The study found that firms that have higher levels of management commitment have more extent for use of accounting services.

2.3.3 Government Support

Government support involves both assistance in terms of motivation and encouragement to the SMEs to adopt and use accounting services (Haithami et al., 2019). Studies have shown that when there is support from government, SMEs are more likely to use accounting services. Governments have therefore been persuaded to provide an environment where SMEs find it easy and appreciate to use accounting services. These include availing easy access to finance, capacity building, and availing current information communication technologies (Abera, 2018). When governments support and give incentives to SMEs, such firms are more likely to use accounting services in their firms (Abera, 2018).

2.3.4 Competition

Competition is a force that exerts pressure on SMEs in order to require them to allocate their scarce resources in an optimal way to gain competitive advantage. When SMEs learn how to use their resources, they become more competitive in an industry (Worrall, 2007). One way of reducing competition is employing a qualified accountant or seek advisory and support services from external accountants (Gooderham, 2004).

The level of competition an SME faces therefore directly affects the accounting services it adopts and uses. Firms going through intense competition need to consider using accounting services especially from external sources due to the limited internal resources

that they have to hire a full competent and qualified accounting team to handle their accounting needs (Kamyabi & Devi, 2011).

2.3.5 Legislation

Accounting legislation particularly on SME accounting laws facilitates accounting tasks and ensures both truthful and rational economic information. Legal frameworks related to SMEs accounting practices include: the systems of accounting standards and guidelines, laws on, and statutory requirements on accounting practices (Hai, 2015). Accountants, significantly influence how firms use accounting legal documents and therefore have a critical role in which their professional judgment and assessment is crucial (Cătălin, Nadia, & Szilveszter, 2010). When legislation exists, and SMEs must comply with such laws, it is more likely to result in burgeoning application and use of the legal requirements by SMEs (Hai, 2015).

2.4 Empirical Literature

Ahmad (2015) investigated the variables influencing the use of management accounting in Malaysian SMEs involved in manufacturing. The study surveyed 500 SMEs and found that firm size, market competition, the commitment by managers and owners of the firms, and advanced technologies of manufacturing determined use of management accounting services. The study supported the contingency based explanation for using management accounting practices and established new factors such as manager or owner commitment as crucial variables influencing use of management accounting services.

Lopez and Heibl (2015) synthesized management accounting in SMEs literature. The study findings reveal that there is low use of management accounting among SMEs and it is different when compared to bigger firms. The study establishes that proper utilization of management accounting is beneficial to improved SME performance.

Phuong (2016) did an exploration and assessment of ways of improving the use of management accounting services in SMEs in Vietnam. The findings show the use of management accounting services in SMEs was influenced by factors such as support management, strategic vision, labor inventory, strategic link simplification and quality standards application. The study further established that the surveyed SMEs mainly focused on financial reporting and accounting due to the demand to avail information for corporate governance.

Kordlouie and Hosseinpour (2018) investigated accounting service use in SMES and focused on organizational DNA, operational technology and commercial potential on management accounting practices. The study surveyed 342 SMEs in Iran and found that organizational DNA had a small role to play in SMEs use of management accounting services. Conversely, the study found that operational technology and commercial potential positively influenced the practice of management accounting in the surveyed SMEs.

Eferakeya (2016) studied adoption of MA in Nigerian SMEs. The findings reveal that a significant moderate use of management accounting methods was related to planning, cost accounting systems, and decision making needs. The study recommended more adoption of management accounting techniques which would have a tremendous impact on both sustainability and profitability of SMEs both in short and long runs.

Khochha (2017) examines the organization of management accounting in fifty five Ukrainian SMEs. The findings of the study reveal that the use of management accounting techniques which characterize SMEs economic activities are the basis for decision making by managers of the studied firms. The study further found out that the practice of managerial accounting is used to improve to improve the financial position of the SMEs. The study concluded that significant time and money expenditures needed to implement management accounting are the main reason for refusal to use it in SMEs.

Dang (2011) investigated the application of various standards of accounting among SMEs in Vietnam. The findings indicate five key variables influencing their use top among them the external pressure for improved information and mandatory compliance requirements. Other factors found were accounting and management deficiency skills, cost benefit relationship, lack of infrastructure and pressure on information.

Hai (2015) in a similar study in Vietnam found that the key factors that influenced the use of accounting legislation to Vietnamese SMEs were accounting infrastructure, cost benefit relationship; need to meet mandatory compliance regulations, accountants, and legislation on accounting.

Inasius (2018) examined the factors that influenced compliance to tax regulations among SMEs as a regulatory requirement in 328 Indonesian firms. The survey revealed that, tax knowledge, likelihood of being audited, and the perception of equity and fairness significantly impacted on tax compliance among the studied SMEs. Particularly, the referral group was found to have the highest influencing role on SME compliance to tax regulations.

Maseko (2013) examines the factors that determine level of compliance to tax regulations among Zimbabwean SMEs. The study specifically examined how perceptions towards taxation, levels of tax knowledge, and uniqueness of business and compliance costs affect use of taxation services by SME taxpayers. The findings of the study show that SMEs faced various conditions that influence their level of compliance. Taxation knowledge was found to have no relationship with compliance, and compliance costs had a major negative effect on the use of taxation services to ensure compliance. The study recommended creation of tax laws that provide incentives for SMEs to encourage voluntary tax compliance.

Lubua (2014) studied influencing compliance to tax regulations in SMEs through adoption of ICTs in Tanzania. The study found that improvements in taxation systems by the government such as more staff, defining administrative blocks and usage of Information communication technologies (ICT) influenced use of taxation services and therefore compliance to tax. The study concluded that the use of such taxation services was however, still low.

Musau (2015) explored the factors influencing tax compliance among SMEs in Nairobi, Kenya. Findings show that growing perception on difficulties of tax evasion increased the likelihood of tax compliance among SMEs. The study also found that individuals who had enough information on tax laws, perceived filing of taxes to be less complex and trusted government officials in handling taxes were more likely to be tax compliant.

Mustapha, Abidoye and Agbaje (2017) did an examination of the role that accounting and audit services in 150 SMEs in Nigeria. The findings indicate that SMEs need motivation to use accounting practices that are sound and costs incurred need to be kept to the

minimum. The findings also show that accounting systems must solve the various issues that SMEs face in order for them to be relevant and useful to the SMEs that use them. This would encourage the use of such audit services by SMEs.

Rudzani and Manda (2016) assessed the obstacles of implementing IFRS standards among South African SMEs. The findings from the study show that SMEs had adopted their use in varying degrees and forms but still generally experienced challenges in implementing to lack of resources. SMEs that had not substantially adopted IFRS were encouraged to adopt them prior to financial statement preparation

Okere, Rachael, Oyebisi, Dorcas, and Qudus (2018) examined compulsory IFRS adoption and its effect on selected Nigerian SMEs. The study found that adoption of IFRS is essential to SME because it aids in comparability of financial reporting. IFRS were found not only to be relevant but crucial requirements to competing in a globalized village by the SMEs

2.5 Conceptual Framework

The conceptual framework for the study is illustrated in Figure 2.1 below.

Independent Variable

Dependent Variable

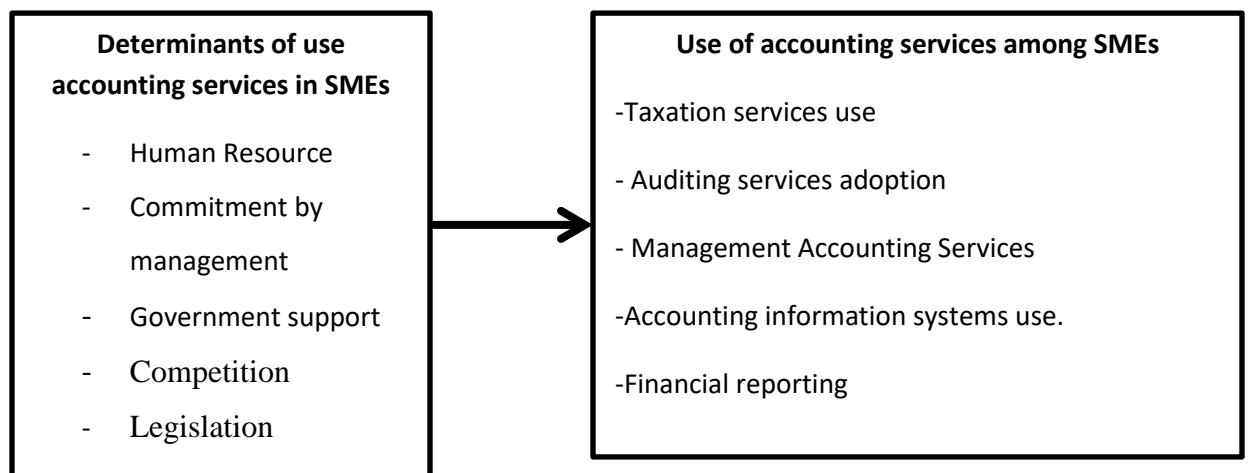


Figure 2.1 Conceptual Framework (Author, 2019)

2.6 Summary and Research Gap

This chapter has discussed literatures that are relevant to the study and how they explain the variables that are being studied. The chapter has also presented empirical literature of studies that have been done in the subject area and what findings they got. The examined literature had not focused on adoption of accounting services among SMEs in Nairobi Kenya.

More research on the variables that determine the use of accounting services among SMEs need to be done which is the aim of the current study. The study makes a contribution to filling this gap by providing new empirical evidence on the determinants of use of accounting services among Kenyan SMEs in Nairobi.

CHAPTER THREE

RESEARCH METHODOLOGY

3.0 Introduction

This chapter discusses the research design, population, sampling, data collection and data analysis methods that were used to carry out the study.

3.1 Research Design

The study used a descriptive research design. This is because it provided a more accurate description of the variables being studied and helped in identification of the determinants of use of accounting services among SMEs in Nairobi County. Ghauri (2005) concur that descriptive research designs are beneficial in studies that are exploratory in nature and are appropriate when seeking for information about the specific characteristics of an infinite population.

3.2 Target Population

Population refers to objects, events or individuals that have a characteristic that is common and which can be observed (Mugenda & Mugenda, 2009). The targeted population included all SMEs operating in Nairobi County that are licensed. The study compiled a list available from <https://www.businesslist.co.ke/category/small-business/city:nairobi> and this made up a list of 567 SMEs which became the population.

3.3 Sampling Size

Simple random sampling was used to pick out the sample size to represent the population. According to Cooper and Chidler (2011), a sample represents a section of the population that is chosen to participate in the study. Mugenda and Mugenda (2009) observed that a survey must have a sample size of at least 10% or more. The sample size was therefore 15% of the 567 SMEs which gave a sample size of 85 that was sampled through stratified random sampling where every 10th SME was selected and included in the sample.

3.4 Data Collection

Data collection in this study was done through use of a questionnaire. The study used structured questionnaires as the primary research tool for collection of primary data. Both qualitative and quantitative data was gathered from the questionnaires. The questionnaire consisted of demographic characteristics, Legal requirements and SMEs use of accounting services, Market competitors, Competence levels and use of accounting services by SMEs in Nairobi.

3.5 Reliability and Validity

Reliability relates whether the results of a research can be replicated using similar methodology and sampling. When a researcher is able to replicate the findings, the instrument used for the research is regarded as being reliable. A popular method commonly used as a measure of reliability is Crobach's Alpha measure which was used in the study.

Validity refers to whether the means used to measure accurately what they were intended to measure. Pilot studies are popular to enable the researcher ascertain the amount of

validity of the instrument. A pilot study was done to ascertain how reliable it was in collecting data for the study.

3.6 Data Analysis

Collected data was prepared for analysis through cleaning, sorting coding and then analyzed to provide both descriptive and inferential statistics. The model below was used to measure the relationship between the variables of the study.

$$Y = B_0 + B_1X_1 + B_2X_2 + B_3X_3 + B_4X_4 + \dots + B_iX_i + e$$

Where, Use of Accounting Services by SMEs = Y

X₁ = Knowledge competence

X₂ = Competition

X₃ = Legal Requirements

X₄ = SME Growth in size

B₀ = Constant variable

3.7 Test of Significance

Exploratory factor analysis was carried out to extract the determinants that have more power in comparison with the others in relation to determinants influencing use of accounting services by SMEs in Nairobi. This was chosen because the method is an appropriate statistical method for validation of constructs. Factors with loading of more than 0.40 on the minimum were interpreted. According to Heir et al., (2010), factors that have a factor loading above 0.33 should be adopted in developing the measurement model and factors with regression weights less than 0.7 should be left out.

CHAPTER FOUR

DATA ANALYSIS, RESULTS AND DISCUSSION

4.1 Introduction

The findings, analysis and reports from the data that was collected for the study are presented in this chapter. The chapter presents the response rate in comparison to what was the planned sample. The findings are based on the realized sample to which administered questionnaires were returned. The sample size and respondents were based on available data collected from SMEs in Nairobi Kenya. Out of the 85 issued questionnaires, 75 of them were returned which resulted in a response rate of 89% that was sufficient for the study. According to Mugenda and Mugenda (2009), when the response rate is more than 50% for a survey it is sufficient to allow data analysis that represents the rest of the population. When the return rate is 60% it is good, and one above 70% is regarded as being very good. Thus the response rate for this study was ascertained to be very good.

4.2 Demographic Characteristics

4.2.1 Level of Education

The education level of the respondents for the study was sought and findings are as illustrated in figure 4.1. The analysis reveals that 67% of those who responded had achieved secondary education, 19% had tertiary education and 14% were university graduates. Based on these findings, it was established that most of the respondents had received secondary education which could have an implication as a determinant of use of accounting services in SMEs.

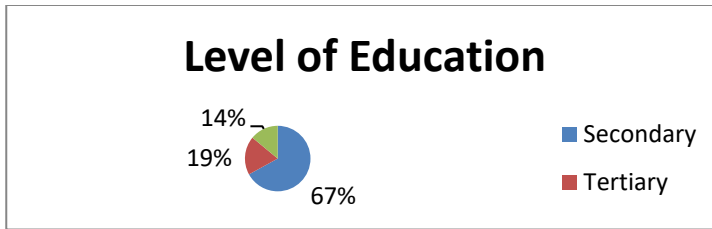


Figure 4.1: Level of Education

4.2.2 Period in Self Employment

The time span in the respondents had been in self-employment was sought by the study. Figure 4.2 below shows the findings which indicate that a majority of the respondents (64%) had been in self-employment for between 2-5 years, 15% of the respondents had in in self-employment for 6-10 years and 13% had been in employment for more than ten years. 8% had only been in employment for less than one year. This finding may indicate influence in use of accounting services, with those who had been in self-employment for longer time periods more likely to use accounting services.

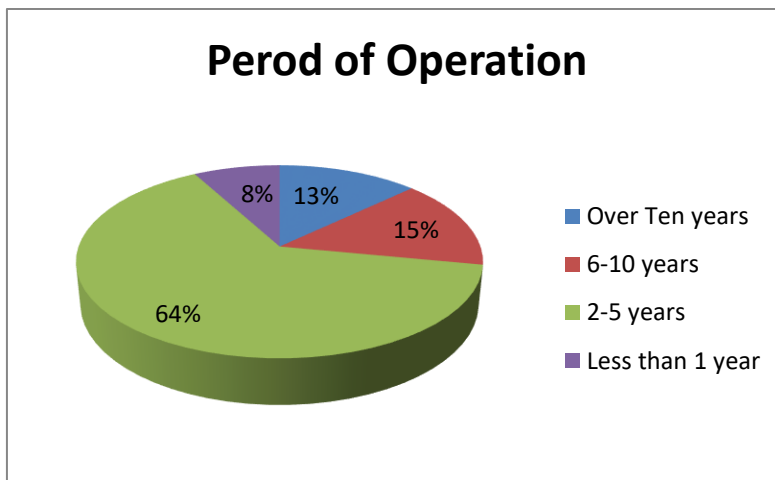


Figure 4.2: Period of Self-employment

4.2.3 Period of Existence

The length of operation of the business was sought by the study and findings are illustrated in figure 4.3 below. Most of those who responded (64%) indicated that their SMEs had operated for 2-5 years, followed by 15% who had operated for 6-10 years, 13% had been in business for more than 10 years and 8% less than 1 year. The length of existence of the business may be a determinant of use of accounting services with businesses that had operated for longer time periods being more likely to use accounting services.

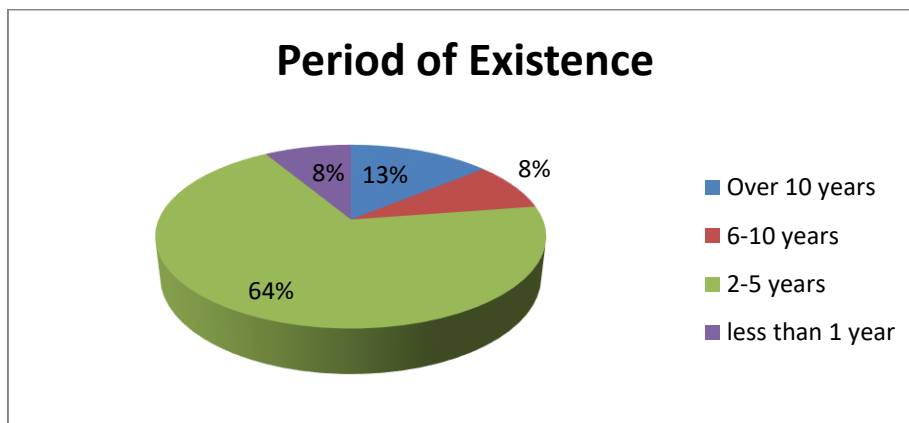


Figure 4.3: Period of Existence

4.2.4 Number of Employees

The size of the human resource in each business was also sought by the study. The findings areas indicated in figure 4.4 below which shows most (63%) employed 1-10 people, 20% employed 11-50 people and 17% had no employees. The finding shows that a majority of the SMEs had fewer employees because they were still small which may have an implication on the use of accounting services between different SMEs based on their size.

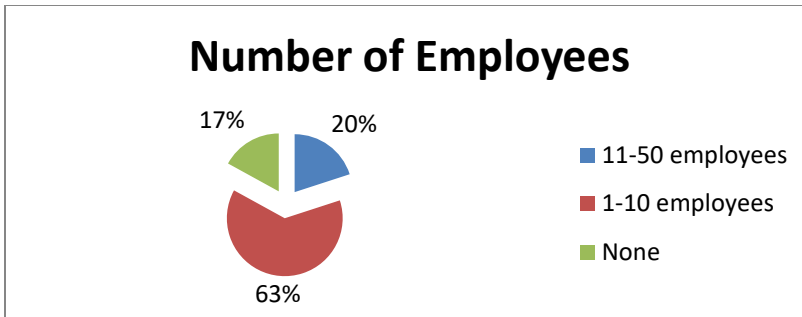


Figure 4.4: Number of Employees

4.2.5 Legal Registration

In terms of the legal registration status of the business, most (72%) were sole proprietors, while partnerships were 28% of the sample SMEs. This finding may have an implication as a determinant of use of accounting services among different SMEs based on their legal status of registration. This is illustrated in figure 4.5 below.

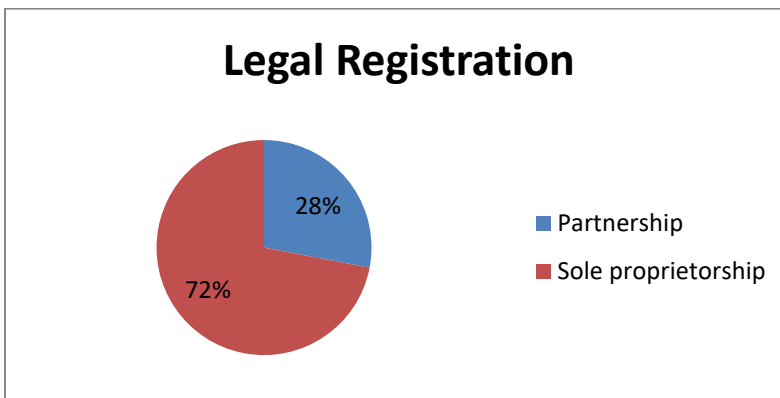


Figure 4.5 Legal Registration

4.3 Knowledge and Competence

The level of knowledge and competence on accounting skills was one of the main aims of the study. Findings illustrated in figure 4.6 shows most of those who responded disagreed strongly of having received training on accounting and book-keeping skills. 29.3% of the respondents disagreed that they had been training on accounting and book-keeping skills which brought the total to 69.3% of respondents who disagreed with this statement. However, 13.35 of those who responded indicated that they had been trained on accounting and book-keeping skills.

Additionally, 44% strongly disagreed and another 20% disagreed they had received computer use training, while 22.75% neither disagreed nor agreed with this statement. However, Only 8% strongly agreed and 5.3% agreed to having attended training courses on computer use. The findings further indicate that 40% disagreed strongly and another 37.3% disagreed to having been trained on sales and marketing skills. A total of 9% neither disagreed nor agreed to having received training on sales and marketing skills.

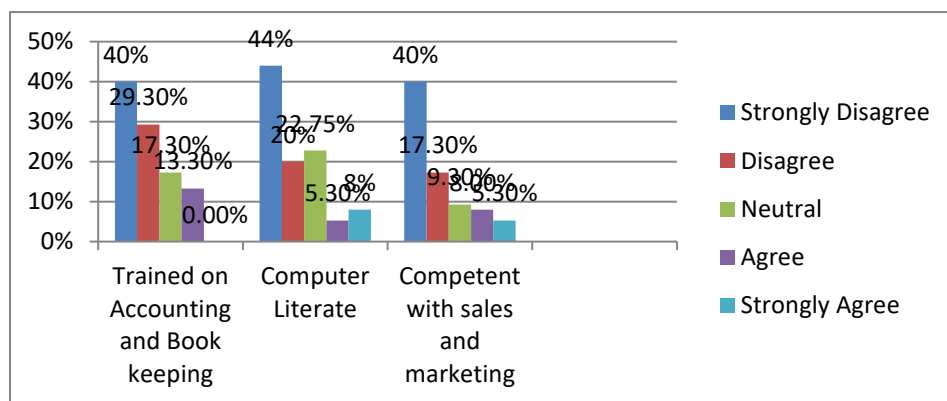


Figure 4.6: Knowledge and Competence

4.4 Competition

The competition levels among the SMEs was another major objective of the study. Figure 4.7 below presents the findings. Based on the findings, a majority of those who responded strongly agreed and another 9.3% indicated that they agreed that there was stiff competition in their businesses that was witnessed by price undercutting. Only a total of 16% of the respondents disagreed and 6.7% of them strong disagreed with this statement. Further, 8% of those who responded did not agree or disagree with this statement.

The results further indicate that most of the respondents 44% strongly agreed and another 26.7% agreed that their businesses had a large number of customers who had a major influence in how they ran their businesses. A total of 12% hose who responded did not agree and 6.7% disagreed strongly. However, 10.8% were indifferent meaning they neither agree nor disagreed with this statement.

With regard to number of suppliers, a majority of those who responded 58.7% had strongly agreed while 10.7% agreed they had larger supplies that had significant influence in their businesses. A total of 14.7% disagreed while 6.7% disagreed strongly and 9.3% of those who responded were indifferent meaning they neither agreed nor disagreed.

Additionally, the findings of the study show that a majority 62.7% strongly agreed and 10.75 disagreed which totaled to 73.4% who said they faced completion form substitute products in the market from other firms. A total of 13.7 disagreed while 6.7% disagreed strongly their businesses was receiving stiff completion from substitute products from other companies in the market.

Finally, most of those who responded (62.7%) strongly agreed and 8% agreed that their business was facing threats from new entrants into the market. A total of 10.9% were indifferent while 12% disagreed and 6.6% strongly disagreed they faced threats from new entrants into the market.

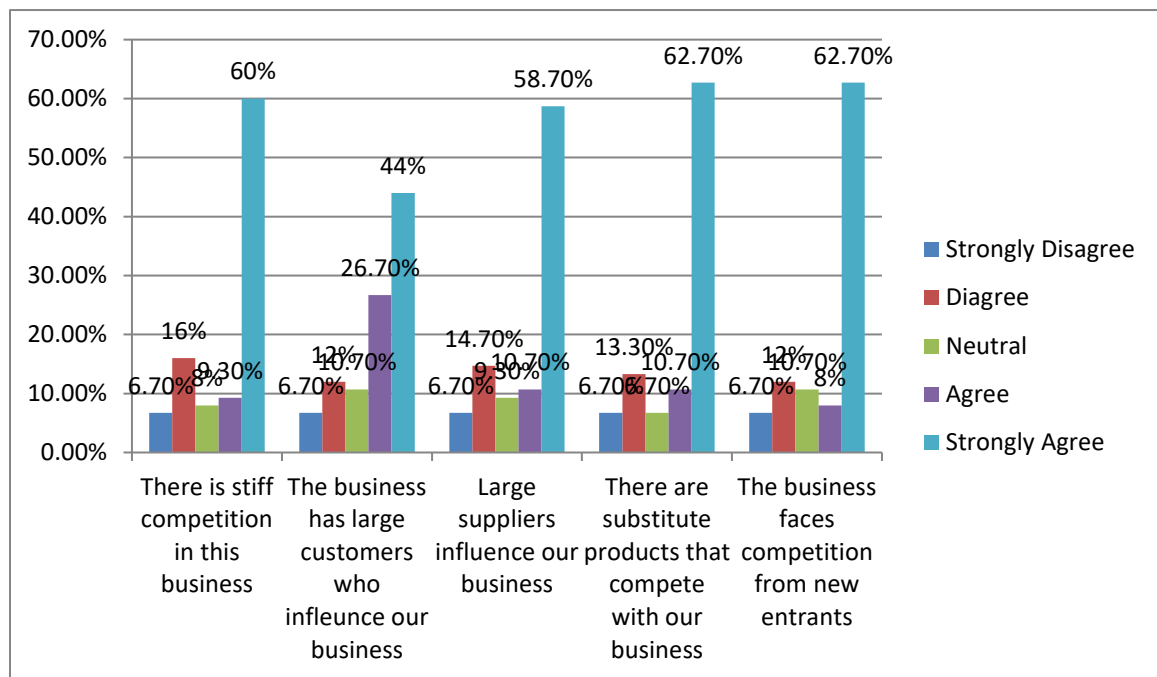


Figure 4.7 Competition

4.5 Legislation and Usage by SMEs of Accounting Services

The study determined the influence of legislation on use of accounting services. The Findings are as illustrate in Table 4.8 below. Most strongly disagreed (49.3%) and 34.7% disagreed which totaled to 84% of respondents who disagreed that they had fully complied with legal requirements to prepare proper books of accounts. Only 5.1% agreed and 10.4% were indifferent because they neither agreed nor disagreed that they had complied with the legal requirement to prepare proper books of accounts.

A majority 41.3% of those who responded strongly disagreed and another 37.3% disagreed which totaled to 78.6% of respondents who disagreed that they had complied with the legal requirement to have tax register machines in order to give tax receipts in their businesses.

A total of 8% agreed while 4% disagreed strongly they had complied. However, 9.35 of the respondents were indifferent meaning that they neither agreed nor disagreed.

Additionally, study findings indicated that 37.3% of those who responded strongly disagreed and another 30.7% disagreed that they have complied with legal requirements of issuing tax receipts in their businesses. 12% agreed while 8% agreed strongly to have complied while 12% were neutral. Finally, the results showed that a majority of the respondents disagreed and another 28% strongly disagreed which totaled to 62.7% of respondents who disagreed that they had complied with legal requirement to file annual tax returns. A total of 14.7% agreed and 9.3% strongly agreed, while 13.3% of the respondents were indifferent meaning they neither agreed nor disagreed with the statement.

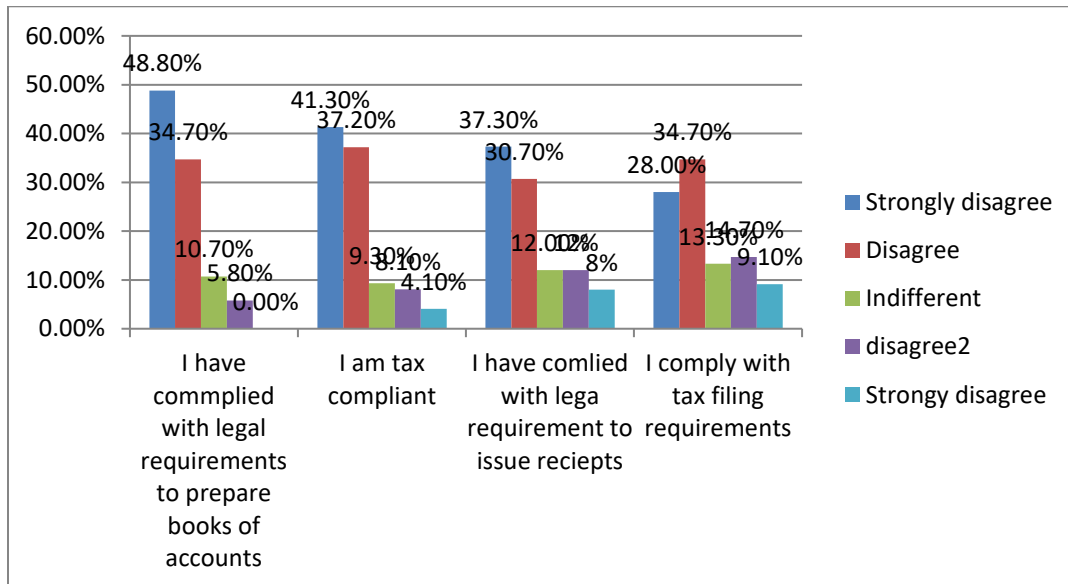


Figure 4.8: Legislation and use of Accounting Services by SMEs

4.6 SME Growth in Size

The study sought to ascertain SME growth in size and how this determined the use of accounting services. Figure 4.9 below illustrates the findings which show a majority

disagreed that they had increased the number of employees over the previous five years that they had been in operation while 20% strongly disagreed with this statement. This totaled to 72% of respondents who disagreed that they had recorded a growth in the size of their human resource in their SMEs. The results showed that 16% agreed that their employees had increased while 12% were neutral.

A total of 42.7% disagreed and another 18.7% disagreed strongly that they had recorded growth in sales over the previous five years that their businesses had been in operation. However, 28% agreed that they had increased their sales volumes in the previous five years that they had been in operation. Further, the findings revealed that 50.7% disagreed and 21.3% disagreed strongly they had recorded increases in assets in the previous five years that they had been in operation. This indicates that across the sampled SMEs, there was recorded minimal growth.

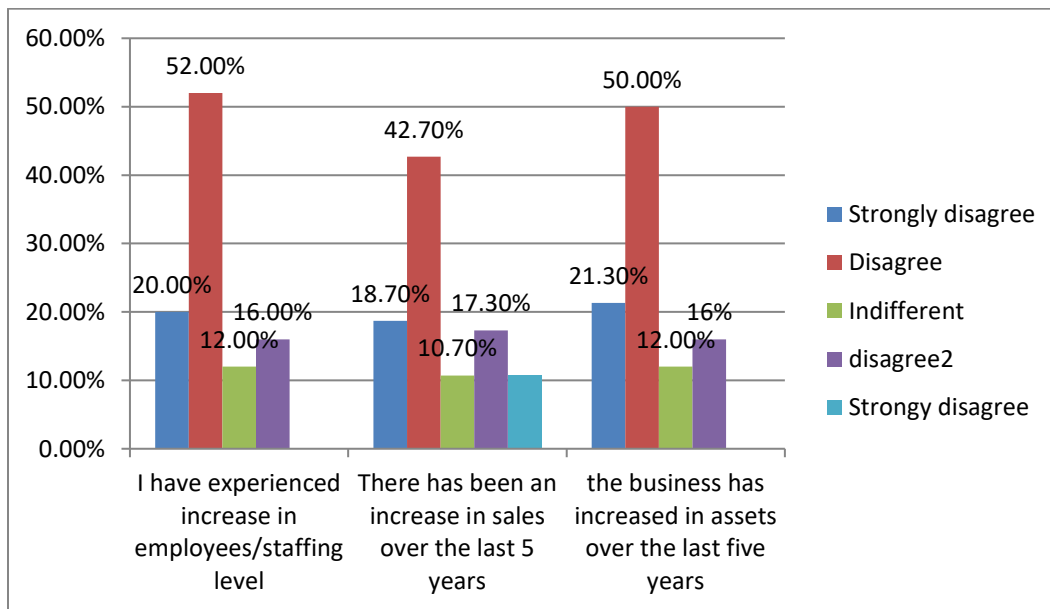


Figure 4.9: SME Growth in size

4.7 Analytical model

In order to empirically determine if the independent variables had a significant effect on use of accounting services in SMEs, regression analysis was done and results are as indicated in table 4.2 below which indicate the goodness of fit between the independent variables and accounting services use was satisfactory. R squared was 0.632 which showed that 63.2% of the variances in SMEs use of accounting services were explained by the independent variable variances.

Table 4.1: Summary

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.794 ^a	.632	.612	42702.936

a. Predictors: (Constant), Growth, Knowledge and Competence, Competition, Legislation

The overall model was significant as indicated by the Anova statistics. The F statistic of 30.021 and p-value of 0.000 supported the argument. Probability that was reported was less than conventional probability of 0.05 (5%) significance level.

Table 4.2: ANOVA

Model	Sum of Squares	df	Mean Square	F	Sig.
1 Regression	2.190E11	4	5.474E10	30.021	0.00 ^a
Residual	1.276E11	70	1.823E9		
Total	3.466E11	75			

a. Predictors: (Constant), Growth, Knowledge and Competence, Competition, Legislation

b. Dependent Variable: Use of Accounting Services

From the findings, the existing relationship between knowledge and competence, competition, legislation, growth, and use of accounting services is positive and significant (b 1= 16303.27, p value, 0.028, bl = 15516.65, p value, 0.040, bl=27920.73. p value, 0.002, bl = 15311.53, p value, 0.018).

This finding gives the implication that ‘Knowledge and Competence’ and ‘Competition’ do not influence accounting services use. ‘Legislation does not determine use of accounting services in SMEs’ and ‘SME growth in size is not a determinant are all rejected at 0.005 level of significance.

The alternative statements are acceptable. Thus,

- a) Knowledge and Competence determine SMEs use of accounting services.
- b) Competition determines SMEs use of accounting services.
- c) Legislation determines SMEs use of accounting services.
- d) Growth in size determines SMEs use of accounting services.

Table 4.3: Coefficients

Model	Unstandardized Coefficients		Standardized Coefficients	t	Sig
	B	Std Error			
1 (Constant)	-126860.781	16351.44		-7.758	0.000
Knowledge and Competence	16303.9	7245.3	.218	2.250	0.28
Competition	15516.6	739603	.203	2.098	0.40
Legislation	27920.0	8565.4	.362	3.260	.002
Growth	15311.1	6319.9	.204	2.423	.018

a. Dependent Variable: Use of Accounting Services

4.8 Discussion

40% strongly disagreed to having attended courses to be trained on accounting and book-keeping skills while 29.3% disagreed with this, which brought the total to 69.3% of respondents who disagreed with this statement.

Only 13.3% agreed and 17.3% were indifferent as to whether they had received training on accounting and bookkeeping. Additionally, 44% of those who responded strongly disagreed and 20% disagreed that they had been trained on computer skills while 22.7% did not agree or disagree with this statement. However, 8% strongly agreed and another 5.3% agreed that they had attended training on computer use. 40% strongly disagreed and

another 37.3% disagreed totaling to 77.3% of respondents who disagreed that they had been trained on sales and marketing. 9% were neutral and only 8% agreed strongly and 5.3% agreed that they had been trained on sales and marketing.

Further, 41.3% disagreed and another 34.7% strongly disagreed totaling to 76% of respondents who disagreed they faced stiff competition shown by price undercutting. Only 9.3% agreed, 6.7% strongly agreed and 8% were indifferent with the statement.

The results further indicate majority 40% of those who responded agreed and another 36% strongly disagreed totaling to 76% of people who disagreed with this statement that a large number of customers exerted their influence in their SMEs. Further, 13.3% agreed and 4% strongly agreed, while 10.7% were indifferent.

Further, 45.3% disagreed and another 29.3% strongly disagreed bringing a total of 74.6% who did not agree they had large suppliers who had major influence in their business. Additionally, 37.3% of those who responded strongly disagreed and another 36% disagreed which brought the total to 73.3% that did not agree their businesses faced stiff competition from substitute products from other firms. Finally, the findings reveal that 38.7% disagreed and another 33.3% disagreed strongly which totaled to 72% of respondents who disagreed that their SMEs faced threats from new entrants into the market.

Further, 49.3% strongly disagreed and another 34.7% disagreed which brought the total to 84 of respondents who had disagreed that they had complied with legal requirements to prepare proper books of accounts. Only 5.3% agreed that they had complied by preparing proper books of accounts.

A majority of those who responded 41.3% strongly disagreed and another 37.3% disagreed which brought the total to 78.6% of respondents who disagreed that they had complied with legal requirements of installing tax registers. A total of 8% agreed while 4% were indifferent meaning they neither agreed nor disagreed with the statement.

Additionally, study findings indicated that 37.3% of those who responded strongly disagreed and another 30.7% disagreed that they have complied with legal requirements of issuing tax receipts in their businesses. Only 12% agreed and 8% agreed strongly they complied while 12% were neutral. Finally, the results showed that a majority of the respondents disagreed and another 28% strongly disagreed which totaled to 62.7% of respondents who disagreed that they had complied with legal requirement to file annual tax returns. A total of 14.7% agreed and 9.3% strongly agreed, while 13.3% of the respondents were indifferent meaning they were indifferent.

R squared was 0.632 which showed that 63.2% of the variances in the use of accounting services by SMEs were explained by independent variable variances.. The overall model was significant as indicated by the Anova statistics. The F statistic of 30.021 and p-value of 0.000 supported this argument. From the findings, the existing relationship between knowledge and competence, competition, legislation, growth, and use of accounting services is positive and significant (b 1= 16303.27, p value, 0.028, bl = 15516.65, p value, 0.040, bl=27920.73. p value, 0.002, bl = 15311.53, p value, 0.018).

CHAPTER FIVE

SUMMARY, CONCLUSIONS AND RECOMMENDATIONS

5.1 Summary of Findings

This study's general objective was to establish the determinants of use of accounting services in SMEs in Nairobi.

Findings reveal 40% were female and 60% male. This implies that most of the sampled organizations were predominantly male. Recent census results in 2019 reveal that a majority of the population is female. The data reveals the inverse despite sensitization efforts for gender equality in Kenya. 20% of the respondents indicated that they were managers of the businesses and 80% owned the business. A majority of the respondents were aged between 18-30 years (60%), and the next large age category was aged between 31-50 years (28%). The finding shows that younger people are starting more businesses when compared to the aged.

The finding further showed that most of the respondents (64%) possessed an experience of 2-5 years, followed by 15% who had an experience of 6-10 years. A majority of the respondents had less than 10 employees (63%) and 28% were partners while 72% of the respondents were sole proprietors. In terms of education, 67% had secondary education, 19% had a form of tertiary education and 14% were graduates from universities.

The study investigated the influence of knowledge and competence on use of accounting services by SMES. A majority of the respondents disagreed with they had a form of training on book keeping and accounting skills (69%). 13.3% only agreed with that statement and

17.3% neither disagreed nor agreed. Additionally, 44% of the respondents strongly disagreed and 20% disagreed which totaled to 60% of respondents who disagreed that they had received a form of training course in computer use, while 22.7% were indifferent. Only 8% strongly agreed and another 5.3% agreed that they had been trained on computer use. The findings further showed that 405 of the respondents strongly disagreed and another 37.3% disagreed totaling to 77.3% of respondents who disagreed that they had been trained on sales and marketing. Nine percent were indifferent on whether they had attended a training on sales and marketing.

The study had another objective of ascertaining the effect that competition in the market had on SMEs use of accounting services. The findings show (41.3%) disagreed and 34.7% strongly disagreed totaling to 76% of respondents who disagreed that competition in their business was stiff with rival firms undercutting their businesses. Respondents who agreed were only 9.3% and 6.7% agreed strongly. Eight percent of those who responded were indifferent.

Further, 40% disagreed and another 36% strongly disagreed totaling to 76% of respondents who were not in agreement with this statement that their business had large customers who had a major influence on their businesses operations. The findings also show that 13% of the respondents agreed and 4% strongly agreed, with 10.7% neither agreeing nor disagreeing with this statement.

45.3% disagreed and another 29.3% strongly disagreed totaling to 74.6% disagreed that their SMEs had a large number of suppliers had a significant influence on their business

operations. A total of 10.7% strongly agreed and 9.3% neither agreed nor disagreed with this statement.

The findings further show that a majority of the respondents 37.3% strongly disagreed and another 36% disagreed totaling to 73.3% of respondents who disagreed with the statement that their business faced stiff competition particularly from substitute products from other SMEs. Only 10.7% agreed and 9.3% strongly agreed totaling to 20% with this statement. The findings finally showed that most of the respondents (38.7%) disagreed and 33.3% strongly disagreed totaling to 72% of respondents who disagreed with the statement that their business faced competition from new market entrants.

This study also sought to determine the effect of legislation on use of accounting services by SMEs in Kenya. The findings of the study show that a majority of the respondents 49.3% strongly disagreed and another 34.7% disagreed totaling to 84.5% of respondents who disagreed that they had fully complied with legal requirements to prepare proper books of accounts. Only 5.3% agreed that they prepare proper books of accounts and 11% of the respondents were indifferent with the statement.

Further the findings of the study showed that 37.3% of the respondents strongly disagreed and another 30.7% disagreed totaling to 68% of respondents who disagreed with the statement that they have fully complied with legal requirements to issue tax receipts for transactions.

Finally, the findings show that a majority of the respondents 34.7% disagreed and 28% disagreed strongly which brought the total to 62.7% of respondents who disagreed that they had fully complied with legal requirements to file annual tax returns. A total of 14.7% of the respondents agreed while 9.3% strongly agreed and 13.3% were indifferent on the statement.

The study also sought to establish the extent to which growth in size of SME determined the use of accounting services by SMEs in Kenya. The findings of the study from this objective show that majority of the respondents (52%) disagreed that the number of employees in their firm had increased over the last five years while 20% strongly disagreed. Forty three percent (43%) of the respondents disagreed and another 19% strongly disagreed that there was an increase in sales in a time span of the previous five years.

Finally, about 51% of the respondents disagreed and another 22 percent strongly disagreed that there was growth in assets in their business over the previous five years that they had been in operation. Most of the firms had experienced little growth as revealed by the findings of the study.

The findings indicated that there was little use of accounting services by SMEs. This is probably due to a lack of investment in accounting services. Regression analysis showed existence of a positive significant and strong relationship. Respondents who highly rated factors that determined use of accounting services were also likely to highly rate use of accounting services.

5.2 Conclusion

From the findings of the study, it could be concluded that knowledge and competence of the respondents was low. This is because a majority of them had not undergone training as they indicated on the statements. Most of the owners of the SMEs had not been trained on sales and marketing skills, accounting and book keeping.

Rivalry among the firms was evident as indicated by price undercuts. The study also concluded that suppliers and customers had a high bargaining power. New entrants and new products also were threats to already existing businesses. The study also concluded that competition was rife among the SMEs hence the need to use accounting services.

The study also concluded that most of the SMEs had not grown in size as indicated by a majority of the respondents who said that they had not had a significant increase in the number of employees in the previous five years that they had been in operation. Based on the findings of the study it was possible to conclude that there was a significant relationship between use of accounting services and knowledge and competence. A positive relationship also exists between legislation, number of competitors and use of accounting services. The growth in SMEs also had a positive and significant relationship as a determinant of use of accounting services.

5.3 Policy Recommendations

The study recommends that more training need to be done in SMEs to equip them with more knowledge and enhance their competence levels. More training on accounting and book keeping, sales and marketing and computer use will enhance the skills and capacity in these SMEs.

SMEs need to hire qualified accountants to address the challenges that SMEs face such as stiff competition. This will enhance proper book keeping and in addition encourage the adherence to legal requirements of maintain proper books of accounts. This will also promote the growth of SMEs

5.4 Limitations of the Study

This study was not industry specific and sampled SMEs operating in various different fields. The SMEs may not be facing the same business operations and challenges and as such, factors such as competition and legal requirements were generalized to all the sampled SMEs.

The findings of the study were also based on small SMEs and cannot be generalized to larger and medium organizations which have different business models and varying business environments.

5.5 Areas for Further Study

A study on SMEs in a specific industry setup such as manufacturing, processing, finch, hospitality, financial services, communication or cyber security among other industries will give industry specific results.

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APPENDICES

Appendix I: Questionnaire

This questionnaire is concerned with investigating the determinants influencing the use of accounting services among SMEs in Nairobi.

SECTION A: Firm and Owner/Manager Characteristics

1. What is the number of years that your business has been in existence?
 - a) One year or less []
 - b) Between 2 and 5 years []
 - c) Between 6 and 10 years []
 - d) 11 years and more []

2. What is the size of employees in your organization?
 - a) Don't have any []
 - b) Between 1 and 10 []
 - c) Between 11 and 50 []
 - d) More than 50 []

3. What is the legal registration status of your business?
 - a) Partnership []
 - b) Sole proprietorship []
 - c) Limited Company []

4. Please indicate your highest level of education attained.
 - a) University []
 - b) Tertiary []
 - c) Secondary []
 - d) Primary []

Section B: Competence levels

5. Please rate the following statements appropriately in relation to your organization.

Scale: 5: strongly agree; 4: Agree; 3: Neutral; 2: Disagree and 1: Strongly disagree.

Statement	1	2	3	4	5
I am conversant with accounting and book keeping skills					
I am conversant with sales and marketing skills					
I have attended training on computer use					

SECTION C: Market competitors

6. This part deals with market competition in your industry. Please indicate appropriately based on your level of agreement.

Statement	1	2	3	4	5
The competition in this business is stiff and rival and this shown by price undercuts					
This business has large customers who exert their influence in our business					
This business has large suppliers who exert their influence in our business					
This business is facing competition with substitute products from other firms					
This business is facing competition from new entrants into the market					

SECTION D: Legal requirements and SMEs use of accounting services

7. This part deals with legal requirements in your industry. Please indicate appropriately based on your level of agreement.

Statement	1	2	3	4	5
The organization has fully complied with legal regulations of preparing and maintain proper books of accounts					
I have installed a tax register as per legal requirements					
I issue tax receipts for all sales done in my business					
I annually file my tax returns as required by law					

E: COST OF THE USE OF ACCOUNTING SERVICES

Year	Cost of hiring an internal professional accountant	Total Cost of preparing books of accounts	Total cost of setting up and maintain internal control systems	Total cost of computing and filing tax returns	Total
2018					
2017					
2016					
2015					
2014					