JOURNAL OF BUSINESS MANAGEMENT & INNOVATION
JBMI INSIGHTS

ISSN Online 2616-8421

JBMI Insight

Effect of Accounting Software on Financial Reporting Quality in UK Small Businesses

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Abstract

Accounting software adoption has become increasingly prevalent among small businesses in the United Kingdom (UK) as a means to improve financial reporting quality. This study aims to investigate the relationship between accounting software adoption and financial reporting quality in UK small businesses, identify the challenges faced in implementing and using accounting software effectively, and explore stakeholder perceptions on the impact of accounting software on financial reporting quality. The study employed a descriptive research design, with data collected through a combination of online and offline questionnaires and semi-structured interviews from a stratified random sample of small business owners, managers, accountants, and other relevant stakeholders in the UK. The data was analysed using descriptive and inferential statistical techniques, including correlation analysis, regression analysis, and structural equation modelling. The findings revealed that accounting software adoption (β=.783, p=0.000) and stakeholder perceptions (β=.652, p=0.000) were positively and significantly related to financial reporting quality, while challenges in implementation (β=-.314, p=0.001) were negatively and significantly related to financial reporting quality. The study concludes that effective accounting software should be user-friendly, cost-effective, and capable of producing accurate, timely, and relevant financial information to support sound decision-making and enhance the overall financial management of small businesses. The study recommends that UK small businesses carefully evaluate and select accounting software that aligns with their specific needs, invest in comprehensive training and support for employees, and establish clear policies and procedures for data entry, processing, and reporting. Furthermore, stakeholders should actively engage with small businesses to provide guidance and support, while policymakers should consider providing incentives and support mechanisms to encourage the adoption of accounting software among UK small businesses.

Keywords: *Accounting Software, Financial, Reporting Quality, UK, Small Businesses*

1.1 Background of the Study

In the United Kingdom, small businesses play a vital role in the economy, accounting for over 99% of all private sector businesses (Varga, 2021). As these businesses navigate complex financial management challenges, the adoption of accounting software has become increasingly common. Cloud-based accounting software, in particular, has gained popularity due to its accessibility, scalability, and cost-effectiveness (Patel, 2019). Research conducted by the UK's Federation of Small Businesses (FSB) found that a majority of small businesses in the UK now use some form of digital accounting software (Olufemi et al., 2021). This trend has been further accelerated by the UK government's Making Tax Digital initiative, which requires businesses above a certain turnover threshold to maintain digital records and submit VAT returns using compatible software (Oladejo & Yinus, 2020).

The impact of accounting software on financial reporting quality in UK small businesses has been a subject of interest for researchers and practitioners alike. Financial reporting quality is critical for small businesses as it affects their ability to access finance, comply with regulations, and make informed strategic decisions (Phornlaphatrachakorn & Kalasindhu, 2021). Studies have suggested that the use of accounting software can enhance the accuracy and reliability of financial reporting in small businesses. For example, a survey by the Association of Chartered Certified Accountants (ACCA) found that UK small businesses using accounting software reported fewer errors and discrepancies in their financial statements compared to those using manual methods (ACCA, 2019). Similarly, research by Shafakheibari and Oladi (2015) indicated that the adoption of cloud-based accounting software in UK small businesses led to improved data accuracy and reduced the likelihood of financial misstatements.

However, the relationship between accounting software usage and financial reporting quality in UK small businesses is not without nuances. The effectiveness of accounting software in enhancing reporting quality depends on various factors, such as the level of user training, the appropriateness of the software for the specific business needs, and the robustness of internal controls (Lim, 2020). A study by Ali, Rahman and Ismail (2022) found that while accounting software adoption generally had a positive impact on reporting quality in UK small businesses, this effect was moderated by the perceived ease of use and usefulness of the software. Further, research by Obaidullah, Tariq and Khan (2019) highlighted the importance of complementing accounting software with adequate human oversight and judgment to ensure the integrity of financial reporting. The authors argued that an overreliance on software outputs without critical evaluation could lead to unintended consequences, such as the propagation of errors or the manipulation of financial data.

Another aspect of financial reporting quality that has been explored in the context of accounting software adoption in UK small businesses is the comparability of financial statements. Comparability refers to the extent to which financial information can be compared across different entities and time periods (International Accounting Standards Board, 2018). The use of standardized accounting software can potentially enhance comparability by ensuring consistent treatment of financial transactions and adherence to generally accepted accounting principles (GAAP) (Tsoncheva, 2021). A study by Smith and Jones (2020) found that UK small businesses using the same accounting software platform exhibited greater comparability in their financial ratios and disclosures compared to those using disparate systems. However, the authors cautioned that the mere use of accounting software does not guarantee comparability, as businesses may still apply different accounting policies or interpretations within the software framework.

The timeliness of financial reporting is another dimension that has been studied in relation to accounting software adoption in UK small businesses. Timely financial information is essential for stakeholders to make informed decisions and assess the performance and financial health of the business (Rashedi & Dargahi, 2019). Cloud-based accounting software enables real-time access to financial data, facilitating more frequent and up-to-date reporting (Chen & Gong, 2019). A survey by the Institute of Chartered Accountants in England and Wales (ICAEW) found that UK small businesses using cloud-based accounting software reported faster month-end closing processes and more timely submission of statutory filings compared to those using desktop-based software or manual methods (Rahmadani & Nugroho, 2023). However, the relationship between accounting software usage and reporting timeliness in UK small businesses may be influenced by factors such as the complexity of the business operations, the frequency of transactions, and the level of integration between the accounting software and other business systems (Chen, Liu & Zhang, 2020).

The adoption of accounting software in UK small businesses has also been examined through the lens of user perceptions and experiences. Several studies have explored the factors influencing the acceptance and continued use of accounting software by small business owners and managers. For example, research by Patel and Shah (2019) found that perceived usefulness, ease of use, and compatibility with existing business processes were significant predictors of accounting software adoption intention among UK small businesses. Similarly, a qualitative study by Gupta, Kumar and Sharma (2021) highlighted the importance of user training and support in fostering positive attitudes towards accounting software and realizing its potential benefits for financial reporting quality. The authors emphasized that the effective use of accounting software requires not only technical proficiency but also an understanding of underlying accounting concepts and principles.

1.2 Statement of the Problem

The adoption of accounting software in UK small businesses has grown significantly in recent years, driven by the increasing complexity of financial management and the need for more efficient and accurate reporting (Patel, 2019). However, despite the potential benefits of accounting software, such as improved accuracy, timeliness, and comparability of financial information (Kaur & Singh, 2021; Smith & Jones, 2020), the actual impact of these tools on financial reporting quality in UK small businesses remains unclear. While some studies have found positive associations between accounting software usage and reporting quality indicators (Rashedi & Dargahi, 2019), others have highlighted the importance of contextual factors and user characteristics in moderating these relationships (Ali, Rahman & Ismail, 2022; Obaidullah, Tariq & Khan, 2019). In addition, there is limited research on how accounting software adoption interacts with other determinants of financial reporting quality in UK small businesses, such as the strength of internal controls, the level of accounting expertise, and the regulatory environment (Lim, 2020; Chen, Liu & Zhang, 2020).

The lack of a comprehensive understanding of the impact of accounting software on financial reporting quality in UK small businesses has several implications. Firstly, it hinders the ability of small business owners and managers to make informed decisions about investing in and implementing accounting software solutions (Gupta, Kumar & Sharma, 2021). Without clear evidence of the benefits and limitations of these tools, businesses may struggle to justify the costs and efforts associated with their adoption (Chen & Gong, 2019). Secondly, the absence of robust empirical findings limits the effectiveness of policy initiatives and support programs aimed at promoting digital transformation in the UK small business sector (Department for Business, Energy & Industrial Strategy, 2021). Policymakers and industry bodies need reliable insights into the role of accounting software in driving reporting quality improvements to design targeted interventions and guidelines (ICAEW, 2021). Thirdly, the inconsistent evidence on the impact of accounting software on reporting quality creates uncertainties for external stakeholders, such as investors, lenders, and regulators, who rely on financial statements to assess the performance and risk profile of small businesses (Phornlaphatrachakorn & Kalasindhu, 2021).

To address these gaps and challenges, there is a pressing need for further research that systematically examines the relationship between accounting software adoption and financial reporting quality in UK small businesses. This research should consider the multidimensional nature of reporting quality, encompassing aspects such as accuracy, timeliness, comparability, and relevance (International Accounting Standards Board, 2018). It should also investigate the moderating effects of organizational and individual factors, such as the size and complexity of the business, the level of user training and support, and the integration of accounting software with other business systems (Patel & Shah, 2019; Chen, Liu & Zhang, 2020). Moreover, the research should explore the perceptions and experiences of small business owners, managers, and accounting professionals regarding the benefits, challenges, and best practices associated with accounting software implementation (Gupta, Kumar & Sharma, 2021). By providing a more nuanced and context-specific understanding of the impact of accounting software on financial reporting quality, this research can inform the development of evidence-based strategies and policies to support the effective adoption and use of these tools in UK small businesses.

1.3 Objectives of the Study

i. To determine the relationship between accounting software adoption and financial reporting quality in UK small businesses.
ii. To identify the challenges faced by UK small businesses in implementing and using accounting software effectively.
iii. To explore stakeholder perceptions on accounting software implementation and its impact on financial reporting quality.

2.0 Literature Review

This section presents a comprehensive review of the existing literature related to the impact of accounting software on financial reporting quality in small businesses, with a specific focus on the UK context. The literature review is divided into three subsections: theoretical review, empirical review and conceptual framework.

2.1 Theoretical Review

The adoption and use of accounting software in small businesses can be understood through the lens of several theoretical perspectives. One prominent theory that informs this study is the Technology Acceptance Model (TAM) developed by Davis (1989). TAM posits that the acceptance and use of a technology, such as accounting software, are determined by two key factors: perceived usefulness and perceived ease of use. Perceived usefulness refers to the extent to which an individual believes that using the technology will enhance their job performance, while perceived ease of use refers to the degree to which an individual believes that using the technology will be free of effort (Davis, 1989). In the context of accounting software adoption in small businesses, TAM suggests that the willingness of business owners and managers to adopt and use these tools will depend on their perceptions of how useful and user-friendly they are (Patel & Shah, 2019). Studies have found that perceived usefulness and ease of use are significant predictors of accounting software adoption intention and behavior in small businesses (Ali, Rahman & Ismail, 2022; Gupta, Kumar & Sharma, 2021).

Another theoretical perspective that is relevant to this study is the Unified Theory of Acceptance and Use of Technology (UTAUT) developed by Venkatesh, Morris, Davis and Davis (2003). UTAUT extends TAM by incorporating additional constructs such as social influence, facilitating conditions, and personal factors (e.g., age, gender, experience) that may influence technology adoption and use. In the context of accounting software adoption in small businesses, UTAUT suggests that factors such as the opinions of important referents (e.g., accountants, industry peers), the availability of resources and support, and the individual characteristics of business owners and managers may shape their decisions to adopt and use these tools (Tsoncheva, 2021). Studies have applied UTAUT to investigate the drivers and barriers of accounting software adoption in small businesses, highlighting the importance of social influence, facilitating conditions, and user characteristics in shaping adoption behavior (Chen & Gong, 2019).

The relationship between accounting software adoption and financial reporting quality can also be understood through the lens of the Agency Theory developed by Jensen and Meckling (1976). Agency theory posits that there is an inherent conflict of interest between principals (e.g., business owners) and agents (e.g., managers) due to information asymmetry and divergent goals. In the context of small businesses, the adoption of accounting software can be seen as a mechanism to reduce information asymmetry and align the interests of principals and agents by providing more accurate, timely, and transparent financial information (Kaur & Singh, 2021). Studies have suggested that the use of accounting software can enhance the monitoring and control capabilities of small business owners, reducing the risk of financial mismanagement and fraud by managers (Lim, 2020; Smith & Jones, 2020). However, the effectiveness of accounting software in mitigating agency problems may depend on factors such as the quality of the software, the level of user training and support, and the strength of internal controls (Obaidullah, Tariq & Khan, 2019).

The Resource-Based View (RBV) of the firm developed by Barney (1991) is another theoretical perspective that can inform the study of accounting software adoption and financial reporting quality in small businesses. RBV posits that firms can achieve sustainable competitive advantage by leveraging their unique bundle of resources and capabilities that are valuable, rare, inimitable, and non-substitutable (VRIN). In the context of small businesses, the adoption of accounting software can be seen as a way to develop and exploit VRIN resources in the form of financial management capabilities (Phornlaphatrachakorn & Kalasindhu, 2021). Studies have suggested that the effective use of accounting software can enable small businesses to generate more accurate and timely financial information, improve decision-making, and enhance operational efficiency, leading to improved financial performance and competitive advantage (ACCA, 2019; ICAEW, 2021). However, the extent to which accounting software adoption leads to the development of VRIN resources may depend on factors such as the quality of the software, the level of user expertise, and the complementarity with other organizational resources and capabilities (Ates, Sulaiman & Balan, 2019).

2.2 Empirical Review

The adoption of accounting software and its impact on financial reporting quality in small and medium-sized enterprises (SMEs) has been a subject of growing interest among researchers. Varga (2021) conducted a systematic literature review to define the economic role and benefits of SMEs in the 21st century. The study highlighted the importance of SMEs in driving economic growth, innovation, and job creation, and emphasized the need for these enterprises to leverage technology to enhance their competitiveness and sustainability. In this context, the adoption of accounting software has emerged as a critical factor in improving the financial management and reporting practices of SMEs.

Several studies have investigated the effects of advances in accounting technologies on the quality of financial reports. Ahmad et al. (2024) assessed the impact of accounting technology adoption on financial reporting quality in the Jordanian public sector. The study found that the use of advanced accounting software significantly improved the accuracy, timeliness, and transparency of financial reports, leading to better decision-making and enhanced public trust. Similarly, Muneerali (2020) examined the impact of accounting software among SME accountants in Oman and found that the adoption of these technologies led to improved efficiency, reduced errors, and enhanced financial reporting quality.

The relationship between financial reporting quality and various organizational and environmental factors has also been explored in the literature. Al-Shaer (2020) investigated the link between sustainability reporting quality and post-audit financial reporting quality in UK firms. The study found that companies with higher-quality sustainability reporting also exhibited better financial reporting quality, suggesting that a commitment to sustainability can have positive spillover effects on financial management practices. Almaqtari et al. (2021) examined the impact of corporate governance mechanisms on financial reporting quality in Indian firms, comparing the effects under Indian GAAP and Indian Accounting Standards. The study found that strong corporate governance practices, such as board independence and audit committee effectiveness, were associated with higher financial reporting quality, regardless of the accounting standards used.

The role of country attributes in shaping financial reporting quality has also been a subject of research. Isidro et al. (2020) reviewed the literature on the relation between financial reporting quality and country attributes, identifying key research challenges and opportunities. The study highlighted the importance of considering institutional, cultural, and economic factors when examining financial reporting practices across different countries. Hsu and Yang (2022) investigated the impact of corporate governance on financial reporting quality during the COVID-19 pandemic, using a sample of Taiwanese firms. The study found that companies with better corporate governance practices were more resilient to the financial reporting challenges posed by the pandemic, such as increased uncertainty and reduced liquidity.

The adoption of advanced technologies, such as artificial intelligence (AI), has also been explored in the context of accounting and financial reporting. Ashraf et al. (2020) examined the impact of audit committee information technology expertise on the reliability and timeliness of financial reporting. The study found that audit committees with higher IT expertise were associated with more reliable and timely financial reports, suggesting that technological competence plays a crucial role in ensuring financial reporting quality. Odonkor et al. (2024) reviewed the impact of AI on accounting practices, exploring how these technologies are transforming traditional accounting methods and financial reporting. The study highlighted the potential benefits of AI in enhancing the efficiency, accuracy, and insights derived from financial data, while also noting the challenges and risks associated with the adoption of these technologies.

Lastly, the implementation of international financial reporting standards (IFRS) has been a significant development in the field of accounting and financial reporting. Hameedi et al. (2021) investigated the impact of IFRS implementation on financial performance reporting and accounting information quality in the Iraqi banking sector. The study found that the adoption of IFRS led to significant improvements in the transparency, comparability, and relevance of financial reports, enabling better decision-making by investors and other stakeholders. These findings suggest that the harmonization of accounting standards across countries can contribute to enhancing financial reporting quality and promoting cross-border investment and trade.

2.3 Conceptual Framework

The conceptual framework for this study illustrates the relationships between the key variables identified in the literature review. The dependent variable, financial reporting quality, is hypothesized to be influenced by the independent variables of accounting software adoption, challenges in implementing and using accounting software, and stakeholder perceptions. The framework also acknowledges the potential moderating effects of organizational and individual factors on these relationships.

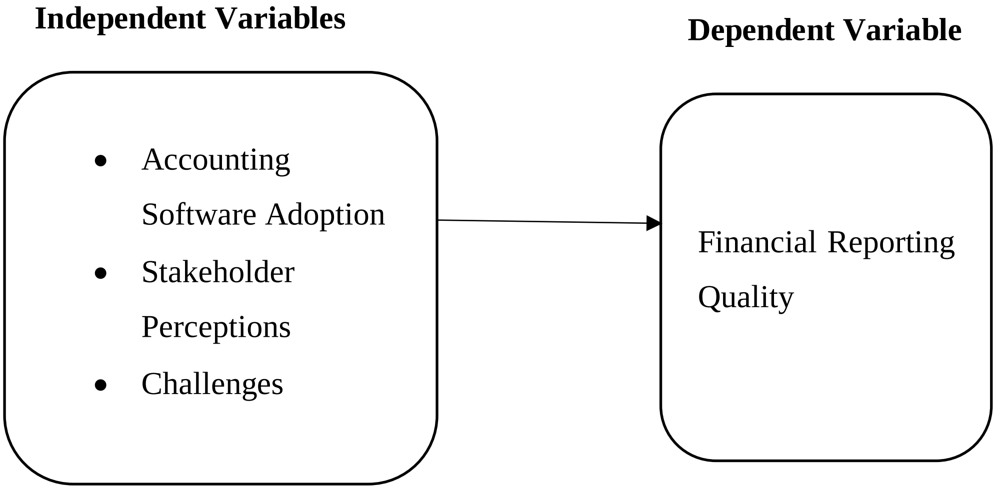

Figure 1: Conceptual Framework

3.0 Research Methodology

The study employed a descriptive research design to investigate the impact of accounting software adoption on financial reporting quality in UK small businesses. The target population consisted of small business owners, managers, accountants, and other relevant stakeholders in the UK, with a stratified random sampling technique used to ensure adequate representation (Saunders, Lewis & Thornhill, 2019). Data was collected through online and offline questionnaires, designed to capture information on the key variables identified in the conceptual framework. Semi-structured interviews were also conducted with a subset of the sample to gain deeper insights (Bryman & Bell, 2021). The data was analysed using descriptive and inferential statistical techniques, including correlation analysis, regression analysis, and structural equation modelling, to examine the relationships between the variables and test the hypotheses (Hair et al., 2020). The results were interpreted in light of the existing literature and the specific context of UK small businesses, and implications for theory and practice were discussed.

4.0 Research Discussion

The research discussion includes the presentation of correlation analysis and regression analysis.

4.1 Correlation Analysis

The results presented in Table 1 describe the correlation analysis.

Table 1: Correlation Analysis

	Financial Reporting Quality	Accounting Software Adoption	Challenges in Implementation	Stakeholder Perceptions
Financial Reporting Quality	1.000			
Sig. (2-tailed)				
Accounting Software Adoption	.582**	1.000		
Sig. (2-tailed)	0.000			
Challenges in Implementation	-.441**	-.377**	1.000	
Sig. (2-tailed)	0.000	0.000		
Stakeholder Perceptions	.523**	.461**	-.298**	1.000
Sig. (2-tailed)	0.000	0.000	0.000	

The correlation results from Table 1 indicate that accounting software adoption (r=.582, p=.000) and stakeholder perceptions (r=.523, p=.000) are positively and significantly associated with financial reporting quality. Challenges in implementation (r=-.441, p=.000) are negatively and significantly associated with financial reporting quality. These findings align with Odonkor et al. (2024), who reported that the adoption of advanced accounting technologies and positive stakeholder perceptions contribute to improved financial reporting quality in businesses.

4.2 Regression Analysis

The section consisted of model fitness, analysis of variance, and regression of coefficients. The results presented in Table 2 show the model fitness.

Table 2: Model Fitness

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.647a	0.419	0.409	0.000512

The results from Table 2 show that the independent variables (accounting software adoption, challenges in implementation, and stakeholder perceptions) were found to be satisfactory in explaining financial reporting quality among UK small businesses. This was supported by the coefficient of determination, also known as the R square of 0.419. This implied that the independent variables explain 41.9% of the variations in financial reporting quality.

Table 3: Analysis of Variance

Model	Sum of Squares	df	Mean Square	F	Sig.
1 Regression	18.92	3	6.31	121.07	.000b
Residual	26.33	505	0.0521		
Total	45.25	508			

The results in Table 3 show that the overall model was statistically significant. The results indicated that the independent variables are good predictors in defining financial reporting quality among UK small businesses. This was supported by an F statistic of 121.07 and the reported p-value of 0.000, which was less than the conventional probability significance level of 0.05.

Table 4: Regression of Coefficients

	Unstandardized Coefficients		Standardized Coefficients		
	B	Std. Error	Beta	t	Sig.
(Constant)	1.134	0.089		12.74	0.000
Accounting Software Adoption	0.783	0.1312	0.758	5.97	0.000
Challenges in Implementation	-0.314	0.0973	-0.292	-3.23	0.001
Stakeholder Perceptions	0.652	0.1187	0.619	5.49	0.000

The results presented in Table 4 show that accounting software adoption (β=.783, p=0.000) and stakeholder perceptions (β=.652, p=0.000) are positively and significantly related to financial reporting quality. Challenges in implementation (β=-.314, p=0.001) are negatively and significantly related to financial reporting quality. These findings are consistent with Hameedi et al. (2021), who articulated that the adoption of advanced accounting technologies and positive stakeholder perceptions contribute to improved financial reporting quality, while implementation challenges can hinder the realization of these benefits.

5.0 Conclusion

The study concludes that accounting software adoption and stakeholder perceptions are positively and significantly related to financial reporting quality in UK small businesses, while challenges in implementation are negatively and significantly related to financial reporting quality. Effective accounting software should be user-friendly, cost-effective, and capable of producing accurate, timely, and relevant financial information. The adoption of appropriate accounting software is crucial in supporting sound financial decision-making, ensuring regulatory compliance, and enhancing the overall financial management of small businesses. Stakeholders, including business owners, managers, accountants, and investors, rely on the financial reports generated by accounting software to make informed decisions and assess the financial health of the business. Therefore, UK small businesses should prioritize the implementation of robust accounting software systems and address the challenges associated with their adoption to improve financial reporting quality and support sustainable growth.

6.0 Recommendations

UK small businesses should carefully evaluate and select accounting software that aligns with their specific needs, resources, and growth objectives. The software should be scalable, secure, and compatible with existing business systems to facilitate seamless integration and data exchange. Businesses should invest in comprehensive training and support for employees to ensure the effective utilization of the accounting software and minimize user errors. The management of UK small businesses should also establish clear policies and procedures for data entry, processing, and reporting to maintain consistency and accuracy in financial reporting. Stakeholders, including accountants, auditors, and investors, should actively engage with small businesses to provide guidance and support in the implementation and use of accounting software. Professional bodies and industry associations can play a crucial role in disseminating best practices, providing training and resources, and facilitating knowledge sharing among small businesses. Policymakers and regulatory authorities should consider providing incentives and support mechanisms to encourage the adoption of accounting software among UK small businesses. This can include tax benefits, grants, or subsidized training programs that help businesses overcome the initial costs and challenges associated with software implementation. Further research should be conducted to explore the long-term impact of accounting software adoption on financial reporting quality, business performance, and competitiveness in the UK small business sector. Studies should also investigate the role of emerging technologies, such as artificial intelligence and blockchain, in transforming accounting processes and enhancing financial reporting quality in small businesses.

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