

Systematic Review Approach on Internal Auditing and Financial Performance on SMEs

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Abstract- *The research study delves into the review of internal auditing and financial performance in Southwest, Nigeria. The purpose of the study is to evaluate the relationship between internal auditing and the financial performance of small and medium-scale enterprises in Southwest Nigeria. It also assesses how internal auditors' qualities contribute to the efficacy of the financial performance of SMEs in lowering poverty. However, some significant barriers remain, including limited access to information, lack of compliance with regulations, and inadequate training. According to the study, auditors' quality significantly improves the efficiency of financial performance among SMEs. The findings of this study will aid in a better understanding of the current status of internal audit effectiveness, including the elements that influence it, as well as gaps and potential for future research. Understanding how internal audit effectiveness may be measured, as well as the elements that may influence it, can help organizations better understand their current performance and, ultimately, improve it in the future.*

I. INTRODUCTION

Small and medium-scale enterprises (SMEs) are generally recognized as the engine of economic growth and development in developed and developing nations, Mokuolu and Oluwaleye, (2023). SMEs play a special role in socio-economic development in Nigeria, where they contribute significantly to job creation, income generation, innovation, poverty reduction, and serve as an engine for national development, Adeosun and Shittu, (2021). In terms of many employees, Justus, *et al.*, (2023) have defined SMEs, with 10-49 employees for small enterprises, while medium-sized enterprises are defined with 50- 99 employees. According to Obe, (2025), SMEs have long been recognized as the backbone of economic growth and industrial development, which contributes to economic growth, job creation, and are constantly emerging, growing, and evolving with the changing business environment Owolabi and Ogan, (2022). According

to the Small and Medium Enterprises Development Agency of Nigeria (SMEDANS), SMEs represent 90% of businesses in Nigeria and employ more than 80% of the workforce in the country. SMEs are particularly significant due to their contribution to Gross Domestic Product (GDP), employment generation, and southwest development. SMEs' activities cut across manufacturing, services, and the agricultural sector as well. This makes SMEs a key to the nation's development because both primary and secondary production are involved. For SMEs in Nigeria, where financial mismanagement, poor record keeping, fraud, and lack of compliance with regulations are recurrent challenges, the adoption of internal auditing practices is particularly relevant, Arni *et al.*, (2023).

Internal auditing, on the other hand, is known as a vital mechanism for improving transparency, accountability, and financial performance in an organization (Ezinwa, *et al.*, (2020). As a systematic and independent appraisal function, internal auditing provides assurance and consulting services designed to add value, strengthen internal control, and enhance risk management processes. The Institute of Internal Auditors (IIA, 2018) defines "Internal auditing as an independent, objective, assurance and consulting activity designed to add value and improve an enterprise's operations. An internal audit is a straightforward administrative process that primarily involves inspecting financial documents for operational reviews and presenting the findings to management. This will assist an enterprise in achieving its objectives by bringing a systematic and disciplined approach for evaluating and improving the effective utilization of an organization's resources, providing a true and fair view of the entity's financial statements. According to Wang, *et al.*, (2022), an internal auditor is charged with the responsibility of safeguarding the assets and liabilities of an organization and other services that

will enhance the efficiency and effectiveness of an organization. Effective internal audit (IA) involves evaluating the organization's internal control system and risk management practices to improve an enterprise's effectiveness, Kamara, (2023). The degree to which internal audits are appropriately implemented is to ensure the continuous growth of an enterprise, most especially the SMEs as a result of a changing competitive environment.

Nevertheless, Financial Performance helps to understand an enterprise's business model, the profitability (or loss) of its operations, and how its spending and investing affect the business organization. According to Nieto, (2022), implementing effective financial compliance solutions ensures adherence to legal and ethical standards, reduces the risk of regulatory penalties, and builds trust with stakeholders. This explores strategies for building a compliance culture, enhancing internal processes, continuous monitoring and improvement, and collaborating with external partners to achieve robust financial compliance. However, the financial performance of SMEs is measured in terms of profitability, liquidity, solvency, and growth, which is linked to the quality of their internal control system, Nieto, (2022).

Hence, this study analyzed the contribution of each auditor's quality to the operational performance of SMEs in Southwest, Nigeria. The next section highlights a literature review on the subject matter, and finally conclusion and recommendations were provided in the last section.

II. LITERATURE REVIEW

Conceptual Review

This section focuses on the key concepts variables; of internal auditing, financial performance as well as small and medium scale enterprises (SMEs).

Small and Medium Scale Enterprises (SMEs)

The contributions of Small and Medium Enterprises in the past two decades have been very impressive in both developed and developing countries, Gavurova, *et al.*, (2020). The pursuit of business growth is a key opening to all types of firms, which is particularly important for SMEs. The firms that seek to excel in business growth should be aware of and manage all necessary things in a balanced manner, Daniel, *et al.*, (2024). According to Alshahrani, *et al.*, (2024),

SMEs play the role of economic development via employment opportunity, income generation, export performance, and domestic saving, which ensures entities are widely known as a cushion for unstable economic situations. Adopting free and open-source software (FOSS) in small and medium-sized enterprises (SMEs) has improved efficiency, regulatory compliance, and contributed to sustainable development, Syamsuriana, *et al.*, (2020). Adoption of technology by SMEs within organizations and provision of an in-depth insight to the economy at large and the benefits derived from small and medium-scale enterprises cannot be overemphasized, Seyede, (2022). SMEs are also a contributor to economic development, job creation, and the general health and welfare of economies (Le Nguyen, (2020). The growth of SMEs relies on the entrepreneurial skills of the entrepreneur, who can manage business effectively, achieve profit, identify market opportunities, and enhance innovation by optimizing all available resources, Dian, Fitri and Bertha, (2024). Some factors concerning SME growth are innovation capability, both in developed and developing countries. As the world economy faces prevailing challenges, governments increasingly start to turn to SMEs as a significant element of sustainable and inclusive economic growth. In developing countries, SMEs contribute to economic growth, job creation, poverty alleviation, and inclusive growth in local areas. SMEs bring sustainability and environmental action together for a better future, Koutsopoulos, (2021). An insight into the knowledge of small and medium scale enterprises, which researchers can benefit from, constructing an in-depth understanding of the state of research, as well as influencing concepts of technology adoption in SMEs as part of the benefit derived, Seyedeh, (2022). Amoah, *et al.*, (2022).

According to Adeosun, and Shittu, (2021), an increase in the number of SMEs formation has led to the growth of the economy. However, an increase in the number of micro-small and medium-scale enterprises not only contributed to the development of the economy but also improved the standard of living of the people. The employment elasticity is positive and significant, and shows that the contribution of entrepreneurship regarding employment is the most essential factor that advances economic growth and reduces unemployment. SMEs have impacted economic development based on various aspects such as competitive market

orientation, employment generation, capacity building, and technology innovation. The role of SMEs is significant since the businesses allow for an increased number of jobs and develop competition, which leads to an improved quality of goods and creates different price segments. SMEs financing has significant positive effects on economic growth in Nigeria, Ibitomi, Dada, Ayedogbon, Micah and Aderotimi, (2024). However, Poor performance among Nigerian SMEs has often been traced to poor internal audit, inadequate monitoring mechanisms, and insufficient attention to risk management, which will be the part of the focus of the study, Aldahdooh, (2022).

Internal Auditing

From the very beginning, audits are performed to ascertain the validity and reliability of information and assess a system's internal control. Afolabi and Olukoya (2019) defined internal audit practice as the examination of an organization's financial report, as represented in the financial statements by the internal auditor in the organization. Internal auditing (IA) work helps an organization accomplish its objectives by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of risk management, control, and governance processes (IIA2018). IA also contributes to enhancing the organization's overall governance and ensuring the achievement of its objectives while minimizing risks, Ezinwa, *et al.*, (2020). In addition, activities related to evaluating compliance with laws and regulations and supporting fraud prevention are critical components of effective IA, Wang, *et al.*, (2022). Ensuring compliance and supporting fraud prevention, IA helps the organization to maintain its integrity, ethical standards, and legal obligations while minimizing the risk of financial loss and reputational damage, Nieto, (2022). Internal audit activity refers to a department, team of consultants, or other practitioners that provide independent, objective assurance and consulting services designed to add value and improve an organization's operations. Internal auditing work helps an organization to accomplish its objectives by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of risk management, control, and governance processes (IIA,2018).

According to Sishumba, Saidi, and Nyambe, (2022). internal audit is a process that involves in evaluating and analysing the internal controls within an

organisation by making sure the organisation complies with laws and regulations. Cameran, Campa and Francis, (2022) also stated that, internal audit also responsible for evaluating and improving the corporate governance and accounting processes of the organisation to makes sure that, there are timely and effective data collection and also accurate financial reporting. Internal audit as an activity designed to add value and improve the operations of a company by maintaining independence and high objectivity was defined by Appah, (2022). Due to the independence and high objectivity, internal audit helps in achieving organisation objectives because it evaluates and improves how effective risk management, control, and governance systems are in the organization. Internal audit practice as the examination of the financial report of an organization as represented in the financial statements by the internal auditor in the organization was examined by Afolabi and Olukoya, (2019). However, the goal of an audit is to express an opinion on the person or organization system in question, under evaluation based on work done on a test basis. Senior management relies on Internal Audit (IA) to enhance the controls and reduce the risk as well as improve its operations, while the audit committee relies on IA to achieve robust internal controls and attain a quality of financial reporting as well as maintain compliance with regulations, Eulerich, Marc, Joleen, and David, 2019. Internal audit helps in making decision, improving resource management, and creating an environment that fosters organizational performance and excellence, Langer, Baum, Hartmann, Hessel, Speith, and Wahl, (2021). Moreover, Internal audit in public organizations poses a unique set of challenges, not limited to internal control oversight and regulatory compliance, but also extending to providing strategic advice and generating value, Black, Elzayn, Chouldechova and Goldin, (2022). Internal audit and control affected the accomplishment of organizational goals, Olukayode and Ndubuisi (2020). The importance of internal audit's advisory role in terms of compliance and oversight, and as a key strategic partner for governance and improving the performance of SMEs, Chammaa and Benazzi, (2024) shall be the focus of this journal.

Basic Qualities of an Auditor

Internal audit is a critical function within an organization that helps to ensure the effective operation of internal controls, compliance with laws

and regulations, and the achievement of the organization's goals and objectives. Internal audit quality is characterized by Independence, Objectivity, Competence, Confidentiality, Professionalism, Due Professional Care, Continuous Improvement, Suleiman, Ayoib and Nor Zalina (2018). According to the Suleiman *et al.*, (2018), the following are the 7 key principles of internal audit that form the foundation for the profession and guide the conduct of internal auditors.

i. Independence concept

One of the key principles of internal audit is independence, which is the foundation of its credibility. Independence refers to both the operational independence of the internal audit function and the professional independence of individual internal auditors. The internal audit function should have a clear reporting structure and should not be influenced by any other function or business unit within the organization. Suleiman *et al.*, (2018). Independence is defined as "the freedom from situations that jeopardize the ability of the Internal Auditing's activity to carry out IA tasks in an unbiased manner", Dejnaronk *et al.*, (2016). The independence of internal auditors enhances the financial reports' integrity, Erasmus and Coetzee, (2018). Internal audit is effective by preventing the organization's management from interference in the scope of internal auditing and controlling the internal audit work, while reporting to the CEO, which assists the internal audit in carrying out its responsibilities without obstacles and addressing difficult issues with other senior leaders (The Institute of Internal Auditors, (2019).

ii. Objectivity concept

Objectivity is another vital principle of internal audit, which requires internal auditors to be impartial and free from conflicts of interest. Internal auditors should not have any vested interests in the outcome of their work and should approach their tasks with impartiality and fairness. This allows them to provide an unbiased assessment of the organization's operations and to identify areas for improvement. Objectivity can be defined as an unbiased mental attitude that permits internal auditors to perform an engagement in such a way that they believe in their work output and that no quality compromises are made, Dejnaronk *et al.*, (2016).

iii. Competence concept

Competence is a critical principle of internal audit, as internal auditors are expected to possess the necessary knowledge, skills, and experience to carry out their work effectively. Internal auditors should continually develop their skills and knowledge, and should be able to apply their expertise to the specific needs of the organization (El Gharbaoui and Chraibi, (2021).

iv. Confidentiality concept

Confidentiality is a fundamental principle of internal audit, as internal auditors often have access to sensitive and confidential information. Internal auditors should maintain the confidentiality of all information obtained during their work and should only use it for the purpose for which it was collected, El Gharbaoui and Chraibi, (2021).

v. Professionalism concept

Professionalism is another important principle of internal audit, as internal auditors are expected to adhere to high standards of ethical conduct and to act with integrity at all times. Internal auditors should also maintain a professional demeanor, be responsive and cooperative, and should not engage in any behavior that might reflect poorly on the internal audit function or the organization, Masoud *et al.*, (2021).

vi. Due Professional Care concept

Masoud *et al.*, (2021) asserted that, due professional care requires internal auditors to apply professional skepticism and to exercise due care and diligence in the performance of their work. Internal auditors should approach their work with a critical eye and should not accept information at face value. Moreover, they should also take steps to verify information and test the validity of assumptions.

vii. Continuous Improvement concept

Continuous improvement is the final key principle of internal audit and refers to the need for the internal audit function to continuously strive to improve its processes, procedures, and techniques, Kotb, Elbardan and Halabi (2020). Internal auditors should continually review their practices and identify opportunities for improvement to enhance the overall effectiveness of the internal audit function. Conclusively, the seven (7) key principles of internal audit serve as a framework for the internal audit function and provide a basis for the conduct of

internal auditors, Suleiman *et al.*, (2018). Adherence to these principles ensures that the internal audit function is credible, effective, and provides value to the organization. The principles of independence, objectivity, competence, confidentiality, professionalism, due professional care, and continuous improvement are essential for the internal audit function to fulfil its role as a trusted advisor to the SMEs, Suleiman, Kotb, Elbardan and Halabi (2020).

Financial Performance on Small and Medium Scale Enterprises

Financial performance refers to how well an organization or business is using its resources to generate income and achieve its financial goals, Alsmady, (2022). According to Alsmady, (2022), the financial health, profitability, and efficiency of a company over a specific period of time usually measured using key indicators such as: Revenue (Sales) which is total income earned from business activities, Net Profit which is, what remains after all expenses are deducted from revenue, Return on Investment (ROI) which is the return earned on invested capital, Earnings Per Share (EPS) is the Profit allocated to each share of stock, Liquidity Ratios is the ability to pay short-term debts (e.g., current ratio), Debt Ratios which is the Level of a company's debt compared to its assets or equity, Alsmady, (2022). A company's success is generally measured by its financial performance: companies with higher earnings are more vulnerable to regulations that require more detailed information to be disclosed in annual reports to justify financial performance, Mondal and Ghosh, (2014). Financial performance is an analysis conducted to see the extent to which a company has carried out using the rules of financial implementation properly and correctly, McNally, Akdeniz, and Calantone, (2011). An organization's financial performance serves as a barometer for how well it controls and manages its finances. Information from the cash flow, balance sheet, profit loss, and capital change may be used by corporate management to make decisions, Fatihudin, Jusni and Mochklas, (2018). However, financial reports must be accurate, transparent, and reliable to provide information to business owners, shareholders, and investors. Financial performance affects the growth of the company and indicates that the higher the financial performance, the higher the growth of the company, Sri Hermuningsih, (2018). Financial Performance is represented by various

financial ratios such as the loan growth ratio, the earnings growth rate, and the total asset growth, Omaliko *et al.*, (2020).

III. THEORETICAL FRAMEWORK

Agency Theory

Agency theory was postulated by Michael and William, (1976). The theory explains the conflicts of interest between principals (owners/shareholders) and agents (managers). Agency theory stated that the company is made up of principals who own the financial assets and agents who supervise the company's assets, Tuan, (2015) and Al-Matari *et al.*, (2014). The fundamental theory applied to internal auditing that explains its existence from an economic and governance perspective in terms of principal-agent relationship, information asymmetry, moral hazard, and internal audit as a monitoring, Juri, Katri, Alistair and Erik, (2022). Agency theory provides valuable insights into the relationships in the supply chain, Raul, (2021). It was stated that the dynamics of performance, risk, sustainability, dyadic and inter-firm relationships, and supplier management are predominant in their study. The principal-agent relations, focusing on the interaction between the shareholder-manager and bondholder in corporate finance, were examined by Hasan and Ali, (2020) and the problems of agency and risk sharing arise due to the separation of ownership and control of a large firm when conflicts of interest exist between principals (owners) and agents (managers). The main source of these problems is asymmetric information, which implies an agency cost for the principal. Since the management carries on the day-to-day operations of the business on behalf of the principal, there exists information asymmetry where the agent has more information than the principal and can be motivated to pursue their self-interest at the expense of the principal. Agency Theory influences decision-making, risk management, and overall dynamics in organizations. It views that the relationship between agents and principals in organizations which can influence individual behaviour in the working environment, Syafriadi, Sitepu, Andini, Muda, Kesuma, (2023). Agency theory is a branch of game theory that studies the design of contracts to motivate rational agents to act on behalf of the principal when the agent's interests' conflict with the principal's Scott, (2012). However, Agency theory provides an important role for accounting, especially in providing information after an event, which is referred to as the

post-decision role. This role is often associated with the accounting stewardship role, where an agent reports to the principal about past events.

Contingency Theory

Contingency theory was postulated by Fred Edward Fiedler around the mid-1960s (specifically 1964 and further developed in 1967 with "A Theory of Leadership Effectiveness". The idea of this theory was that, there is no single best way to manage or lead; effectiveness depends on the situation (contingencies). "Contingency means that one thing depends on another. Contingency theory means that the theory depends on one thing or the other." Contingency approach to management attempts should outline the conditions or situations in which various management methods have the best chance of success, Mark and Erude, (2023). The main message from the contingency theory to managers is that, there is no best way to manage an organization than to adopt managerial style which depends on the circumstances within the organizational environment. Managers should carefully analyze the various variables in a given organizational situation or environment and take appropriate action that will suit the situation. The contingency approach to management is an opinion that an organization recognizes and responds to in different situations as they occur, Mrinalini, (2022). The fundamental concept approach of contingency leadership is that, leaders would be more effective if their attitude and style of leadership were contingent and considered internal as well as external situational forces, Victor, (2020). According to Victor, (2020), the approach of contingent leadership is based on the assumption that leaders are proven effective if they make their attitude reliant on situational forces, which was forecasted to offer huge opportunities for effective practices of leadership and also, identify key personality factors of different employees, whose personality shows how to cope with different situations based on their way of thinking, refers to their leadership style. Job satisfaction greatly affects the effectiveness of the leader's work in placing him or her in the appropriate place, Prebreza and Ramosaj, (2021). The development of a contingency theory of organizational capability based on the identification of decision variables relevant to the design of firms, Victor, (2020). The theory established that superior performance is the result of the proper fit between applied knowledge and organizational structure. Contingency theory provides an explanation of

organizational behavior based on contingent factors; thus, there is no generalized best fit in leadership style. However, Contingency theory supplies data on leadership styles (profile) that could be useful to organizations in developing leadership profiles for human resource planning. Contingency theory was summarized as an approach to the study of organizational behavior in which explanations were given as to how contingent factors influence the design and functions of the organizations, Jesmin and Hui, (2012).

Resource-Based View (RBV) theory

The proponents of the resource-based view (RBV) theory were Wernerfelt (1984), Hamel and Prahalad (1989) and Barney (1991), in his work on firm resources and sustained competitive advantage. RBVs emphasize how a firm's resources contribute to its competitive advantage and elucidate how firms can cultivate a competitive advantage in fluctuating environments, Chalchissa and Addisalem, (2023). The resource-based view (RBV) theory is a strategic management framework that focuses on a company's internal resources as the key of achieving and sustaining competitive advantage. Resource-based view (RBV), is a firm's ability to maintain competitiveness depends on its access to valuable, rare, inimitable, and non-substitutable resources, Božič, and Dimovski, (2019). The theory proposes that firms gain a competitive edge primarily by leveraging valuable, rare, inimitable, and organized resources both tangible and intangible rather than through external market positioning alone. A firm can possess various resources and capabilities, and most of these capabilities are closely associated with improved performance, Chahal, Gupta, Bhan, and Cheng, (2020). RBV emphasizes that sustainable competitive advantage arises from resources that meet specific criteria known as valuable. A company will strive to exploit its resources to implement a strategy to win a competition. A significant inquiry arises in selecting and configuring the best resources to achieve performance, James & Joseph, (2015). The RBV shifts the strategic focus inward, encouraging firms to identify, develop, and protect key resources and capabilities that competitors cannot easily duplicate. Decision-making for combining resources becomes significant in strategic planning to leverage a company's core competencies to exceed its average return, Donnellan & Rutledge, (2019). This inside-out perspective contrasts with traditional industry-focused approaches and highlights how leveraging

unique internal resources can lead to superior firm performance and long-term success. RBV Theory helps explain the conditions under which a firm's resources provide a competitive advantage (Barney, 1991).

Theory of Inspired Confidence

The theory of inspired confidence was postulated by Limperg (1932). The core ideas of the theory existed because society demanded it. Public confidence in financial reporting is the basis for auditing; if confidence fails, the value of auditing collapses. According to Limperg, the demand for audit services is the direct consequence of the participation of outside stakeholders in the company. These stakeholders demand accountability from the management in return for their contribution to the company. Minimizing Audit Anticipation Gap (AAG) in a developing country, on exploring the occurrence, causes, and consequent effects of the Audit Anticipation Gap in Sudan. This was achieved by surveying the opinions of practicing auditors, key users of financial statements, and accounting educators Ghandour, (2023). Examine market behavior towards management aggressiveness from the perspective of screening theory, Kristabel and Wijaya (2021). Screening theory assumes that the market has limited information on companies. The researcher also examines whether the board of commissioners, foreign institutional ownership, and the presence of auditors are capable of improving market response to management aggressiveness. This provides evidence that the market does not respond to management aggressiveness. It means that the screening theory can explain that the market does not consider whether management is aggressive or not in making its investment decisions. However, the market has responded positively to their existence in suppressing management aggressiveness. Thus, Screening theory proves that the market has limited information about company management. Kristabel and Wijaya (2021). Value-for-money audit can enhance the reduction in costs of governance, misappropriation, and theft of public funds, assist the government in redirecting scarce public resources to priority areas, and restore public confidence in the management of national economies. However, SMEs are advised to instill the culture of regular value-for-money audits in all public sector institutions to ensure the protection and proper utilization of public funds, Owolabi and Ogunode, (2020).

The underpinning theory linking internal auditing to financial performance in SMEs is the Agency Theory, as it explains how internal auditing functions as a control mechanism that minimizes agency conflicts, enhances transparency, and improves organizational performance.

Supporting theories such as contingency theory, Resourced Based Theory and theory of inspired confidence further strengthen this relationship by emphasizing the role trust, contextual adaptation and resource utilization.

Empirical Review on internal auditing and financial performance of SMEs

An "empirical review" refers to a critical analysis of existing research studies that are based on collected data and empirical evidence. This relies on observation and experimentation to test hypotheses and draw conclusions, rather than purely theoretical concepts. Al-Haddad¹, Safdar Sial, Ali, Alam, Vinh Khuong, and Khanh, (2019), examined the Role of Small and Medium Enterprises (SMEs) in Employment Generation and Economic Growth: A Study of the Marble Industry in an Emerging Economy. Their study exposes that SMEs play a vital role in employment generation and a positive relationship between SMEs and unemployment reduction. Gherghina, Botezatu, Hosszu, and Simionesc, (2020) investigated Small and Medium-Sized Enterprises (SMEs): The Engine of Economic Growth through Investments and Innovation. The result showed a positive impact on turnover for all enterprises and big companies, but a lack of association was established in the case of SMEs. Bayraktar and Algan (2019), investigated the importance of SMEs on World Economies. The result showed the importance of SMEs to economic growth, poverty reduction, innovation, and job creation, also social cohesion, are the key elements to nation's development. Amoah, Belas, Dziwornu, and Khan, (2022), assessed the contributions of SMEs in an emerging economy, using ADANCO version 2.0 of the partial least squares structural equation model (PLS-SEM). The results reveal that SMEs continue to provide maximum support and contributions to Gross Domestic Product (GDP), as well as employ about 70 percent of the entire working population.

Eniola, Abiodun, Tonade, Abiola and Adeniji, (2021), investigated on Internal Audit Structures and Financial Performance: Evidence from Listed

Companies in Nigeria's South-West Region. The findings indicated a favorable association between internal audit control, risk management, monitoring practices and operational performance, pointing to the objectives. Their analysis would be helpful to corporate managers because it demonstrates the elements that are overlooked in internal control systems and strategies to improve the performance of the internal control system. Lawal and Alabi, (2023), studied how internal audit practice affects the effectiveness of SMEs in Kwara State by assessing how much remuneration and information technology expertise of internal auditors' impact efficiency. The result showed that the remuneration for internal auditors has a favourable and significant impact on the organizational effectiveness of SMEs in Kwara State. Dadem, Ongono, Deutou, Tsiaze and Manetsa, (2023), examined the impact of Internal Control on the Performance of SMEs in Cameroon. Multiple regression analysis, and the technique of estimation was the ordinary least squares, was used, and the results found a positive and significant relationship between internal tools, determinants of performance, challenges of internal control, and the performance of SMEs in Cameroon. The study area of their research was limited to the city of Dschang in (Cameroon). Eniola, Tonade and Adeniji, (2021), examined the internal control mechanisms and financial results of listed companies in Nigeria's southwest area. Multi-level random sampling and multiple regression models were used. The findings indicated a favourable association between internal audit control, risk management, monitoring practices, and operational performance, pointing to the objectives. Monitoring practices and control environments have a significant negative impact on asset returns, and Poor management discipline was the limitation to their research work. Lawal and Alabi (2023), investigated internal audit practices and organizational effectiveness: insights from SMEs in Kwara state. Their research used a survey research methodology, and a statistical procedure developed by Yamane (1967) was used to determine the sample size of the respondents, and partial least squares structural equation modelling (PLS-SEM) was used as an estimation approach to analyse the data. The outcome shows that the remuneration for internal auditors has a favourable and significant impact on the organizational effectiveness of SMEs in Kwara State, and discouraged financial and material irregularities was the gap established from their research work. Gyamera and Eklemet, (2024),

investigated the effects of Audit services on SMEs' financial performance. PLS-SEM Software was used to analyse the data collected from the respondents. The findings indicate that the use of audit services results in the avoidance and detection of financial irregularities, resulting in an improvement in SMEs' financial performance. The study also found a positive relationship between information technology and the financial performance of SMEs and the limitation to their research work was the poor use of technology Shehu, Jimoh and Shehu, (2025), analysed the Internal Control Mechanism and Operating Efficiency of Manufacturing Firms in Nigeria. The outcome showed the implementation of effective internal controls as the key to unlock greater operational performance and ensuring that manufacturing firms are well-positioned to thrive in a changing global marketplace.

Babatunde and Olawale, (2025). Examined the compliance with Environmental Regulations: Insights from Small and Medium Scale Enterprises in the Food and Beverage Sector in Southwestern Nigeria. The result showed that the small-sized firms were more compliant than medium-sized businesses in having a waste management plan, integrating sustainability into business operations, preparing periodic environmental audits and assessments, and responding to community complaints on waste. Igbojioyibo, (2024), examined the Impact of Internal Control Systems on Asset Protection and Financial Reporting Accuracy in SMEs. The findings illustrated the essential role that internal control systems play in fostering a culture of accountability and transparency within SMEs, which is increasingly relevant in today's dynamic business environment. Dadem, Ongono, Deutou, Tsiaze and Manetsa, (2023), examined the impact of internal control on the performance of SMEs in Cameroon. The results found a positive and significant relationship between internal tools, determinants of performance, challenges of internal control, and the performance of SMEs in Cameroon. Obafemi and Olajide, (2023), investigated the effects of internal control activities and control environment on organizational performance of selected tertiary institutions in Osun state. Using multiple regression analysis. The results of the findings revealed that internal control activities have a positive and significant relationship with organizational performance in the tertiary institutions in Osun State at 5% level of significance, and that control environment has no significant relationship

with organizational performance at 5% level of significance. The study concluded that internal control activities and environment were the key determinants of promoting organizational performance. Mujalli, (2024), studied the factors affecting risk-based internal audit (RBIA) implementation in public sector organizations in Saudi Arabia by applying partial least squares–structural equation modelling (PLS-SEM), and the results showed that management support, internal auditor role, risk management system, and training in risk management all positively and significantly influence the RBIA. Improved internal auditing procedures and an efficient internal monitoring system will significantly curtail any risks impeding the organization’s goals, diminish the temptation to fabricate financial data or statistics, and enhance the accuracy of financial reporting/statements.

Yousif and Mohamed, (2022), verified the Role of Internal Auditing in assessing the Risks of Strategic Operations (Acquisition) and then reflected on management decisions. The result showed the role of internal auditing regarding acquisition. The value of the research clarifies the role of internal auditing in assessing the risks of acquisition processes and encourages the adoption of the idea in the Iraqi environment. Oyedokun, Godwin and Muhammad (2023), investigated the internal control system and financial performance of small and medium-scale enterprises in Nigeria. A descriptive survey approach and Pearson Product-Moment Correlation Coefficient Analysis with a two-tailed test were used. The finding showed that SMEs in Kebbi State, Nigeria, may save money by adopting several components of internal control, and the Lack of annual evaluation of the financial reporting process and implementation of an internal auditing system to monitor performance was their limitation.

Csapi and Balogh (2020), investigated the financial performance-based assessment of SMEs’ competitiveness – an analysis of Hungarian and US small businesses. A panel data model was tested on Hungarian small and medium-sized enterprises (SMEs) and US SMEs. The collected data cover the period between 2013 and 2017. The research found a significant difference between the two-sample dataset results, which differences can be connected to country, industry, and, in general, to economic development characteristics. The results provide decision-making support and hint at the managerial

tools and techniques aiming to control the firm characteristics, performance, and firm-level competitiveness. Based on the results, further research can be dedicated to the development characteristics of firm-level competitiveness and the analysis of the relationship between the competitiveness dimensions and competitiveness itself. Akanbi and Adekunle, (2025), examined the effect of finance on the financial performance of SMEs in the pharmaceutical business in Kwara State, Nigeria. Using a survey research approach, data were collected from 140 registered SMEs in the pharmaceutical business through structured questionnaires. Descriptive statistics and ordered logistic regression were employed to analyse the data. The research findings indicated that the financial performance of small and medium-sized pharmaceutical businesses in Kwara State, Nigeria, is considerably enhanced by timely and reasonably priced financing from microfinance institutions and unofficial microcredit sources. Their study recommended that pharmaceutical SMEs should implement cost-saving measures, explore local sourcing options, and adopt pricing strategies to maintain competitiveness in the market. It also advocates for enhanced financial literacy, the adoption of digital lending platforms, and strengthened security measures to address systemic barriers and improve financial performance across the State and Nigeria at large. Hassan & Gunalan (2023), determined the key factors influencing SMEs’ performance: A systematic literature review and experts’ verification. The findings indicated that 13 factors significantly impact a firm’s strategic orientation and performance in today’s knowledge-based and uncertain global business environment and it should be noted that other relevant factors may have been overlooked, and future research should consider a more detailed approach, such as meta-analysis, to broaden the field’s knowledge. Mpora *et al.*, (2025), investigated the impact of financial distress on the performance of small and medium enterprises (SMEs) in Sheema, Buhweju, Rubirizi, and Bushenyi Districts, Uganda. Specifically, it examined the effects of excessive debt, inadequate capital, poor management practices, unwise expansion, intense competition, litigation, and unfavourable contracts on SMEs. A descriptive research design was adopted, and the findings revealed a significant negative correlation between financial distress and SME performance. As financial strain increased, financial performance declined, and

vice versa. Poor technical know-how and an unqualified employee were limitations to their research work. Thi and Chien-Van (2025), examined the factors affecting corporate financial performance listed on Vietnam stock market. The research results also indicate that revenue growth can significantly increase firm performance, and firm size, investment in fixed assets, and choice of equity sources can create higher profits. Poor financial reporting quality, poor governance quality, and poor macroeconomic stabilization strategy were the limitations to their research work. Serrasqueiro, Pinto, and Sardo, (2023), analysed the relationships between profitability, productivity, external debt, and growth in SMEs. An estimation method that includes Descriptive statistics and panel data model estimations was used to analyse the data. The result showed that Productivity positively influences the firm's growth, and the research work was limited to a sample of Portuguese SMEs.

IV. SUMMARY, CONCLUSION AND RECOMMENDATIONS

Summary

SMEs play a special role in socio-economic development in Nigeria, where they contribute significantly to job creation, income generation, innovation, poverty reduction, and serve as an engine for national development, Adeosun and Shittu, (2021). Internal auditing (IA) work helps an organization accomplish its objectives by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of risk management, control, and governance processes (IIA2018). Financial performance refers to how well an organization or business is using its resources to generate income and achieve its financial goals. The purpose of the study is to evaluate the relationship between internal auditing and the financial performance of small and medium-scale enterprises in Southwest Nigeria. It also assesses how internal auditors' qualities contribute to the efficacy of the financial performance of SMEs in lowering poverty. Some significant barriers including limited access to information, lack of compliance with regulations, and inadequate training has been looked into. According to the study, auditors' quality significantly improves the efficiency of financial performance among SMEs based on the literatures. The findings of this study will aid in a better understanding of the current status of internal audit effectiveness, including the elements

that influence it, as well as gaps and potential for future research. The result revealed the empirical data, Internal auditing positively relates to the financial performance of Small and Medium Scale Enterprises by improving operational efficiency, risk management, and internal controls, ultimately enhancing profitability and sustainability.

Conclusion

Based on the findings, internal audits provide an independent evaluation that helps identify and mitigate financial risks, ensure compliance with regulations, and streamline processes to reduce waste. For Small and Medium Scale Enterprises, this support is crucial for building a solid foundation for growth.

Recommendation

It is recommended that SMEs should pay attention to internal auditing practices, SMEs should commit more to integrity, ethical value, competence, accountability, as well as development of preventive and detective control activities through the engagement of technology, and standardization of policies and procedures for transaction approval, verification and reconciliation. However, information and communication and even monitoring activities needs to be upgraded so as not to undermine the role of the internal control system.

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