

Moderating Effect of Firm Size on the Relationship Between Enterprise Risk Management and Quality of Financial Reporting among Commercial State-Owned Entities in Kenya

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DOI: <https://doi.org/10.47772/IJRISS.2026.100900431>

Received: 19 September 2026; Accepted: 24 September 2026; Published: 13 October 2026

ABSTRACT

Enterprise Risk Management (ERM) is widely promoted as a mechanism for improving the quality of financial reporting, yet its effectiveness may depend on organisational characteristics such as firm size, an area that has received limited attention among Kenya's State-Owned Commercial Entities (SOCEs). This study established the moderating effect of firm size on the relationship between Enterprise Risk Management and the quality of financial reporting among commercial SOCEs in Kenya. The study was anchored on Contingency Theory and adopted an explanatory research design. The target population comprised 420 management and finance staff drawn from commercial SOCEs in Kenya, from which a sample of 205 respondents was drawn using the Yamane (1967) formula and selected through stratified and cluster random sampling. Primary data were collected using a structured questionnaire, and 160 questionnaires were returned complete and usable, a response rate of 78.0%. The firm size construct, which captured respondents' perceptions of the scale of an entity's asset base and its influence on risk management and reporting, achieved a Cronbach's Alpha of 0.793, confirming its reliability, while a Kaiser-Meyer-Olkin value of 0.765 and a statistically significant Bartlett's test ($p < .001$) confirmed that the item set was factorable and suitable for data reduction. A three-step hierarchical moderated regression was conducted using mean-centred variables, with the composite Enterprise Risk Management score entered in Step 1, firm size added in Step 2, and the Enterprise Risk Management by firm size interaction term added in Step 3, computed using SPSS Version 27. Firm size significantly moderated the relationship between Enterprise Risk Management and financial reporting quality (interaction $B = -0.152$, $p = .036$), with the addition of the interaction term producing a statistically significant, though practically modest, increase in explained variance (ΔR Square = 0.011, F -change = 4.465, $p = .036$), leading to rejection of the null hypothesis. The negative interaction coefficient indicated that the positive effect of Enterprise Risk Management on financial reporting quality was stronger among smaller commercial SOCEs than among larger ones. The study concludes that firm size is not a neutral background characteristic but an active moderator of how Enterprise Risk Management practice translates into reporting quality, with larger entities' closer external oversight from bodies such as the Office of the Auditor-General plausibly reducing their dependence on internal ERM practice relative to smaller entities. The study recommends that the National Treasury prioritise Enterprise Risk Management capacity-building support disproportionately toward smaller and medium-sized commercial SOCEs, which appear to have the most to gain, in reporting-quality terms, from strengthened risk management practice.

Keywords: Firm Size, Moderation, Enterprise Risk Management, Financial Reporting Quality, State-Owned Commercial Entities, Kenya

INTRODUCTION

Firm size refers to the scale or capacity of an organization's operations, and larger firms typically command more resources, more complex structures, and a broader range of risk exposures than smaller ones (Margono & Gantino, 2021). Because these differences may shape how effectively organisational practices such as Enterprise Risk Management (ERM) translate into outcomes, firm size is frequently examined as a moderating variable in organisational research. Vij and Farooq (2016), for instance, found that firm size significantly and positively

moderated the relationship between information technology orientation and business performance in India, illustrating that the same organisational practice can produce systematically different outcomes depending on the scale at which it is applied.

Within Kenya's State-Owned Commercial Entities (SOCEs), firm size may plausibly shape the effectiveness of ERM practice in influencing financial reporting quality. Larger SOCEs, such as those in the energy, ports, and infrastructure sectors, often face more diverse risk exposures and manage more extensive resources, which may necessitate more structured ERM systems, whereas smaller entities may operate with simpler, less formalised risk management mechanisms (Margono & Gantino, 2021). At the same time, larger SOCEs typically operate under closer and more continuous external scrutiny from the Office of the Auditor-General, the National Treasury, and other oversight bodies, which may itself substitute for, or reduce the marginal contribution of, strong internal ERM practice.

Empirical evidence on the moderating role of firm size, both globally and within Kenya, has produced mixed and inconsistent results. Obaje and Abdullahi (2021) found that firm size negatively moderated the relationship between board structure and financial performance among Nigerian deposit money banks. Within Kenya, Kibe et al. (2024) found that firm size did not significantly moderate the relationship between financial indicators and financial distress among commercial and manufacturing state corporations, a result the authors noted contradicted theoretical expectations, whereas Ochoi et al. (2025) found that business size significantly and negatively moderated the relationship between inclusive marketing and enterprise survival among micro and small enterprises in Nyamira County, with larger firms experiencing improved survival outcomes. This inconsistency, together with the largely unexamined moderating role of firm size in the specific relationship between ERM and financial reporting quality among Kenyan SOCEs, motivates the present study.

Problem Statement

Enterprise Risk Management is widely recognized as a critical framework for enhancing the quality of financial reporting in State-Owned Commercial Entities. Despite the adoption of various public sector reforms, Kenyan SOCEs continue to experience recurring audit qualifications, inconsistencies in financial disclosures, and compliance deficiencies that compromise the reliability, transparency, and credibility of financial reports. While ERM has been promoted as a solution to these challenges, existing studies have paid little attention to whether, and how, the effectiveness of ERM in improving financial reporting quality depends on organisational size, despite evidence from other contexts and other relationships suggesting that organisational size may significantly alter how effectively organisational practices translate into outcomes. This knowledge gap is particularly consequential for policy, because uniform ERM capacity-building strategies applied across SOCEs of very different scales may not be equally effective, or equally necessary, across the portfolio. This study therefore sought to establish the moderating effect of firm size on the relationship between Enterprise Risk Management and the quality of financial reporting in State-Owned Commercial Entities in Kenya.

Hypothesis

HO5: There is no statistically significant moderating effect of firm size on the effect of Enterprise Risk Management on the quality of financial reporting in State-Owned Commercial Entities in Kenya.

LITERATURE REVIEW

Theoretical Framework

This study was anchored on Contingency Theory, originating from Woodward (1958) and later expanded by Lawrence and Lorsch (1967) and Otley (1980). Contingency Theory holds that there is no single organisational practice or control system that is universally optimal; rather, the effectiveness of a given practice is conditional on situational or contextual factors such as organisational size, complexity, and the external environment (Otley, 1980; Fiedler, 1967). Applied to ERM, the theory suggests that the same risk governance, assessment, mitigation, and monitoring practices may produce different outcomes depending on an organisation's scale: sophisticated, formalised ERM systems may be more readily absorbed and impactful in larger, better-resourced entities, or,

conversely, may matter comparatively more for smaller entities that lack the buffer of extensive external oversight enjoyed by larger ones. Contingency Theory therefore provides the theoretical basis for treating firm size as a moderating, rather than merely a control, variable in the relationship between ERM and financial reporting quality.

Empirical Literature Review

Vij and Farooq (2016) examined the moderating role of firm size on the relationship between information technology orientation and business performance in India and found a significant positive moderating effect, indicating that larger firms derived greater performance benefit from IT orientation than smaller firms did. Obaje and Abdullahi (2021) examined the moderating effect of firm size on the relationship between board structure and financial performance among quoted deposit money banks in Nigeria using secondary data and random effects regression, finding that firm size had a negative and significant moderating effect on the relationship between board independence and Return on Assets, and a negative and significant moderating effect for board gender diversity, though an insignificant effect for board size.

Within Kenya, Kibe et al. (2024) conducted a census of 25 commercial and manufacturing state corporations using secondary audited-account data and logit regression, and found that firm size did not significantly moderate the relationship between profitability, leverage, efficiency, and financial distress, a result that contradicted the theory of small firms. In contrast, Ochoi et al. (2025), studying micro and small enterprises in Nyamira County using hierarchical regression on primary survey data, found that business size significantly and negatively moderated the relationship between inclusive marketing and enterprise survival, such that larger firms experienced improved survival outcomes relative to smaller ones. Beyond the ERM literature specifically, Dagwom Yohanna et al. (2024), studying listed consumer goods companies in Nigeria, found that firm size alone had a marginally significant negative effect on financial reporting quality, but that this effect became clearly significant once audit quality was introduced as a moderator, with a positive and significant firm size by audit quality interaction term, illustrating more broadly that firm size shapes financial reporting quality primarily through its interaction with an accompanying oversight or governance mechanism rather than in isolation.

Taken together, this evidence demonstrates that the moderating role of firm size is neither universal nor uniformly directional: it strengthens some relationships (Vij & Farooq, 2016), weakens others (Obaje & Abdullahi, 2021; Ochoi et al., 2025), and is statistically absent in others (Kibe et al., 2024), depending on the relationship being moderated, the sector, and the institutional context. This variability, combined with the distinctive regulatory and oversight environment of Kenyan SOCEs shaped by the Mwongozo Code of Governance and the Public Finance Management Act (2012), indicates that firm size may play a context-dependent role in moderating the relationship between ERM and financial reporting quality that warrants direct empirical examination, rather than being assumed from findings obtained in other relationships or sectors.

CONCEPTUAL FRAMEWORK

The conceptual framework underlying this study positions the composite Enterprise Risk Management construct as the independent variable and financial reporting quality as the dependent variable, with perceived firm size, operationalised through respondents' perceptions of the scale of an entity's asset base and its influence on risk management implementation, introduced as a moderating variable expected to alter the strength of the relationship between the two. This perception-based operationalisation is a deliberate scope choice rather than a direct measure of objective organisational size, and is revisited in the Limitations section below. Consistent with standard moderation analysis, the framework specifies that firm size may condition, rather than directly determine, the extent to which ERM practice translates into improved financial reporting quality.

Research Design

The study adopted the positivist research philosophy and an explanatory research design. The target population comprised 420 management and finance staff, including non-senior finance officers, internal auditors, risk management officers, external auditors, and legal officers, drawn from the 30 commercial SOCEs in Kenya. Using the Yamane (1967) formula at a 5% margin of error, a sample of 205 respondents was drawn through

stratified random sampling by professional role, combined with cluster and systematic random sampling within strata.

Primary data on perceived firm size, operationalised through four Likert-type items capturing respondents' perceptions of the scale of an entity's asset base and its perceived influence on risk management implementation and reporting quality, were collected using a structured questionnaire administered through Google Forms, email, and physical drop-and-pick distribution. This scale therefore measures respondents' perceptions of asset scale and its consequences rather than an objective, balance-sheet-based measure of organisational size such as total assets. Content validity was established through expert review, and the firm size item set recorded a Kaiser-Meyer-Olkin value of 0.765 and a statistically significant Bartlett's test ($p < .001$), indicating that the items were factorable and suitable for data reduction; these sampling-adequacy statistics establish factorability rather than construct validity in their own right. A pilot test conducted at the Kenya Meat Commission informed refinement of the instrument, and the firm size construct achieved a Cronbach's Alpha of 0.793, exceeding the 0.70 threshold for acceptable internal consistency.

Of the 205 questionnaires administered, 160 were returned complete and usable, a response rate of 78.0%. The moderating effect of firm size was tested using the Baron and Kenny (1986) approach through a three-step hierarchical moderated regression, specified as $Y = \beta_0 + \beta_1 X + \beta_2 M + \beta_3 (X \times M) + \varepsilon$, where Y is financial reporting quality, X is the composite Enterprise Risk Management score (the mean of risk governance, risk assessment, risk mitigation, and risk monitoring), M is firm size, and $(X \times M)$ is their interaction term. To reduce non-essential multicollinearity between the interaction term and its constituent variables, ERM and firm size were mean-centred prior to computing the interaction term. Step 1 entered composite ERM alone, Step 2 added firm size, and Step 3 added the ERM by firm size interaction term; a statistically significant interaction coefficient and a statistically significant change in R Square at Step 3 were the criteria for confirming moderation, computed using SPSS Version 27 and tested at the 5% level of significance.

FINDINGS AND DISCUSSION

Response Rate and Reliability

Of the 205 questionnaires administered, 160 were returned complete and usable, a response rate of 78.0%. The firm size construct achieved a Cronbach's Alpha of 0.793, confirming the internal-consistency reliability of the instrument, and a KMO value of 0.765 with a statistically significant Bartlett's test ($p < .001$), confirming that the item set was factorable rather than independently establishing construct validity.

Firm Size

Table 1 presents the descriptive statistics for the four firm size items, measured on a five-point Likert scale.

Table 1: Descriptive Statistics for Firm Size (Moderator)

Statement	Mean	Std. Dev.
The enterprise has a large asset base that supports effective implementation of risk management practices.	3.59	0.95
The size of the asset base enhances the quality and reliability of financial reporting.	3.48	1.02
The value of assets owned by the enterprise influences the comprehensiveness of financial disclosures.	3.46	1.06
A larger asset base enables better control and monitoring of financial reporting processes.	3.46	1.05

Table 1 shows that firm size recorded comparatively modest item means, ranging from 3.46 to 3.59, the lowest of all constructs measured in the wider study. Respondents agreed most strongly that a large asset base supports effective implementation of risk management practices (mean = 3.59), but were comparatively more reserved about whether asset value directly enhances the comprehensiveness of disclosures or the control of reporting processes (both 3.46). The composite mean for firm size was 3.50 (SD = 0.80). This more cautious pattern lends

only qualified, perception-based support to the theoretical expectation, drawn from Vij and Farooq (2016), that firm size shapes how effectively organisational processes translate into outcomes; the formal statistical test of this moderating role is presented in the following section.

Pearson correlation analysis showed that firm size was moderately and significantly correlated with financial reporting quality ($r = 0.630$, $p < .001$), and was also significantly correlated with each of the four ERM dimensions ($r = 0.547$ to 0.701 , $p < .001$), providing initial bivariate support for examining its role as a moderator of the ERM-financial reporting quality relationship.

Hypothesis Testing: Moderated Regression

Hypothesis HO5 stated that there is no statistically significant moderating effect of firm size on the effect of Enterprise Risk Management on the quality of financial reporting in State-Owned Commercial Entities in Kenya. A three-step hierarchical moderated regression was conducted, with composite ERM and firm size mean-centred before computing the interaction term. Table 2 presents the results of all three steps.

Table 2: Hierarchical Moderated Regression Results

Step / Variable	B	t	Sig.	R Square	Adjusted R Square
Step 1				0.584	
ERM (composite)	0.681	14.881	<.001		
Step 2				0.614	0.031
ERM (composite)	0.547	9.399	<.001		
Firm Size	0.193	3.541	<.001		
Step 3				0.625	0.011
ERM (composite)	0.457	6.376	<.001		
Firm Size	0.247	4.138	<.001		
ERM x Firm Size	-0.152	-2.113	0.036		

Based on the coefficients in Table 2, with ERM (composite) and firm size mean-centred, the fitted equations for each step are: Step 1: $FRQ = 3.878 + 0.681(ERM_c)$; Step 2: $FRQ = 3.878 + 0.547(ERM_c) + 0.193(FS_c)$; Step 3: $FRQ = 3.937 + 0.457(ERM_c) + 0.247(FS_c) - 0.152(ERM_c \times FS_c)$, where ERM_c and FS_c denote mean-centred ERM and firm size, respectively.

Step 1 shows that composite ERM alone explains 58.4% of the variance in financial reporting quality ($B = 0.681$, $p < .001$). Adding firm size in Step 2 increased R Square to 0.614, with firm size itself a significant direct predictor ($B = 0.193$, $p < .001$). Adding the ERM by firm size interaction term in Step 3 produced a further, statistically significant increase in R Square of 0.011 ($F\text{-change} = 4.465$, $p = 0.036$), and the interaction term itself was statistically significant ($B = -0.152$, $p = 0.036$). Because the interaction term is statistically significant, firm size is confirmed to significantly moderate the relationship between ERM and financial reporting quality, and HO5 is rejected. The negative sign of the interaction coefficient indicates that the positive effect of ERM on financial reporting quality is weaker among larger entities and stronger among smaller entities; enterprise risk management practice therefore appears to matter more for reporting quality in smaller commercial SOCEs than in larger ones. It should be noted, however, that the interaction term added only 1.1 percentage points of explained variance ($\Delta R\text{ Square} = 0.011$) beyond the additive model in Step 2, so while the moderation effect is statistically significant, its practical magnitude is modest; formal simple-slopes or marginal-effects analysis, together with confidence intervals around the interaction coefficient, would allow this magnitude to be interpreted with greater precision than the significance test alone permits.

DISCUSSION

This study sought to establish the moderating effect of firm size on the relationship between Enterprise Risk Management and the quality of financial reporting among commercial SOCEs in Kenya. The interaction term was statistically significant ($B = -0.152$, $p = .036$), leading to the rejection of HO5. This confirms, consistent with Vij and Farooq (2016), that firm size does significantly moderate the translation of organisational practices

into outcomes. However, the direction found here diverges from the straightforward positive moderation Vij and Farooq (2016) reported for information technology orientation and business performance in India: in the present study, the negative interaction coefficient indicates that ERM matters more for reporting quality in smaller SOCEs than in larger ones. A plausible explanation is that Kenya's larger commercial SOCEs, such as those in the energy and ports sectors, already operate under closer scrutiny from the Office of the Auditor-General, the National Treasury, and other oversight bodies, so their reporting quality may be less dependent on the strength of their own internal ERM practices. Smaller SOCEs, by contrast, may rely more heavily on their own internal risk governance, assessment, mitigation, and monitoring architecture to achieve comparable reporting quality, making ERM practice a comparatively higher-stakes determinant of reporting quality for them.

This finding also diverges from Kibe et al. (2024), who found no significant moderating effect of firm size on the relationship between financial indicators and financial distress among Kenyan commercial and manufacturing state corporations, and from Ochoi et al. (2025), who found that firm size significantly and negatively moderated the relationship between inclusive marketing and enterprise survival, but in the opposite direction, with larger firms benefiting more. That firm size moderates different relationships in different directions across these three Kenyan studies underscores that its moderating role is highly specific to the relationship, sector, and outcome being examined, rather than reflecting a single, generalisable size effect. This pattern of firm size interacting with a governance or oversight mechanism to shape financial reporting quality is also documented outside the ERM literature: Dagwom Yohanna et al. (2024), studying listed consumer goods companies in Nigeria, found that firm size alone had only a marginally significant negative effect on financial reporting quality, but that this negative effect became clearly significant once audit quality was introduced as a moderator, with a positive and significant firm size by audit quality interaction, and a substantially larger share of variance explained by the moderated model. Read together with the present findings, both studies support a broader proposition that firm size does not act on reporting quality in isolation, but through its interaction with whichever oversight mechanism, whether an internal governance architecture such as ERM or an external assurance mechanism such as audit quality, is most consequential in a given institutional setting.

Limitations And Suggestions for Further Research

Two measurement limitations qualify the findings above. First, firm size in this study was operationalised as a perception-based construct, capturing respondents' views on whether a large asset base supports risk management and reporting quality, rather than as an objective, balance-sheet-based measure. Financial reporting quality was likewise captured through respondents' self-reported perceptions via the same structured questionnaire, rather than through an externally verifiable indicator. This matters because the study's interpretation of the interaction, that ERM matters more for smaller than for larger SOCEs, rests on how respondents perceive scale and reporting quality rather than on independently verifiable organisational or reporting characteristics. This is a common limitation of single-source, perception-based survey designs, but it is worth stating plainly rather than allowing the factorability statistics reported above to be read as validating the substantive claim. Where reliable secondary data are available, future studies of ERM and financial reporting quality among Kenyan SOCEs could operationalise firm size objectively, for example as the logarithm of total assets, and could triangulate or replace the perception-based financial reporting quality measure with an archival, audit-based indicator. Public-sector accounting research elsewhere has used the type of audit opinion issued on an entity's financial statements, ranging from unqualified to disclaimer, as such an indicator: Rakhman and Wijayana (2019, 2024) applied this approach across 3,018 and 4,254 Indonesian local-government financial reports respectively, and Al-Maraghi and Nagari (2026) similarly used audit opinion type across 1,089 Indonesian local-government reports from 2021 to 2023. Pobrić (2024) applied the same logic to 135 audit reports of government-owned enterprises in Bosnia and Herzegovina, finding that 81.5% carried modified opinions, a context close to that of Kenyan SOCEs. Audit opinion is not without its own limitations as an FRQ proxy, but because it is assigned by an independent external auditor rather than self-reported by the entity being assessed, it would offer a useful complement to, or robustness check on, the perception-based measure used here.

Second, the moderation analysis itself could be extended. The present analysis relies on the significance of the interaction coefficient and the associated change in R Square; it does not report confidence intervals around the interaction term, a simple-slopes or marginal-effects analysis showing how the ERM-financial reporting quality relationship changes at representative levels of firm size, or multicollinearity diagnostics for the mean-centred

predictors. Future work on this dataset, or replications with new data, should report these statistics to allow the modest but statistically significant moderation effect identified here to be interpreted with greater precision. Finally, the explanation offered above, that larger SOCEs' closer external oversight reduces their dependence on internal ERM practice, is a plausible interpretation of the pattern of results rather than a directly tested mechanism, since external oversight intensity was not itself measured in this study; studies that measure oversight intensity directly, for example through the frequency or scope of Auditor-General engagement, would be able to test this explanation rather than infer it.

CONCLUSION AND RECOMMENDATION

The study concludes that firm size is not a neutral background characteristic but an active moderator of how Enterprise Risk Management practice translates into financial reporting quality among commercial SOCEs in Kenya, and that smaller commercial SOCEs derive comparatively greater reporting-quality benefit from strong ERM practice than larger, more heavily externally scrutinised entities do. This finding provides direct empirical support for Contingency Theory's proposition that the effectiveness of an organisational practice is conditional on situational factors, in this instance organisational size and, plausibly, the intensity of the external oversight environment that typically accompanies it, an explanation that remains speculative in this study because external oversight was not directly measured, rather than universal across all organisations.

The study recommends that the National Treasury and the State Corporations Advisory Committee consider targeting ERM capacity-building support disproportionately toward smaller and medium-sized commercial SOCEs, which appear to have the most to gain, in reporting-quality terms, from strengthened risk management practice, rather than distributing such support uniformly across the SOCE portfolio irrespective of scale. Larger SOCEs, which already operate under closer scrutiny from the Office of the Auditor-General and the National Treasury, should nonetheless continue to maintain their internal ERM architecture, since external oversight and internal risk management are best treated as complementary rather than substitutable mechanisms for safeguarding financial reporting quality.

ACKNOWLEDGEMENTS

The authors thank the University of Kabianga and the respondents who participated in this study. The authors would also like to thank the anonymous reviewers for their valuable time, effort, and constructive feedback, which significantly improved the quality and clarity of this manuscript.

Declaration Of Interest:

The author declare that they have no known competing financial interests or personal relationships that could have appeared to influence the work reported in this paper.

Declaration Of Ai Use

This manuscript was prepared through the combined contributions of all authors, including contributions to the study design, data, content development, results, interpretation, and related scholarly work. The author(s) acknowledge the use of Grammarly to assist with grammar checking, language refinement, and reference formatting. These AI-assisted tools were not used as authors and did not replace the intellectual contributions or scholarly judgment of the author(s). The author(s) accept full responsibility for the accuracy, integrity, and final content of the manuscript.

Funding:

This research did not receive any specific grant from funding agencies in the public, commercial, or not-for-profit sectors. It was conducted as part of the primary author's masters studies at the University of Kabianga, Kenya.

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