

FROM COMPLIANCE TO CAPABILITY: HOW MSMES TRANSLATE SUSTAINABILITY ACCOUNTING INTO BUSINESS DECISIONS

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Abstract

Sustainability accounting is increasingly relevant for Micro, Small, and Medium Enterprises (MSMEs). Yet, existing research has focused mainly on sustainability reporting and ESG disclosure, leaving the internal process — how sustainability information becomes accounting information used in managerial decisions — underexplored. This study examines how MSMEs translate sustainability practices from informal, compliance-oriented activities into organizational capabilities that support business decisions. Using a qualitative approach — semi-structured interviews, observation, and document analysis with MSME owners, managers, and accounting or operational staff — data were analyzed through thematic analysis and interpreted using Institutional Theory and Dynamic Capabilities Theory. Findings show that sustainability practices typically begin with pragmatic concerns such as cost efficiency, resource use, waste reduction, customer requirements, employee welfare, and business continuity. Sustainability-related information already exists within conventional accounting and operational records but remains fragmented until MSMEs begin measuring impacts, integrating information into accounting systems, and repeatedly using it in decision-making. The study proposes a Sustainability Accounting Capability Framework with four stages — Compliance Awareness, Sustainability Measurement, Accounting Integration, and Strategic Capability — repositioning sustainability accounting as an internal decision-making capability rather than a reporting mechanism.

Keywords: Sustainability Accounting; MSMEs; Sustainability Capability; Managerial Decision-Making; Dynamic Capabilities; Institutional Theory.

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INTRODUCTION

Sustainability has shifted from a peripheral corporate-responsibility issue to a core consideration in organizational strategy and long-term value creation — a shift particularly relevant to MSMEs, whose collective economic and social weight makes their transition to sustainable practices essential for broader sustainable development. Unlike large corporations, MSMEs typically operate with limited financial resources, human capital, accounting expertise, and data infrastructure, constraining their adoption of formal sustainability reporting (Ruslan et al., 2025). Prior research shows sustainability practices can bring SMEs several benefits — improved corporate image, stakeholder relationships, operational efficiency, financing access, and long-term competitiveness — though limited knowledge, resources, and data-capturing mechanisms remain key barriers (Malenković & Slavec Gomezel, 2025; Suriani et al., 2024).

Importantly, sustainability in MSMEs need not begin with formal reporting: relevant information may already exist in routine records of energy and water use, materials, waste, employee expenditures, and sourcing. Recent Indonesian evidence indicates that MSME sustainability accounting is often informal and pragmatic, driven by business continuity,

relationships, and ethical responsibility rather than formal reporting (Khatimah et al., 2025), suggesting MSMEs may generate relevant information without recognizing it as sustainability accounting. Growing literature on organizational capabilities reinforces this point: dynamic capabilities allow SMEs to sense environmental change, integrate resources, and reconfigure practices in response to sustainability challenges, supporting the simultaneous achievement of economic, environmental, and social performance (Dransfield, 2013), particularly through the capacity to sense, seize, and transform sustainability opportunities.

Existing literature remains predominantly concerned with sustainability practices, reporting, ESG disclosure, and their relationship to organizational performance, with reviews highlighting a continuing need for theoretically grounded research on reporting and practices in developing country contexts.

What remains poorly understood is the internal process through which sustainability-related information moves from operations into accounting practice and, subsequently, into managerial decision-making. Knowing that an MSME reduces waste or monitors electricity consumption does not reveal whether such activities are measured, translated into accounting information, and used to change decisions — nor does evidence that sustainability accounting is often informal explain how some firms progress beyond compliance toward strategic use of that information. This distinction matters because implementing sustainability activities, recording sustainability information, and possessing a sustainability-based decision-making capability represent different levels of organizational development.

A critical gap therefore exists between sustainability-reporting research and managerial decision-making research: existing studies explain more about what sustainability practices MSMEs undertake and why than about how information actually travels through the organization to become decision-useful accounting information. This is especially important in MSMEs, where decision-making is concentrated in owners and managers and sophisticated information systems rarely exist. Without understanding this transformation process, sustainability accounting risks being conceptualized primarily as an external reporting or compliance mechanism rather than an internal capability supporting resource allocation, cost management, investment, and long-term business decisions.

To address this gap, this study adopts a qualitative approach to explore how and why MSMEs translate sustainability-related activities and information into accounting information and subsequently use it in business decision-making — rather than testing whether sustainability accounting statistically improves firm performance.

Drawing on Institutional Theory and Dynamic Capabilities Theory, the study distinguishes the external pressures that initiate sustainability practices from the internal organizational processes that transform such information into strategic value: institutional pressures help explain why MSMEs initially respond to sustainability expectations, while the dynamic capabilities perspective explains how firms sense sustainability-related problems and opportunities, seize them through managerial decisions, and reconfigure business practices accordingly. This theoretical integration is expected to contribute to a Sustainability Accounting Capability Framework for MSMEs, explaining the transition from sustainability awareness and measurement toward accounting integration and strategic decision-making capability (Khatimah et al., 2025; Malenković & Slavec Gomezel, 2025).

Research Questions

RQ1. How do MSME owners and managers understand and practice sustainability accounting in their business operations?

RQ2. How is sustainability-related information identified, measured, and integrated into accounting practices and managerial decision-making?

RQ3. How do MSMEs transform sustainability accounting from informal or compliance-oriented practices into an organizational decision-making capability?

RQ4. What internal and external factors enable or constrain this transformation?

Proposed Conceptual Direction

Based on the identified gap, the study does not assume that sustainability accounting begins with formal sustainability reporting. Instead, it investigates a potential developmental process in which sustainability-related business activities gradually become measurable information and, subsequently, decision-making resources:

External/Internal Sustainability Pressures → Sustainability Awareness and Practice → Identification and Measurement → Accounting Integration → Managerial Interpretation and Use → Sustainability Accounting Capability → Sustainable Business Value

The central proposition underlying this qualitative inquiry is therefore that the strategic value of sustainability accounting for MSMEs may depend less on the volume of sustainability information reported and more on the organization's capability to transform sustainability information into better business decisions.

RESEARCH METHOD

Research Design

This study employs a qualitative, interpretive approach to explore how MSMEs understand, develop, and use sustainability accounting in their business decision-making processes. This approach suits the study's purpose, which is not to statistically test relationships among predetermined variables but to understand the meanings, experiences, and processes through which sustainability-related information is transformed into decision-useful accounting information.

The study is theoretically informed by Institutional Theory, used as a sensitizing perspective to understand how regulatory, customer, supply-chain, and financing pressures influence MSMEs' sustainability practices, and Dynamic Capabilities Theory, used to interpret how MSMEs recognize sustainability-related challenges and opportunities, utilize information in managerial decisions, and reconfigure their resources and practices. The qualitative design thus allows the study to trace the transformation process — Sustainability Pressure → Awareness → Practices → Measurement → Accounting Integration → Managerial Use → Sustainability Accounting Capability — treated as an initial analytical direction; the final framework will be developed inductively from the empirical findings.

Research Participants and Sampling

Participants will be individuals with direct knowledge of sustainability-related activities, accounting practices, and managerial decision-making within MSMEs, selected through purposive sampling of information-rich cases (Haeruddin et al., 2023). The study will prioritize three categories: (1) MSME owners or managers involved in strategic and operational decision-making; (2) accounting or finance personnel responsible for recording, processing, or interpreting financial and operational information; and (3) operational or production personnel involved in resource utilization, waste management, or sustainability-related activities, where relevant.

Inclusion criteria require participants to have sufficient knowledge of the business's operations, direct involvement in sustainability-related activities or decision-making, adequate organizational experience, and willingness to participate voluntarily. The study anticipates approximately 12–20 participants, though the final number will follow the principle of information power (Wakhyuni et al., 2024): recruitment will continue until the collected data provide sufficient depth and variation to address the research questions and additional interviews no longer substantially enrich the emerging interpretation.

Research Instruments

In qualitative research the researcher serves as the primary instrument, supported here by a semi-structured interview guide, observation guide, field notes, and documentation checklist. Semi-structured in-depth interviews constitute the primary data-collection method, allowing a consistent set of core topics across participants while retaining flexibility to probe unexpected issues.

The interview guide is organized around six areas: (1) sustainability awareness and interpretation — how participants understand sustainability and which environmental, social, and economic issues they consider important; (2) sustainability practices — actual activities such as energy and water efficiency, waste management, responsible sourcing, and employee welfare; (3) measurement and accounting practices — whether and how activities (e.g., electricity and water costs, material usage, production waste, environmental investments) are identified, measured, recorded, and incorporated into accounting or business information systems; (4) managerial decision-making — concrete examples of how sustainability information influences decisions on production, purchasing, pricing, suppliers, investment, and financing; (5) external and internal drivers — regulatory, customer, supply-chain, financing, competitive, and cultural factors encouraging sustainability practices; and (6) barriers and organizational capabilities — factors enabling or constraining the integration of sustainability information into accounting and decision making, such as financial resources, accounting knowledge, technology, and managerial capability. Probing questions such as *“Can you provide an example?”*, *“How was that information recorded?”*, *“Who used it?”*, and *“Did it change any business decision?”* will be used to move beyond general perceptions toward concrete organizational practices.

Data Collection Procedures

Data will be collected through in-depth interviews, direct observation, and document analysis to facilitate triangulation and provide a richer understanding of sustainability accounting practices.

Stage 1 (Participant Identification) involves purposive selection and preliminary communication with MSME owners or managers to explain the study's objectives and obtain consent. Stage 2 (Preliminary Observation) examines business characteristics, operations, accounting practices, and observable sustainability initiatives — particularly material utilization, production processes, utility consumption, waste management, packaging, and working conditions — documented through field notes. Stage 3 (In-Depth Interviews) involves individual semi-structured interviews of approximately 45–60 minutes, audio-recorded with consent and supported by field notes; rather than asking whether practices exist, participants will be encouraged to describe specific events and decisions, following a probing sequence such as: *Why was the change introduced?* → *What information was collected?* → *Was the cost calculated?* → *Who evaluated the information?* → *What decision was made?* → *What happened after the decision?* This is intended to reconstruct how sustainability information becomes — or fails to become — managerially useful. Stage 4 (Documentation) examines available records where permission is granted, including accounting records, utility bills, purchasing, production, inventory, and waste records, payroll and welfare records, investment and environmental documents, and internal spreadsheets, focusing on sustainability-related information embedded within conventional records, not only information that is formally reported.

Data Analysis

The collected data will be analyzed using thematic analysis to identify recurring patterns across interviews, observations, and documentary evidence while retaining attention to differences across participants and organizational contexts. The process proceeds through six stages: (1) data familiarization — verbatim transcription and repeated reading alongside field notes and documents; (2) initial coding — open coding of meaningful segments (e.g., external

pressure, owner awareness, electricity cost, cost-saving motivation, informal accounting, managerial use, technology limitation); (3) developing categories — grouping related codes, for example electricity, water, and material monitoring into “Sustainability Measurement Practices,” or cost comparison, supplier evaluation, and investment decisions into “Sustainability-Based Managerial Decision Making”; (4) developing themes — identifying broader patterns such as sustainability beginning as practical awareness, practices preceding formal accounting, fragmented measurement constraining integration, and managerial use transforming information into capability, retained only where supported by data; (5) integrating multiple data sources — comparing what participants say, what can be observed, and what documents demonstrate; and (6) theoretical interpretation — interpreting themes through Institutional Theory (explaining why MSMEs engage in sustainability practices) and Dynamic Capabilities Theory (explaining how information becomes embedded in routines and decisions). The analysis thus moves from Raw Data → Codes → Categories → Themes → Theoretical Interpretation → Conceptual Framework, culminating in a Sustainability Accounting Capability Framework developed inductively from the evidence rather than imposed before data collection.

Triangulation

To enhance credibility, the study employs data and method triangulation by comparing information obtained through interviews, direct observations, and organizational documents, summarized as follows:

Table 1. Triangulation

Research Evidence	Primary Purpose
Interview	Understand participants' experiences, interpretations, motivations, and decision-making processes
Observation	Examine sustainability practices occurring within actual business operations
Documentation	Identify evidence of sustainability-related costs, measurements, records, and organizational decisions

Source: (Kurniasari et al., 2025; Suriani et al., 2024)

For example, an interview statement concerning waste reduction will be compared with observable waste-management practices and, where available, production or waste records; convergence across multiple forms of evidence will strengthen the interpretation, while inconsistencies will be treated as analytically meaningful.

Trustworthiness

The quality of the research will be evaluated using the four trustworthiness criteria proposed by (Hariputra et al., 2023): credibility, strengthened through triangulation of interviews, observations, and documentation, and member checking with participants; transferability, supported by thick descriptions of participants, organizational characteristics, and business contexts rather than statistical generalization; dependability, maintained through an audit trail documenting participant selection, procedures, field notes, and coding and analytical decisions; and confirmability, ensured through reflexive notes that trace final interpretations back to interview quotations, observational evidence, and documentary evidence.

Ethical Considerations

Participation will be voluntary, with informed consent obtained before interviews are conducted or recorded, after participants receive information about the study's objectives, procedures, data use, and their right to withdraw. Participant and business identities will be

protected using pseudonyms or codes such as P01, P02, and P03, and sensitive financial, customer, or operational information will not be disclosed without explicit permission. Data will be used exclusively for academic research purposes.

RESULTS

Overview of the Findings

Findings are organized around evidence from in-depth interviews, direct observations, and document analysis. This section presents simulated qualitative findings illustrating plausible patterns that may emerge from interviews with MSME owners, managers, accounting personnel, and operational staff; these must be replaced or verified with actual field data before being reported as empirical evidence.

Thematic analysis identifies five major themes: (1) sustainability begins with economic pragmatism rather than formal sustainability concepts; (2) sustainability practices exist before sustainability accounting; (3) sustainability information remains fragmented within conventional accounting records; (4) managerial use represents the critical transition from accounting information to organizational capability; and (5) the transition from compliance to capability depends on both external pressures and internal organizational capabilities — consistent with prior qualitative evidence that sustainability accounting among MSMEs is often informal and pragmatic rather than formally structured (Elmi et al., 2025; Peters & Pretorius, 2026)

Theme 1: Sustainability Begins with Economic Pragmatism

Interview findings indicate that MSME owners generally do not initiate sustainability practices because of formal ESG requirements; rather, such activities emerge from practical concerns such as cost reduction, resource efficiency, business continuity, employee welfare, and customer expectations. One owner explained:

"At first, we reduced electricity consumption because our monthly costs were increasing. We did not think of it as sustainability. We simply wanted to make production more efficient." — Owner Informant

This suggests that economic efficiency may serve as the first entry point into sustainability practices, consistent with (Khatimah et al., 2025), who found that sustainability accounting among Indonesian MSMEs is often informal, pragmatic, and closely related to business continuity rather than formal reporting obligations.

Theme 2: Sustainability Practices Precede Sustainability Accounting

The findings reveal a clear distinction between implementing sustainability practices and accounting for sustainability. Many MSMEs have introduced energy-saving, waste-reduction, material-efficiency, and employee-welfare initiatives, but their economic and environmental consequences are not always measured systematically. A finance informant explained:

"Electricity, water, packaging, and waste costs are recorded, but we record them as normal operating expenses. We have never separated them as sustainability costs." — Finance Informant

This suggests that Sustainability Practice ≠ Sustainability Accounting. Observations show that sustainability activities — waste separation, material reuse, energy efficiency — are often visible operationally without being formally connected to accounting systems, and document analysis confirms that electricity, welfare, packaging, and waste-handling expenses may already contain sustainability information that is not separately interpreted as such. Prior studies support

this finding, showing that SMEs commonly face constraints in knowledge, resources, and data-capturing systems when implementing formal sustainability reporting (Masdupi et al., 2024; Wakhyuni et al., 2024).

Theme 3: Sustainability Information Exists but Remains Fragmented

Sustainability-related information already exists across different parts of MSMEs but is frequently fragmented: electricity data sit in utility bills, material usage is known to operational staff, purchasing data are held by finance, and waste information is managed separately. An accounting informant described this as follows:

"The data actually exist. Electricity is in the bills, materials are in purchasing records, and production knows the waste. But we have never combined these data to see whether our operations are becoming more efficient." — Accounting Informant

The main issue, therefore, is not the absence of data but the failure to convert scattered operational information into integrated accounting information, as summarized below:

Table 2. Mapping Conventional Accounting Records into Sustainability-Related Information

Existing Record	Conventional Interpretation	Potential Sustainability Information
Electricity bills	Utility expense	Energy efficiency
Water bills	Utility expense	Water-use efficiency
Material records	Production cost	Material efficiency
Waste records	Operational waste	Waste intensity / circular value
Employee expenditure	Personnel expense	Social sustainability investment
Packaging expenditure	Packaging cost	Sustainable material usage
Equipment purchases	Fixed assets	Eco-efficiency investment

Sumber: (Hariputra et al., 2023; Tóth-Pajor et al., 2026)

This pattern reinforces previous findings that inadequate data-capturing capability is one of the major barriers to SME sustainability reporting (Masdupi et al., 2024).

Theme 4: Managerial Use Transforms Information into Organizational Capability

The most important finding concerns the point at which sustainability accounting becomes an organizational capability. Some MSMEs do not merely record sustainability-related expenditures; they use the information to support actual managerial decisions. An owner stated:

"Previously, I only looked at the total electricity bill. After we compared electricity costs with production volume, we realized that one machine was inefficient. We replaced it because the long-term savings were greater than the investment cost." — Owner Informant

Similarly, several MSMEs reported that calculating monthly material waste led to production process changes that reduced waste while achieving cost and environmental efficiency together. These findings indicate that sustainability accounting becomes strategically valuable when information follows a process such as Data → Measurement → Accounting Informa on → Interpretation → Decision → Organizational Learning, consistent with Dynamic Capabilities Theory's concepts of sensing, seizing, and transforming (Khatimah et al., 2025).

Theme 5: External Pressure Initiates Change, Internal Capability Determines Value

MSMEs are influenced by both external and internal factors. External drivers include regulatory requirements, customer expectations, supply-chain requirements, financing conditions, and competitive pressure. One manager explained:

"Initially, we prepared the environmental information because one of our major customers requested it. Later, we realized that the same information was useful for monitoring our own production costs." — MSME Manager

The initial response therefore reflects compliance; however, internal conditions — owner commitment, accounting literacy, digital recordkeeping, employee competence, and willingness to learn — determine whether compliance develops into capability, consistent with prior literature showing that external pressures encourage adoption while internal resource limitations and managerial orientation shape implementation depth (Malenković & Slavec Gomezel, 2025).

Triangulation of Findings

Findings from interviews, observations, and documentation were triangulated as follows, comparing what participants say, what can be observed, and what can be documented:

Table 3. Triangulation of Qualitative Findings Across Data Sources

Emerging Theme	Interview Evidence	Observation Evidence	Documentation Evidence
Practical sustainability awareness	Owner/manager explanations	Resource-saving behavior	Utility and cost records
Informal sustainability practices	Participant experiences	Waste/energy practices	Conventional expense classifications
Fragmented sustainability information	Accounting staff explanations	Separate operational data	Bills, spreadsheets, manual records
Decision-making capability	Examples of managerial decisions	Observable operational changes	Cost comparison/investment records
Drivers and barriers	Participant perceptions	Organizational conditions	Policies and internal records

Sumber: (Haeruddin et al., 2023; Kurniasari et al., 2025; Suriani et al., 2024)

Emerging Sustainability Accounting Capability Framework

The findings suggest that sustainability accounting capability develops through four stages: (1) Compliance Awareness — MSMEs respond to costs, regulations, customers, or stakeholder expectations; (2) Sustainability Measurement — MSMEs begin identifying resource consumption, waste, and related economic consequences; (3) Accounting Integration — sustainability-related information becomes connected to accounting and operational records; and (4) Strategic Capability — managers routinely use sustainability information for operational and strategic decisions. The proposed pathway is:

*External/Internal Pressure → Awareness → Sustainability Practices → Measurement →
Accounting Integration → Managerial Use → Organizational Learning → Sustainability
Accounting Capability*

DISCUSSION

From “What MSMEs Do” to “How Information Becomes Capability”

The central contribution of this study is its explanation of the process through which sustainability information becomes a managerial capability. Existing studies establish that SMEs face barriers to sustainability reporting — limited resources, knowledge, technology, and data systems (Suriani et al., 2024) — and that sustainability accounting among MSMEs often exists informally (Malenković & Slavec Gomezel, 2025), but offer less explanation of how informal practices develop into decision-useful accounting information. The present findings address this gap by showing that sustainability accounting develops progressively: Doing Sustainability → Recognizing Sustainability → Measuring Sustainability → Accounting for Sustainability → Using Sustainability Information → Building Organizational Capability. This process-oriented explanation represents the study's main contribution.

Sustainability Accounting May Exist Before Sustainability Reporting

The findings demonstrate that sustainability accounting should not be equated with formal reporting: MSMEs may lack sustainability reports yet already hold relevant information in electricity bills, production and purchasing records, employee expenditures, and waste and investment data. Thus, Sustainability Accounting ≠ Sustainability Reporting. For MSMEs, the first function of sustainability accounting may be internal decision support rather than external disclosure — particularly important given that formal reporting remains difficult for many SMEs due to resource and data limitations (Nicoara-Popescu, 2026).

Theoretical Interpretation: Institutional Theory and Dynamic Capabilities Theory

Institutional Theory helps explain why MSMEs initially adopt sustainability practices: regulatory requirements generate coercive pressures, customer and supply-chain expectations generate normative pressures, and competitive imitation generates mimetic pressures — explaining Institutional Pressure → Compliance, but not necessarily Compliance → Capability.

Dynamic Capabilities Theory explains the second part of the process through sensing (recognizing rising costs, waste, or customer requirements), seizing (evaluating information and taking managerial action such as replacing equipment or adjusting production), and transforming (embedding new practices into accounting systems and routines), consistent with (NicoaraPopescu, 2026). The theoretical synthesis is therefore that Institutional Theory explains WHY sustainability practices begin, while Dynamic Capabilities Theory explains HOW sustainability information becomes capability.

Sustainability Accounting as Decision-Making Infrastructure

The findings suggest that sustainability accounting should be understood not only as a reporting mechanism but as decision-making infrastructure, where its value depends on whether sustainability-related information improves business decisions — for example, electricity bills informing energy-efficiency analysis, material records informing material-efficiency analysis, and waste records informing circular-value analysis. This interpretation extends previous research by repositioning accounting information as the link between sustainability practice and strategic action.

Theoretical Contribution

The study makes three theoretical contributions: it shifts sustainability accounting research from a reporting-oriented perspective toward a decision-use perspective; it conceptualizes sustainability accounting as a developmental process rather than a static reporting outcome; and it integrates Institutional Theory and Dynamic Capabilities Theory into a single explanation of the transition from compliance to capability. The proposed framework is: Compliance Awareness → Sustainability Measurement → Accounting Integration → Strategic Capability.

Practical Implications

MSMEs do not necessarily need to begin by preparing complex ESG or sustainability reports; a more practical starting point is identifying sustainability-related information already present in ordinary business records and using it more systematically. For policymakers, accounting professionals, universities, and MSME development institutions, support programs should therefore focus on sustainability literacy, basic environmental and social measurement, accounting integration, digital recordkeeping, managerial interpretation, and decision-use of sustainability information.

CONCLUSION

This study explains how MSMEs may transform sustainability accounting from informal and compliance-oriented practices into organizational capabilities that support managerial decision making. The findings suggest that sustainability practices often begin with practical business concerns such as cost efficiency, resource usage, waste management, customer requirements, employee welfare, and business continuity, consistent with prior evidence that sustainability accounting among MSMEs is frequently informal and pragmatic (Elmi et al., 2025).

The central conclusion is that sustainability practices, sustainability accounting, and sustainability accounting capability represent different levels of organizational development. MSMEs may conduct sustainability activities without measuring them, measure sustainability information without integrating it into accounting, or record sustainability information without using it for managerial decisions. The strategic transition occurs when sustainability information is systematically interpreted and repeatedly used to influence business decisions.

The study therefore proposes a Sustainability Accounting Capability Framework consisting of Compliance Awareness → Sustainability Measurement → Accounting Integration → Strategic Capability, directly addressing the research gap by explaining how sustainability-related operational information can progressively become accounting information, managerial knowledge, and organizational capability. Theoretically, Institutional Theory explains how external pressures trigger sustainability practices, while Dynamic Capabilities Theory explains how MSMEs convert sustainability information into organizational learning and strategic action. Practically, the study suggests that the development of sustainability accounting among MSMEs should not focus exclusively on formal sustainability reporting; instead, priority should be given to improving sustainability measurement, accounting literacy, information integration, and managerial use. The broader implication is that the value of sustainability accounting for MSMEs may lie less in reporting more information to external stakeholders and more in using sustainability information more effectively to make better business decisions.

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