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External accountants' business advice and SME performance

Peter John Carey
School Accounting, Economics and Finance, Deakin University, Melbourne, Australia

Abstract

Purpose – This study aims to investigate whether "small- and medium-sized enterprises" (SMEs) benefit from their external accountants' business advice through enhanced firm performance. Most SMEs draw on external support, and their main advisors are external accountants (Bennett and Robson, 1999). The resource-based view of the firm suggests that firms will seek external support if they perceive a gap in their internal resources.

Design/methodology/approach – Data were collected from a questionnaire mailed to a random sample of Australian SMEs, defined as businesses having between 5 and 200 full-time employees.

Findings – An analysis of 380 survey respondents confirms a positive relationship between the voluntary purchase of business advice and SME performance, and that SME performance is further enhanced when business advice is purchased jointly with auditing. These relationships apply to the small (5-49 employees) but not to the medium-sized (50-200 employees) businesses. Findings are consistent with smaller firms having narrower resource bases and thus a greater need to source business advice.

Practical implications – The accounting profession has long encouraged a broadening of its service base, and evidence that small businesses perceive a performance benefit from their accountants' business advice provides support for the profession's strategy.

Originality/value – This research extends the empirical literature investigating the link between the business advice of an external accountant and SME performance. It explains small firms' demand for business advice by extending the application of the resource-based view of the firm and provides new evidence consistent with "knowledge spillover" from auditing to business advice in the small firm environment.

Keywords Performance, SME, Auditing, Business advice, Knowledge spillover

Paper type Research paper

1. Introduction

Small- and medium-sized enterprises (SMEs) are critical to most developed and developing economies. They represent the main generator of economic activity and the largest private sector employer group. For example, in Australia, businesses with < 20 employees account for almost half of employment in the private non-financial sector and

JEL classification – M40, M42

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over a third of production (Connolly *et al.*, 2012). SMEs (< 200 employees) contribute over 50 per cent of the value added by industry to gross domestic product (ABS, 2006a). In the USA, small- and medium-sized businesses create more than half of the non-farm gross domestic product (www.sba.gov). While there is wide variation in international definitions of SMEs, this study adopts the categorisation from The Australian Bureau of Statistics (ABS, 2006b) and the Australian Corporations Law 2001, where a small business employs 5-49 employees and a medium-sized business 50-200 employees[1].

Most SMEs draw on external support, and their main advisors are external accountants (Bennett and Robson, 1999). While SMEs primarily use their external accountants to help fulfil regulatory requirements or satisfy contractual constraints (e.g. taxation, compilation and audit), there is evidence that most SMEs also purchase business advisory services from their accountants (Blackburn and Jarvis, 2010; Berry *et al.*, 2006; Carey *et al.*, 2005; Gooderham *et al.*, 2004; Deakins *et al.*, 2001; Kirby *et al.*, 1998). There is a strong a priori case that SMEs require external support because of deficiencies in in-house expertise or resources (Bennett and Robson, 2005; Collis and Jarvis, 2002; Robson and Bennett, 2000; Marriott and Marriott, 2000). The business advice of an external accountant can encapsulate a range of competencies that support the SME's intangible resources, providing a potential source of competitive advantage (Gooderham *et al.*, 2004). SMEs will source external support if they perceive a gap between their existing internal resources and the resources required to achieve business objectives (Johnson *et al.*, 2007). This resource gap is likely to be greatest in smaller firms (Deakins *et al.*, 2001; Jennings and Beaver, 1997).

The main contribution of this study is to measure whether there is a positive association between SMEs voluntarily purchasing business advice and SME performance. Evidence of voluntary demand for business advice provides prima facie evidence that external accountants are perceived to provide a benefit. A positive association between the voluntary purchasing of business advice and SME performance would provide more direct evidence that external accountants provide a benefit to their SME clients. However, previous empirical research investigating the relationship between business advice and performance in the SME environment is mixed and inconclusive (Berry *et al.*, 2006; Bennett and Robson, 1999; Kirby *et al.*, 1998). This study presents fresh empirical evidence as to whether SMEs buying business advice benefit through superior operating performance, and whether small firms exhibit a greater performance benefit.

A further contribution of this study is to investigate whether SMEs that simultaneously buy business advice and auditing services from their external accountants demonstrate superior performance over and above the benefit from business advice alone. While theory suggests that the primary value of an audit is to enhance the credibility of financial information used in monitoring performance (Wallace, 1980), this study investigates whether knowledge the accountant gains while auditing translates to effective business advice that enhances firm performance. An auditors' capacity to add value through business advice is identified, first, by drawing on literature that identifies the long-standing role of the auditor in providing advice (formal or informal) on matters of control (Arens and Loebbecke, 1976; Abdel-Khalik, 1993), and, second, by extending the argument developed by Simunic (1984) that knowledge can "spill over" from auditing to business advice. It is argued that auditors can draw on their industry- or client-specific knowledge gained during the audit process

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to support the information needs of their SME clients. This study accordingly predicts that the benefit to SME performance will be greater if business advice is sourced from an external accountant who also provides audit services.

The SME environment provides a unique opportunity to observe the link between business advice, auditing and SME performance. Unlike public-interest entities, there are no regulatory restrictions on external accountants providing business advice to their SME clients[2], and not all SMEs are subject to a mandatory audit requirement[3].

The next section develops hypotheses concerning business advice from external accountants and SME performance, followed by methodology, results and the conclusion, limitations and recommendations for future research.

2. Literature review and hypothesis development

2.1 Business advice and performance

In response to perceived demand for external support by business, the international governing bodies of the accounting profession have, since the mid-1990s, embraced and encouraged a model of multi-disciplinary practices that are capable of providing a broad range of services to their clients (Blackburn and Jarvis, 2010; Fogarty *et al.*, 2006; Greenwood *et al.*, 2002; Parker, 2001). The ongoing acquisition of distinct knowledge and expertise has long been the basis of an external accountant's competitive advantage (Power, 1997). Despite early reluctance by smaller accounting practices to broaden their service base (Fogarty *et al.*, 2006), some small- and medium-sized accounting practices (SMPs) appear to be emulating their Big N counterparts by merging into larger business consulting practices focussed on niche industries or services to accommodate the broader information needs of their clients (Blackburn and Jarvis, 2010; Frank *et al.*, 2001; Farrell, 1998). One explanation as to why SMPs are focussing more on business advisory services is that the market for traditional compliance services is diminishing because of a reduction in statutory lodgement and audit requirements amongst SMEs (Kitching *et al.*, 2011; Blackburn and Jarvis, 2010). This mirrors the trend in the public company market segment where advisory services are acknowledged as an important source of growth as revenue from traditional audit and taxation services stagnates (The Economist, 2010).

The business advice of external accountants is defined in the present study as advice supporting the information needs of management in the operation of the business. It has been described using a variety of labels, including "business advisory services", "management advisory services" (MAS), "management consulting services" or, when provided by the firm's external auditor, "non-audit (assurance) services" (NAS). Parker (2001) argues that during the twentieth century, the accounting profession broadened the scope of services offered. Parker characterised advisory services as:

> […] taxation planning, accounting systems design and installation, business investigations, corporate reconstructions, executive search, pre-acquisition investigations, manufacturing plant layout design, and the array of services (p. 427).

The professional guidance highlights the extensive range of NAS that external accountants might offer and the difficulty in categorising these services: "New developments in business, the evolution of financial markets and changes in information technology make it impossible to draw up an all inclusive list of non-assurance services" (APES, 2006, p. 110, paragraph 290.157).

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The resource-based view of the firm as a basis for the competitive advantage of a firm lies in the application of tangible or intangible resources at the firm's disposal (Acedo *et al.*, 2006; Teece *et al.*, 1997). Firms can gain competitive advantage using knowledge and information accessed from both within and outside the firm (Peteraf, 1993). SMEs will seek external support from advisors if they perceive a gap in their internal resources (Johnson *et al.*, 2007).

There is a strong a priori case that SMEs seek external support because of a lack of in-house expertise. Demand for advice arises because, although owner-managers of SMEs may be proficient in the product (services) markets within which they operate, they are not necessarily trained or proficient in all aspects of business management. There is evidence that deficiencies exist in the skills base of SME owner-managers (Collis and Jarvis, 2002; Marriott and Marriott, 2000). Business advice might, therefore, be purchased to fill a gap in internal staff or management expertise, to access specialist knowledge, for specific and one-off tasks or to develop new internal procedures and processes (Bennett and Robson, 2005; Robson and Bennett, 2000). Coyte *et al.* (2012) find that SMEs primarily use informal knowledge management organisational strategy rather than a formal approach, which suggests that the business advice of an external accountant is likely to support an SME's informal systems and processes. While most SMEs buy business advice from an external accountant (Bennett and Robson, 1999), they are a heterogeneous group with different characteristics, which explains the variations in the nature and type of external business support sought (Blackburn and Jarvis, 2010).

Despite the emerging evidence that many SMEs rely on the business advice of an external accountant (Blackburn and Jarvis, 2010; Gooderham *et al.*, 2004; Deakins *et al.*, 2001; Kirby *et al.*, 1998), there is mixed evidence as to whether the business advice of an external accountant adds value by improving SME performance. While empirical results from Berry *et al.* (2006) and Bennett and Robson (1999) identify a positive association between the services of an external accountant and SME performance, Robson and Bennett (2000) find no association. Bennett and Robson (1999) base their conclusion on the finding that the proportion of SMEs using an accountant (for any purpose measured as a binary variable) was higher in the fast-growth category (89.9 per cent) than in the medium-growth category (84 per cent) and the declining/stable-growth category (77.3 per cent). Berry *et al.* (2006, p. 33) base their conclusion on the difference in average annual growth rate between "users" and "non-users" of "financial management support". These results should be interpreted with caution because they do not control for the range of factors likely to affect SME performance. The only relevant large-scale multivariate analysis is in the study by Robson and Bennett (2000), who report no association between the services of an external accountant (any service) and SME performance, using three measures of SME performance:

(1) change in number employed by client;

(2) percentage change in firm turnover; and

(3) change in profitability per employee.

The relationship between the business advice of an external accountant and SME performance remains an open empirical question.

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The preceding discussion suggests latent demand for business advice by SMEs due to resource constraints, and that external accountants are responding by providing business advice to their SME clients. If business advice delivered by external accountants to SMEs is effective in supporting the information needs of SME management in the operation of their businesses, a positive relationship between business advice and firm performance is predicted. The arguments are summarised in the following hypothesis:

H1a. SME performance is positively associated with the voluntary purchase of business advice.

Deakins *et al.* (2001) argue that smaller firms seek the support of external accountants because they often lack important skills such as knowledge of financial controls. Similarly, Jennings and Beaver (1997) suggest that small firms in particular have difficulty obtaining and retaining competent staff because of their inability to offer competitive salaries and benefits. Notwithstanding their need for external support, smaller firms might also face greater internal resource constraints that limit their capacity to access advice (Gooderham *et al.*, 2004).

Smaller firms are likely to have a greater gap in their resource capacity compared to medium-sized firms. When purchasing business advice, smaller firms are, therefore, likely to experience greater benefit compared to medium-sized firms. The arguments are summarised in the following hypothesis:

H1b. The positive association between SME performance and the voluntary purchase of business advice will be greater for small firms than for medium-sized firms.

2.2 Joint provision of business advice and auditing and SME performance

Auditors have a long tradition of supporting client management with business advice. In addition to an audit report, Arens and Loebbecke (1976) describe the "management letter" used to inform the audit client of recommendations for improving their business, ranging from suggestions regarding internal control to suggestions for more efficient operations. There is evidence that auditors routinely provide advice and guidance to clients on matters pertaining to internal control discovered during the course of the audit (Clarke and Carey, 1997). Such advice may be provided formally [i.e. Communication by the auditor to those charged with governance, IFAC, ISA 260 (2009a)], or informally through discussions and conversations during the course of the audit. Focussing on privately owned companies, Abdel-Khalik (1993) argues that the primary purpose of an audit of an owner-managed firm is to support the quality and adequacy of the system of internal control. Rather than serving a monitoring role for the benefit of external stakeholders, Abdel-Khalik concludes that external auditors of private firms assist owner-managers to control their organisations.

In a related argument, Simunic (1984) suggests that auditors' in-depth industry or client-specific knowledge can "spill over" to business advice, creating further potential to enhance SME performance. It is argued that "knowledge may flow from auditing to MAS (management advisory services), or MAS to auditing, or in both directions". The auditing standards require auditors to gain an understanding of the client's business and industry in the process of assessing audit risk (IFAC, ISA 315, 2009b; Knechel, 2007; AUASB, ASA 315, 2006b; Eilifsen *et al.*, 2001). Therefore, the present study argues that

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auditors have the potential to draw on their broader industry or client-specific knowledge to identify unique opportunities to support their SME clients' business needs.

Industry- and client-specific knowledge gained during the audit process is also likely to give the auditor a greater depth of understanding of their client's business needs than is available to an external accountant providing routine taxation or accounting services. While the business advice of an external accountant is predicted to enhance SME performance (*H1*), the benefit to SME performance will be greater if the advice is sourced from an external accountant who also provides auditing services because of the auditor's greater depth of understanding of their client's business. A positive relationship between the voluntary purchasing of business advice and performance for firms that also engage the services of an auditor is therefore predicted. This argument is summarised in the following hypothesis:

H2. SME performance is positively associated with the joint provision by an external accountant of business advice and auditing.

3. Methodology

3.1 Questionnaire

Data analysed in the present study were collected using a questionnaire survey of SME characteristics. The national survey of SMEs, titled "Value of Services Purchased from an External Accountant", was funded by CPA Australia. The mailed survey package included a covering letter explaining the purpose of the research, a copy of the questionnaire and a postage-paid envelope for returning the survey. A reminder letter was posted three weeks after the initial mail-out.

The questionnaire comprised five sections:

(1) Services of an External Accountant;

(2) Business Performance;

(3) Background of Business;

(4) Business Loans; and

(4) Ownership and Management.

Given the potential for poor responses to lengthy and complex surveys, the questionnaire was refined after pre-testing with relevant stakeholders (i.e. public practitioners, SME owner-managers and academics) to a four-page document to ensure that it achieved a sufficiently high response rate while attaining desired data collection outcomes.

3.2 Sample

Data were compiled from a survey of 2,200 SMEs randomly selected from the Dun and Bradstreet list of Australian businesses[4]. Dun and Bradstreet were instructed to draw a random sample reflecting the population characteristics around the number of employees in the range 5-200 and industry category (micro-businesses employing < 5 employees are excluded from the present study)[5].

In total, 485 businesses responded to the mail survey, representing a response rate of 22 per cent. Of the initial respondents, 16 were excluded because they indicated that they employed more than 200 staff (Dun and Bradstreet had originally classified these 16

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companies as employing < 200 employees, but perhaps they had grown in size). A further 89 observations were deleted because of missing data for one or more of the variables used in Model 1, leaving a usable sample of 380 observations (17.3 per cent usable responses).

Possible response bias was tested by examining differences between the sample mean and early and late responses across key demographic variables (and the variable of interest), where late responses are used to proxy non-respondents (see, for example, Wallace and Mellor, 1988). Questionnaire responses received from the first 50 surveys returned (early) and the final 50 surveys returned (late) were investigated. No significant differences were found when comparing early responses and the sample mean for the number of full-time employees ($p = 0.942$), the log of full-time employees (*SIZE_EMP*) ($p = 0.476$), the age of the business ($p = 0.104$), the log of the age of the business (*AGE*) ($p = 0.262$), whether the business is downsizing (*DOWNSIZE*) ($p = 0.352$) or if the business is in a growth phase (*BUSPhase*) ($p = 0.219$). Similarly, there were no significant differences between the late responses and the sample mean for the number of full-time employees ($p = 0.696$), the log of full-time employees (*SIZE_EMP*) ($p = 0.962$), the age of the business ($p = 0.322$), the log of the age of the business (*AGE*) ($p = 0.675$), whether the business is downsizing (*DOWNSIZE*) ($p = 0.249$) or if the business is in a growth phase (*BUSPhase*) ($p = 0.430$). There was, however, a significant difference between early responses (84 per cent) and the sample mean (69 per cent) for the variable of interest *BusAdvice* (voluntary purchase of business advice from the external accountant) ($p = 0.030$), but no difference with the sample mean when comparing late respondents ($p = 0.400$). Early respondents were more likely to purchase business advice which might simply reflect their heightened interest in the services provided by their accountants. Late responses proxy non-respondents, and non-significant differences with the sample mean and key demographic variables (and variable of interest) suggest that answers to questions were not systematically linked to the willingness to respond, and the results therefore support the absence of significant non-response bias.

3.3 The model

This study develops the following regression analysis:

$$Perform\_1 = f(\alpha + \beta_1\, BusAdvice\ (BusAdv\&Audit,\ BusAdv\_NoAudit) + \beta_2\, SIZE\_Emp + \beta_3\, AGE + \beta_4\, DOWNSIZE + \beta_5\, BUSPhase + \varepsilon)$$

(Model 1)

DEPENDENT VARIABLE

Perform_1 aggregate measure of SME self-rating of performance relative to their competitors' performance scaled by importance for seven dimensions of performance.

VARIABLES OF INTEREST

H1a and *H1b*

BusAdvice Binary variable, where 1 = the voluntary purchase of business advice from an external accountant.

H2

BusAdv&Audit Binary variable, where 1 = simultaneous purchase of business advice and external audit from an external accountant.

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BusAdv_NoAudit Binary variable, where 1 = the voluntary purchase of business advice from an external accountant without also purchasing auditing.

CONTROL VARIABLES

SIZE_Emp Natural log of the number of full-time employees.

AGE Natural log of the number of years the business has been registered.

DOWNSIZE Binary variable, where 1 = decrease in the total number of full-time employees during the past 12 months.

BUSPhase Binary variable, where 1 = growth phase during the past year.

Dependent variable (Perform_1)

This study adopts a self-rating measure of SME performance commonly used in survey methodology, which captures performance relative to competitors across a range of financial and non-financial success factors (Dunk, 2011; Grafton *et al.*, 2010; Pizzini, 2006; Baines and Langfield-Smith, 2003; Chenhall and Langfield-Smith, 1998; Govindarajan and Fisher, 1990; Govindarajan, 1988, 1984).

The dependent variable *Perform_1* is adapted from the two-part measure developed by Govindarajan (1984). The measure aggregates seven performance dimensions, each of which captures a unique element of SME performance (i.e. Profit, Cash Flow, Cost Control, Revenue Growth, Market Share, New Product/Service Development and Market Development)[6].

For each of the seven performance dimensions, part one of the measure requires respondents to rate their own performance relative to their competitors' performance over the past year, measured on a seven-point Likert-type scale that ranges from "Significantly lower" to "Significantly higher"[7] Against each of the seven performance dimensions, part two of the measure requires respondents to rate the importance of the dimensions on a seven-point Likert-type scale, ranging from "Not important" to "Extremely important". *Perform_1* is calculated by adding the seven performance dimensions, scaled by the respondent's assessment of the relative importance of each dimension. Scaling (weighting) is undertaken to control for variability between respondents in the perceived importance of each dimension. The importance score is scaled such that the combined total importance for each respondent adds up to one, so that the aggregate score for *Perform_1* adds up to a maximum of 7. The measure of SME performance, therefore, emphasises those components of business performance to which SME management attaches greatest importance. In measuring performance relative to competitors, and scaling (weighting) by the importance of each component, the measure controls for the perceived impact of industry and other external factors on performance because industry and other external factors are necessarily considered by respondents when rating relative performance.

Variables of interest

The voluntary purchasing by an SME of business advice from an external accountant is measured using the binary variable *BusAdvice* (*H1a* and *H1b*). The present study adopts a parsimonious characterisation of business advice, defined as advice relating to corporate finance, financial planning and advice focussed on planning, systems and control. This categorisation was developed following feedback from questionnaire pre-testing[8].

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To test *H2*, the variable *BusAdvice* is then split into its two unique components to capture the unique influence of auditing and business advice on SME performance. *BusAdv&Audit* is a binary variable measuring the joint purchases of auditing and business advice. *BusAdv_NoAudit*, is a binary variable measuring the purchases of business advice without also purchasing an audit.

Prior research has typically combined traditional compliance (accounting, taxation) with business advisory services (Robson and Bennett, 2000; Bennett and Robson, 1999), despite only the latter being likely to directly impact firm performance. This study therefore more directly measures the influence of business advice on SME performance using a binary measure of business advice. However, in additional analyses (Section 4.4.1), the variable *BusAdvice* is replaced with a number of alternative measures of business advice.

Control variables

Prior studies using self-rating performance measures do not adopt control variables because, it is argued, implicit in the measure of respondents' assessment of performance relative to that of competitors is control for the impact of industry and external factors on performance (Grafton *et al.*, 2010; Pizzini, 2006; Baines and Langfield-Smith, 2003; Chenhall and Langfield-Smith, 1998; Govindarajan and Fisher, 1990; Govindarajan, 1988, 1984). Notwithstanding this argument, the present study incorporates three additional control variables predicted to impact SME performance. First, firm size was found to predict SME revenue and profit growth by Robson and Bennett (2000). The present study accordingly controls for firm size using the natural log of the number of employees (*SIZE_Emp*). Second, Robson and Bennett (2000) find that firm age is negatively associated with SME revenue growth, which they attribute to younger organisations being less risk averse and more focussed on a high-growth strategy. This study controls for SME age using the natural log of the number of years since the business was first registered (*AGE*). Third, research modelling absolute performance (i.e. profitability) identifies past performance as a critical predictor of current performance (Ittner *et al.*, 2002). Replicating the control measure used by Ittner *et al.* (2002), this study uses the extent of downsizing employee numbers (DOWNSIZE) to proxy past performance. Finally, the performance of an SME is likely to vary depending on the firm's strategic goals. Robson and Bennett (2000) refer to suggestions in the economics and management literature (Gibb and Scott, 1985; Williamson 1964) that management objectives are an important determinant of firm growth in the SME environment. The relevance of the business phase for SME performance was highlighted by practitioners during pre-testing (i.e. an SME might trade more profitably during a growth phase). The binary variable *BUSPhase* controls for business phase and is calculated as the respondent's assessment as to whether their business was in a growth phase during the previous year (Y/N).

4. Results

4.1 Descriptive results

Table I provides descriptive statistics for the variables in Model 1 for the usable sample of 380 SMEs. The composite measure of performance *Perform_1* ranges from 1.46 to 7, with a mean score of 4.66[9]. Most SMEs (69 per cent) indicated they had bought business advice from their external accountant in the previous financial year[10]. In total, 32 per cent of SMEs had purchased both business advice and audit services

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Variables	Mean	Median	SD	Minimum	Maximum
Dependent variables					
Perform_1 (Composite performance measure)	4.66	4.71	0.87	1.46	7
Variables of interest					
BusAdvice (1 = purchase business advice from external accountant) (n = 261)	0.69	NA	NA	0	1
BusAdv&Audit (1 = simultaneous purchase of business advice and external audit) (n = 122)	0.32	NA	NA	0	1
BusAdv_NoAudit (1 = purchase external audit but not business advice) (n = 139)	0.37	NA	NA	0	1
Control variables					
Small Firms (5-49 employees) (n = 255)	0.67	NA	NA	0	1
SIZE_Emp (Natural log of number of full-time employees)	3.25	3.22	1.04	1.61	5.30
Number of full-time employees	42.68	25.00	42.68	5	200
AGE (Natural log of age of business)	2.64	2.77	0.88	0	4.98
Age of business	19.75	16.00	18.02	0	146
DOWNSIZE (1 = decrease number of employees over past year)	0.21	0	NA	0	1
BUSPhase (1 = growth phase)	0.52	1.0	NA	0	1

Table I.
Descriptive statistics (n = 380)

simultaneously (*BusAdv&Audit*), and 37 per cent had purchased business advice without also purchasing an audit (*BusAdv_NoAudit*).

In total, 67 per cent (n = 255) were small firms employing between 5 and 49 employees, and 33 per cent (n = 125) were medium-sized firms employing from 50 to 200 employees. Untabulated results indicated that 68 per cent of small firms and 70 per cent of medium-sized firms had bought business advice from their external accountant in the previous financial year, with non-significant differences in the propensity to buy business advice between the two groups ($\chi^2 = 0.73$, $p = 0.788$). The mean number of full-time employees is 42.68. The average age of respondent SMEs was 19.75 years (median 16 years). Further, 21 per cent of businesses had reduced (*DOWNSIZE*) their number of employees during the previous year; 52 per cent indicated that their business was in a growth phase (*BUSPhase*).

Correlations between the variables in Model 1 are presented in Table II. The strongest correlation, with a Pearson's r of −0.342 between *BUSPhase* and *DOWNSIZE*

Variables	1	2	3	4	5
1. *Perform_1*	1				
2. *SIZE_Emp*	0.126*	1			
3. *AGE*	−0.051	0.260***	1		
4. *DOWNSIZE*	−0.178***	−0.103*	0.016	1	
5. *BUSPhase*	0.211***	0.008	−0.315***	−0.342***	1

Notes: *$p < 0.05$; **$p < 0.01$; ***$p < 0.0005$

Table II.
Correlation matrix (n = 380)

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suggests, not surprisingly, that firms in the process of downsizing are not in a growth phase. The relatively low correlations between control variables suggest that multi-collinearity is not a concern. This conclusion was corroborated with two collinearity diagnostic tests. Neither the tolerance nor variance inflation factor (VIF) statistics indicated that there was a collinearity concern (i.e. both the tolerance and VIF statistics are near 1.00, which indicates no close association with the other independent variables).

4.2 Descriptive results – business advice and SME performance

Table III provides descriptive statistics comparing the performance of firms that buy business advice ($n = 261$) with the performance of firms that do not buy business advice ($n = 119$). Firms buying business advice perceive their performance as superior to that of firms that choose not to buy business advice, although the difference is marginal ($p = 066$)[11]. Group comparisons reveal non-significant differences across the characteristics of the size of business (*Size_Emp*), business age (*AGE*), whether the businesses had reduced the number of employees during the previous year (*DOWNSIZE*) and whether the business is in a growth phase (*BUSPhase*).

The final two panels in Table III show descriptive statistics comparing the performance of small- ($n = 255$) and medium-sized ($n = 125$) firms that buy business advice, and the performance of small- and medium-sized firms that do not buy business advice. Only small firms buying business advice ($n = 174$) perceive their

Variables	Business advice Yes Mean (SD)	Business advice No Mean (SD)	*t* (*p*-value)
All small- and medium-sized firms (n = 380)	*n = 261*	*n = 119*	
Perform_1 (sum of the seven performance ratings scaled by relative importance of each dimension)	4.72 (0.83)	4.54 (0.95)	−1.85 (0.066)
Control variables			
SIZE_Emp (natural log of number of full-time employees)	3.27	3.19	−0.736 (0.462)
Number of full-time employees	43.83	39.51	−0.914 (0.361)
AGE (natural log of age of business)	2.65	2.62	−0.212 (0.832)
Age of business	20.61	19.18	−0.418 (0.676)
DOWNSIZE (1 = decrease number of employees over past year)	0.20	0.21	0.157 (0.876)
BUSPhase (1 = yes growth phase)	0.48	0.59	1.912 (0.057)
Small-sized firms (n = 255)	*n = 174*	*n = 81*	
Perform_1	4.66 (0.84)	4.38 (1.0)	−2.34 (0.020)*
Medium-sized firms (n = 125)	*n = 87*	*n = 38*	
Perform_1	4.83 (0.80)	4.87 (0.77)	0.299 (0.766)

Table III.
Descriptive statistics

Notes: SMEs buying business advice compared with SMEs not buying business advice; $*p < 0.05$; $**p < 0.01$; $***p < 0.0005$

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performance as superior to that of small firms that do not buy business advice (n = 81) (p = *0.02*).

Table IV compares the performance of firms that simultaneously buy business advice and financial statement auditing (Column 1) with the performance of firms that do not buy business advice (Column 2). Firms simultaneously buying business advice and auditing services perceive their performance to be superior to that of firms that do not buy business advice (p = *0.008*)[12]. The superior performance of firms simultaneously buying business advice and auditing services is observed within the small firm subsample (p = *0.013*) but not in the medium-sized firm subsample (p = *0.684*). Columns 3 and 4 in Table IV compare the performance of firms that buy business advice alone (i.e. without also buying auditing services) (n = 139) with the performance of firms that do not buy business advice (n = 119). Firms buying business advice (without also buying auditing) perceive no difference in their performance when compared with firms that do not buy business advice (p = 0.550). Within the small firm subsample, the performance of firms buying business advice alone is marginally greater (p = 0.115), and there is no performance difference in the medium-sized firm subsample (p = 0.271).

4.3 Hypothesis testing: regression results for SME performance

Table V presents ordinary least squares (OLS) regression results for Model (1), testing the hypothesised relations between SME performance and the voluntary purchase of business advice (*H1a*), and the hypothesised relations between SME performance and the simultaneous purchase of business advice and auditing (*H2*). Both models are significant predictors of SME performance.

Consistent with the prediction in *H1*, SME performance is positively associated with the voluntary purchase of business advice (*BusAdvice*) (p = 0.032)[13]. To test H2, the variable of interest *BusAdvice* is divided into two components: SME purchasing both auditing and business advice (*BusAdv&Audit)* and SME purchasing business advice without also purchasing auditing (*BusAdv_NoAudit).* Results presented in the final column of Table V demonstrate that SME performance is positively associated with the joint provision of business advice and auditing. The variable *BusAdv&Audit* is positively associated with performance (p = 0.009), but the variable *BusAdv_NoAudit* is not associated with performance (p = 0.236). This result provides support for *H2* that SME performance is positively associated with the joint provision of business advice and auditing. The variable *BusAdv_NoAudit* is not significant, indicating no performance gain for firms that buy business advice alone. The joint provision of business advice and auditing, with the associated "knowledge spillover", appears to produce the benefit of enhancing SME performance.

Table VI presents OLS regression results for Model (1), testing whether the hypothesised relationship between SME performance and the voluntary purchase of business advice is greater for small firms than for medium-sized firms (*H1b*). Results presented in Column 1 for the subset of small firms (n = 255) demonstrate that SME performance is positively associated with the voluntary purchase of business advice from an external accountant (*BusAdvice*) (p = 0.005). Results presented in Column 2 reveal for the subset of small firms that the simultaneous purchase of auditing and business advice *BusAdvice&Audit* (p = 0.005) and the purchase of business advice without also purchasing auditing *BusAdv_NoAudit* (p = 0.027) are positively

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Table IV.
Descriptive statistics

	Business advice and audit Yes Mean (SD) $n = 122$ (1)	Business advice No Mean (SD) $n = 119$ (2)	t (p-value)	Bus advice No audit Mean (SD) $n = 139$ (3)	Bus advice No Mean (SD) $n = 119$ (4)	t (p-value)
All Firms (n = 380)						
Perform_1	4.84 (0.89)	4.54 (0.95)	−2.699 (0.008)**	4.61 (0.84)	4.54 (0.95)	−0.598 (0.550)
Control variables						
SIZE_Emp	3.53	3.19	−2.538 (0.012)*	3.05	3.19	1.098 (0.273)
Number of full-time employees	54.44	39.51	−2.598 (0.010)**	34.51	39.51	1.064 (0.288)
AGE	2.68	2.62	−0.481 (0.631)	2.61	2.62	0.098 (0.922)
Age of business	21.34	19.18	−0.926 (0.355)	18.84	19.18	0.162 (0.871)
DOWNSIZE	0.16	0.21	0.917 (0.360)	0.24	0.21	−0.522 (0.602)
BUSPhase	0.52	0.59	1.120 (0.264)	0.45	0.59	2.174 (0.031)*
Small Sized Firms (n = 255)	**n = 68**	**n = 81**		**n = 106**	**n = 81**	
Perform_1	4.77 (0.86)	4.38 (1.0)	−2.52 (0.013)*	4.59 (0.82)	4.38 (1.0)	−1.58 (0.115)
Medium-Sized Firms (n = 125)	**n = 54**	**n = 38**		**n = 33**	**n = 38**	
Perform_1	4.94 (0.70)	4.87 (0.77)	−0.409 (0.684)	4.65 (0.94)	4.87 (0.77)	1.11 (0.271)

Notes: SMEs simultaneous buying business advice and auditing (*BusAdv&Audit)/SMEs* Buying business advice and no audit *(BusAdv_NoAudit)* compared with SMEs not buying business advice; $*p < 0.05$; $**p < 0.01$; $p < 0.0005$

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Variables	Expected sign	β SE (*t*-value) *H1a*	β SE (*t*-value) *H2*
SIZE_Emp	+	0.098	0.086
		0.043	0.044
		(2.256)*	(1.947)
AGE	?	−0.025	−0.025
		0.053	0.053
		(0.470)	(0.442)
DOWNSIZE	_	−0.266	−0.218
		0.115	0.115
		(1.967)*	(1.904)
BUSPhase	+	0.307	0.303
		0.098	0.098
		(3.136)*	(3.094)**
BusAdvice	+	0.201	
		0.094	
		(2.148)*	
BusAdv&Audit	+		0.288
			0.109
			(2.637)**
BusAdv_NoAudit	+		0.125
			0.106
			(1.187)
Constant		4.160	4.199
		0.211	0.212
		(19.698)***	(19.777)***
F-statistic		6.692***	5.990***
Adjusted R^2		0.070	0.073
$n = 380$			

Notes: $*p < 0.05$; $**p < 0.01$; $***p < 0.0005$; *Perform_1* = self-rating of performance relative to competitors scaled by importance; *BusAdvice 1* = purchase business advice from external accountant; *BusAdv&Audit* 1 = simultaneous purchase of business advice and external audit; *BusAdv_NoAudit* 1 = purchase business advice from external accountant without also purchasing auditing; SIZE_Emp = Natural log of the number of full-time employees; AGE = natural log of the number of years the business has been registered; DOWNSIZE 1 = decrease in the total number of full-time employees during the past 12 months; BUSPhase 1 = respondent's assessment as to whether their business was in a growth phase during the previous year

Table V. Ordinary least squares regression examining the association between SMEs buying business advice and firm performance (*Perform_1*)

associated with SME firm performance. In contrast, results for the subset of medium-sized firms ($n = 125$) presented in Columns 3 and 4 reveal that *BusAdvice&Audit* ($p = 0.688$) or *BusAdvice&Audit* ($p = 0.809$) and *BusAdv_NoAudit* ($p = 0.239$) are not associated with firm performance. These results provide support for *H1b* that the performance benefit is greater for small firms than for medium-sized firms. This analysis suggests the business advice of an external accountant enhances small firm performance irrespective of whether it is purchased in addition to audit services. In contrast to the aggregated result presented in Table V, the joint provision of audit and business advice services is not necessary for a small firm to derive a performance benefit from the business advice of an external accountant[14].

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Variables	Expected sign	Small-sized firms (<50 Employees) (n = 255) β SE (t-value) (1)	β SE (t-value) (2)	Medium-sized firms (50-200 Employees) (n = 125) β SE (t-value) (3)	β SE (t-value) (4)
SIZE_Emp	+	−0.033	−0.038	0.051	0.029
		0.081	0.081	0.183	0.183
		(0.414)	(0.467)	(0.277)	(0.156)
AGE	?	0.008	0.007	−0.077	−0.076
		0.068	0.068	0.085	0.084
		(0.112)	(0.099)	(0.916)	(0.902)
DOWNSIZE	−	−0.211	−0.210	−0.353	−0.319
		0.141	0.141	0.196	0.197
		(1.504)	(1.490)	(1.799)	(1.624)
BUSPhase	+	0.435	0.426	0.074	0.093
		0.123	0.123	0.161	0.161
		(3.553)***	(3.459)**	(0.456)	(0.580)
BusAdvice	+	0.330		−0.062	
		0.116		0.155	
		(2.837)**		(0.403)	
BusAdv&Audit			0.400		0.041
			0.142		0.169
			(2.816)**		(0.243)
BusAdv_NoAudit			0.284		−0.221
			0.128		0.187
			(2.220)*		(1.184)
Constant		4.233	4.253	4.913	4.988
		0.283	0.284	0.829	0.826
		(14.974)***	(14.987)***	(5.925)***	(6.036)***
F-statistic		5.622***	4.802***	1.288	1.462
Adjusted R^2					
n = 380		0.083	0.082	0.022	0.022

Table VI.
Ordinary least squares regression examining the association between SMEs buying business advice and firm performance (*Perform_1*)

Notes: *$p < 0.05$; **$p < 0.01$; ***$p < 0.000$; *Perform_1* = self-rating of performance relative to competitors scaled by importance; *BusAdvice 1* = purchase business advice from external accountant; *BusAdv&Audit* 1 = simultaneous purchase of business advice and external audit; *BusAdv_NoAudit* 1 = purchase business advice from external accountant without also purchasing auditing; SIZE_Emp = natural log of the number of full-time employees; AGE = natural log of the number of years the business has been registered; DOWNSIZE 1 = decrease in the total number of full-time employees during the past 12 months; BUSPhase 1 = respondent's assessment as to whether their business was in a growth phase during the previous year

The analyses reported in Tables V and VI control for a number of SME characteristics predicted to be associated with SME performance. Results indicate that, as expected, SMEs in the process of downsizing (*DOWNSIZE*) exhibited poor performance, and SMEs in a growth phase (*BUSPhase*) exhibited stronger performance. While firm size (*SIZE_Emp*) is positively associated with performance in the full data set (Table V), size is not influential within the small- or medium-sized

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firm subsets (Table VI). Medium-sized firms appear to be better performers than small firms, highlighting the need for smaller firms to seek external support.

4.4 Additional analyses

4.4.1 Alternative measures of business advice. This study develops three alternative measures of the variable of interest *BusAdvice* which is used to test *H1a* and *H1b*. First, replicating the measure developed in Gooderham *et al.* (2004), *Bus_Advisor* measures on a seven-point scale "the degree to which the firm relies on their external accountant as a business advisor" (mean = 3.34). Second, the continuous variable *BUSAdv_Spend* measures the natural log of the fee paid to an external accountant for business advice. Third, because it may take time before the advice of an external accountant is implemented and has a measurable impact on SME performance, a time-lagged variable is developed. The binary variable *Lag2_BUSAdv* is calculated based on whether the SME purchased business advice between one and two years prior to the time of the performance measure. In total, 62 per cent of respondents indicated they had purchased business advice between one and two years prior to the current year's performance (*Lag2_BUSAdv*).

In untabulated results, Model (1) is re-estimated substituting the variable of interest *BusAdvice* with the three alternative measures of business advice. All three measures are significantly associated with performance. The degree to which the firm relies on the external accountant as a business advisor (*Bus_Advisor*) is associated with performance ($B = 0.041$, $SE = 0.023$, $t = 1.751$, $p = 0.084$), the fee paid to the external accountant for business advice (*BUSAdv_Spend*) is associated with performance ($B = 0.022$, $SE = 0.011$, $t = 2.058$, $p = 0.04$) and the lagged variable measuring when the SME purchased business advice between one and two years prior to the time of the performance measure (*Lag2_BUSAdv*) is also associated with performance ($B = 0.193$, $SE = 0.090$, $t = 2.130$, $p = 0.017$)[15]. As in the main analysis, for the subset of small firms ($n = 255$), SME performance is positively associated with *Bus_Advisor* ($p = 0.017$) *BUSAdv_Spend* ($p = 0.011$) and *Lag2_BUSAdv* ($p = 0.015$). However, for the subset of medium-sized firms ($n = 125$), *Bus_Advisor* ($p = 0.463$), *BUSAdv_Spend* ($p = 0.954$) or *Lag2_BUSAdv* ($p = 0.824$) are not associated with SME performance. These findings provide further support for the influence of the business advice of an external accountant on performance among small firms.

4.4.2 SMPs and performance. In recent years, literature has emerged investigating the role of SMPs in the provision of business support to SMEs (Blackburn and Jarvis, 2010; Doving and Gooderham, 2008). A number of authors conjecture that accounting firms, particularly small- and medium-sized accounting firms (SMPs), do not have the capacity to provide SME clients with services other than traditional compliance and monitoring work (Blackburn and Jarvis, 2010; Burke and Jarratt, 2004; Deakins *et al.*, 2001). Additional analysis is undertaken to investigate whether the size of the accounting practice impacts on the extent to which an SME purchases business advice and the ensuing implications for SME performance.

The questionnaire requested respondents to classify their external accountant into one of three groups: small local firm/sole practitioner ($n = 134$), medium to large firm ($n = 205$) and Big 4 international firm ($n = 40$)[16]. The proportion of SMEs buying advice from each group is 69, 70 and 60 per cent, respectively, with no significant differences between the groups ($\chi^2 = 1.54$, df = 2, $p = 0.463$). Similarly, group comparison reveals no significant difference in the performance of SMEs in the three

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groups ($F = 1.831$, $p = 0.162$). Thus, the size of the accounting firm does not appear to influence a SME's decision to buy business advice from their external accountant and there is no ensuing impact on SME performance.

5. Conclusion

This study investigates whether SMEs derive a benefit in the form of enhanced performance following the purchase of business advice from their external accountant. Empirical results confirm that firms buying business advice exhibit superior performance. SME performance is perceived to be further enhanced when business advice and auditing are jointly purchased, which suggests that auditors' depth of knowledge is beneficial to SME management. These benefits are confined to the small businesses subgroup (5 to 49 employees), consistent with smaller firms having a narrower resource base and thus, having a greater need to source business advice from an external accountant. Findings are robust across alternative methods of measuring when an SME buys business advice, and are not influenced by the external accountants' firm size.

These findings have implications for the international accounting profession. In response to strategic concerns about the reliability of future revenue from traditional compliance and monitoring services, the profession has long supported and encouraged a broadening of the service base (Carnegie and Napier, 2009; Fogarty *et al.*, 2006; Greenwood *et al.*, 2002; Parker, 2001). In particular, the accounting profession characterises external accountants as being not only experts in compliance and monitoring services but also capable of adding value to clients with their business expertise. The profession's strategy has been applied in practice in the absence of empirical support. The finding that small firms perceive a performance benefit from the purchase of business advice gives further incentive and support to the profession to continue promoting the expertise of external accountants as business advisors, particularly to small businesses. In addition, evidence presented in this study helps quantify a potential cost of regulation restricting the joint provision of auditing/NAS to support auditor independence.

The results of this study should be considered in the light of the following limitations. First, because legislation in some jurisdictions prevents auditors from also providing business advisory services (e.g. USA under SOX), the findings in the present study cannot be generalised to countries where the joint provision of audit and business advisory services is banned. Second, while results indicate that SMEs buying business advice perceive that their businesses outperform competitors, there is no evidence as to the impact on actual firm performance. Future research exploring the influence of business advice on actual performance is warranted. Third, a potential limitation in the research design is that a component of the composite measure of performance Perform_1 (Sales volume/Revenue growth) is correlated with one of the control variable BUSPhase (Binary variable, where 1 = growth phase during past year). Future research might measure actual performance to overcome this potential limitation. Fourth, while these findings confirm a link between external accountants' business advice and SME performance, it is not possible to conclude with certainty the causality of the business advice-performance relationship. While this study argues for a theoretical link between business advice and performance, it is not clear whether it is business advice leading to better performance or better performance leading to the purchase of business advice.

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Indeed, the relationship might be more complex, with a "virtuous spiral" of advice and performance (Berry *et al.*, 2006). Future research might explore the relationship between business advice and SME performance using a longitudinal study to provide further insight into causality and whether the hypothesised association varies across international jurisdictions.

Notes

1. Alternative definitions of SMEs are used by the European Commission, which classifies small business as having 10-49 employees and medium-sized business as having 50-250 employees (European Commission, 2003); the US Government "Small Business Administration", which classifies small businesses as those employing fewer than 500 people (www.sba.gov); and developing countries, which, on average, classify small businesses as having 5-19 employees and medium-sized businesses as having 20-99 employees (Katto, 2008). Dunn and Bradstreet highlight in an article published on their website (6/01/2014) that there is currently no standardised definition of SMEs. D&B identify employee count as a frequently used indicator and acknowledge the ABS definition (Small business < 20 employees; medium-sized business < 200). See (http://dnbsmallbusiness.com.au/News/SMEs_call_for_universal_definition_of_small_business/indexdl_8518.aspx).
2. The international ethical standards allow the joint provision of auditing and NAS subject to any threats to independence being reduced to an acceptable level (IFAC, 2014).
3. The Australian Corporations Act 2001, S310(1), required large private companies to engage the services of an external auditor to audit their annual financial statements, exempting small companies unless directors specifically request an audit [S.301(2)]. (i.e., a large private company is defined as one that satisfies at least two of the following three criteria: operating revenue $10 million or more; gross assets $5 million or more; and 50 or more employees [Division 5A S45A(3)]). However, large private companies can apply to ASIC for audit relief (i.e., permission to forego an audit) under Policy Statement 115 – Audit Relief for Proprietary Companies (Commonwealth of Australia, 2001), making auditing voluntary for many medium-sized companies.
4. The questionnaire was administered in September 2004.
5. The Dun and Bradstreet database is the largest publicly-available subset of the population of Australian businesses employing staff ("employing businesses") from which a mailing list can be derived.
6. The seven dimensions of performance aggregated to create *Perform_1* are: Perform_Profit = SME self-rating of business performance relative to competitors on the dimension "profit" (measured on a seven-point scale), Perform_CashFlow = SME self-rating of business performance relative to competitors on the dimension "Cash flow from operations" (measured on a seven-point scale), Perform_CostControl = SME self-rating of business performance relative to competitors on the dimension "Cost control" (measured on a seven-point scale), Perform_RevGrow = SME self-rating of business performance relative to competitors on the dimension "Sales volume/Revenue growth" (measured on a seven-point scale), Perform_MktShare = SME self-rating of business performance relative to competitors on the dimension "Market share" (measured on a seven-point scale), Perform_NewProd = SME self-rating of business performance relative to competitors on the dimension "New service/product development" (measured on a seven-point scale), Perform_MktDev = SME

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self-rating of business performance relative to competitors on the dimension "Market development" (measured on a seven-point scale).

7. Respondents were also given the option to answer "0" = "Don't know". Where a respondent answered "Don't know", this response required adjustment to avoid distortion in the aggregate performance measure (Perform_1). The approach used is a mean replacement based on the respondent's other item scores (i.e., as previously indicated, there are seven performance measures. Where a respondent answered six of the seven questions, the mean score from those six questions is used as the score for the missing seventh value). In a sensitivity analysis, where the response was missing on any item, the respondent is deleted from the analysis, resulting in a reduced sample of 333. Regression results are substantially unaltered using the smaller data set.
8. Pretesting using an extensive list of advisory services was undertaken with six SME owner-managers and three CPAs, all of whom were members of the Victorian Small and Medium-Sized Entities Committee of CPA Australia. Participants favoured the parsimonious measure used in the present study. Items deleted included "Profit/Cash flow control", "Other assurance and related activities (e.g., OH&S, Fraud reviews etc)". The measure of individual advisory services was simplified to a Yes/No response.
9. *Perform_1* aggregates seven performance dimensions. The mean performance rating for each of the seven dimensions is 4.55 for *Perform_Profit*, 4.60 for *Perform_CashFlow*, 4.54 for *Perform_CostControl*, 4.85 for *Perform_RevGrow*, 4.54 for *Perform_MktShare*, 4.63 for *Perform_NewProd* and 4.65 for *Perform_MktDev*.
10. SMEs also indicated that they bought accounting (80 per cent), taxation (83 per cent) and audit (54 per cent) services.
11. Group comparison of the seven dimensions of performance upon which Perform_1 is based, reveals significant differences for one of the seven dimensions. SMEs that buy business advice perceive superior performance to that of firms that do not buy business advice on the dimension "profit" (*Perform_Profit*; $p = 0.028$).
12. Group comparison of the seven dimensions of performance upon which Perform_1 is based, reveals differences for five of the seven dimensions. SMEs that simultaneously buy business advice and auditing perceive superior performance to that of firms that do not buy business advice on the dimension "profit" (*Perform_Profit*; $p = 0.01$), "cash flow" (*Perform_CashFlow*; $p = 0.066$); "cost control" (*Perform_CostControl*; $p = .074$), "revenue growth" (*Perform_RevGrow*; $p = 0.022$) and "market development" (*Perform_MktDev*; $p = 0.096$).
13. In sensitivity analysis, I undertake seven regressions, substituting for Perform_1 the seven dimensions of performance upon which Perform_1 is based. The variable of interest *BusAdvice* is significant in two of the seven regression analyses. *BusAdvice* is associated with performance relative to competitors when the dependent variable is measured as profit (Perform_Profit) ($\beta = 0.312$, SE = 0.136, $t = 2.291$, $p = 0.024$) and sales volume/ revenue growth (Perform_RevGrow) ($\beta = 0.264$, SE = 0.138, $t = 1.916$, $p = 0.056$).
14. In untabulated results, Model 1 is re-estimated with the inclusion of an additional binary variable which measures circumstances where an SME purchased an audit, but did not also buy business advice (n = 61). The additional audit variable is a non-significant predictor of

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SME performance, suggesting that auditors who do not also sell business advice do not appear to provide advice supporting the performance of their SME clients.

15. The sample size is reduced to 372 for Lag2_BUSAdv because of 8 missing values.

16. 134 + 205 + 40 = 379. There were missing data on accounting firm size for 1 observation.

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About the author

Peter John Carey is a Professor of Accounting at Deakin University, Melbourne, Australia. Peter's research and teaching interests are mainly in the areas of audit and assurance services, SMEs, corporate governance and financial reporting. Peter is a Chartered Accountant and Registered Company Auditor with work experience in both professional practice and industry. Peter John Carey can be contacted at: pcarey@deakin.edu.au

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