Proactivity, Economic Performance, and Internationalization of Local and Regional Public Accounting Firms in Western New York

by

Linda J. Kuechler
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Advisor: Sharmistha Bagchi-Sen, PhD

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UMI Number: 9719140

UMI
300 North Zeeb Road
Ann Arbor, MI 48103

ABSTRACT

This dissertation explores the characteristics that differentiate successful small and medium-sized (SMEs) producer service firms from less successful ones, specifically studying the local and regional public accounting firm in Western New York. It develops a proactivity index, composed of five elements, and analyzes the association between the proactivity index and economic performance.

In addition, the study investigates the relationship between four different stages of proactivity (passive, passive/reactive, reactive, and proactive) and other characteristics of SMEs. These other characteristics include whether the firm serves a niche market, utilizes collaborative relationships, and recognizes and utilizes locational advantages. Furthermore, by use of the Proactivity Index and the other characteristics mentioned above, the study differentiates between the firms that have internationalized their practices and those that have not.

In general, the proactivity index identifies consistent differences between groups, and indications are that economic performance and proactivity are associated. In addition, the use of niches in conjunction with collaborative relationships and the recognition of locational advantages are other characteristics of the successful firms. Furthermore, the majority of these 'local' and 'regional' public accounting firms are either internationalizing their practices or are interested in doing so. The firms that are successfully internationalized are larger, more proactive, make greater use of marketing and promotion strategies, and information technology than the firms that are not successfully internationalized.

Key Words: SMEs, Producer Service, Proactivity, Internationalization, Local and Regional Public Accounting Firms.

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Introduction and Purpose

1.1 Introduction and Motivation

The motivation for this study of the determinants of success and the internationalization of small and medium-sized public accounting firms in the Western New York (WNY) area stems from five sources. First, accounting is classified as an advanced producer service, and, in the majority of research on producer services, their economic impact is alluded to in the aggregate only (Coffey and Polese, 1989; Harrington, 1989; Daniels et al. 1993). The assumption of homogeneity of the producer service sector underlies this previous research, and this assumption not only applies to specific services but also to firms of different sizes in the same service category. However, Goddard (1978) and Marshall (1982, 1983) found that it is possible that the sector mix, sophistication, pricing, and specialization of locally-produced services could affect the competitiveness of local economic activity in general, especially for the local and regional companies that do not have organizational links to corporate services outside the region. Illeris and Phillipe (1993) note that variations do exist in different types of service activities and suggest that future research take such variations into account. The local and regional public accounting firm is unique in a number of characteristics, including the wide range of legal and professional regulations that govern both their employees and types of services. Because of these regulations, the public accounting firm is very different from other producer service firms, and this study will provide an empirical analysis of success determinants and internationalization status of the small and medium-sized firm in the public accounting sector.

Second, this research is intended to reveal what determines the survival and development of small and medium-sized firms in the producer service sector. Although past research has investigated the elements that enhance economic performance of small and medium-sized firms, it has done so mainly for manufacturing firms by examining one element at a time. For example, strategic planning and economic performance have been studied together (Khan and Rocha, 1982: Stoner, 1983; Lyles et al. 1993). A more comprehensive framework that includes the major elements enhancing economic performance or success of the firm is necessary. In the context of this study, the comprehensive framework includes a Proactivity Index, and a determination of whether the firm serves a niche market, collaborates with other firms, and recognizes locational advantages. The Proactivity Index includes the major elements of long-range planning, short-range planning, preparation of up-to-date financial statements, personnel policies, and marketing and promotion strategies.

Third, this study is also motivated by the role of the small and medium-sized producer service firm in generating export revenue, non-local and international. The small and medium-sized public accounting firm can directly generate non-local and international revenues through exporting their own services, and indirectly by assisting their clients internationalize their operations. Local and regional public accounting firms may have a larger role to play in the economic development of WNY than other small and medium-sized producer service firms because of the education and training of their professional staff. Trained in financial matters, the highly skilled employees of these firms can help attract venture capital for their own firms, and, through their management consulting activities, help other firms in the region obtain the needed expertise and financing for international expansion. Therefore, in the context of this research, the description of the process of internationalization has been modified to include the two major ways that public accounting firms generate non-local and international revenues. Internationalization, therefore, is defined in this study as either rendering management advisory services that will help domestic clients internationalize their operations, or by providing tax, auditing, or other services to foreign companies that have entered the U.S. environment. By including the revenues generated by helping other firms internationalize, a more accurate measure of the true impact on internationalization will be determined.

Fourth, these local and regional public accounting firms are locationally bound not simply by the geographical market they serve, but also by the governmental body that certifies them (Bodewyn et al. 1986). In the United States alone, 54 different sets of certification and licensing requirements limit the geographical expansion of these firms (Mednick, 1996). Added to this, different country-level certification and licensing requirements make this a service with unique characteristics and problems that differentiate it from other advanced producer services. Therefore, the different means of internationalization utilized by these firms will be investigated to determine if and how they are overcoming the barriers to internationalization.

The fifth and final motivation stems from understanding the interrelations of the above four in a declining manufacturing region with a medium-sized metropolitan area at its core. MacPherson (1988a, 1988b) and Britton (1989) provide examples of how a wide range of specialized and sophisticated producer services is necessary to continually support and upgrade the industrial sector. It is conceivable that the region could continually lose additional manufacturing companies if a field of local producer service vendors cannot support the industrial sector. Therefore, successful local and regional public accounting firms will not only stimulate the region by their own activities, but will also contribute by making it an attractive place for the industrial sector.

1.2 Research Questions and Hypotheses

Many studies have been conducted to identify the elements that influence the economic performance of a small and medium-sized firm (Bracker et al. 1988; Moriarity and Field, 1990; Berry and Parasuraman, 1991). Some of these elements can be quantified into a numerical index. Five elements that can be quantified and particularly stand out from these studies are long-term planning policies, short-term planning policies, personnel policies, financial statement preparation, and marketing and promotion policies. However, even though each of these elements has been individually tied to economic performance, the interaction in an overall framework has not been researched. Therefore, the first issue addressed by this research is to develop an overall framework of proactivity that includes the five elements of long-term planning, short-term-planning, personnel policies, financial statement preparation, and marketing and promotion policies. By combining these elements into a proactivity index, the following research question is addressed: are proactivity and economic performance of a local and regional public accounting firm related? Economic performance is measured in two ways: net income per owner and growth-orientation. In addition, the differences in proactivity between single-owner and multi-owner firms is analyzed. These different measures of economic performance are used to demonstrate that not all small and medium-sized firms are homogenous. The specific hypotheses that will be tested to help answer this question are:

H1: Successful local and regional public accounting firms are more proactive than less successful firms.
H2: As a firm becomes larger in terms of owners, more elements of proactivity will be present.
H3: Growth-oriented firms have higher levels of proactivity.

In addition, the association between proactivity and a number of other characteristics will be analyzed. These include whether or not the firm serves a niche or specific market (Daniels et al. 1988; Brock and Evans, 1989; Porter, 1990; Wood, 1991; Dodd et al. 1995), whether the firm collaborates or utilizes strategic networks with other firms (Batty, 1991; Butler and Hansen, 1991; Snodgrass, 1993; Ozcan, 1995), and whether the firm recognizes locational advantages and disadvantages. The three hypotheses that will address this association are:

H4: Proactive firms serve niche markets more often than firms that are not proactive
H5: Proactive firms utilize collaborative networks more often than firms that are not proactive
H6: Proactive firms are able to mitigate locational disadvantages and utilize locational advantages to a greater extent than firms that are not proactive.

The terms 'local' and 'regional' used to describe these firms would seem to limit their geographic expansion into foreign markets. Indeed, Daniels et al. (1988, p. 320) seem to indicate that the only place for these smaller firms in the global economy may involve "finding niches in the accounting market, such as subcontract work on accounting records for larger firms which prefer to concentrate on more lucrative consultancy and advisory work." However, many articles in the accounting literature indicate that local and regional firms are interested in internationalization, and that they are successful at it in ways other than acting as subcontractors for larger firms (Codron, 1989; Israeloff, 1992; Chudd, 1993). Therefore, the second research question to be addressed is: are the local and regional public accounting firms in the WNY area internationalizing their practices, and, if so, what characteristics differentiate these firms from the firms that are not internationalizing? The hypotheses related to this question are:

H7: Local and regional public accounting firms that have internationalized are more proactive than those that have not internationalized.

H8: Local and regional public accounting firms that have internationalized have more elements of proactivity than those that have not internationalized.

H9: The average employment size is larger for local and regional public accounting firms with international revenues than the overall average employment size.

Any firm entering the global arena faces certain internal and external barriers. Effective policies by governmental bodies or professional organizations to aid the expansion of these firms will have to be grounded in a thorough understanding of the true barriers faced by the firms. In the accounting profession, many of the barriers frequently quoted in the literature are the barriers faced by the Big Six International Firms (Daniels et al. 1988). These include the lack-of-reciprocity, immigration issues, cultural differences and right-of-establishment. However, the smaller local and regional firms may face completely different barriers. For example, negotiating reciprocity in licensing procedures with Canada may not result in additional export of services by these firms. The reason is simply that the lack-of-reciprocity is not the biggest barrier faced by these firms because, in order to practice in Canada, a whole new set of accounting and tax rules would need to be learned, and these small firms do not have the time or resources to do this. This is consistent with McConnell's (1977, 1979) suggestion that firm size, financial performance requirements, risk willingness, and in-house marketing expertise are the largest barriers to export-orientation by small and medium-sized companies. Therefore, the third research question to be addressed is: what are the true barriers faced by these local and regional public accounting firms, and do these barriers change according to certain characteristics of the firm? The following five hypotheses relate to this question:

H10: Proactivity reduces the impact of internally determined barriers to internationalization.

H11: Internal barriers are regarded as larger obstacles to internationalization for the firms not successful at internationalization.

H12: The largest perceived external barrier to the non-exporting firms is lack-of-reciprocity (licensing requirements).

H13: The largest external barrier to internationalization of local and regional public accounting firms is cultural differences.

H14: The use of information technology is more widespread in the firms that have internationalized than in those that have not internationalized.

In addition to barriers, three kinds of spatial behavior have evolved through time and can be used to interpret change in the structure of the urban system (Camagni, 1990).

The most widespread is territorial behavior: firms buy and sell within areas (markets) with geographically definable limits. In the second case, where competitive behavior is uppermost, service firms are not confined to a delimited geographical market area but compete to obtain a share of a national or global market. Marketing, rather than transport, becomes the key part of a service. The third and most recent form of spatial behavior is based on the organization of networks (Batty, 1991) that are not constrained by geographical limits to markets. The Big Six Accounting Firms have internationalized by conquering physical space. The local and regional firm cannot internationalize this way, and will have to employ the organization of networks. Therefore, the fourth question addressed by this research is: what types of strategic networks are being utilized by local and regional public accounting firms? The hypotheses related to this question are:

H15: Local and regional public accounting firms successful at internationalization have formed strategic networks with other firms.

H16: The geographical spread of the clients of exporting local and regional firms is wider for the firms that have joined international associations of accountants than for those that have not joined.

1.3 Research Area

The focus of this study is the eight western-most counties of New York: Allegany, Cattaraugus, Chautuagua, Erie, Genesee, Niagara, Orleans, and Wyoming. The Western New York Area is a declining manufacturing region situated on the second largest border crossing with Canada. Because of its unique border location, the WNY region is the area within New York State most likely to experience the effects of the Canada-United States

Free Trade Agreement (FTA). A recent article (Turner, 1996) confirmed this by describing the stunning 38 percent growth in exports in 1994 in the Buffalo-Niagara Falls area, a growth rate second only to Detroit in foreign-trade expansion among the nation's largest markets. Moreover, the trade agreement in particular, and the border location in general, place the region in the midst of larger, macroeconomic developments. The development of a sector of service and professional expertise in implementing the FTA has developed in this region, and the challenge is to find ways to strengthen and develop this advantage. The professional expertise necessary may be present or may have the potential to be developed in the small and medium-sized public accounting firm in WNY. It is one of the goals of this research to help find ways to strengthen and develop this expertise in these firms.

Indeed, McConnell (1994) has identified two principal opportunities to broaden the economic development base of this region. The first is to expand the export sector to other regions within North America or foreign countries. The second opportunity is to expand local economic growth and development by attracting direct capital investment in the region. Local and regional public accounting firms can be instrumental in both of these situations. Not only can they export their own services inter-regionally or internationally, they can provide the necessary expertise to help other companies do so, and, through their expertise and training in financial matters, serve as liaisons to attract venture capital into the region.

1.4 Research Implications

This study has a number of theoretical and methodological implications.

First, the theoretical contributions include identifying the determinants of success for the small and medium-sized public accounting firm, and identifying the differential characteristics of small and medium-sized public accounting firms that have internationalized. The literature to date has ignored the small and medium-sized accounting firm in terms of internationalization. This study provides empirical evidence that these firms are internationalizing, and that they face obstacles different from those faced by the well-publicized larger firms.

Second, the methodological contributions include developing a proactivity index that can be utilized by different researchers in other geographic areas and by other types of firms. It can also be used as a management tool in corporate decision-making to help determine and strengthen the ingredients necessary by a firm for success.

Third, the unique definition of internationalization offers an alternate measurement of the economic impact of the global economy on the WNY area, and may be used in other geographic regions as well. By including the traditional notion of the revenues generated by a domestic firm exporting its services with the revenues generated by helping other firms internationalize, it provides a more accurate picture of the role of these firms. Emphasis of this dual role may influence local policy makers to establish programs that will aid the local and regional public accounting firm in the internationalization process.

Fourth, the study disaggregates the small and medium-sized firm from the larger firms, but it also separates firms into different categories according to growth-orientation, number of owners, and proactivity groups. By doing so, it shows the impact other than size on economic performance.

Fifth, the study is also cross-disciplinary. It combines literature from a number of different fields including accounting, economics, geography, management, and planning. In so doing, it fosters respect and combines different points of view. For example, the locational advantages and disadvantages are not directly tied to success in the accounting literature, and may not be viewed as important by accounting firms. However, this study shows that the recognition and utilization of locational advantages and disadvantages may have an impact on a firm's economic performance.

Sixth, the study provides empirical evidence that supplements other research endeavors. Although the Texas Society of CPAs (1994) publishes a "National Study" that collects data on the local and regional public accounting firm, the study only collects data in 18 states and does not include firms in New York State. Beyers and Lindahl (1994) study the management consulting activities of accounting firms, but do not address the firm as a whole. Although one of the motivations of this study was to address the "misconception of homogeneity" in the service sector, it may provide a way to identify the true similarities when combined with research of other types of firms in the producer service sector.

1.5 Overview of Dissertation

The dissertation, based upon a mail survey of local and regional public accounting firms in the eight counties of WNY, is organized into two parts. Part one (chapters two and three) provides a theoretical basis for the research by reviewing three strands of literature. Chapter 2 provides a theoretical framework for services including producer services and accounting. Its purpose is to show the impact of the service sector on the economy today, and also to specifically present the role of advanced producer services and accounting, a professional service. In addition, it discusses the economic impact of the small and medium-sized firm over the post-war years. Its purpose is to demonstrate the difficulties in the measurement of the activity of these firms, and to present some of the elements that have in the past been shown to contribute to their economic impact. Chapter 3 provides a theoretical framework for the internationalization process reviewing why firms internationalize, and describes how current theories of internationalization may or may not apply to the small and medium-sized producer service firm. It also examines the internationalization behavior of accounting firms in particular.

Part two of the dissertation (chapters four, five, and six) presents and analyzes the empirical data collected through the mail survey. Chapter 4 describes the data collection method, and provides an empirical profile of one type of advanced producer service in the WNY region. Chapter 5 presents a proactivity index and, by utilizing this index, attempts to identify the determinants of success for these firms. The chapter specifically investigates the relation of the proactivity index to the economic performance of the small and medium-sized accounting firm using a number of different measures: net income per owner, ownership, and growth orientation. It also includes an analysis of other firm-level characteristics such as the factors contributing toward a competitive advantage, marketing and delivery methods, the use of niche markets and strategic networks, and the recognition of locational variables in success. Chapter 6 looks at the internationalization status of the surveyed firms specifically focusing on the characteristics of the firms that have been successful at internationalizing their practices. It goes on to analyze the various barriers to internationalization faced by the surveyed firms, and discusses characteristics of the firms that may help them overcome these barriers. Finally, it details the strategic networks utilized by these firms. Chapter 7 summarizes the results of the research questions, discusses the short comings of the research, and provides several possible directions for future research.

Chapter 2

Services: Producer Services and The Accounting Profession

Service industries account for at least two-thirds of total employment in developed economies and for at least 50 per cent of gross domestic product (GDP). As high-income countries move toward a service economy, trade in services has grown and become a significant component of the current account of these countries. In 1992, the United States exported $180 billion and imported $123 billion of services. Its trade surplus in services partly offsets its merchandise trade deficit (Rugman & Hodgetts, 1995).

Such changes are not without geographical consequences: they are influencing the relative growth of nations, regions, and cities around the globe. Services that are based on the production and delivery of knowledge and information are acknowledged as having a key role in the ability of countries to adapt and apply advanced technologies to the production process, to innovations in production, and to improved efficiency, and ultimately to be able to respond more effectively to competitive forces in global markets. These information or producer services help enhance the human capital of countries, and trade in these services is becoming as important for attracting foreign exchange as trade based on merchandise goods (Daniels et al, 1993).

There is a family of general theories in which the rise of services is seen as a stage in the long-term transformation of economies. Examples of these "stage" theories include the three-sector model (Fisher, 1935; Forastie, 1949), the emergence of a post-industrial economy (Bell, 1973; Hirschorn, 1988), deindustrialization (Blackaby, 1979) or the transition to an information economy (Porat, 1976; Hepworth, 1989). According to these theories, the service industries herald the arrival of the final stage in economic progress. They were preceded by agriculture and manufacturing (Fisher, 1935); by substitution of white-collar for blue-collar occupations and the trend towards upskilling and upgrading the labor force as the key resource (Bell, 1973); or by access to, and availability of, information as the principal factor of production in place of raw material or labor (Porat, 1976). Although these stage theories describe a process of economic and/or social change that results in services becoming the largest group of economic activity or employment by occupation, they do not provide an explanation as to how these service firms sustain and grow in industrially declining regions of advanced economies. Most explanations of firm-level growth focuses upon large producer service firms, thereby generalizing outcomes and ignoring sector-specific differences in terms of determinants of economic performance. This study focuses upon small and medium-sized public accounting firms, a major group of professional services, to understand sector-specific trends in strategic planning, collaborations, internationalization, and economic performance. The next sections provide an understanding of the characteristics of services and small and medium-sized firms. It discusses the planning characteristics of small and medium-sized firms and the sources of their competitive advantage.

2.1 Characteristics of Services

The classification of services has always been a problem They have been classified on the basis of the utility they provide, whether they meet final demand or intermediate demand (Marshall et al. 1987), whether they are consumer, producer, or circulation services (Allen, 1988); or whether they are distributive, producer, social, or personal services (Singelman, 1978). The definition and classification problems that have plagued the study of services will persist because classification presupposes that the service sector is somehow exclusive; in practice, the boundaries between it and the other sectors are becoming blurred as some manufacturers also produce services. Taken to its extreme, the conclusion might be reached that "there is not a service sector" (Castells, 1989, p.130); but, rather there is a set of activities that have increased in diversity or specialization as society has evolved, and services are "in fact, a way of absorbing the surplus population generated by increased productivity in agriculture and industry" (Castells, 1989, p.130).

Another difficulty in determining the role of services in the economy is the measurement of output from this sector. Riddle (1986) attempts to do this by examining the independent determinants of total economic activity: rate of urbanization, economic growth, financial indicators, sectoral percentages for GDP and employment, debt variables, trade variables and quality of life indicators. However, as Elfring (1989a, 1989b) has observed, the expansion of services is intertwined, in a matrix of growing complexity, with other parts of the economy. Increasing specialization in production has stimulated the rapid expansion of producer services, while changes in household structure and greater participation in the labor force by females have raised the demand for personal services. Therefore, because of this dynamic intertwining, the true output may never be measured. However, attempts to measure this output should continue.

Both demand- and supply-side factors explain the increased share of services in GNP (Dunning, 1989). The first is the growth in demand for discretionary consumer services following the growth of per capita output. The second is the steady emergence of a role for producer or intermediate services in the value added to a good or service. The third is the trend towards external purchase of services by non-service firms. The fourth is the significance attached by producers to effective marketing, distribution, after-sales maintenance and servicing of their products, and by governments to investment in social and community services or infrastructures such as telecommunications. The fifth is the more specialized or sophisticated demand of contemporary societies for legal, insurance, transport, banking, entertainment and financial services. The sixth is the ability of service producers to create new products and new markets in areas such as securities, value-added services, and data transmission and manipulation (Daniels et al. 1993).

In order for services to become more prominent actors in the world economy, they must possess attributes that enable them to be exchanged across geographical space. This is essentially dependent on the extent to which they are tradable. Hirsch (1986) has used the expression "simultaneity factor" to explain the difference between tradable and non-tradable services: the lower the proportion of their total costs incurred by the producer and the user during their interaction, the greater the tradability of a particular service. Marshall et al (1988,13) has defined traded services as those supplying "business and government organizations, rather than private individuals...and may even be indirectly tradable through their contribution to the competitiveness of other sectors of the economy." These are the producer services (or intermediate services) that can be grouped into either information processing services such as accountancy and goods-related services such as distribution.

Since the latter part of the 1970s, considerable optimism has been generated concerning the potential of producer services to stimulate economic development in lagging or peripheral regions (Beyers and Lindahl, 1994; Coffey and Bailey, 1992; MacPherson, 1991, 1996; Coffey and Polese, 1989; Illeris and Philippe, 1993). Coffey and Polese (1989) attribute this optimism to the perception that these types of activities are relatively footloose or free of locational constraints that have made such regions relatively unattractive to the investment in traditional forms of manufacturing. Four reasons why producer services have the greatest potential for stimulating economic development of lagging regions include the perception that producer services are the most rapidly growing sector in the majority of developed countries due to the changing organizational structure of goods-producing activities, and of the enhanced role of product innovation and of market differentiation. In addition, producer services can also constitute an important element of the economic base of a region because a significant proportion of these services must be regarded as a basic activity because they are not only exportable (tradable) but also highly responsive to external demand. Finally, producer services are also characterized by a spatial distribution that is significantly different from the population-based ones of consumer services which require physical proximity to their clients, and, the role of producer services in investment, innovation, and technological change may contribute to the spatial variation in the economic development process.

2.2 Small and Medium-Sized Firms and the Service Sector

A heated debate has recently been revived concerning the relative roles and importance of large and small firms. On the one hand is the view, which has prevailed for the better part of this century, that small firms do not perform an important role in the economy, and that they will play an increasingly diminished role in the future (Kaplan, 1954; Galbraith, 1957; Berger and Piore, 1980; and Harrison, 1994). Until the mid-1970s, the evidence indicated that small firms were indeed becoming less important over time (Brock and Evans, 1986) due to the fact that small and medium-sized enterprises were increasingly integrated and incorporated into large-scale activity and thereby diversified into various industries (conglomerate integration). As a consequence of such industrial restructuring, various indicators show that the relative importance of the small and medium-sized enterprise (SME) in industrialized economies had decreased by the early 1970s. For example, United States SMEs accounted for only 39 per cent of GNP by the mid-1970s, down from a share of approximately 43 per cent during the 1950s and early 1960s (United States Small Business Administration, 1982, p. 229).

The period following the 1974 oil crisis, however, witnessed a rekindling of governmental and academic interest in SMEs and their contribution to domestic economies (Bannock, 1981). Many large firms failed to adjust to abrupt changes in demand and relative costs. Inflation, unemployment and declining or stagnant investments were among the critical issues facing national governments. Theorists and policy makers hoped that SMEs could alleviate some of these problems by being more responsive than large firms to changed market conditions. The hypothesis was that by being individually owned or operated by a small team of managers, SMEs were able to move quickly in response to change; that as price-takers in most markets they tended not aggravate inflationary pressures; and that, due to their higher share of net firm establishment (compared to large firms), they would contribute to job generation and to the innovation of products, processes, and organizational structures. In countries such as the United States, where industrial concentration is a prominent feature of the economy, greater activity by SMEs can play a role in reducing the excessive powers of a limited number of firms (United Nations, 1993).

In most countries SMEs account for more than one half of the total share on a number of measures, including the contribution of SMEs to employment, sales and value added, while constituting a predominate share of all enterprises in each economy (United Nations, 1993, p.11). This evidence refutes a general notion that a higher share of SMEs in the economy is an indication of poor economic performance.

Small firms and entrepreneurship are playing a much more important role in the economy than had previously been acknowledged. Small firms make at least five important contributions to industrial markets. First, they play an important role in the process of technological change. Recent work suggests that service-to-manufacturing linkages are particularly important in terms of scientific and technical interactions (Illeris, 1994). These types of interactions can play a major role in the innovative performance of users, especially with regard to new product development (Tyson, 1995). Evidence suggests that professionally qualified consultants can deliver strategic benefits to industrial clients, often at relatively low cost based upon numerous studies (Berman, 1995; Smallbone et al. 1995, MacPherson, 1996). The second important contribution of small firms is that they generate much of the market turbulence that not only creates an additional dimension of competition not captured in the traditional static measures of market structure, such as concentration, but also provides a mechanism for regeneration of markets (Beesley and Hamilton, 1984). In this sense, small entrepreneurial firms serve as agents of change in a market. One example can be found in the work of Lipparini and Sobrero (1994). They cite the entrepreneur's ability to create, manage, and recombine the set of relationships with external suppliers. The ability to glue external expertise and capabilities in an original and unique way is considered the key factor in pursuing innovative performance. A third contribution, which is related to the first two, is promotion of international competitiveness through newly created niches (Brock and Evans, 1989).

The fourth contribution emanating from small firms in recent years has been their preponderant share of newly generated jobs. Although SMEs have a tendency to create more jobs per unit of capital than large firms, results of different analyses are divided over the exact proportions and also over the source of employment growth in SMEs. According to the United States Small Business Administration, employment changes due to net births (births minus deaths) and net internal growth (expansion minus contraction) accounted for 45 percent and 55 percent of total change in employment, respectively, for SMEs and 96 percent and 4 percent, respectively, for large firms between 1980-1986 (United States Small Business Administration, 1988, p.137). Growth in United States' SMEs is equally the result of formation and expansion, while for large firms' growth has been mainly due to formation. Other analysis, however, has found that SMEs create jobs mainly by new firm formation (Birch, 1988). In any event, contributions to employment by SMEs is substantial and continues to be so in the early 1990s. For example, in 1992, as much as four fifths of new employment was generated by smaller firms with 100 or fewer employees (Nihon Keizai Shimbun, 1992). Small and medium-sized enterprises are not only established more easily than large firms (a higher start-up rate), but are also likely to be spin-offs from large firms. Furthermore, a considerable proportion of the births of large firms is the result of expansion by SMEs or mergers and acquisitions between SMEs. All this suggests that the role of SMEs in employment is substantial.

The fifth major contribution of SMEs is their contribution to national economies from exporting. Although the contribution is generally small, in some countries exports by SMEs are increasing at a faster rate than exports by large firms. Many reasons exist for this increased export activity by SMEs. Increased exports not only elevate the level of sales and employment, but prolong the life cycle of goods and services by exposing them to new markets. This is especially the case in the intensely competitive international environment involving both domestic firms and transnational corporations (TNCs). Firms need to improve the quality of their goods and services to remain competitive, and exporting gives them the chance to test their products in various markets. This may result in the improvement of quality as firms come to know more about customers' needs and preferences. Furthermore, expansion of markets allows SMEs to enjoy scale economies of production to some extent. In the United States complete data on exports by firm size is not available. It is necessary to rely on a variety of sources, and the data is somewhat inconclusive. The Small Business Administration estimates for 1985 show that one half of the value added of goods exported by manufacturers was accounted for by SMEs (Wall Street Journal, 1989). However, another source contradicts this by indicating that in 1983, the top 250 export firms controlled 85 percent of the value of United States exports (General Accounting Office, 1983). In terms of the number of firms, 37 percent of United States SMEs are exporters, and 87 per cent of 51,000 exporting firms are SMEs (Rosen, 1992). There are also a number of potential exporters among United States SMEs. According to the General Accounting Office, there were 11.000 firms that had the potential to export but were not exporting in 1983 (General Accounting Office, 1983).

In addition to these five contributions, there are a number of other putative benefits of SMEs participation in the economy. They expand consumer choice by catering to consumer needs for more diversified, sophisticated, and specialized products and services. Flatter management structures (or even the absence of echelons in very small firms) and the frequent identity of owners and managers are significant features of SMEs' organizational structure. Because of this, SMEs are agile, and they are less likely to lose managerial control than large firms and can disseminate information in a shorter time. Less complex decision-making processes can reduce time in taking actions. As SMEs are quickly influenced by market forces, they react rapidly to meet changed conditions. These organizational and behavioral characteristics of SMEs can save costs associated with control and management, thereby offsetting some disadvantages related to a smaller scale of operations.

Although SMEs appear to make a large contribution to the economy in a number of ways, Harrison (1994) makes cautionary four points regarding the demise of large firms. First, the case against big business has been overstated. IBM and Daimler-Benz may have run into trouble; but other big firms such as Coca-Cola, McDonnell's and Toyota, have prospered. The most vigorous challengers to established big businesses are often other big businesses. Thus Sears Roebuck is losing market share to other big retailers, such as Wal-Mart, rather than to thousands of niche distributors. Wal-Mart increased its payroll by 182,000 in 1992-1994. In certain sorts of enterprise, such as the oil or car businesses, economies of scale still give giant concerns an edge.

Second, whatever its earlier weaknesses, big business is on the rebound, particularly in the United States. In the 1980s, a succession of American giants went in for a harsh bout of restructuring. In the process, they proved that their real problem was not so much that they were too big, but that they were too diverse (like ITT and countless other conglomerates) or poorly managed (like AT&T). Firms such as Hewlett Packard, Xerox and 3M are now proving that it is possible to be both big and lean.

Third, small businesses are not the job-generators and technology-innovators of legend. In the United States between 1973-1988, plants with more than 100 employees accounted for nearly three-quarters of gross job creation, and firms with more than 500 employees accounted for more than half of it, according to a recent study from the National Bureau of Economic Research (Davis et al. 1993). The jobs that small firms create are often short-lived; small companies account for a disproportionate share of job losses as well as job gains. Small companies provide, on average, lower wages and stingier benefits than big firms. They are also less likely to use fancy technology such as computer-controlled machine tools.

Fourth, Harrison (1994) argues that many small firms are independent in name only. The fashion for contracting out has certainly reduced the average size of businesses. In America, for example, the average plant size fell from 1,100 employees in 1967 to 665 in 1985. However, many small businesses rely on larger ones for finance or contracts. Indeed, contracting out often does little more than shift people from the internal to the external payroll.

The debate concerning the impact of small businesses will not be resolved any time soon. While there is no shortage of theoretical arguments about the relative roles of large and small firms, empirical knowledge is generally based upon a collection of anecdotal evidence and case studies. Some casual evidence does exist that suggests that small firms in at least several countries are outperforming their larger counterparts. The best example being in the steel industry where new firms entered in the form of "mini-mills" and small firm employment expanded, while the incumbent large companies shut down plants and reduced employment in a number of countries. Although no systematic evidence exists unequivocally to identify whether small units (firms and plants) of production are equally as efficient as large firms, or are, in fact, actually more efficient than their larger counterparts, Aiginger and Tichy (1991) conclude that the accumulated evidence to date indicates that small firms and plants are at least not burdened with an inherent size disadvantage.

2.3 Small and Medium-Sized Firms: Success Determinants

Strategic planning literature has found that the more small businesses engage in planning activities, the better their economic performance. However, although planning is one important element, other elements also contribute to the success of small and medium-sized firms. Among these other elements are: whether the firm can be characterized as growing rather than maintaining; identifying new niches rather than entering pre-existing niches; having up-to-date financial statements rather than using the "shoe box" method; having personnel policies rather than waiting for problems to arise; and having goals and objectives, and following through on them (Dodd et al., 1995).

Empirical support for the value of planning is mixed. Planning versus no planning does distinguish performance but small businesses are often not very systematic when it comes to either short- or long-range planning. The propensity of small businesses to engage in planning was demonstrated in a survey by Stoner (1983) which showed that among small manufacturing firms, more than 50 percent of the firms prepared short-term objectives, but these objectives were often kept in the mind of the owner/manager rather than being written down. This conclusion about planning formality was supported by Lyles et al. (1993), who examined formal and non-formal planners and found no significant performance differences. Orpen (1985) found that while the extent of long-range planning performed by small businesses was unrelated to company financial performance, the quality of long-range planning differentiated high and low performing firms. Bracker, Keats, and Pearson (1988) found that among small businesses in a growth industry, those who engaged in structured strategic planning financially outperformed other businesses, while Cragg and King (1988) found no significant relationships between planning and financial performance.

The findings of Khan and Rocha (1982) and Rocha and Kahn (1984, 1985) are supportive of the proactivity/reactivity dimension in that they found some of the major problems of small businesses to include lack of knowledge of the target market, no systematic accounting procedures and a lack of financial reports. These are all symptoms of reactivity.

Another avenue of support can be found in the work of Covin and Covin (1990) who studied the concept of small-firm aggressiveness, described as a "general managerial disposition reflected in a firm's willingness to take on and desire to dominate competitors through a combination of proactive moves and innovative efforts" (1990, p.36). They characterized businesses as aggressive if they typically took action to which the competition responded. They describe passive businesses as those which "typically respond to actions which competitors initiate; are seldom first to introduce new products, administrative techniques, operating technologies, etc.; and typically seek to avoid competitive clashes" (1990, p.36). Covin and Covin found a low correlation between aggressiveness and performance, suggesting that as measured (a very general 3-item scale), aggressiveness did not have a strong independent effect on the performance of small firms. They concluded that aggressiveness was generally an effective strategy for small firms with more than 30 employees.

Utilizing this literature, Dodd et al. (1995) developed an index of proactivity to determine if it affected the survival rate of small-to-medium size manufacturing firms.

They determined, in this investigatory analysis, that it did have some impact on the firms' survival. As a result, it can be suggested that small and medium-sized firms follow several strategies for survival and growth such as strategic planning to become proactive businesses rather than passive or reactive. The proactivity literature does not specifically focus upon the maintenance and creation of competitive advantage. Sometimes competitive advantage is a function of scale and scope economies, and other times it is cost-based. However, in the 1990s, competitive advantage is based on flexible specialization or quality and delivery (Gertler, 1988; Christopherson, 1989; Schoenberger, 1989;). Such advantages are proliferated by marketing and promotion strategies, networking/niching, and expansion of markets in the global arena.

2.4 Competitive Advantage, Information Technology, Marketing/ Promotion, Collaboration/Networking.

Competitive Advantage. Proactivity is one factor that provides a competitive advantage, or the advantage that one firm has over another. Porter's basic theory is that prosperity is created not inherited, and that nations can increase their wealth if they are forced to innovate in order to compete against their better-endowed rivals (Porter, 1990). He argues that information is the most crucial economic resource, and that nations that know how to innovate can easily overcome any lack of natural resources. Porter also discredits a further myth about global competition: the notion that local markets are becoming less important in an era of globalization. Quite the contrary, national and local market, he argues, are crucial to corporate success. He accepts that markets are becoming more global, but his research suggests that domestic markets give international companies their competitive advantage. Corporations learn to compete by first satisfying the demands of their home market. Domestic competition, and loss of it, prepares corporations to compete on the global scene.

Porter emphasizes the importance of four critical "home-based" conditions that determine the success in developing international industries: factor or supply conditions, demand conditions, the existence of supplier and related industries, and the intensity of domestic rivalry/competition. His general arguments concerning these four factors were extended to services in his 1990 work. Critical to this view is the notion that firms perceive opportunities for innovation or differentiation (niche markets). In Porter's view it is critically important to innovate in the face of new technologies (creativity and/ or R&D capabilities), new or shifting buyer needs (ability to quickly adapt to shifting client needs), emerging new industry segments, shifting input cost or availability, and changes in government regulation (Porter, 1990, pp. 45-47). For producer services firms, these five factors can be considered as recognition of new business opportunities which can be filled by increasingly specialized providers of services (specialized expertise), or by broadening the scope of offerings (range of expertise) within individual establishments.

Porter argues that when opportunities of this type are evident, it is important for firms to move early in order to exploit these opportunities prior to other competitors to get initial early mover advantages. A proactive firm which stay on top of the market and adjusts to its need have the ability to get initial early mover advantages. In the early phases of innovations, taking advantage of opportunities stemming from these innovations will be in a relatively powerful position to gain competitive advantage in their market-place (Porter, 1990, 48-49). To sustain this initial advantage (if it is obtained), Porter argues firm's need to solidify leadership on three dimensions: (1) dominating the particular source of initial advantage (established reputation), (2) developing a broad base of factors leading to competitive advantage (speed of service delivery; cost of service), and (3) developing an institutional framework within which the initial sources for competitive advantage are constantly improved and upgraded (personal attention to client needs) (Porter, 1990, pp. 49-53).

This general conceptualization is further developed in a model which Porter argues defines national advantage, but which can also be 'read' as regional advantage, or capacities of individual firms. The critical dimensions in this line of argument are the marketplaces within which the various components of the model operate, moving from the firm to industry within a national level of abstraction. Porter develops a model built around the four conditions mentioned above. Table2.1 shows the four dimensions in relation to services.

Many of the factors identified by Porter apply to the small and medium-sized public accounting firm. Personal attention to a client's needs is a requirement of all professional services. An established reputation, which conveys this personal attention to client's needs, is a method of both keeping and acquiring new clients, and attests to the service quality. In addition, the range of expertise, whether internal or available though a networking strategy, or specialized expertise are part of an accounting firm's structure, strategy and organization. Speed of service, creativity, and the ability to quickly adapt to shifting client needs is a manifestation of the flexibility of the firm, and allows it to be innovative in the face of new technologies (creativity and/ or R&D capabilities), new or shifting buyer needs (ability to quickly adapt to shifting client needs), emerging new industry segments, shifting input cost or availability, and changes in government regulation (Porter, 1990, pp. 45-47). A firm that is innovative will also use the new technologies, including information technology. The difference between the economic success of firms that use the new technology and those who don't contribute to the competitive advantage of a firm.

Table 2.1: Porter's Competitive Diamond Applied to Services

Factor Conditions	**Related & Supporting Industries**	**Demand Conditions**	**Firm Strategy, Structure & Rivalry**
Skilled Personnel	Geographical proximity to suppliers and clients	Composition	Price of service rendered
Information Technology		Size & Timing:	Range of expertise
		a. household income levels	Service Quality & Design
		b. industry mix within area	Generic strategy
		c. speed of initial entry	
		d. barriers or encouragement by government	
		Internationalization	

Source: Porter(1990)

Information Technology. The factors that have permitted or encouraged worldwide transactions in services, whether between or within organizations, as well as the internationalization of the sources of supply, are information technology (IT), transport technology, the development of service multinationals, and government influences. According to Hepworth (1989,7), "the information economy is a new phase of economic development, wherein the production of information, goods and services dominates wealth and job creation with computers and telecommunications providing the technological potential for product and process innovation." The requirement for information exchange to advance individual or organizational interests has always been present. What IT has done is to greatly enhance the way in which information is handled by persons or machines, to revolutionize the capacity and speed of the 'channels' used to move it between origins and destinations, and to diversify the methods and opportunities for delivering services. All have been keys to advancing competitiveness in services-especially those that are tradable. Barriers to market entry have also been lowered by IT. The convergence of microelectronics (computers) and telecommunications are significant for the tradability of services. Firstly, the convergence has allowed services to be produced and made available using a common storage and transmission medium. Secondly, it has enhanced connectivity and interpretability in that a large number of users, whether person or machines, can process or otherwise share resources across boundaries of telecommunications networks. The key feature of the IT revolution is the way in which it has virtually eliminated the effect of distance on the time required to communicate an item of information between interacting locations. It has effectively eliminated the role of national borders as physical or legal barriers to service transactions. Although this last statement may be true in terms of services in general and some services in particular, it is not true of accounting services. National boundaries are still important because of different certification and licensing procedures in the accounting services. However, the effect of information technology on the delivery of services by local and regional public accounting firms will be investigated. It is hypothesized in this study that the use of information technology is more widespread in the firms that have internationalized than in those that have not internationalized.

Although IT revolutionized the market for services and their delivery, the location of producer services is more complicated because of their involvement in more complicated industrial complexes of goods and services production, as well as by the economic structures associated with the development of large manufacturing and service corporations. Some producer services depend on proximity to their customers much in the same way as consumer services. This is the case of commonplace services which many small and medium sized firms use frequently: banks, lawyers, accountants, technical or computer consultants. The most important parameter of competition is a thorough knowledge of the needs of their clients and that requires proximity (Illeris and Philippe, 1993).

Marketing/Promotion. Marketing also provides firms with a competitive advantage in the public accounting profession. The basic components of marketing are the same worldwide: product, pricing, promotion, distribution, and customer service (Princeton Training Press, 1992). The product of the public accountant is the type and range of services offered. The price of service is generally determined on an hourly basis, but is modified by market forces, or in this profession, what other firms charge for the same service.

Promotion and distribution of services are the factors that differ the most between small and medium-sized public accounting firms. Advertising is a recent (past twenty years) method for public accountants to publicize their services, and numerous articles in the professional literature encourage the accountant to utilize promotional techniques (see for example, The Praciting CPA, 1987, 1988, 1992). The firms that have actively promoted their services have a competitive advantage over those firms which have not. The method of delivery also may provide a firm with a competitive advantage over another. Although all public accounting firms depend on personal attention to their clients, some firms have adopted up-to-date technology in the form of local area networks (LAN) and wide area networks (WAN) to deliver these services on a more timely basis, to minimize the effect of distance, and to be more flexible. Customer service is evident in the speed and creativity in the delivery of services, and the ability to adapt to shifting client needs. The firms which have adopted these up-to-date technologies have a competitive advantage over the others.

Networks/Collaborations. Networks are also crucial to the entrepreneurial process. The thrust of network theory is that the information needed to start a business is passed to the entrepreneur through an existing social network of friends (Butler and Hansen, 1991; Johannisson and Nilsson, 1989; Aldrich and Zimmer, 1986). While formal institutions provide very little capital for new companies, most venture capital comes from the entrepreneur's own resources, family and friends. They not only contribute to the firm's assets but also provide unpaid employment as well as management control over the business (Hitchens and O'Farrell, 1987; Lewis and Williams, 1987; Dokopoulou, 1986; Scase and Goffee, 1985; Dubetsky, 1976). Brown and Butler (1993) emphasize that the entrepreneur's social network is like an opportunity set--once the firm is already established, information needs change and inter-organizational linkages become necessary.

Lipparini and Sobrero (1994) believe that in SMEs, competitiveness emerges as a network-embedded capability and the coordination among firms, maximizing firm-specific competencies, represents a strategic leverage in accomplishing and maintaining a sustainable competitive advantage. As orchestrators of inter-firm linkages, entrepreneurs are able to identify possible sources of knowledge. As coordinators of such innovative ties, they combine a wide set of diverse competencies not only to overcome size constraints through development cost reduction, but also to recoup ideas and creativity for the realization of more complex typologies of innovation. These elements reduce the level of uncertainly, while enhancing early cooperation between firms.

Aharoni (1995a) views the use of networking in professional business services as a means to use scarce managerial talents effectively. Although networking originally was used as a means of overcoming obstacles to international operations, it has become a major tool to focusing on variables, allowing value-added to increase. It created a new era in which markets have become less essential than belonging to a network, and firms' boundaries are being increasingly altered without hierarchical changes. Networking has also reduced the importance of size and has allowed much more flexibility as a means of coping with uncertainty. Arm's length transactions among individual firms in different nations are sometimes preferred to an integrated structure within a firm because they reduce co-ordination costs. Some of these variables are common to all professional business services. Others are industry specific. The configuration of advantages varies because of the degree of heterogeneity of the service, the degree of professional responsibility, the specific difference e between countries' laws, cultures and norms, and the relative size of firms (Aharoni, 1995a).

Snodgrass (1993) investigated the use of networks in cross border competition. Although the Canada-U.S. Free Trade Agreement lessened technical barriers, it did not remove cultural barriers. Therefore, in order to develop strategies for penetrating the markets on either side of the border, Canadian and American managers need to understand how managers develop and maintain strategic networks, the network stability and importance. Snodgrass concluded that if Canadian and American firms have a similar understanding of the market, they will not face an impenetrable network and that the only thing that would prevent either Canadian or American firms from taking advantage of the FTA would be a lack of willingness to try. Networking, therefore, may be the natural method used by the small and medium-sized firm to internationalize.

The study analyzes and provides empirical evidence concerning the utilization of networks by the small and medium-sized public accounting firm in domestic and international operations. Specifically, it addresses how the local and regional public accounting firm in WNY is using networking to increase the range of their services and expertise, and to provide creativity and flexibility in service delivery. The use of networking may provide a competitive advantage to these firms, and aid in their internationalization.

Chapter 3

Internationalization

Many theories have been developed to explain trade and the internationalization process. These theories have been generated at many levels including the country level, the industry level and the firm level (Linder, 1961; Kindelberger, 1969; Caves, 1972; Hymer, 1976). In most cases, these theories address the trade of goods, and at the firm level, deal with the internationalization of oligopolistic or large firms. Only recently have theories been developed to explain trade in services, and these theories are still based upon the large or oligopolistic firms. This chapter first explains why firms internationalize, and then discusses the internationalization of service firms, specifically accounting services. Finally, it addresses the small and medium-sized public accounting firm and its internationalization process.

3.1 Why Firms Internationalize

Dunning (1995) lists four reasons why firms generally engage in international business. The first is to acquire inputs for further processing activities in other parts of the investing firm's operation, or for export to external markets. The second motive is to supply foreign markets with goods and services more beneficially than by alternative routes, e.g. by exports. This strategy may either be a defense response to protectionism or to the actions of competitors, or as an aggressive strategy to relocate existing production to where it is likely to be more profitable in the future, or to gain first mover advantages against competitors. The third motive grows out of the first two--it represents an international division of labor of the production of multinational enterprises so as to maximize the benefits of differences in factor endowments (both natural and acquired), to exploit economies of specialization and scope and to minimize environmental volatility (Kogut, 1989). The most noticeable manifestation of multinational enterprises (MNEs) practicing a 'rationalized' rather than a 'resource-based' or 'market seeking' investment strategy is the extent and pattern of cross-border trade within their own networks (Dunning, 1995). The fourth motivation is primarily motivated to acquire assets or some kind of competitive advantage rather than to exploit the use of an existing competitive advantage, so that the complementarity between the asset acquired and those already owned by the purchasing firms will improve the firm's overall competitive position in a particular market or in a group of markets (Dunning, 1995).

Data available suggest that acquisitions and mergers among accounting firms appear to have some of the characteristics of strategic, asset-seeking manufacturing investments (Dunning, 1995). There have also been substantial cross-border purchases of service firms by manufacturing firms to gains access to distribution channels and marketing outlets. But, in almost all goods-producing sectors, the proportion of service-intensive inputs and 'created' factor endowments is rising fast. This, then, might suggest that new investment by information or capital-intensive service firms might be increasingly motivated by the desire to acquire, protect or advance a competitive position (Dunning, 1995).

Two core paradigms have evolved from the literature on goods-producing MNEs. The first is the *internalization* paradigm which essentially views the MNE as a particular forms of multi-activity firm, and attempts to identify advantages which MNEs may have over uni-activity firms which specifically arise from their being multi-activity. The internalization paradigm then goes on to explain why the location of the plants may be outside the home country of the owning company. The entry of multi-activity firms is explained by the presence of market imperfections in intermediate product markets which give rise to certain transaction costs. Firms replace or bypass the market by undertaking themselves the production leading to the goods or services being transmitted.

The internalization paradigm has also been applied to the service sector (Casson 1989, 1990; Buckley, 1988). Each offers a persuasive explanation of why MNEs may engage in FDI rather than in some other form of international involvement, e.g. licensing. In the case of some kinds of investment, i.e. those made to acquire a competitive advantage, the gains anticipated from internalizing foreign markets may provide a sufficient reason for the investment.

The internalization paradigm cannot provide a full explanation for all foreign value added activities undertaken by MNEs. This is because it regards ownership specific assets of MNEs as exogenous variables which have nothing to do with the internalization of cross-border intermediate products. The advantage is the ability of a firm to supply consumers efficiently with the products they require independently of where it locates its plants or whether the cross-border markets for products exported from the home country are internalized or not.

The *eclectic* paradigm of international production seeks to overcome this particular problem by arguing that at a given point of time the propensity of firms is to invest and produce outside their boundaries. This reflects three things. The first is the ability to produce saleable goods and services to intermediate or final consumer profitably in comparison to their competitors or to their own performance over the past year. The second is the extent to which it is profitable to combine these advantages with factor endowments in a foreign country, rather than undertake further value adding activities from domestic plants for export. The third is that the firm possessing the capabilities may find it profitable to add value to these assets, rather than to sell the right to do so to other firms.

The eclectic paradigm of international production asserts that it is the interaction between the competitive or ownership (O) advantage of MNEs, and the competitive or locational (L) advantage of countries which will decide the structure of the foreign value activities of firms. In addition, the way in which these activities are organized, e.g. by hierarchies or markets, will depend upon the extent to which there are imperfections in cross-border intermediate product markets and the extent to which there are economies of scale or scope and risk-reducing economies which might be derived from the common ownership of cross-border activities, i.e. internalization (I) advantages.

The OIL paradigm is, perhaps, the dominant paradigm of international production. The configuration of OLI advantages will vary according to industry-, country- (or region), and firm-specific characteristics. Two firms faced with an identical OLI configuration would not necessarily react (as far as their foreign value activities are concerned) in the same way. Indeed, there is no homogeneity of competitive strategies or of modes of servicing global market expansion, for example, the Big Six accounting firms. Any paradigm of international production of services must take these firm-specific differences into account.

Dunning (1995) recommends incorporating strategic behavior as a specific and dynamic add-on variable to the OLI tripod of factors. Economists such as Caves et al. (1980), Buckley (1989), Casson (1987, 1990a), ?Teece (1984) and Kay (1991) and business analysts such as Chandler (1962, 1977), Kogut (1989) and Bartlett and Ghosal (1989) have attempted to identify and/or evaluate the significance of strategy-related variables as factors influencing not just the decision of a firm to adopt a hierarchical structure rather than a market solution to reduce transactions and/or production costs, but the form of organizational structure which optimizes decision taking. Similarly, marketing scholars have given some attention to the role of strategy-related variables in influencing the modes of entry (or expansion) into particular markets; while the main thrust of business analysts has been to evaluate not only why certain kinds of firms build up and/or sustain a competitive advantage, and why they choose a particular strategy towards such activities as product development, product diversity, marketing rather than another strategy. Out of all this research, a sense of a generic or core strategy is beginning to emerge; but as yet it tends to be confined to particular functional areas of the firm. Examples include Porter's (1980) cost reduction and product differentiation strategy and Douglas's five kinds of marketing strategy (Douglas and Rhee, 1989).

Some attention has been given to the application of overseas market entry strategies to the services sector by Shamia and Johnson (1987) and Erramilli and Rao (1990). Erramilli and Rao, for example, suggest that it is possible to relate the entry mode to the motives for entry, and these, in turn, to different kinds of service firms. In particular, the authors distinguish between client following and market seeking entry strategies. The first of these strategies is for service firms to follow clients who have preceded them abroad. Thus, many professional service firms initially follow their goods-producing clients to the countries in which they set up their factories. Today, firms are expected to offer global services tot heir global clients. The second strategy of service firms is to enter foreign markets to supply new foreign (or foreign and domestic) clients.

3.2 Internationalization of Service Firms

Ownership Advantages and the Service MNE. The OLI model has also been applied to services (Dunning, 1995; Bagchi Sen and Sen , 1997). Dunning has identified five competitive or ownership advantages in the case of service supplying firms. They are quality consistency, reputation and product differentiation; economies of scope; economies of scale and specialization; access to, control of and ability to process and disseminate information effectively; and favored access to inputs and/or markets.

Rugman (1981) identifies the ownership-specific advantages of the service MNE to include intangible advantages such as consumer perceptions of high quality through brand-image, the capability of managing global distribution and marketing networks, economies of scope or specialization due mainly to size offer similar incentive as “hard” technology does to typical manufacturing MNEs. In addition, experience in the home market is a major source of firm-specific advantages. Product specialization and a distinct corporate identity become valuable assets in some service industries requiring supplier-client confidentiality, such as in accounting, constancy, and banking (Bagchi-Sen and Sen, 1997).

Locational Advantages and the Service MNE. Two variables of particular significance can explain the locational advantages of countries (Dunning, 1995). The first is the extent to which the service is tradable--either in its own right or embodied in goods or people. Many services are location bound, i.e. immovable across space. Such services can only be provided to consumers by a foreign firm via inward direct investment or by an indigenous firm under license to the foreign producer or in a networking relationship with a foreign producer. The second factor. especially relevant to the location of services, is the regulatory environment of host countries. Countries have greater controls on trade and investment in services than in goods. In the past, entry or performance requirements have been widespread in the provision of business services and in the operation of financial and commodity markets. Country-specific laws and regulations tend to govern entry into many professional trades while price fixing and/or market sharing is common-and often upheld by governments-e.g. in the air transport, education and training, and public utility sectors. More generally, the locational variable affecting the siting of service activities by MNEs will depend upon the type of services being provided (Dunning, 1995).

In the case of business and professional services, including accounting, numerous locational barriers inhibit their internationalization. The barriers to individuals and firms in business and professional services have been outlined and discussed in various publications (Feketekuty, 1986, 1988; Noyelle and Dutka, 1987; UNCTAD, 1989). In attempting to service foreign clients, individuals face licensing-type restriction by government and/or professional bodies, including:

1. non-recognition of credentials and qualifications;
2. pre-condition for licensing:
    a. requirements for local education;
    b. requirements for revalidation of college degrees:
    c. requirements for additional education in the host country and practical experience in the host country;
3. requirements for citizenship and residence in the host country.

Individuals who travel for temporary periods to visit foreign clients or to work in foreign branch offices may encounter visa or work permit problems. Those who seek to migrate to another country to practice their profession or establish a business service face immigration problems (Ascher, 1995).

Firms face restrictions on foreign ownership (including licensing requirements; the use of the international firm name; the scope of practice; the hiring of nationals and/or non-nationals; the temporary entry of personnel; the flow of funds (through exchange controls, taxation or other means) affecting repatriation of earnings and transfers to other offices; the flow of information; and government procurement. Accountants may also face limits on their cope of practice in foreign countries; i.e. they may not be permitted to sign audits or they may have to represent themselves as bookkeepers or tax advisors; they may not be able to serve as management consultants or investment advisors.

In addition to these political barriers, other barriers exist that can be categorized as cultural. Differing languages, legal systems, and social structures are all barriers that may have to be overcome in a foreign land. Erramilli (1991) study indicated that service firms chose culturally similar countries at low levels of international experience, and began moving into culturally distant markets upon building greater international experience through a more diversified geographic scope of experience. Therefore, it appears that cultural barriers are larger for the firm inexperienced at internationalization.

In addition, Bagchi-Sen (1995) identifies the following as location advantages that influence the service MNEs' decision between domestic (exporting) versus foreign-owned production: the transportability of the type of service (i.e., the degree of location boundedness); agglomeration economies provided by available infrastructure in commercial, financial, legal, educational, transport, and telecommunications; the size and character of the market; regulation of markets; host government incentives for inward FDI, the location of human (skilled labor) and physical assets.

Internalization Advantages and the Service MNE. A number of factors influence the internalization decision by MNEs. As in the case of manufacturing MNEs, risk diversification through avoidance of search and negotiating costs, reduction of buyer uncertainty about the nature and the quality of technological inputs, avoidance of government tariffs, or nontariff barriers are those mentioned by Bagchi-Sen and Sen (1997). Dunning (1995), however, states it in terms of transactions costs. The exchange of services through the market is likely to involve higher transaction costs (relative to total costs of production and transaction) than those of goods. Six reasons explain this statement, First, services contain a larger element of customer tailoring than do goods, and they are more idiosyncratic. Second, owing to a greater human element in their production their quality is likely to vary much more than that of many goods. Third, a major proportion of information provided, and, until recently, knowledge and experience connected with interpreting and evaluating the information, was tacit and non-codifiable. Because of this, the fourth reason is that information or knowledge related to service activities may be inexpensive to replicate, the possibility of an abuse of that knowledge is a real threat to the firm possessing it. Fifth, because markets for many services are highly segmented, the opportunities for price discrimination, which can best be exploited via hierarchies, are considerable. Finally, the control of some service activities may be perceived to a decisive element in the success of non-service-producing companies. Together with the fact that many services are impossible or difficult to trade over space, the above reason explain both the presence and the rapid growth of MNE activity in this sector. Both people and firms tend to spend more on services as incomes rise. Non-service firms are becoming increasingly involved in service activities and new specialized service companies are being set up as the provision of some services becomes more complex. All these trends are making for an intensification of international activity of services in its varied forms (Enderwick, 1989; UNCTAD, 1989; Aharoni, 1995; Dunning, 1995).

3.3 The Internationalization of Accounting Services

Traditionally, geographers have provided the classification basis for public accounting firms. Daniels and his associates (1988) suggest a three-tiered, size structure. This structure defines the upper level as being composed of large firms "all of which possess a *national* network of offices, many with extensive networks" (Daniels et al. 1988, p. 319). At the lowest level are small accounting practices which are characterized by the local and specialized nature of their services. The medium-sized firms are the regional firms which fall between the upper-tier firms and the small firms.

Another classification scheme divides firms into local, regional, national and international firms. Any public accountant can readily classify the firm in which he/she is employed into this four-level, classification scheme, although the literature does not provide any generally-accepted definitions of these classifications.

Although accounting services were originally centered within the nation-state, and standards for these services continue to be set almost exclusively by nations presumably in response to the perceived needs for accounting and financial information within the nation-state, a change is occurring. In recent decades, great increases in international trade and business, fostered by innovations in transportation and communication, have made the focus of many business activities global in scope. International accounting services have grown in keeping with the needs of international business or, perhaps, more accurately, in keeping with the needs of the international economy. In doing so, little doubt exists that they have influenced the direction of its components, both territorial and economic. Hopwood (1989, p. 9) suggests that "accounting has never been a purely national phenomenon," and went on to point out that "both its techniques and the significances that are in part created by them have a history of penetrating national boundaries, moving along the pathways established by commerce and patterns of political influence." From the point of view of the firms themselves, recent practice has generated increased interest in the international aspects of their practice and, as might be expected, has heightened interest in standardization and harmonization (Hopwood, 1989, p.1).

In order to meet the demands of globalization, the industry has become more concentrated in the developed nations. Establishing new offices, buying practices of other firms, and merging practices are the three main routes to internationalization followed by the large firms. Berton (1989, p.A6) suggests that "over the long-run..., it's possible that the merged firms could better serve their clients...because the mergers will fill in geographic and service gaps and weaknesses, and will pool capital needed to provide...expensive consulting services." Research has focused mainly on the large public accounting firms, and the literature suggests that it is unlikely that the smaller firms will have much to contribute to the international economy (McKee and Garner, 1992). Daniels et al. (1988) suggest that a survival strategy for the smaller firms may involve "finding niches in the accounting market, such as subcontract work on accounting records for larger firms which prefer to concentrate on more lucrative consultancy and advisory work" (1988, p.320). The firms in the lower tiers have virtually been ignored in the literature, even though the American Institute of Certified Public Accountants (AICPA) has estimated that between sixty and seventy-five percent of CPA firms operate as sole practitioners (McKee & Garner, 1992, p. 20).

However, local and regional firms are interested in internationalizing their practices. A review of the *Practicing CPA* (1981-1994), an AICPA publication for the local firm, reveals this interest. A number of paths are recommended by this publication for the internationalization of local and regional firms that do not include acting as subcontractors for the larger public accounting firms. These recommendations include joining international associations of independent CPAs (Israeloff, 1992; Codron,1989) and networking with other professionals such as international lawyers, actuaries, U.S. banks with foreign clients, and foreign embassies. Whether or not these recommendations are being implemented are also investigated in this study. It is hypothesized that local and regional public accounting firms successful at internationalization have formed strategic networks with other firms, and that the geographical spread of the clients of exporting local and regional firms is wider for the firms that have joined international associations of accountants than for those that have not joined. In addition, increasing their knowledge of the international arena to service clients who are already in international operations, and to help clients go international by selling their products and services overseas, or to participate in joint ventures here in the United States (Israeloff, 1992, p.1) are also recommended..

An article in *INC.* magazine (January, 1993) supports the premise that these local and regional firms can internationalize their practices. It describes a manufacturing company that originally relied upon the advice of a Big Six accounting firm but found it too costly and bureaucratic. The manufacturing company switched to a regional accounting firm that was part of an international network-a compromise between the sophistication of a Big Six firm and the corporate hand-holding that comes naturally to partners at small accounting firms.

It can no longer be assumed that the small and medium-sized firms are simply willing to act as subcontractors to the large firms. Harrington (1989,1990) found that particular business services, including accounting, seem to offer high potential for export-led growth. Harrington and Lombard (1989) also found that accounting firms with an average size of twenty-three people reported both extra-regional and international revenues. This firm size is considered to be in the small-to- medium sized range for public accounting firms. Therefore, it is necessary to investigate the market-expansion and market-deepening behavior of these local and regional accounting firms, and how they internationalize their practices. Because of the unique characteristics of these small and medium-sized public accounting firms, the definition of internationalization is extended in this study to capture the number of ways that these firms can become involved in the global marketplace. Traditionally, internationalization by service firms include opening a subsidiary (e.g. fully-owned or partnerships) or exporting. In this study, the definition of internationalization includes two other criteria: (a) management advisory services that help U.S. clients internationalize their operations, and (b) providing tax, auditing, or other services to foreign companies that have entered the U.S. environment.

Chapter 4

Data Collection Technique and Respondent Profile

The purpose of this chapter is to discuss the survey methodology, and present an overview of the general firm characteristics of the sample gathered in the survey. This chapter also provides a comparison of the Western New York Sample of local and regional public accounting firms with a study of similar firms at the national scale.

4.1 Data Collection Technique

A questionnaire was mailed to the population of local and regional Certified Public Accounting Firms in the eight counties of Western New York. Three sources were utilized to develop a list of the local and regional public accounting firms including the membership roster of the Buffalo Chapter of the New York State Society of Certified Public Accountants (1994), the Directory of Member Firms published by the Division for CPA Firms of the American Institute of Public Accountants (January 1, 1994), and the yellow pages of the appropriate telephone books for these localities. Difficulties were encountered in the development of this list because of the different organizational forms of CPA firms, and the fact that a comprehensive list at the firm-level was not available.

The survey was mailed on December 21, 1995 accompanied by two letters (Appendix A). The first letter addressed the purpose of the research, and the second letter, written by the President of the Buffalo Chapter of the New York State Society of Certified Public Accountants (NYSSCPAs), encouraged the firms to reply. A second request was mailed two weeks later, and was followed by a telephone call. In total, 195 surveys were mailed, 11 were returned for incorrect addresses, and 3 were returned with notes stating that the firm was not a public accounting firm. Of the 11 surveys returned for incorrect addresses, 5 addresses were corrected. In total, 55 completed surveys were received yielding a response rate of 30 percent (55/186).

Many problems are associated with survey-based research (Babbie, 1973, 1989). Some of these complications include the potential for influencing the respondents into researcher-determined answers, the differing interpretations of questions and answers between the researcher and the respondent, and the difficulty in estimating non-response or late-response bias. In order to mitigate the distorting effects of the first two problems, the survey was pretested by 10 local and regional public accounting firms of the target population, and modified based on their identification of potential misinterpretation or misleading areas.

The problem of measuring non-response bias or late-response bias is more difficult to address. The survey was anonymous because of the proprietary information requested. Therefore, it is not possible to identify the non-respondents. However, the surveys were divided into two categories: the early-respondents and the late-respondents. The early-respondents returned the surveys before the second request and follow-up telephone call. The surveys of the late-respondents were received after these events. It must be noted, however, that a time period of only six weeks separated the first and last survey returned.

The early respondents were compared to the late respondents on the basis of difference of means or percentage distribution for several variables, including total revenue, employment levels, revenue growth, type of services offered, and international orientation. The late respondents were larger than the early respondents in terms of the average number of owners (2.5 versus 1.8) and the average number of employees (13.3 versus 8.8). This, however, could be due to the fact that in larger firms the time period necessary to route the survey to the appropriate person(s) is longer than in a smaller firm. The firms in the largest total revenue group (over $900,000) also were among the late respondents.

On an average, the goals regarding economic performance between the early and late respondents (e.g. growth in revenue) did not differ. The late respondents did include a larger number of firms that were interested in internationalization or that had successfully internationalized (Table 4.1). However, the international orientation is reflective of the size of the firm as shown later in the research.

Table 4.1: International Orientation: Early Versus Late Respondents

International orientation	**Early Respondents**	**Late Respondents**
Not Interested	68%	33%
Interested, Not Successful	28%	40%
Successful	4%	27%
Total	100%	100%

Source: Dec. 1995-Jan. 1996 Researcher's Survey

The types of services offered by these firms on an average were similar (Table 4.2). The category, Management Advisory Services, was the one exception. The late respondents offered more management advisory services than the early respondents (11.27 percent versus 8.80 percent). Size, once again, may be the explanation for this difference, because the larger firms are more capable of offering these types of services due to the greater number of employees and their varied expertise.

Table 4.2: Types of Services Offered: Early Versus Late Respondents

Types of Service	Early Respondents	Late Respondents
Audit	20.40%	19.60%
Tax	45.60%	44.33%
Management Advisory Services	8.80%	11.27%
Other	25.20%	24.80%
Total	100.00%	100.00%

Source: Dec. 1995-Jan. 1996 Researcher's Survey

It is difficult from this information to estimate the non-response bias. However, in section 4.2, the average responding firm is compared to a national survey of local and regional public accounting firms. In a number of characteristics such as size distribution of firms, types of services offered, and average employment size, the WNY sample closely matches the national sample.

4.2 Respondent Profile

The questionnaire was designed to solicit information in six main categories: the firm demographics and organizational structure; the client base and the type of services offered; the procedures utilized for the survival and growth of the firm; strategic alliances formed; the effect of locational variables; and the internationalization status of the firm (Appendix A). The respondents were advised to leave any question blank that they were uncomfortable answering. Although anonymity was guaranteed, the conservatism of the profession, the proprietary information sought, and the relatively limited geographic area of the study caused some questions to be left unanswered, particularly question 7 that requested the Total Net Fees and the Firm Net Income.

Using the responses to the questionnaire, this section provides a descriptive analysis, some comparisons and observations regarding this group of firms. Specifically, the characteristics described are type and organizational form, revenue distribution, main clients/sectors served, employment size, factors providing the firms with a competitive advantage, and the impact of locational variables on the firm's net fees.

The average firm started business in 1975 with the oldest firm starting in 1915 and the newest in 1994. Most firms considered themselves to be local (87.3%) followed by regional (10.9%). Only one firm was a national firm, and no questionnaires were mailed to multinational firms such as Deloitte and Touche. The organizational forms were: partnership (25.5%), professional corporation (34.5%), and sole proprietorship (34.5%). The other organization (5.5%) included limited liability partnerships (LLPs) and limited liability corporations (LLCs).

The size distribution of the firms by total revenues (Table 4.3) shows that the majority of these firms earned total revenue in the range of $50,000 to $500,000. In comparison to a national survey (The Texas Society of CPAs, 1994), a similar size distribution was found in the WNY sample (Table 4.4). Using the taxonomy developed by the Texas Society, the individual practitioners are the largest category in both surveys representing 51% of the total local and regional firms, followed by the medium-sized, multi-owner firms and the large, multi-owner firms (Table 4.4). The small, multi-owner firm represents the smallest group. The taxonomy developed by the Texas Society is used in Chapter 6 to divide the firms into successful and less successful categories based upon net income per owner.

Table 4.3: Size Distribution by Total Revenue Groups

Revenue Group	% of Responding Firms
1. Under $50,000	5%
2. $ 50,001 - $ 150,000	15%
3. $150,001 - $ 350,000	24%
4. $350,001 - $ 500,000	22%
5. $500,001 - $ 650,000	7%
6. $650,001 - $ 850,000	7%
7. $850,001 - $1,000,000	4%
8. Over $1,000,000	16%

Source: Dec. 1995-Jan. 1996 Researcher's Survey

Table 4.4: National Survey Versus WNY Sample - Size Distribution

Firm Group	National Survey	WNY Survey
Individual practitioners	51%	51%
Small multi-owner firms Revenues < $350,000.	9%	4%
Medium-sized multi-owner firms $350,000 to $900,000	20%	24%
Large multi-owner firms Revenues >$900,000	20%	21%
Total Firms	100%	100

Source: Dec. 1995 - Jan. 1996 Researcher's Survey and Texas Society of CPAs (1994)

Table 4.4 helps explain why 46 percent of the WNY sample are in revenue group 3 ($150,001-$350,000) and revenue group 4 ($350,001-$500,000). The majority of the firms are individual practitioners who may not want to expand their practices by adding more owners. Categorizing single-owner and multi-owner firms by revenue group shows that the top revenue group for the single-owner firm is group 5 ($500,001-$650,000) (Table 4.5). Although, revenue may not be the best indicator of success, it is one of the most widely used measures of economic performance. In Chapter 6, the firms are divided into single-owner and multi-owner categories that capture classifications based upon revenue.

Table 4.5: Single-Owner and Multi-Owner Firms by Revenue Group

Revenue Group	**Number of Responding Firms**	
	Single Owner	Multi-owner
1. Under $50,000	3	0
2. $ 50,001 - $ 150,000	8	0
3. $150,001 - $ 350,000	10	2
4. $350,001 - $ 500,000	6	7
5. $500,001 - $ 650,000	1	3
6. $650,001 - $ 850,000	0	3
7. $850,001 - $1,000,000	0	2
8. Over $1,000,000	0	9

Source: Dec. 1995 - Jan. 1996 Researcher's Survey

The total revenue of the average firm over the last five years grew 11 percent with one firm reporting an average decrease of 6 percent while another firm reported a 300 percent increase. Growth-orientation of the firm is important in analyzing the local and regional public accounting firm because of the heterogeneity of firms. A number of sole practitioners may want to limit their growth. For example, a woman may be working as a sole practitioner to supplement the family income during the time when her children are at home, and is satisfied with a certain amount of income. Therefore, for analytical purposes in Chapter 6, the firms are divided according to their growth orientation (Table 4.6). If a firm reported that their goal concerning growth was 1% or higher in revenues per year, the firm was classified as growth-oriented. If the firm reported its goal as being maintenance of the status quo or survival (1% or more decrease in revenues per year), the firm was classified as not growth-oriented.

Table 4.6: Growth Orientation

Growth Orientation	**Revenue Growth**	**# of Firms**
Growth-Oriented	Aggressive	1
	Moderate	13
	Modest	29
Not-Growth Oriented	Maintenance of Status Quo	8
	Survival	3

Source: Based on responses to question #22 from Researcher's Survey

The main type of service offered by the average WNY firm is tax preparation, planning and representation (45%), followed by audit (20%), review and compilation (19%), management advisory services (10%), and other (6%). Review and compilation is a relatively new service offered to small- and medium-sized businesses needing credit. It replaces the requirement for audits on these businesses by banks and credit-granting institutions. It is interesting to note that the Texas survey showed a similar breakdown of revenue: tax preparation, planning and representation (44%), audit (12%), review and compilation (16%), management advisory services (8%), and other (20%) (Texas Society of CPAs, 1994).

Table 4.7 shows the main clients/sectors served by the firms. The top-ranked clients/sectors are manufacturing, individuals, and retailing. It is not surprising that manufacturing firms are the main clients of 31 of the 55 firms. Even though WNY experienced a decline in the share of manufacturing employment from approximately 40 percent of the total employment in the 1960s to approximately 18 percent in the 1990s, manufacturing is still considered to be one of the major employers in the WNY region (U.S. Census, 1990).

Table 4.7: Number of Firms Listing Each Sector as a Main Client
(each firm could check more than one)

Clients/Sectors	**Number of Firms**
Manufacturing	31
Individuals	28
Retail	24
Construction Companies	9
Government Markets	8
Insurance, banks or finance	8
Transportation Companies	7
Medical Related	5
Travel	4
Utility	1
Other	18

Source: Dec. 1995 - Jan. 1996 Researcher's Survey

The largest firm employs 69 on a full-time basis while the smallest firm employed one. The average number of full-time employees equals 10. The national survey showed an average employment of 9 for this group of firms (Texas Society of CPAs, 1994). Size distribution by number of owners and number of employees is found in Table 4.8. This table indicates that the largest number of firms in the WNY sample are single-owner firms (28 firms) and employ between 6 to 10 people.

Table 4.8: Size Breakdown by Number of Owners and Employees

Number of Owners	**Number of Firms**	**Number of Employees**	**Number of Firms**
1	28	1 - 5	16
2	14	6 - 10	26
3	5	11 - 15	4
4	1	16 - 20	1
5	2	21 - 25	1
6	2	26 - 30	3
7	1	31 - 35	1
8	1	36 - 40	1
9	0	41 - 45	0
10	1	66 - 70	2

Source: Dec. 1995 - Jan. 1996 Researcher's Survey

In evaluating the factors that give the firm a competitive advantage, defined as the advantage one firm has over another, personal attention was ranked first and marketing activities was ranked last (Table 4.9). Personal attention was the top ranked factor at 4.8 indicating that it is considered to be critically important in providing a competitive advantage. It is noteworthy that geographical proximity to customers only received a moderate rating (2.9), and will be discussed later. The factor that is perceived as least important in giving the firm a competitive advantage is marketing activities at 2.7 which places it between minor and moderate importance. However, later in the research, it will be pointed out that marketing activities contribute to distinguishing firms that are more successful, larger in terms of owners, more growth-oriented, and have internationalized. It appears that the average firm is not aware of the impact that marketing can have on their practice.

Table 4.9: Competitive Advantage

Factor	**Average Importance***
Personal Attention	4.8
Established Reputation	4.3
Ability To Adapt	4.0
Speed of Service	3.9
Quality or Design of Service	3.9
Creativity	3.9
Expertise	3.7
Range of Expertise	3.7
Price	3.6
Geographical Proximity	2.9
Marketing Activities	2.7

*Based upon Likert Scale (1 = no importance, 5 = critically important)
Source: Dec. 1995 - Jan. 1996 Researcher's Survey

The WNY firms were asked to evaluate the impact of a selected group of locational variables on their net fees (Table 4.9). Their response indicates that the WNY economy and the declining manufacturing sector have lowered net fees. Fifty-eight percent of the firms reported that the WNY economy had a negative impact on their net fees, and 51 percent reported that the declining manufacturing sector had a negative impact. This result is expected due to fact that 31 of the 55 firms listed manufacturing clients as one of their main clients (Table 4.5), and that the decline in the economy of this area is often linked to the performance of this sector. The numbers in the last column of this table may be the most revealing of all--the firms are not aware of opportunities provided them by locational factors. For example, 70 percent of the firms reported that the large number of educational institutions in the area had no impact on their firm's net revenues. Further discussion of the locational advantages and disadvantages by categories of firms will be done later in the research. Table 4.10 shows the percentage of firms that responded to each factor:

Table 4.10: Impact of WNY Locational Variables on Firm Net Fees

Factor	**% of Firms Reporting**		
	Positive Impact	**Negative Impact**	**No Impact**
WNY Economy	13%	58%	29%
Border Crossing	29%	0%	71%
Free Trade Agreement	22%	0%	78%
NAFTA	9%	0%	91%
Proximity to Toronto	34%	2%	64%
Decreasing Manufacturing Sector	5%	51%	44%
Concentration of Medical Industry	22%	9%	69%
Concentration of Financial Sector	13%	15%	72%
Large Number of Educational Institutions	25%	5%	70%

Source: Dec. 1995 - Jan. 1996 Researcher's Survey

The size distribution using the Texas taxonomy, the types of services offered, and the average number of employees support the premise that these WNY firms match the profile of the average national small to medium-sized public accounting firm. As a result, the findings in this research serve as a basis for understanding firm-level efforts in improving economic performance in other geographic locations.

Chapter 5

Proactivity and Economic Performance

The economic performance of local and regional accounting firms depends upon firm-specific characteristics, networking relationships, and location. This chapter analyzes the interrelationships between some of these firm-specific characteristics, networking relationships, location, and economic performance. A major group of firm-specific characteristics included in this analysis pertain to the planning strategies utilized by these organizations to sustain and grow in a declining industrial market, namely the Western New York area. More specifically, the planning strategies include long term and short term plans, personnel policies, preparation of financial statements, and marketing strategies. In this chapter, these strategies are combined to develop an index which is used to classify firms into the following four categories: proactive, reactive, reactive/passive, passive. It is hypothesized that proactive firms are more successful than the others (Table 5.1). The criteria used to categorize firms as successful and less successful in terms of income are discussed below.

Networking relationships are used by the small to medium-sized firm for a number of reasons, such as to help retain an existing client base, expand the firm's range of expertise or to develop specialized services. These networking relationships are either formalized through fee payment or remain informal. In addition, these networking relationships include collaboration with other service firms in areas such as legal, insurance, banking, and information technology. Such collaborations allow firms to explore new markets through functional diversification and client referrals without equity investment. It is hypothesized that proactive firms utilize collaborative relationships more often than the others (Table 5.1).

Location-specific characteristics are of utmost importance to these local and regional firms from the following aspects: human resources, client base, and cross-border relationships. It is further hypothesized that proactive firms have the means to mitigate the effects of locational disadvantages and utilize locational advantages on their revenue structures more often than the others (Table 5.1).

The rest of the chapter has three sections. First, the proactivity index is developed. Second, the following associations are examined: (i) proactivity and success; (ii) proactivity and ownership patterns; (iii) proactivity and growth orientation.; (iv) proactivity and marketing/collaboration. Third, the impact of location-specific characteristics on revenue structure is determined. Here, the nature of the impact is further analyzed for the four proactivity groups. Table 5.1 lists the specific hypotheses tested in this chapter.

Table 5.1: Research Hypotheses

Hypotheses	
H1:	Proactive local and regional public accounting firms are more successful than the others.
H2:	As a firm becomes larger in terms of owners, more elements of proactivity will be present.
H3:	Growth-oriented firms have higher levels of proactivity
H4:	Proactive firms serve niche markets more often than firms that are not proactive.
H5:	Proactive firms utilize collaborative networks more often than firms that are not proactive.
H6:	Proactive firms are able to mitigate locational disadvantages and utilize locational advantages to a greater extent than firms that are not proactive.

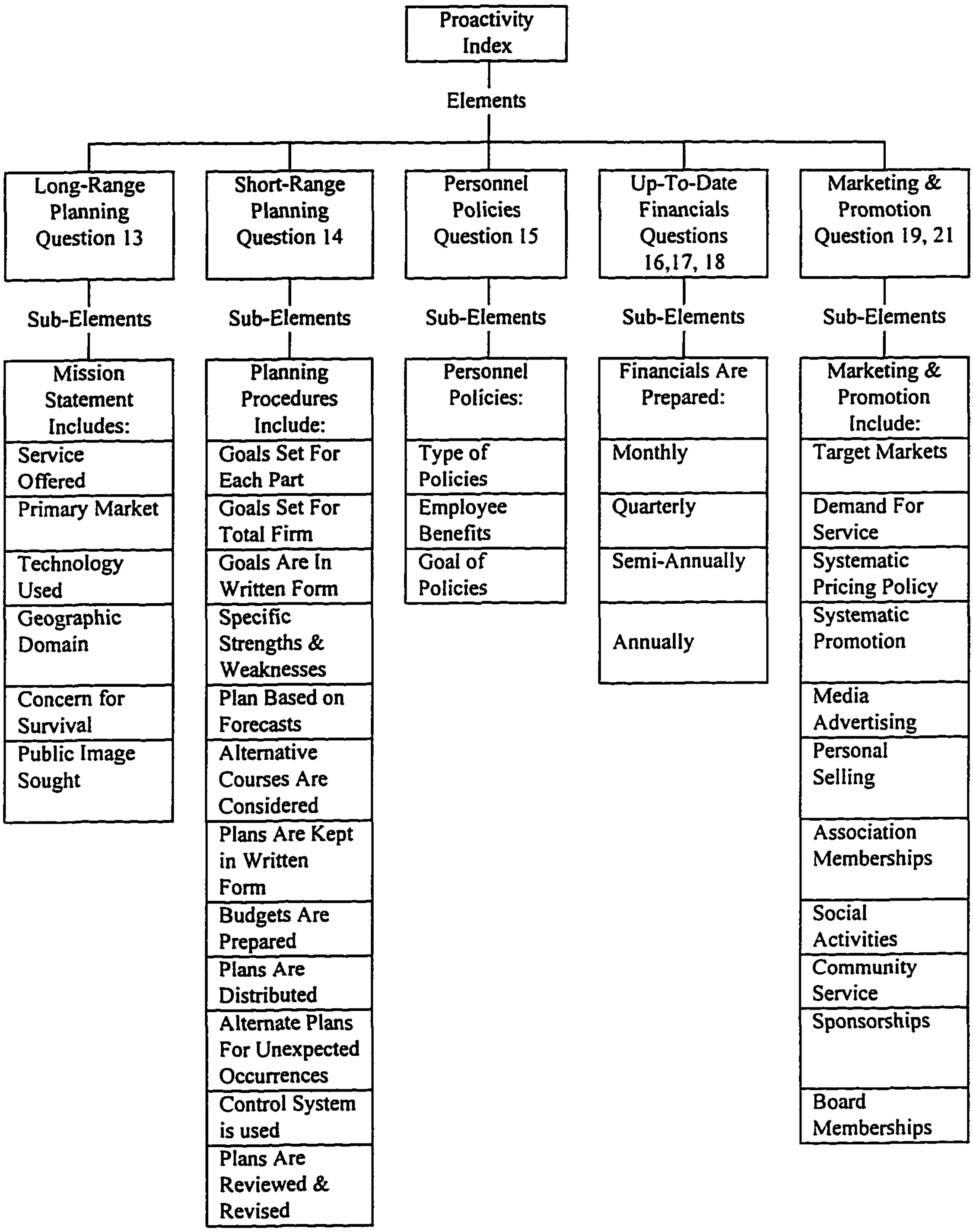
5.1 The Proactivity Index

This section formulates a proactivity index composed of five individual elements that have been shown to contribute to the economic performance of the small to medium-sized firm. The five elements are based upon strategies relating to planning, financial management, personnel management, and marketing and promotion activities. The five separate elements are long-range planning, short-range planning, up-to-date financial statements, personnel policies, systematic marketing and promotion strategies. Literature support for each of these five elements is listed in Table 5.2. Figure 5.1 illustrates the sub-elements of each of the five main elements of the Proactivity Index, and lists their relationship to the questionnaire.

Table 5.2: Selected Literature Support and Questionnaire Relationship for Proactivity

Proactive characteristics	Support from research literature	Practitioner's Publications/ Trade Journals	Questionnaire Relationship
1. Firm is strategic	Robinson & Pearce (1984) Ackelsberg & Arlow (1985) Bracker, Keats & Pearson (1988) Lyles, Baird, Orris & Kuratko (1993)	Ancona (1990) Firth (1991) Smitt (1985) The Practicing CPA (12/88)	Long-term Planning Question #13 Short-term Planning Question #14
2. Up to date financial records	Kahn and Rocha (1982) Rocha and Khan (1984, 1985)	Tribble and Litter (1992)	Question #15
3. Personnel policies	Moriarity and Field (1990)	Clopton (1992) Lewis (1992) The Practicing CPA (2/94) The Practicing CPA (1/84)	Question #16, 17, 18
4. Systematic marketing	Donnelly, Berry, & Thompson (1985) Berry & Parasuraman (1991)	Bell (1990) Marketing (1992) The Practicing CPA (4/85) The Practicing CPA (8/87) The Practicing CPA (1/92)	Question #19, 21

Figure 5.1



Source: Dec. 1995 - Jan. 1996 Researcher's Survey

The formulation of the proactivity index is based on the methodological approach discussed in Dodd et al (1995) for small manufacturing firms. In Dodd's study, a proactivity score was assigned to each company based upon a qualitative assessment of a firm's behavior on each of the following five characteristics. The characteristics were: the firm is strategic, financial data is complete, up-to-date and clear; the company has formal or informal personnel policies developed; the company engages in systematic marketing efforts; and the company is looking to develop a new niche. The concept of performance was operationalized by including several elements: the owner's perception (and definition) of success, the changes occurring in the business over the last five years, gross profit, and management policies. An interviewer assigned a qualitative score for performance to each company. Using Pearson's correlation analysis, a relationship was found between proactivity and overall success ($r=.481$, $p<.01$). The conclusion of the authors was that this correlation indicates that proactive firms were more likely to enjoy overall success than less proactive firms (Dodd, Swinth, and Vinton, 1995). Therefore, proactivity can be used as a surrogate for success and/or growth-orientation.

In the current study of local and regional public accounting firms in the Western New York Region, the proactivity index is quantified, the elements are slightly different, and the measure of economic performance differs. The economic performance of small and medium-size local and regional firms is measured using net income per owner and growth-orientation in terms of revenue. In addition, the differences in proactivity for single-owner versus multi-owner firms are analyzed. The reason that different measures of economic performance are used is to demonstrate that not all small to medium-sized firms are homogenous. Even within the small to medium-sized grouping, different firm characteristics impact economic performance. For example, a CPA may work out of a home to supplement the family income when children are small or to supplement retirement income. The desire for growth in revenue is absent in these firms, and as a result the importance of proactivity differs.

Using the five elements of proactivity (Figure 5.1), an index of proactivity is created by totaling each of the firm's answers to survey questions 13 through 19 and 21. Although the maximum index is 175, the highest index of the 55 firms was 154 and the lowest was 44 (Table 5.3).

Table 5.3: Descriptive Statistics on the Proactivity Index

N	Mean	Median	Standard Deviation	Minimum	Maximum	Quartile	Quartile
55	97.25	97.00	24.79	44.00	154.00	86.00	111.00

Source: Dec. 1995 - Jan. 1996 Researcher's Survey

By using the quartiles as cutoffs, the responding firms are divided into four proactivity groups (Table 5.4) that will be used later in the research. For example, the passive firms are the firms with a proactivity index in the bottom quartile or below 86, and the proactive firms are the firms in the top quartile, that is, firms with a proactivity index greater than or equal to 111.

Table 5.4: Proactivity Groupings

Group	Proactivity Index	Number of Firms
Passive	PI < 86	12
Passive/Reactive	PI 86 - 97	13
Reactive	PI 97 - 110	15
Proactive	PI > 110	15

Source: Dec. 1995 - Jan., 1996 Researcher's Survey

The meaning of the terms passive, passive/reactive, reactive, and proactive are not absolute. Instead, the categorization is meant to show a relative position on a continuum. At the bottom extreme, passive firms "typically respond to actions which competitors initiate; seldom are first to introduce new products, administrative techniques, operating technologies, etc.; and typically seek to avoid competitive clashes" (Covin and Covin, 1990, p. 36). Proactive firms, on the other hand, are described as having a general managerial disposition reflected in a firm's willingness to take on and dominate competitors through a combination of proactive moves and innovative efforts (Covin and Covin, 1990, p.36). In addition, a proactive firm is managed by those who have both the determination and the vision to keep current with the marketplace and can make adjustments necessary to stay on top (Torrence, 1987, p.23). "Proactive firms can be characterized as growing rather than maintaining, being receptive to hearing problems, seeking a new niche rather than entering an existing niche, using financial ratios, having up to date financials rather than using the 'shoe box' method, having personnel policies rather than waiting for problems to arise, and having goals and objectives and following through rather than failing to plan and not following through on goals" (Dodd et al. 1995, p.203). The passive/reactive and reactive firms have some problems that generally are associated with small firms, and include a combination of lack of knowledge of the target market, no systematic accounting procedures, a lack of financial reports, and a lack of personnel policies (Khan and Rocha, 1982).

The methodologies that are used in the following sections include a number of quantitative and qualitative measures. To determine if the proactivity index differs between groups of firms (successful and less successful, single-owner and multi-owner, growth and not growth oriented), the mean Proactivity Index and the means of each element of proactivity is calculated. If each of the group sizes is greater than 25, one way Analysis of Variance (ANOVA) is used to determine if the difference the difference in proactivity is significant. If the group sizes are less than 25, the Student's t-test is used to determine if the differences are statistically significant. Also, in the groups with fewer than 25 firms, the means of the sub-elements are calculated for each group and any difference greater than 1.0 is considered to be significant. A 1.0 difference is used because, on an average, it means that the sub-element is given the next level of importance on a 5.0 point Likert scale (for example, see question 13 and 14 in Appendix A).

5.2 Proactivity and Economic Performance

5.2.1 Proactivity and Success. It is hypothesized that successful local and regional public accounting firms are more proactive than less successful firms. In order to categorize successful and less successful firms, net income before salaries and withdrawals per owner is used. "Successful" firms are identified by a two step process. First, net income before salaries or withdrawals per owner is determined. Second, using a taxonomy published by The Texas Society of Certified Public Accountants in their 1994 Management of an Accounting Practice (MAP) Survey, the firms are categorized as successful (top 50%) or less successful (bottom 50%). This survey is the largest national compilation of CPA firm operating statistics. It excludes the large national and international firms, and has traditionally been used by the local and regional firm to determine how well they are doing in comparison to other firms of the same size. Table 5.5 illustrates the MAP taxonomy. For the individual practitioner group, the firms in the top 50% earned an average of $71,379 per owner.

One of the difficulties with the actual data was the reluctance of the firms to reveal proprietary information. Of the 55 firms responding to the questionnaire, only 23 disclosed their net income. These 23 firms are divided using the above taxonomy resulting in 15 firms falling into the individual practitioner group, 4 firms into the medium-sized, multi-owner group, and 4 firms into the large, multi-owner group (Table 5.5). The only group that contained firms that exceeded the national benchmark of the average value of net income per owner ($71,379) is the individual practitioners. Therefore, this group is used to determine if any differences exist in the proactivity index between the "successful" firms (average net income per owner more than $71,399) and the "less successful" firms (average net income per owner less than $71,399).

Table 5.5: MAP Survey Taxonomy

Firm Group	Net Income per Owner	# of Respondents Reporting Net Income
Individual practitioners	71,379	15
Small multi-owner firms Revenues < $350,000.	55,085	0
Medium-sized multi-owner firms Revenues $350,000 to $900,000	92,560	4
Large, multi-owner firms Revenues >$900,000	128,261	4

Source: Texas Society of CPAs (1994)

The mean proactivity index and the mean index for the five elements of proactivity are calculated for the successful and less successful groups. The firms in the "successful" category had a higher mean proactivity index (104.00) than the less successful firms (82.67). This supports hypothesis H1 that states proactive local and regional public accounting firms are more successful than the others. It also provides support for the assumption that proactivity is a surrogate for success and growth.

The two elements that had the largest differences in their mean values are short-range planning (maximum value is 60) and personnel policies (maximum value is 11). The mean of the short-range planning element is 39 for the successful firms and 26.2 for the less successful firms. The mean value with regard to personnel policies is 7.83 for the successful firms and 4.56 for the less successful firms (Table 5.6). T-test is used to determine whether or not to accept the null hypothesis that there is no significant difference between the successful and less successful firm in the mean value of the proactivity index. Table 5.6 shows that the difference in the overall level of proactivity is statistically significant for the successful and less successful firms. More specifically two elements (short-range planning and personnel policies) differentiate between the successful and less successful firms.

Table 5.6: Difference in the Proactivity Index between Successful and Less- Successful Firms*

Elements	Successful	Less Successful	t-Test	Probability
Long-Range Planning	23.17	21.56	-0.60	0.560
Short-Range Planning	39.00	26.20	-2.39	0.034
Up-To-Date Financials	2.50	2.78	0.33	0.750
Personnel Policies	7.83	4.56	-2.06	0.062
Marketing & Promotion	31.50	27.56	-1.02	0.330
Proactivity Index	104.00	82.70	-2.13	0.055

*Based on net income/owner
Source: Dec. 1995 - Jan. 1996 Researcher's Survey

Short-Range Planning. The difference in the proactivity index for the sub-elements of short-range planning is examined using a 1.0 difference in the mean response between the successful and less successful firms as significant because it indicates, on an average, the next level of importance on a 5 point Likert scale. The sub-elements (Table 5.7) showing a difference greater than 1.0 are: 'setting goals for each part of the business', 'distributing plans to those responsible for execution', 'keeping goals in written form', 'keeping plans in written form', 'reviewing and revising plans', 'considering specific strengths and weakness in making plans', and 'preparing alternate plans for unexpected occurrences'.

Table 5.7: Short-Range Planning: Successful and Less-Successful Firms

	Mean Values		
Sub-Elements	**Successful**	**Less Successful**	**Difference**
Goals are set for each part of the business	3.33	1.67	1.67
Goals are set for the total firm	4.00	3.11	0.89
Goals are kept in written form	3.67	2.11	1.56
Specific strengths/weaknesses are considered in making plans	3.67	2.56	1.11
Plans are based on forecasts	2.50	2.44	0.06
Alternative courses of action are considered in making plans	2.67	2.22	0.44
Plans are kept in written form	3.33	1.89	1.44
Budgets are prepared	3.17	2.33	0.83
Plans are distributed to those responsible for execution	3.17	1.56	1.61
Alternate plans are prepared for unexpected occurrences	2.67	1.67	1.00
A control system is used comparing planned & actual results	3.17	2.22	0.94
Plans are reviewed and revised	3.67	2.44	1.22
Total	39.00	26.20	12.80

Source: Dec. 1995 - Jan. 1996 Researcher's Survey

Some of these differences are attributed to the larger average size of the firm, such as 'keeping goals in written form.' The successful firms employed an average of 6.8 employees, while the less successful firms employed 3.2 on an average. The larger a firm, the more likely to keep goals in written form for distribution to the employees. However, other differences can indicate a more proactive stance on the part of the firm. For example, 'considering strengths and weaknesses in making plans' indicates a thoughtful and analytical approach to setting goals and objectives. Setting goals for each part of the business and distributing them to those responsible provide extra motivation that the goals are accomplished. This fits the definition of proactivity which states that a proactive firm has goals and objectives that are carried out. Staying on top of current conditions by reviewing and revising plans also is characteristic of a proactive stance because it indicates that the firm has the vision to keep current with the marketplace, and make adjustments necessary to stay on top.

Personnel Policies. The difference in the personnel policy element can be explained by the number of employees, a proactive stance toward employees, or a combination of both. As the number of employees grows, personnel policies tend to become more formal. However, in a firm that values its employees, personnel policies can be aimed toward empowering the employee or attracting the best employees by offering better benefits than the competition. The successful firms employed an average of 6.8 employees, while the less successful firms employed 3.2 on an average. This explains the difference in the responses to question #16. The firms were asked what type of personnel policies they had in place: no policies, informal policies, or formal policies.

The successful firms were more likely to have formal policies than the less successful firms. Sixty-seven percent of the successful firms reported having formal personnel policies as compared to only 11 percent of the less successful firms (Table 5.8). At the other extreme, all of the successful firms have some form of personnel policies, whereas 44 percent of the less successful firms lack personnel policies altogether.

The firms were requested to describe the extent of their employee benefits as either having no benefits, some benefits, average benefits, above average benefits, or excellent benefits (question #17). This reflects the firm's commitment toward attracting the best personnel. In a profession that ranks personal attention as the number one factor in giving the firm a competitive advantage, the proactive firm attempts to attract the best and brightest personnel. The majority of the less successful firms had either 'no benefits' (44%) or 'average employee benefits' (44%), while 51 percent of the successful firms had 'average' (17%), 'above average' (17%) or 'excellent benefits' (17%) (Table 5.8).

The firms were also requested to describe the goal of their personnel policies. The goal could either be 'employee maintenance', 'employee development', or 'employee empowerment'. A proactive firm would attempt to empower their employees, or provide the policies that would permit the firm to delegate authority to these employees. Sixty-seven percent of the less successful firms responded the goal of their personnel policies was 'employee maintenance', and only 11 percent stated that the goal of their personnel policies was 'employee empowerment' (Table 5.8). The majority of successful firms, however, responded that their goal was either 'employee development'

(33%) or 'employee empowerment' (50%). Only 17 percent of the successful firms reported that their goal was 'employee maintenance' (Table 5.8).

Table 5.8: Personnel Policies: Successful and Less Successful Categories

	Successful	Less successful
Type of Policies		
None	0%	44%
Informal	33%	44%
Formal	67%	11%
Employee Benefits		
No Benefits	17%	44%
Some Benefits	33%	0%
Average Benefits	17%	44%
Above Average Benefits	17%	0%
Excellent Benefits	17%	11%
Goal of Personnel Policies		
Employee Maintenance	17%	67%
Employee Development	33%	22%
Employee Empowerment	50%	11%

Source: Dec. 1995 - Jan. 1996 Researcher's Survey

It appears that the difference in the personnel policy element of the Proactivity Index can be explained by a combination of a larger size and a more proactive stance that attempts to attract the best employees through offering better benefits than the competition, and developing and empowering these employees once hired. The employees of the successful firms are a firm-specific advantage that provides the firm with its most important source of competitive advantage, i.e., personal attention.

Proactivity and Success Controlling for Size. The successful firms are all in revenue category 3 ($150,001-$300,000) or category 4 ($350,001-$500,000). In addition, a number of less successful firms are also in these revenue categories. Using the firms in revenue category 3 and 4, the Total Proactivity Index was once again larger for the successful firms (104.0 versus 84.67) providing additional support for the hypothesis that states proactive firms are more successful than the others.

Differences also are found in the means of the elements of proactivity. Specifically, the less successful firms placed more importance on long-range planning and up-to-date financials. The successful firms place greater importance on short-range planning, personnel policies, and marketing and promotion strategies (Table 5.9). T-test is used to determine whether or not to accept the null hypothesis that states there is no significant difference in the mean value of the proactivity index between successful and less successful firms. Table 5.9 shows that the mean value of proactivity is significantly different between the successful and less successful firms for the overall Proactivity Index (104.0 versus 84.67) and for the element of short-range planning (39.00 versus 20.33). The null hypothesis for long-range planning, up-to-date financials, personnel policies, and marketing and promotion cannot be rejected.

Table 5.9: Differences in the Proactivity Index between Successful and Less Successful Firms Controlling for Size

Elements	**Successful**	**Less Successful**	**t-Test**	**Probability**
Long-Range Planning	23.17	26.00	0.55	0.640
Short-Range Planning	39.00	20.33	-3.09	0.037
Up-To-Date Financials	2.50	3.00	0.42	0.710
Personnel Policies	7.83	6.33	-1.10	0.320
Marketing & Promotion	31.50	27.56	-1.02	0.330
Proactivity Index	104.00	82.70	-2.13	0.055

Source: Dec. 1995 - Jan. 1996 Researcher's Survey

Differences greater than 1.0 are found in all of the sub-elements of short range planning except 'plans being based on forecasts' and 'budgets are prepared' (Table 5.10). The sub-elements that become more important by controlling for size in short-range planning are: ‘goals are kept for the total firm’, ‘alternative courses of action are considered in making plans’, and a ‘control system is used for comparing planned and actual results’. All of these sub-elements indicate a more proactive stance. ‘Goals kept for the total firm’ and the ‘use of a control system’ depict a more thorough approach to planning. ‘Considering alternative courses of action in making plans’ helps the firm anticipate changes in the environment, and prepare for the changes.

In comparison to the differences listed in Table 5.7, the differences in Table 5.10 are greater for all of the sub-elements.

Table 5.10: Differences in Short-Range Planning elements
Successful and Less Successful Firms*

	Mean Values		
Sub-Elements	**Successful**	**Less successful**	**Difference**
Goals are set for each part of the business	3.33	1.00	2.33
Goals are set for the total firm	4.00	2.33	1.67
Goals are kept in written form	3.67	1.33	2.34
Specific strengths/weaknesses are considered in making plans	3.67	2.00	1.67
Plans are based on forecasts	2.50	2.00	.50
Alternative courses of action are considered in making plans	2.67	1.67	1.00
Plans are kept in written form	3.33	1.33	2.00
Budgets are prepared	3.17	2.33	.84
Plans are distributed to those responsible for execution	3.17	1.33	1.84
Alternate plans are prepared for unexpected occurrences	2.67	1.00	1.67
A control system is used comparing planned/actual results	3.17	2.00	1.17
Plans are reviewed and revised	3.67	2.00	1.67
Total	39.00	20.33	18.67

*Revenue categories 3 & 4 only
Source: Dec. 1995 - Jan. 1996 Researcher's Survey

In Table 5.7, the mean of short-range planning for the less successful firms is 26.20, showing a difference of 12.80 with the successful firms. In Table 5.10, the mean of short-range planning for the less successful firms in Revenue categories 3 & 4 is only 20.33, showing a difference of 18.67. This indicates that the successful firms in revenue categories 3 and 4 place a much greater value on short-range planning than the less successful firms in the same revenue groups.

The average employment size for the less successful firms in revenue categories 3 and 4 is 5.8 employees as compared to 6.8 for the successful firms. Even though the null hypothesis cannot be rejected for the personnel policy element in revenue categories 3 and 4, an analysis indicates the same findings as in the previous section. All of the less successful firms reported either no personnel policies (33%) or informal personnel policies (67%). The successful firms, on the other hand, reported having informal policies 33% of the time and formal polices 67% of the time. The employee benefits offered by the less successful firms were average, and the goals of their personnel policies were either employee maintenance (67%) or employee empowerment (33%). A larger percentage of the successful firms offered above average benefits (17%) or excellent benefits (17%), and 50 percent of the successful firms had employee empowerment as the goal of their personnel policies. Again, the less successful firms did not value their employees as highly as the successful firms.

For the firms in revenue categories 3 and 4, one sub-element that showed a difference of more than 1.0 in marketing and promotion was 'Identifying and Analyzing Target Markets'. The successful firms place a higher value on this than the less successful firms. This activity is indicative of proactivity. It shows that these firms are keeping current with the marketplace (Torrence, 1987). This result is different from the section where all revenue categories were included to measure success. There were no differences of more than 1.0 in either long-range planning or up-to-date financials.

5.2.2 Proactivity and Ownership. In order to investigate whether the Proactivity Index increased with size of the firm, the firms are divided into single-owner (28 firms) and multi-owner firms (27 firms). As the number of owners in a firm increases, it becomes necessary to adopt more control procedures to insure communication to and acceptance by all the owners. For example, written communication will become more important to safeguard against misunderstanding as the number of owners increase. Formal personnel policies will not be as important in a small firm with a few employees as in a larger firm. Therefore, the elements of proactivity may change depending upon the firm size.

The means of the Proactivity Elements and each sub-elements are calculated for both the single-owner and multi-owner firms. The mean Proactivity Index for the single-owner firms is 90.7 and for the multi-owner firms is 104.99 (Table 5.11). The means for the elements of short-range planning, personal policies, and marketing and promotion strategies also show large differences with the multi-owner firms placing more importance on these elements than the single-owner firms (Table 5.11).

Table 5.11: Differences in the Proactivity Index
between Multi-Owner and Single-Owner Firms

Elements	**Multi-Owner (Average Score)**	**Single-Owner (Average Score)**	**Difference**
Long-Range Planning	21.50	22.21	-0.71
Short-Range Planning	38.92	29.89	9.03
Up-To-Date Financials	3.00	2.64	0.36
Personnel Policies	8.19	5.75	2.44
Marketing & Promotion	33.38	29.57	3.81
Proactivity Index	105.00	90.7	24.30

Source: Dec. 1995 - Jan. 1996 Researcher's Survey

Analysis of Variance (ANOVA) shows that statistically significant differences exist between single and multi-owner firms in terms of short-range planning and personnel policies: multi-owner firms are more proactive than the others in short-range planning and personnel policies. The overall index of proactivity is also significantly higher for multi-owner firms (Table 5.12).

Short Range Planning. In the previous section, the two elements under short-range planning that did not differ between the successful and less successful firms in revenue categories 3 & 4 are: 'plans are based on forecasts' and 'budgets are prepared'. These two elements do differ between the single-owner and multi-owner firms indicating a stronger emphasis on planning by basing plans on forecasts, and a stronger emphasis on insuring goals are met by preparing budgets. Both of these sub-elements differ between a single-owner and multi-owner firm because a sole owner may mentally base plans on forecasts and prepare budgets without realizing it. In a multi-owner firm, agreement between the owners is necessary, and the importance of formalizing plans based on forecasts and preparation of budgets becomes more important. In the categorization of successful and less successful firms, all of the firms were sole proprietorships, or single owner firms. Therefore, the difference in these two sub-elements did not appear.

Table 5.12: ANOVA Results-
Multi-Owner Firms Versus Single-Owner Firms

Elements	**F**	**p**
I. Total Proactivity	5.16	.027*
a. Total Long-Range Planning	0.31	.578
b. Total Short-Range Planning	6.40	.014*
Goals are set for each part of the business.	7.40	.009*
Goals are kept in written form	4.80	.033*
Specific Strengths/Weaknesses are considered	7.29	.009*
Plans are based on forecasts	7.93	.007*
Alternative courses of action are considered in making plans	4.27	.044*
Plans are kept in written form	4.42	.040*
Budgets are prepared	4.52	.038*
Plans are distributed to those responsible for execution	8.01	.007*
Alternate plans are prepared for unexpected occurrences	6.23	.016*
Control System	4.88	.032*
Plans are reviewed and revised	4.47	.039*
c. Total Financials	0.62	.044*
d. Total Personnel	15.04	.000*
Employee Benefits	8.94	.004*
e. Total Marketing & Promotion	1.38	.245
Identifying and analyzing target markets	6.19	.016*
Engaging in systematic promotion efforts	8.70	.005*
Personal Selling	5.45	.023*
Associations	10.63	.012*
Sponsorships	6.11	.017*

* Differences significant at the 5% level
Source: Dec. 1995 - Jan. 1996 Researcher's Survey

Personnel Policies. The difference in personnel policies can be explained by the larger number of employees in the multi-owner firms (18.65 vs. 4.86), but also by the firms offering better benefits. Only 24 percent of the single-owner firms have formal personnel policies as compared to 88 percent of the multi-owner firms (Table 5.13). Like the successful firms in the previous section, the multi-owner firms are more proactive by offering better benefits to attract personnel. Fifty percent of the multi-owner firms offer above average benefits (38%) or excellent benefits (12%), whereas only 20 percent of the single-owner firms offer above average (12%) or excellent benefits (8%). The goals of personnel policies are relatively similar between these two groups with 20 percent of the multi-owner firms trying to empower their employees and 17 percent of the single-owner firms doing the same (Table 5.13).

Table 5.13: Personnel Policies: Firms in Single-Owner and Multi-Owner Groups

	Single-Owner	**Multi Owner**
Type of Policies		
None	8%	0%
Informal	69%	12%
Formal	24%	88%
Employee Benefits		
No Benefits	12%	0%
Some Benefits	28%	12%
Average Benefits	40%	38%
Above Average Benefits	12%	38%
Excellent Benefits	8%	12%
Goal of Personnel Policies		
Employee Maintenance	33%	32%
Employee Development	50%	48%
Employee Empowerment	17%	20%

Source: Dec. 1995 - Jan. 1996 Researcher's Survey, Responses to Survey Questions #16,17 & 18.

Marketing and Promotion. The element of marketing and promotion strategies does not show a significant difference at the total level, however, many of the sub-elements do. As a firm becomes larger, more importance is placed on 'identifying and analyzing target markets', 'engaging in systematic promotion efforts', 'the use of personal selling', 'joining associations', and 'sponsoring community events'. Generating a marketing strategy that is constantly recreated to keep abreast of changing markets and changing customer attitudes is indicative of proactivity (Torrence, 1987). Again, like the successful and less successful firms in revenue categories 3 and 4, 'identifying and analyzing target markets' is a differential sub-element, and in section 5.2.4 whether or not the target market is a niche will be analyzed. In summary, as a firm becomes larger, more elements of proactivity are present. This analysis supports H2: as a firm becomes larger in terms of owners, more elements of proactivity will be present. In the case of Western New York, the elements of short-range planning and personnel policies became more important for the larger firms, as did a number of sub-elements in marketing and promotion strategies.

5.2.3 Proactivity and Growth-Orientation. In this section, the sample firms are divided into two categories to gain support for H3 that states that growth-oriented firms have higher levels of proactivity. One of the characteristics of a proactive firm is that it is "growing rather than maintaining" (Dodd et al. 1995). Using question # 22, the responding firms are divided into two categories. The not growth-oriented firms were those which checked survival or maintenance of the status quo as their firm's goal concerning growth. The growth-oriented firms are those which were seeking modest, moderate or aggressive growth. Once again the means are calculated for the Proactivity Index and the Elements of Proactivity, and Student's t-Test is used to determine statistically significant differences between groups. The total Proactivity Index is 101.34 for the growth-oriented firms and 80.91 for the not growth-oriented firms (Table 5.14). The element of proactivity that showed the greatest difference was marketing and promotion (33.52 for the growth-oriented firms compared to 22.91 for the not growth-oriented firms). A proactive firm is one that keeps abreast of changing markets and changing customer attitudes. The growth-oriented firms accomplish this through their marketing and promotion strategies. Proactivity indices based on short-range planning and personnel policies also show statistically significant differences between growth-oriented and not growth-oriented firms.

Table 5.14: Differences in the Proactivity Index
Between Growth- and Not Growth-Oriented Firms

Elements	**Growth-Oriented**	**Not Growth-Oriented**	**t- Test**	**P**
Long-Range Planning	21.82	21.91	0.00	1.000
Short-Range Planning	36.02	27.36	-2.09	0.052
Up-To-Date Financials	2.68	3.18	1.24	0.230
Personnel Policies	7.30	5.55	-1.92	0.076
Marketing & Promotion	33.52	22.91	-4.53	0.000
Total Proactivity	101.34	80.91	-2.70	0.016

Source: Dec. 1995 - Jan. 1996 Researcher's Survey

The sub-elements of short-range planning that have positive differences greater than 1.0 in their means included: 'keeping goals in written form' and 'keeping plans in written form.' In marketing and promotion strategies, the sub-elements with a greater than 1.0 difference include: 'identifying and analyzing target markets'; 'promoting the firm through personal selling'; 'social activities'; 'sponsorships'; and 'board memberships'.

The difference in the personnel policy element can again be explained by the difference in the average number of employees. The growth-oriented firms employ 13 on an average and the not-growth oriented employ 6 on an average. This is one reason why 64 percent of the growth-oriented firms have formal personnel policies as compared to only 20 percent of the not growth oriented firms (Table 5.15). Seventy-seven percent of the growth-oriented firms offer their employees average (36%), above average (29%) or excellent benefits (11%), while only 20 percent of the not-growth oriented firms offered their employees average benefits and none offered above average or excellent benefits (Table 5.15). A slightly larger percent of the growth-oriented firms empower their employees (20%) than do the not growth-oriented (12%) firms (Table 5.15).

Table 5.15: : Percent of Firms in Growth-Oriented and Not Growth-Oriented Groups

	Not-Growth Oriented	Growth-Oriented
Type of Policies		
None	10%	2%
Informal	70%	33%
Formal	20%	64%
Employee Benefits		
No Benefits	10%	7%
Some Benefits	70%	17%
Average Benefits	20%	36%
Above Average Benefits	0%	29%
Excellent Benefits	0%	12%
Goal of Personnel Policies		
Employee Maintenance	44%	30%
Employee Development	44%	50%
Employee Empowerment	12%	20%

Source: Dec. 1995 - Jan. 1996 Researcher's Survey, Responses to Survey Questions #16, 17 & 18

5.2.4 Proactivity, Competitive Advantage, Markets and Collaborative Networks. Competitive advantages in small and medium-sized professional and business service firms are based on several firm-specific and location-specific factors such as the quality of service, range of expertise, flexibility, reputation, customization, price, proximity to clients, and marketing as well as promotion of services (Princeton Training Press, 1992). Categorizing the firms by proactivity group indicates that 'personal attention' is ranked as the most important element of competitive advantage by all four proactivity groups in the WNY sample (Table 5.16). The passive, passive/reactive and reactive firms all rank 'established reputation' as the second most important element of competitive advantage. This factor indirectly suggests the importance of 'trust' in the relationship with clients, especially in a market where repeat business is one of the major sources of income. However, for the proactive firms, the 'ability to adapt' or flexibility, is ranked second. This reflects the basic managerial disposition of the proactive firm which by definition is managed by those who have both the determination and the vision to keep current with the marketplace, and can make adjustments to stay on top (Torrence, 1987, 23). In addition, the importance of three other elements providing a competitive advantage -expertise, creativity, and marketing activities- increase along the continuum of proactivity from passive to proactive. (Table 5.16). Creativity and expertise are required for innovation, and all three are required 'to take on and dominate competitors' (Covin and Covin, 1990,36). These three elements of competitive advantage reflect the importance of scope economies for small and medium-sized firms in professional services.

'Geographical proximity to customers' is given the least importance by the proactive firms as compared to the passive, passive/reactive and reactive firms. The proactive firms may have developed the ability to overcome geographic proximity through their creativity and ability to adapt, as well as through improved communications and information technology. In addition, the proactive group put the least value on price as an element of competitive advantage compared to the other proactivity groups. Being the market leaders and innovators, the proactive firm does not need to compete on a price basis (Table 5.16).

Table 5.16: Competitive Advantage by Proactivity Groups*

Elements of Competitive Advantage	Passive	Pass/React	Reactive	Proactive
Personal Attention	4.83	4.77	4.87	4.80
Established Reputation	4.33	4.25	4.47	4.27
Price	3.83	3.33	4.00	3.27
Expertise	3.50	3.50	3.80	4.00
Quality or Design of Service	3.33	4.00	4.20	4.13
Range of Expertise	3.67	3.50	3.73	3.87
Speed of Service	3.75	3.50	4.13	4.20
Creativity	3.50	3.67	4.07	4.20
Ability to Adapt	3.75	3.75	4.07	4.53
Geographical Proximity to Clients	2.92	2.83	3.07	2.73
Marketing Activities	2.33	2.58	2.80	3.07

* Based on Likert scale (1= not important, 5= critically important)
Source: Dec. 1995 - Jan. 1996 Researcher's Survey

Proactivity is also evident in the manner in which services are promoted and delivered. The importance of 'personal attention' as the main source of competitive advantage indicates that service promotion and delivery would be regarded as key strategic components in retaining and expanding client-base. The methods of promotion considered in this study are use of the media, personal selling, association memberships, social activities, and community involvement. These promotional strategies show the use of both formal (association memberships, sponsorships, and board memberships) and informal (social activities and community involvement) networks in order to establish trust and reputation with clients. Furthermore, the small and medium-sized firm in public accounting also utilize direct personal selling and the media. The use of media and advertising in public accounting is relatively new, and a certain reluctance still exists on the part of public accounting firms to utilize this marketing and promotion strategy. This is evident in the large number of articles published in the profession's publications encouraging the use of advertising (for example, The Praciticng CPA,1985,1987,1992). The importance of personal selling, sponsorships and board memberships for promotion of the firm increase along the proactivity continuum (Table 5.17) These promotional methods involve a personal relationship that help the firm stay on top of the market. Although all of the proactivity groups list personal attention as the most important element of competitive advantage, the proactive group maximize this personal attention in their marketing and promotion strategies in all seven marketing and promotion strategies: media, personal selling, association memberships, social activities, community involvement, sponsorships and board memberships (Table 5.17).

Table 5.17: Importance of Promotion by Proactivity Groups*

Promotion Methods	**Passive**	**Pass/React**	**Reactive**	**Proactive**
Media	1.18	2.00	1.69	2.27
Personal Selling	2.64	3.15	3.62	4.27
Association Memberships	2.18	2.62	2.77	3.20
Social Activities	2.45	3.08	2.85	3.60
Community Involvement	2.27	3.31	2.77	4.00
Sponsorships	1.27	1.69	2.31	2.87
Board Memberships	1.91	2.46	2.62	3.07

*Based on Likert scale (1= not important, 5= critically important)
Source: Dec. 1995 - Jan. 1996 Researcher's Survey

In addition, differences exist in the mode of service delivery along the continuum from the passive to the proactive firms. The three main modes of services delivery are through people talking, through computer files, and through written graphical documents. The older service delivery modes include people talking or presenting written documents face-to-face at the client's or firm's offices or through telephone conversations. These modes of delivery all utilize the top ranked element of competitive advantage for these small and medium-sized public accounting firms - 'personal attention.' The newer modes of delivery - computer file transfer, video conferencing and fax - provide the firm with flexibility in their mode of delivery. By utilizing computers, they increase their speed of service and can quickly adapt to their client's needs. In addition, computers may decrease the need for geographical proximity to clients.

The proactive firms place more importance on all modes of delivery than the passive, passive/reactive and reactive firms (Table 5.18).

Table 5.18: Service Delivery by Proactivity Groups*

Service Delivery	**Passive**	**Pass/React**	**Reactive**	**Proactive**
People Talking:				
Face-to-face (client's office)	3.58	4.23	3.85	4.07
Face-to-face (firm's office)	3.33	4.15	3.92	4.07
Telephone Conversations	3.83	4.23	4.08	4.00
Video conferencing	1.00	0.92	1.08	1.29
Computer File Transfer:				
Via modem	1.00	1.23	1.54	1.93
Via information network	1.00	1.08	1.31	1.36
Local Area Network	1.33	2.15	2.38	2.79
Wide Area Network	1.00	0.92	1.08	1.43
Via Mail/Courier (disks or tapes)	1.67	2.69	2.00	2.86
Written Graphical Documents:				
Face-to-face (at clients)	3.58	4.08	3.62	4.14
Face-to-face (at firm)	3.67	4.08	3.54	4.21
Via Mail/Courier	3.25	2.92	3.62	3.79
Via Fax	3.50	3.08	3.38	3.79

* Based on Likert scale (1= not important, 5= critically important)
Source: Dec. 1995 - Jan. 1996 Researcher's Survey

The modes of delivery that utilize personal attention - face-to-face conversations at the clients or the firms office, face-to-face presentation of graphical/written documents, and telephone conversations - are given an average importance of over 4.0 by the proactive group of firms indicating that the proactive group of firms rate these modes as 'very important.' The proactive firms recognize and utilize their competitive advantage to a greater extent than the other groups of firms. In addition, the importance of file transfer via modem, information networks and local area networks (LAN) increase along the proactivity continuum from passive to proactive (Table 5.18). Again this is indicative of the proactive firm staying on top of the marketplace by utilizing the current technologies. This may also help explain why the proactive group of firms rank the importance of 'geographical proximity to customers' as the least important element of competitive advantage. By utilizing the current technologies, the proactive group of firms has developed the means of overcoming the necessity of geographical proximity to deliver services to clients more than the passive, passive/reactive, and reactive groups of firms.

Niche Markets. Servicing a niche market and participating in collaborative relationships are two determinants of success in small and medium-sized firms that are not considered in the literature on proactivity (Daniels et al. 1988; Brock and Evans, 1989; Porter, 1990; Wood, 1991; Dodd et al. 1995; Batty, 1991; Butler and Hansen, 1991; Snodgrass, 1993; Ozcan, 1995). In sections 5.2, one of the sub-elements that consistently differed between successful and less-successful and growth and not growth-oriented firms is 'identifying and analyzing target markets.' The question arises as to whether these target markets are niche markets?

It is hypothesized that proactive firms serve niche markets more than firms that are not proactive. On an average, 60 percent of all respondents serve a niche. Among the proactivity categories, 67 percent of the passive group, 46 percent of the passive/reactive, 53 percent of the reactive, and 60 percent of the proactive group serve a niche. This finding shows that the hypothesis cannot be supported. It is shown in the next section that 25 percent of the passive firms collaborate with larger accounting firms on a formal or fee paying basis, and may simply be operating as subcontractors to large firms. Therefore, the large percent (67 percent) of passive firms that serve a niche is explained by the fact that their niche is created by the subcontracting strategies of larger accounting firms. Niches served by each proactivity group (Table 5.19) shows that the niche most often utilized by all proactivity groups are service niches followed by industry niches. The niche markets are divided into service niches (23 firms), industry niches (19), geographic niches (7 firms), or other (5 firms). Each firm could select more than one niche. The service niche most often served was taxes (13 firms), the industry niche was construction (7 firms), and the geographic market was the WNY area (7 firms). All of the firms that serve a geographic niche also checked other types of niches.

Table 5.19: Type of Niches Served by Proactivity Groups*

Niches	Passive	Pass./React.	Reactive	Proactive	Total
Service	5	7	5	6	23
Industry	5	2	6	6	19
Geographic	1	2	3	1	7
Other	1	1	3	0	5

*number of firms
Source: Dec. 1995 - Jan. 1996 Researcher's Survey

Table 5.20 shows that the less successful, single owner and not growth-oriented firms serve niche markets more often than the successful, multi-owner and growth-oriented firms (the latter group being more proactive than the former). This further confirms the lack of support for hypothesis H4. Niche marketing may prove to be extremely limited for small and medium-sized public accounting firms especially when they continually face competition from large public accounting firms and other large firms with in-house accounting and accounting-related expertise.

Table 5.20: The Percent of Firms Using Niche Marketing

	Section 5.2.1		Section 5.2.2		Section 5.2.3	
	Success	**Less Success**	**Multi-Owner**	**Single-Owner**	**Growth-Oriented**	**Not Growth-Oriented**
Niche	50%	67%	48%	71%	58%	64%
No Niche	50%	33%	52%	29%	42%	36%

Source: Dec. 1995 - Jan. 1996 Researcher's Survey

Collaborative Relationships. The linkage between collaboration and economic performance has been discussed in the literature on manufacturing firms. There is limited theoretical and empirical work on collaboration in the service industry. Furthermore, the discussions are only limited to large producer service firms (Aharoni, 1995). Several reasons are discussed in the literature explaining how collaborations may improve a firm's competitive advantage -- some of these reasons pertaining to professional services are listed in Table 5.21. The WNY survey show that the two must important reasons for collaboration are to retain existing clients or to expand the range of expertise.

Table 5.21: Reasons for Collaboration
(Each Firm Can Provide More Than One Reason)

Reason	**# of Firms**
Help retain existing client base	12
Expand range of expertise	11
Development of specialist services	6
Provide access to new domestic markets	5
Improve finance and market credibility	5
Assist in management/staff development	4
Provide access to new foreign markets	1
Share research and development costs	0
Other	0

Source: Dec. 1995 - Jan. 1996 Researcher's Survey

The collaborators of public accounting firms are other service firms and other accounting firms. The other service firms such as legal, banking and others provide complementary services. Other accounting firms subcontract work to these small and medium-sized firms (Table 5.22). The survey asked three questions pertaining to collaboration: how many firms collaborated with other service firms (for example, 10 firms collaborated with legal firms), are these collaborations stable (one used every year) and/or formal (indicating payment of fees or other methods of remuneration(, and whether or not such collaborations had any impact on firms economic performance.

Of all respondents (55 firms), 31 percent collaborated. Most firms collaborated with legal, banking, insurance, management consulting, and other accounting firms (more than 5 collaborations a year). These complementary services are also stable. The relationship with other accounting firms are expected to be mainly subcontracting work, therefore, the arrangements are formal (project-by-project basis in some cases). The most important collaborations are with banking, legal, and insurance firms. In many cases, the small and medium-sized public accounting firm serves as the financial advisor to clients who do not have the expertise in-house. Therefore, referrals to reputable banks, lawyers and insurance companies are commonly made by the certified public accountant. In turn, banks, lawyers and insurance companies may also have clients who need a reputable accounting firm. Therefore, referrals are made in both directions.

Collaborations with other accounting firms has a small impact. In general, collaborations with other accounting firms involve outsourcing routine bookkeeping functions that provide flexibility for the outsourcing firm. An example is to outsource tax returns during the busy tax season. The outsourcing firm does not need to hire and train their own employees.

In addition, collaborations with advertising and marketing firms has the small impact indicative of the small and medium-sized public accounting firm's hesitation to participate in this activity. If they do advertising and marketing, they attempt to do it in-house to control the expense of an activity that as a profession has not yet fully recognized the importance of.

Table 5.22: Characteristics of Collaborators and Their Economic Impact

Industry	# of Firms			Average Impact*
	Collaborating	Stable	Formal	
Legal	10	9	1	3.5
Advertising & Marketing	2	1	1	2.0
Other Accounting	12	8	7	2.6
Insurance	7	7	0	3.3
Financial Planners	3	3	0	2.7
Banking	7	7	0	4.0
Management Consulting	6	6	0	3.3
Information Technology	3	3	0	3.0
Computer Companies	3	3	0	2.7
Other	1	1	0	4.0

* Based on Likert scale (1 = no impact, 5 = critically important impact)
Source: Dec. 1995 - Jan., 1996 Researcher's Survey

Thirty-three percent of both the successful and less successful firms collaborate. The multi-owner firms and the growth-oriented firms collaborate more than the average firm in the sample (35%). Forty-one percent of the multi-owner firms use collaborative relationships, and 37 percent of the growth-oriented firms use this type of relationship.

Using the proactivity groups in conjunction with collaborations indicates that 53 percent of the proactive group uses collaborative relationships. This is much higher than the 35 percent average in the survey as a whole. As proactivity increases from the passive/reactive to the proactive group, the use of collaborations increases. Twenty-three percent of the of the passive/reactive group and 26 percent of the reactive group collaborates. Thirty-three percent or 4 firms in the passive group collaborates. Of the four firms that collaborate in the passive group, 3 of the firms collaborate with Other Accounting Firms on a formal basis. Therefore, the passive firms may simply be acting as subcontractors to the larger accounting firms, and not actively seeking business through other channels. In summary, collaboration is used to increase the scope of the firm's service in terms of retaining clients and, at the same time, expanding expertise to gain new clients. This lends support to H5: Proactive firms utilize collaborative networks more often than firms that are not proactive.

Niche, Collaboration and Proactivity. Firms in the proactive group combine the use of niches and collaborative relationships more than the other three groups. Thirty-three percent of the proactive firms combine the use of niches and collaboration, compared to 25 percent of the passive firms, 8 percent of the passive/reactive, and 13 percent of the reactive (Table 5.23). The smallest percentage of the proactive firms (27%) serve a 'niche alone' compared with 42 percent of the passive firms, 38 percent of the passive/reactive, and 40 percent of the reactive. These relationships show that proactive firms are relatively more flexible compared to the other groups in terms of marketing, promotion, delivery, and collaboration. The proactive small and medium-sized firm is expanding its range of expertise through collaborations rather than focusing on a specific niche. Such strategies may also suggest risk avoidance by the small and medium-sized firm in an industrially declining region such as WNY.

Table 5.23: Niches and Collaboration by Proactivity Group

Use of Niches & Networks	Passive	Pass/React.	Reactive	Proactive
No Niche, No Collaboration	25%	38%	33%	20%
Niche Only	42%	38%	40%	27%
Collaborate Only	8%	15%	13%	20%
Both Niche and Collaborate	25%	8%	13%	33%

Source: Dec. 1995 - Jan. 1996 Researcher's Survey

5.3 Proactivity and Location

This section analyses the relationship between proactivity and locational factors. It is hypothesized that proactive firms are able to mitigate locational disadvantages and utilize locational advantages to a greater extent than firms that are not proactive. Dunning (1976), Porter (1990), Rugman (1991), and others present examples and case studies in which locational advantages or disadvantages affect the economic performance of a firm. Locational characteristics such as markets are of critical importance to local and regional firms because most of these firms have limited resources or scope in expanding their services to other geographical markets.

The firms were asked to evaluate the impact of a number of locational factors on their net fees. These factors were WNY's position on a border crossing, Free Trade Agreement, NAFTA, proximity to Toronto, concentration of the medical industry and the financial sector, the large number of educational institutions in the area, the decreasing manufacturing sector, and the WNY economy. The latter two are considered to be locational disadvantages. Two of the locational factors are locational disadvantages: decreasing manufacturing sector and the WNY economy. The declining manufacturing sector is a disadvantage because 31 of the firms listed manufacturing clients as a main client. The other seven are locational advantages. Four of these seven have an international orientation: border crossing, Free Trade Agreement, NAFTA, and proximity to Toronto. The other three locational advantages are the concentration of the medical industry, the concentration of the financial sector, and the large number of educational institutions in the area.

Proactive firms are competitive and flexible. Therefore, the proactive firm should suffer the least as a result of locational disadvantages. In responding to the locational disadvantages (Table 5.24), the smallest percentage of proactive firms responded that the location disadvantages have a negative impact on their net fees, and the largest percentage said that they had no impact. For example, 40 percent of the proactive firms reported that the declining manufacturing sector has a negative impact on their net fees, while a higher percent of the passive, passive/reactive and reactive firms (42%, 62%, 60% respectively) reported the same (Table 5.23). Forty percent of the proactive firms also reported that the declining manufacturing sector did not have any impact on their net fees while a smaller percentage of the passive, passive/reactive, and reactive firms (i.e. 42%, 38%, 39%) responded in the same way. Therefore, the proactive firms appear to have the means to mitigate the negative effects to a greater degree than the other categories of firms

The same pattern held for the second locational disadvantage, the Western New York economy. Forty-seven percent of the proactive firms reported a negative impact as compared to 60 percent of the reactive firms, 77 percent of the passive/reactive, and 50 percent of the passive firms (Table 5.24)

Table 5.24: Negative Effect of Locational Disadvantages on Net Fees

Locational Disadvantage	Passive	Pass./React	Reactive	Proactive
Manufacturing Sector	42%	62%	60%	40%
WNY Economy	50%	77%	60%	47%

Source: Dec. 1995 - Jan. 1996 Researcher's Survey

A greater percentage of proactive firms reported positive effects on net fees due to the four locational factors with an international orientation than the others. For example, 73% of the proactive firms reported a positive impact by being on a border crossing as compared to only 0%, 15%, and 20% of the passive, passive/reactive and reactive firms (Table 5.25)

Table 5.25: Positive Effect of Selected Locational Factors on Net Fees

Locational Factor	Passive	Pass./React	Reactive	Proactive
Border Crossing	0%	15%	20%	73%
Free Trade Agreement	0%	8%	33%	40%
NAFTA	0%	0%	7%	27%
Proximity to Toronto	17%	23%	13%	73%

Source: Dec. 1995 - Jan. 1996 Researcher's Survey

It should be noted, however, that even though the proactive firms are more aware of the positive impact of these locational factors, the majority still believed that no effect existed in relation to FTA (60%) and NAFTA (75%). Therefore, the opportunities afforded by free trade have not yet been fully realized by these firms, or that FTA and NAFTA may not have any direct and short term effect on the small and medium-sized firm in producer services. Similar response to FTA and NAFTA by small and medium-sized manufacturing firms, are shown by others (Bagchi-Sen and Chandra, 1997).

Seventy-three percent of the proactive firms reported a positive impact on their fees as a result of their proximity to the Canada-United States border. None of the passive group report a positive impact, and only 15 percent of the passive/reactive group as well as 20 percent of the reactive group report a positive impact. The Canada-U.S. Free Trade Agreement and NAFTA also had a reported zero positive impact on the net fees of the passive firms, although the percentage of firms reporting a positive impact increased with proactivity (Table 5.25). Proximity to Toronto had no effect on only 27 percent of the proactive firm's net fees, but on 87 percent of the reactive firm's, 77 percent of the passive/reactive firms, and 75 percent of the passive firm's net fees (Table 5.25).

Forty seven percent of the proactive firms reported a positive effect on their net fees as a result of the presence of educational institutions compared with only 25% of the passive firms, 15% of the passive/reactive firms, and 7% of the reactive firms (Table 5.25). However, the majority of firms in all categories still did not report a positive impact. A larger percent of the proactive firms also reported a positive effect of the presence of the medical industry and financial sector than the other groups (Table 5.26).

Table 5.26: Positive Effect of Locational Advantages on Net Fees

Locational Factor	**Passive**	**Passive/ Reactive**	**Reactive**	**Proactive**
Medical Industry	20%	23%	13%	27%
Financial Sector	8%	0%	20%	20%
Educational Institutions	25%	15%	7%	47%

Source: Dec. 1995 - Jan. 1996 Researcher's Survey

All of the proactivity groups reported a negative impact on net fees due to the presence of the medical industry except the proactive group. Eight percent of the passive group, 15 percent of the passive/reactive group and 20 percent of the reactive group report a negative impact. Hospitals and health related facilities are down sizing WNY area (Davis, 1996), and only the proactive group is able to overcome the negative impact of this down sizing. A percentage of all groups report a negative impact from the financial sector - 17 percent of the passive group, 23 percent of the passive/reactive group, 13 percent of the reactive group and 13 percent of the proactive group. This negative effect could be the result of financial institutions expanding the range of their in-house services into areas that the public accounting firm traditionally serve such as personal financial planning and small business consulting .

The majority of firms in all of the proactivity groups reported that the area's educational institutions had no effect or a negative effect - 75 % of the passive group, 85% of the passive/reactive group, 93% of the reactive group and 54% of the proactive group. One firm filled in a comment saying that the educational institutions produced too many accountants for the area. The large percentage of firms in all of the proactivity groups reporting 'no effect' or a 'negative effect' is not surprising. The AICPA has established an Accounting Education Change Commission (AECC) in conjunction with the Big Six Accounting firms in an attempt to change the manner in which accountants are educated. The incorporation of stronger communication skills, critical thinking and ethical considerations into formal education programs is a major goal of this commission.

However, the response in this survey could be based on other considerations by this small and medium-sized group of firms. The major influence on the profession has been by the large, international firms. As stated in Chapter 2, the small and medium-sized public accounting firm is no longer simply willing to act as subcontractors to these large firms, and to passively accept their leadership. When these firms report 'no impact' by the educational institutions, it could be the result of the exclusion of any reference to the unique problems of the small and medium-sized firm in the accounting curricula of educational institutions, or the lack of continuing education for this type of firm offered by the educational institutions in the WNY area. Additional recommendations regarding this are presented in Chapter 8.

It does appear that the proactive group of firms were better able to overcome the effects of locational disadvantages, and were able to benefit the most from the locational advantages. This supports H6: proactive firms are able to mitigate locational disadvantages and utilize locational advantages to a greater extent than firms that are not proactive. However, a large percentage of all groups reports no effect on net fees by each of the location factors.

5.4 Conclusion

First, this chapter analyzed the relationship between proactivity and economic performance. Second, the linkages between proactivity, marketing and collaboration are established. Finally, the interrelationship between proactivity, locational factors, and economic performance is determined. All respondents from WNY are grouped into four proactivity categories based on an index: passive, passive/reactive, reactive, and proactive. This index considered firm level responses to questions on long-range planning, short-range planning, financial statements, personnel policies, and marketing. Economic performance is based on net income and revenue/ownership categories. The findings show that successful, multi-owner (multi-owner firms have large amount of revenue) and growth-oriented firms are more proactive than others. Therefore, proactivity becomes a surrogate of success (that is, higher levels of net income and revenue). Most firms regard the ability to provide personal attention to clients and flexibility as the main sources of competitive advantage. An understanding of sources of competitive advantage and the relationship between proactivity and performance are further explained through the analysis of marketing and promotion, as well as collaborative strategies of these small and medium-sized firms. Proactive or successful firms (also multi-owner and growth-oriented) do not show a preference for serving niche markets. Rather, most firms collaborate to access complementary services such as legal, management consulting, and banking to expand their range of expertise and retain existing clients (some clients may demand a variety of new services). The modes of promotion further justify why the ability to provide personal attention is the main source of competitive advantage. Services are promoted through direct/personal selling as well as through informal and formal networks. The networking activities provide firms with an established reputation and convey a sense of trust to the potential clients. The preferred modes of service delivery are face-to-face contacts with clients but increased use of information technology is also noted for transferring data and documentation. These findings show that pricing or the structure of professional fees does not provide firms with competitive advantages. Therefore, competition or success is based on quality (expertise, range of services, and flexibility) than cost-based. At the same time, these firms are specializing in several markets (service-group, industries, and geographies) and establishing close relationship with clients (it must be noted that repeat business is a major characteristic of the clientele). Quality-based approach and relationship with clients are not based on ad hoc decision making. The results on proactivity show that the two most important elements for success are short-range planning and personnel policies. Short-range planning establishes goals and personnel policies are geared toward improving human capital--this human capital ultimately maintains and improves the firm-client relationship.

The small and medium-sized firms included in this survey serve local and regional markets. Their main clients are within the manufacturing sector -- therefore, most firms except firms in the proactive category indicate that the WNY economy and the declining manufacturing sector have negative impact on net fees. Few firms realize the advantages of being in the cross-border region. Most firms have faced internal and external barriers in expanding their market access international borders (discussed in Chapter 6). Furthermore, most firms indicate that educational institutions are creating an oversupply of accountants and, therefore, are detrimental to the success of these firms. The local and regional firms' opinion regarding the impact of educational institutions may be based on the fact that most institutions train accountants using large firms as models and very few are trained to understand the day-today business activities, problems of the small and medium-sized firm in public accounting. Furthermore, discussion of this topic is beyond the scope of this dissertation. However, this finding suggests that increased communication is necessary between educational institutions and small and medium-sized firms. The next chapter analyzes the interrelationships between proactivity, international orientation, and performance.

'Chapter 6

The Internationalization Status of Local and Regional Public Accounting Firms: WNY

This chapter analyzes the interrelationship between internationalization and proactivity, internationalization and collaboration, and the effect of location factors on the economic performance of accounting firms with various orientations toward internationalization (Table 6.1).

Table 6.1: Research Hypotheses

Hypotheses	
H7:	Local and regional public accounting firms that have internationalized are more proactive than those that have not internationalized.
H8:	Local and regional public accounting firms that have internationalized have more elements of proactivity than those that have not internationalized.
H9:	The average employment size is larger for local and regional public accounting firms with international revenues than the overall average employment size.
H10:	Proactivity reduces the impact of internally determined barriers to internationalization.
H11:	Internal barriers are regarded as larger obstacles to internationalization for the firms not successful at internationalization.
H12:	The largest perceived external barrier to the non-exporting firms is lack-of-reciprocity (licensing requirements).
H13:	The largest external barrier to internationalization of local and regional public accounting firms are cultural differences.
H14:	The use of information technology is more widespread in the firms that have internationalized than in those that have not internationalized.
H15:	Local and regional public accounting firms successful at internationalization have formed strategic networks with other firms.
H16:	The geographical spread of the clients of exporting local and regional firms is wider for the firms that have joined international associations of accountants than for those that have not joined.

6.1 Characteristics of Successfully Internationalized Firms

In this study, internationalization is defined as either rendering management advisory services that will help a domestic client internationalize their operations, or by providing tax, auditing, or other services to foreign companies that have entered the U.S. environment. The respondents showed three types of orientation toward internationalization: 24 firms were not interested in internationalizing, 19 firms were interested but not yet successful, 9 firms had successfully internationalized, and 3 firms did not answer question # 23 giving their international orientation. In the same question, the firms were asked to define success in terms of internationalization. The definitions are summarized as follows: the firm is able to provide a full range of services for entities crossing the border either way; ongoing services are provided whenever required by clients; five percent of total revenues are earned from international sources; and the firm joined a world-wide accounting association.

The average firm successful at internationalization started business in 1963, employed 25 people on a full time basis and had 4 owners. Two of the firms are organized as partnerships, five as professional corporations, and two as other. None of the sole proprietorships in this study characterized themselves as successful at internationalization. Four of the firms are described as local, four as regional and one as national.

Of the top three main clients/sectors served (Table 6.2), a larger percentage of the successfully internationalized firms listed manufacturing (78%) and individuals (67%) as their main clients, and a smaller percentage listed the retail sector (33%) as one of their main clients than did the other firms. The breakdown of revenue (Table 6.2) reveals a greater emphasis on audit and management advisory services, and a relatively smaller emphasis on tax and review and compilations by the successfully internationalized firms than the not successful firm. The successfully internationalized firms earn 37.22 percent of revenue from audit, and 17.44 percent from management advisory services while the not interested and interested, not successful firms earn 16.08 percent and 21.05 percent from audits respectively, and 7.12 percent and 11.74 percent from management advisory services. The internationalized firms are larger and, therefore, have a greater range of expertise on their staff to perform audits, and provide management advisory services. Review and compilations are services offered to smaller clients in place of an audit. This explains why the not interested and the interested, not successful firms earn 13.40 percent and 11.44 percent of their revenue from review and compilation ad compared to only 2.2 percent earned by the successfully internationalized firms. Therefore, the internationalized firms which do more audits have a smaller percentage of their revenue comprised of review and compilations.

The survey revealed that even small and medium-sized firms in public accounting are actively planning to increase their revenues from internationalization. The planning options provided to the firms were: integrate goals into firms mission and planning procedures; quantify the portion of business desired from international arena, identify the type of service to offer in the international arena, identify the foreign origination of the entities to offer these services, establish an international division, join an international association of accountants or formally assign personnel to develop international revenues.

Seven of the nine firms with successful international activities identified the type of services to offer in the international arena, and formally assign personnel to develop international revenues. Three of the firms integrated international goals into the firm's mission statements and planning procedures, identified the foreign origination of the entities to which to offer these services, and joined international associations of accountants. One firm quantified the portion of business desired from the international area, and one also established an international division. All of these actions would indicate a proactive approach toward internationalization. The firms planned to enter the international arena, and made organizational changes to ensure that they were successful at it.

Table 6.2: Characteristics of Firms by International Orientation

	Not Interested	**Interested, Not Successful**	**Successfully Internationalized**
Main Clients			
Individual	58%	42%	67%
Manufacturing	44%	63%	78%
Retailing	44%	53%	33%
Construction	20%	16%	22%
Insurance and Banking	20%	11%	11%
Travel	0%	16%	11%
Medical-Related	32%	5%	11%
Utility	0%	0%	11%
Government	4%	26%	22%
Transportation	8%	21%	11%
Type of Services Offered			
Tax	49.04%	43.11%	37.22%
Audit	16.08%	21.05%	30.22%
Review & Compilation	13.40%	11.44%	2.22%
Mgt. Advisory Services	7.12%	11.74%	17.44%
Other	14.36%	12.66%	12.90%
Total	100.00%	100.00%	100.00%

Source: Dec. 1995 - Jan. 1996 Researcher's Survey

6.2 Internationalization and Economic Performance

6.2.1 Proactivity and Internationalization. The internationalized firms also have a higher mean proactivity index than the firms that had not successfully internationalized (123.30 versus 92.20). This supports hypothesis H7 that states that local and regional accounting firms that have successfully internationalized are more proactive than those that have not successfully internationalized, i.e. 'not interested' and 'interested, not successful'. T-test is used to determine whether or not to accept the null hypothesis that there is no significant difference in the mean value of the proactivity index for successfully internationalized and not successfully internationalized firms. The null hypothesis for the overall Proactivity Index, and the elements of short-range planning and personnel policies can be rejected. In addition, the null hypothesis for the element of marketing & promotion strategies can be rejected at the 10 percent significance level (Table 6.3). The null hypothesis cannot be rejected for the elements of long-range planning and up-to-date financials. Although not statistically significant, the findings indicate a larger emphasis on long-range planning by the successfully internationalized firms.

Table 6.3: Difference in the Proactivity Index
Between Successfully Internationalized and Not Successfully Internationalized Firms

Elements	Successful	Not Successful	t-Test	Probability
Long-Range Planning	23.78	21.46	-1.44	0.17
Short-Range Planning	50.02	31.20	-5.00	0.00
Up-To-Date Financials	2.67	2.80	0.25	0.81
Personnel Policies	9.00	6.54	-4.56	0.00
Marketing & Promotion	37.70	30.20	1.88	0.08
Proactivity Index	123.30	92.20	3.93	0.00

Source: Dec. 1995 - Jan. 1996 Researcher's Survey

Short-Range Planning. The difference in the element of short-range planning is analyzed by calculating the average mean for each of its sub-elements. A difference in the mean of more than 1.0 is considered to be significant because on a 5 point Likert scale it indicates the next higher degree of importance to the firm's planning procedure. All of the elements in short-range planning showed differences of more than 1.0 (Table 6.4). This emphasis on all aspects of planning is characteristic of a proactive firm because it indicates a thoughtful and analytical approach to planning, and the implementation of control measures to insure that the goals and objectives are met.

Table 6.4: Differences in the Means of the Sub-Elements of Short-Range Planning-Successfully Internationalized versus Not Successfully Internationalized Firms

Sub-elements	Successful	Not Successful	Difference
Goals are set for each part of the business	4.11	2.48	1.63
Goals are set for the total firm	4.44	3.22	1.23
Goals are kept in written form	4.00	2.39	1.61
Specific strengths/weaknesses are considered in making plans	4.44	3.09	1.36
Plans are based on forecasts	4.00	2.71	1.29
Alternative courses of action are considered in making plans	4.00	2.51	1.49
Plans are kept in written form	3.89	2.27	1.62
Budgets are prepared	4.44	2.80	1.64
Plans are distributed to those responsible for execution	4.44	2.44	2.00
Alternate plans are prepared for unexpected occurrences	3.78	2.09	1.69
A control system is used comparing planned & actual results	4.33	2.69	1.64
Plans are reviewed and revised	4.33	2.93	1.40
Total	50.02	31.20	18.82

Source: Dec. 1995 - Jan. 1996 Researcher's Survey

Table 6.4 also lends support to hypothesis H8 that local and regional public accounting firms that have internationalized have more elements of proactivity than those that have not internationalized. The successfully internationalized firms place greater importance on a number of proactivity elements in short-range planning than the firms that have not internationalized.

Personnel Policies. All of the firms that had successfully internationalized have formal personnel policies. This could be due to the larger average employment size of the successfully internationalized firms as compared to the not successfully internationalized firms - 25 versus 9 employees. However, the successfully internationalized firms once again showed a higher level of concern for their employees than the not successfully internationalized firms comparing employee benefits and the goal of personnel policies (Table 6.5). All of the internationalized firms had average (44%), above average (44%), or excellent benefits (12%) for their employees. The goals of their personnel policies are employee maintenance (11%), employee development (44%), and employee empowerment (44%). A larger percentage of these firms sought to empower their employees. Again, this is a characteristic of a proactive firm. Offering better benefits than the competitors provides a competitive advantage to the firm by attracting better employees. Empowering the employee, once hired, will provide a labor pool that will act rather than react to a situation.

Table 6.5: Employee Benefits and Goals of Personnel Policies-
Successfully Internationalized Versus Not Successfully Internationalized Firms.

	Successfully Internationalized	Not Successfully Internationalized
Employee Benefits		
No Benefits	0%	7%
Some Benefits	0%	24%
Average Benefits	44%	38%
Above Average Benefits	44%	21%
Excellent Benefits	12%	10%
Goal of Personnel Policies		
Employee Maintenance	11%	38%
Employee Development	44%	50%
Employee Empowerment	44%	13%

Source: Dec. 1995 - Jan. 1996 Researcher's Survey

Marketing and Promotion. The sub-elements in marketing and promotion that have differences greater than 1.0 are: 'identifying and analyzing target markets', 'identifying demand for service/product', 'engaging in systematic promotion efforts', and 'personal selling'. 'Identifying and analyzing target markets' and 'identifying demand for service/product' are characteristics of a firm that is keeping current with the market place, and preparing itself to make adjustments if necessary. 'Engaging in systematic promotion efforts' and 'personal selling' reflects a managerial disposition that seeks out the market. In addition, engaging in personal selling provides the firm with immediate feedback on what the market wants, and provides the means to quickly make adjustments if necessary.

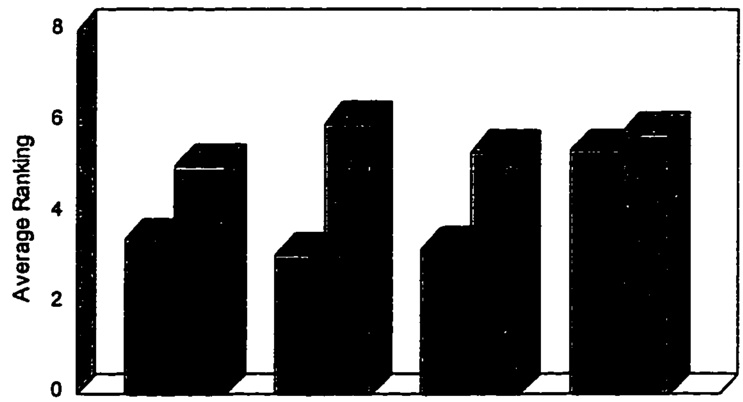
The analysis in this section supports hypothesis H7 that states that the successfully internationalized firm are more proactive than the not successfully internationalized firms, and also supports hypothesis H8 that states that the successfully internationalized firms have more elements of proactivity than the not successfully internationalized firms. The elements of proactivity that are differential are short-range planning, personnel policies and, to a lesser statistical significance, marketing and promotion strategies. Furthermore, hypothesis H9 is substantiated -- the employment size of successfully internationalized firms are on an average higher than the size of employment for the sample as a whole. The successfully internationalized firms had an average employment size of 25, whereas the overall employment size of the sample is 10.

6.2.2 Barriers to Internationalization and Proactivity. This section provides support for hypotheses H10, H11 and H12. The British Overseas Trade Board (BOTB) (1987) found that active exporters dismiss procedural problems such as customs declarations and export documentation as minor inconveniences, while passive exporters and non-exporters saw them as important barriers. In addition, passive and non-exporters perceived financing as a major barrier, but active exporters had little difficulty in acquiring financing. Passive and non-exporters were apprehensive about language barriers, but active exporters did not think language differences were significant obstacles.

McConnell (1977, 1979) has suggested that firm size, financial performance requirements, risk willingness, and the lack of in-house marketing expertise are the largest barriers to export-orientation by small and medium-sized companies. Nothdurft (1992) cites such factors as the lack of executive time and success in home market as barriers to internationalization of businesses by small and medium-sized firms. In accounting, Noyelle and Dutka (1988) suggest that the greatest restrictions are likely to be those on the right of establishment, rather than on the right of individuals to practice (reciprocity). Feketekuty (1986) cites licensing issues, immigration issues, and networking issues as the major barriers to trade in professional services. Categorizing these barriers into internally-determined barriers, as cited by McConnell, Nothdurft, and externally-determined barriers, as cited by Noyelle, Dutka, and Feketekuty, it is the researcher's belief that as a firm becomes more proactive, the internally-determined barriers become less important.

The survey requested the firms to rank a list of obstacles to internationalization from 1 (largest) to 9 (smallest). The internal barriers are size, in-house expertise, financial requirements, time requirements and risk. The external barriers are licensing requirements, right of establishment, immigration issues, and cultural differences. Using the four proactivity groups, the rankings given to the internal and external barriers are summarized. The total score for internal barriers is divided by 5 (the number of internal barriers), and the total score for the external barriers is divided by 4 (the number of the external barriers). A smaller number indicates a larger barrier. For all four proactivity groups, the internal barriers are larger than the external barriers (Figure 6.1). However, the proactive group shows the smallest difference between the internal and external barriers indicating that proactivity helps overcome some of the internal barriers. This supports hypothesis H10 which states that proactivity reduces the impact of internally determined barriers to internationalization.

Figure 6.1: The Ranking of Internal and External Barriers
by Proactivity Groups



Barriers	Passive	Pass./React.	Reactive	Proactive
Internal	3.4	3.09	3.22	5.35
External	5.03	5.94	5.31	5.73

A smaller number indicates a larger barrier

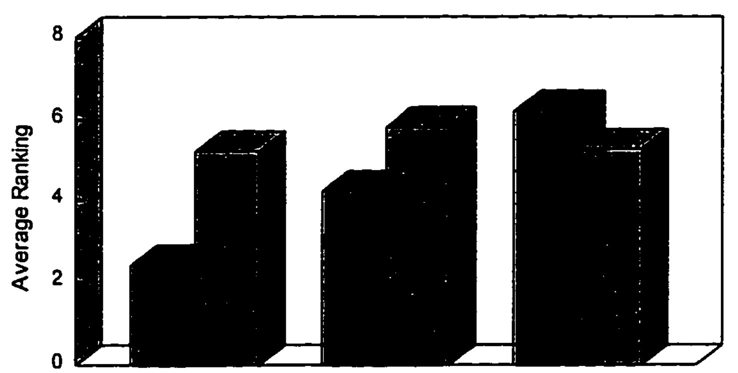
Source: Dec. 1995 - Jan. 1996 Researcher's Survey

Barriers and International Orientation. This section analyzes how the importance of internal and external barriers differ for small and medium-sized firms in public accounting based on their orientation toward internationalization (Hypothesis 11). For both not interested and interested, but not successful groups the internal barriers are ranked as larger obstacles than external barriers (Figure 6.2). In contrast, the external barriers are seen as larger obstacles compared to the internal barriers for the successfully internationalized firms.

Table 6.6 shows how the three groups rank the internal and external barriers. The major barrier for firm 'not interested' in internationalization is size or scale economies. They 'interested, but not successful' firms rank a related category as their major barrier -- the lack of in-house expertise. The successful firms do not regard size of the firm as a barrier -- they consider the amount of time needed to pursue international clients as a major barrier.

The major external barrier for the 'not successful' groups is licensing requirements (the lack of reciprocity) for practicing outside the United States. This finding substantiates hypothesis H12. The successful firms, however, indicate that cultural differences are much more difficult to overcome compared to licensing requirements, the right of establishment, and immigration issues (H13).

Figure 6.2: The Ranking of Internal and External Barriers by International Orientation



Barriers	Not Interested	Interested	Successful
Internal	2.39	4.22	6.2
External	5.21	5.78	5.25

A smaller number indicates a larger barrier.

Source: Dec. 1995 - Jan., 1996 Researcher's Survey

Although licensing requirements, right-of-establishment, and immigration issues are the external barriers most often addressed in free trade agreements, the largest external barrier for the local and regional public accounting firm that has successfully internationalized is expected to be cultural differences (i.e. language, legal, political and religious differences). Local and regional public accounting firms are physically bound to a certain location, and even though they may export their services, they probably will not physically perform work in a foreign country. Their proactivity may be sufficient to overcome the internal barriers, but is not sufficient to overcome cultural barriers. Lack-of-reciprocity and right of establishment will not be viewed as the largest, external barriers because these firms are bound to a certain location because of size.

Firms, however, that do not export may believe that the only method to export their services is by physical presence in a foreign country. Therefore, lack-of- reciprocity (licensing requirements) will be perceived as the largest external barrier to them. The firms were grouped by stage of internationalization, the rankings of each obstacle were averaged by group, and then were ranked. Table 6.6 lends support to hypothesis H13 that states that the largest external barrier for the successfully internationalized firms is cultural differences, and for hypothesis H12 that states the largest perceived barrier for the not successfully internationalized firms is lack of reciprocity (licensing requirements). The firms successful at internationalization, on an average, ranked cultural differences as the number 1 barrier. The firms that had not internationalized ranked licensing requirements as number 6 that gave it the highest ranking of the external barriers. All of the internal barriers, however, still ranked higher for these firms that had not internationalized.

Table 6.6: Average Ranking* of Barriers by International Orientation

Type of Barrier	Not Interested	Interested	Not International**	Successfully Internationalized
Internal barriers:				
Size	1	2	2	7
In-House Expertise	2	1	1	3
Financial Requirements	3	5	4	8
Time Requirements	4	3	3	2
Risk	5	4	5	9
External Barriers:				
Licensing Requirements	6	6	6	4
Right of Establishment	7	7	7	5
Immigration Issues	8	9	8	6
Cultural Differences	9	8	9	1

*1 = largest, 9 = smallest, **Not interested and interested, not successful
Source: Dec. 1995 - Jan., 1996 Researcher's Survey

6.3 Internationalization: Marketing/Promotion, Niche Markets, and Collaborative Relationships

In describing the factors that give the firm a competitive advantage over another (Table 6.7), the firms with all international orientations rank personal attention as the number one factor, followed by established reputation. The internationalized firms placed more importance on expertise, range of expertise, speed of service, and marketing activities as providing competitive advantage than the other firms. They regarded price-based competition and geographic proximity to clients as less important factors determining competitive advantage. The decreased importance of price is a function of lower costs compared to the large multinational firms. The increased importance of marketing activities would be necessary to attract clients in a larger geographic area because firms that are successfully internationalized are competing with the other large international firms. The successfully internationalized firms in the WNY sample have one competitive advantage over the large, multinational firms, and that is the ability to deliver services more efficiently. Therefore, because of their competition in the international arena, price is not as important. The increased importance of expertise and range of expertise is explained by comparison to the other local and regional firms that have not internationalized, and are more likely to service a niche only.

Table 6.7: Average Importance of Factors Contributing to Firm's Competitive Advantage

	Not Successfully Internationalized		Internationalized
Competitive Advantage	**Not Interested**	**Interested**	**Successful**
Personal Attention	4.84	4.79	4.78
Established Reputation	4.28	4.42	4.33
Price	3.80	3.58	3.11
Expertise	3.60	3.79	4.11
Quality of Service	3.60	4.21	4.11
Range of Expertise	3.60	3.79	3.89
Speed of Service	3.84	3.89	4.00
Creativity	3.88	4.05	3.89
Ability to Adapt	3.84	4.21	4.11
Geographical Location	3.00	2.79	2.78
Marketing Activities	2.64	2.63	3.11

Source: Dec. 1995 - Jan., 1996 Researcher's Survey

The promotion and delivery of services also differs for firms with different levels of international orientation (Table 6.8). The importance of all methods of promotion show an increase from the 'not interested firms' to the 'successfully internationalized firms' with the exception of board memberships. The successfully internationalized firms recognize that the major factor of their competitive advantage is personal attention, and place more importance on the methods that utilize personal attention than the not internationalized firms. Personal selling, association memberships, social activities, community service, and sponsorships all require personal interaction.

The delivery of services of the internationalized firms also shows an increased importance of the methods requiring personal attention (Table 6.8). The successfully internationalized firms place more importance on the face-to-face delivery of services at the client's office either through people talking or presenting written documents than the firms that have not successfully internationalized.

In addition, the successfully internationalized firms placed greater importance on the use of information technology (Table 6.8). New information and communications technology may make it possible to transact business in the producer service sector without face-to-face contact. Therefore, these local and regional firms that cannot conquer physical space by locating offices in foreign countries will depend upon new information and communication technology to deliver their services. The successfully internationalized firms place greater importance on the use of local area networks (LAN), wide area networks (WAN), and mailing disks or computer tapes via mail/courier than the firms that have not internationalized. One of the sub-elements of long-range planning in the Proactivity Index is to include a statement concerning the 'technology used'. The successfully internationalized firms considered this sub-element very important in their mission statement, and its mean impact on a 5 point Likert scale was a 4.0. The not successfully internationalized firms considered this sub-element less important, and, for these firms, its mean impact was a 3.4. The greater use of information technology may be aiding these firms overcome the distance barrier in their internationalization process. In addition, it may be a contributing factor to their greater proactivity. They make use of the improved technology that, in turn, makes planning procedures easier and less time-consuming, and makes the delivery of their services more efficient. This analysis supports H14 which states that the use of information technology is more widespread in the firms that have internationalized than in those that have not internationalized.

Table 6.8: The Importance of Promotion and Service Delivery by International Orientation

Methods of Promotion and Delivery	**Not Internationalized**		**Internationalized**
	Not Interested	**Interested**	**Successful**
Promotion of Services:			
Media Advertising	1.67	1.94	2.11
Personal Selling	3.14	3.67	4.56
Association Memberships	2.71	3.00	3.44
Social Activities	3.00	3.17	3.67
Community Service	2.90	3.44	3.78
Sponsorships	1.86	2.28	2.56
Board Memberships	4.33	3.06	3.44
Delivery of Services:			
People Talking:			
At Client's Office	3.81	4.05	4.33
At Firm's Office	3.67	4.05	3.89
Telephone Conversations	3.95	4.00	4.22
Video Conferencing	0.95	1.21	1.11
Computer File Transfer:			
Via Modem to client	1.14	1.84	1.44
Via Information Network	1.19	1.26	1.11
Local Area Network (LAN)	1.52	2.47	3.56
Wide Area Network (WAN)	0.95	1.16	1.44
Via Mail/Courier (disks/tapes)	1.95	2.37	3.11
Written Graphical Documents:			
Face-to-face (Client's Office)	3.57	4.00	4.33
Face-to-face (At Firm)	3.67	3.95	4.11
Via Mail/Courier	2.81	3.47	3.89
Via Fax	3.00	3.63	3.67

Source: Dec. 1995 - Jan., 1996 Researcher's Survey

Niches and Collaborative Relationships. The current study has consistently identified 'analyzing and identifying target markets' as one of the elements of marketing and promotion which shows a significant difference between successful and not successful firms. Section 6.2.4 addresses whether or not these target markets are niches, and the interrelationship between niche marketing, collaborative relationships and proactivity groups. No significant relationship can be established between niche marketing and proactivity. This section explores the relationship between international orientation, niche marketing, and proactivity. Eleven percent of the internationalized firms serve a niche, 22% collaborate, and 33% do both together (Table 6.9).

Table 6.9: The Utilization of Niches and Strategic Networks by International Orientation

	Not Internationalized		**Internationalized**
Use of Niches and Networks	**Not Interested**	**Interested**	**Successful**
Neither	28%	21%	33%
Niche Only	52%	37%	11%
Collaboration Only	8%	21%	22%
Both	12%	21%	33%
Total	100%	100%	100%

Source: Dec. 1995 - Jan., 1996 Researcher's Survey

Comparing this with the proactive group of firms (Table 6.10), the internationalized firms serve a 'niche only' less frequently than the proactive firms. They either serve a niche in combination with collaboration (23%) or do not do neither (33%). This lends additional support to the conclusion of section 6.2.4 that niches by themselves may not be enough for economic success. As the firm becomes larger, the niche should be used as a foundation to develop other relationships. This supports H15 which states that local and regional public accounting firms successful at internationalization have formed strategic networks with other firms.

Table 6.10: Percent of Firms Utilizing Niches and Collaborations-
Successfully Internationalized and Proactive Firms

	International	Proactive	Difference
Neither	33%	20%	13
Niche Only	11%	27%	-16
Collaborate Only	23%	20%	3
Both	33%	33%	0

Source: Dec. 1995 - Jan. 1996 Researcher's Survey

Comparing the type of collaborators used by the internationalized firms with the not internationalized firms also indicates some differences (Table 6.11). Insurance companies, banks and information technology companies are the top ranked collaborators of the internationalized firms. Indeed, all of the collaborations with information technology companies are done with the internationalized firms. In contrast, the top-ranked collaborations of the not internationalized firms are with other accounting firms, followed by legal firms.

Table 6.11: Successfully Internationalized and Not Successfully Internationalized Firms:
Collaborators

Collaborators	Internationalized	Not Internationalized
Information Technology	3	0
Banks	3	4
Insurance Companies	3	4
Legal	2	8
Other Accounting	2	10
Management Consultants	1	5
Computer Companies	1	2
Advertising & Marketing	0	2
Financial Planners	0	3
Other	0	1

Source: Dec. 1995 - Jan. 1996 Researcher's Survey

Only two of the internationalized firms collaborate with other accounting firms, and the mean economic impact of the collaborations is only 1.6 (between zero and minor). Therefore, it appears that other ways exist for small-to-medium size accounting firms to internationalize rather than serving as subcontractors for the larger accounting firms. Table 6.12 also shows that in most cases the collaborations of the internationalized firms are informal. There is no payment of fees between the two collaborators. The largest average impact comes from collaborations with banks, legal firms, and management consulting firms. These collaborations yield clients through referrals (Aharoni, 1995).

Table 6.12: Characteristics of Internationalized Firms' Collaborators-
Stability and Formality of Relationships

Industry	# of Firms			Average Impact*
	Collaborating	Stable	Formal	
Banks	3	3	0	4.0
Insurance	3	3	0	2.6
Information Technology	3	3	0	3.0
Legal	2	1	1	3.6
Accounting	2	2	2	1.6
Management Consulting	1	1	0	3.3
Computer Companies	1	1	0	2.0

*Based on Likert scale (1=no impact, 5=critically important)
Source: Dec. 1995 - Jan. 1996 Researcher's Survey

6.4 Internationalization and Location

This section analyzes how the firms that have successfully internationalized evaluate the impact of the locational factors in the Western New York region on their net fees. All four factors incorporating the advantage of a cross-border location are viewed by the majority of the successfully internationalized firms as having a positive effect on net fees with the exception of --only 44 percent viewed NAFTA as having a positive effect (Table 6.13). Comparing these results with the proactive group of Section 6.3, a larger percentage of the international group indicates a positive effect on net fees (Table 6.13). For example, two-thirds (67%) percent of the successfully internationalized firms report a positive impact on net fees due to the Canada-U.S. Free Trade Agreement as compared to less than half (40%) of the proactive firms. This finding suggests the internationalized firms may have observed some benefits of NAFTA.

Table 6.13: The Positive Effect of Locational Factors With International Orientation: A Comparison Between Successfully Internationalized and Proactive Firms

Locational Factor	**Successfully Internationalized**	**Proactive firms**
Border Crossing	78%	73%
Free Trade Agreement	67%	40%
NAFTA	44%	27%
Toronto	89%	73%

Source: Dec. 1995 - Jan. 1996 Researcher's Survey

Among the locational advantages, the presence of clients in the medical and finance sectors have a positive effect on the net fees of the successfully internationalized firms. For example, over one-half (50%) of the internationalized firm report that the presence of the medical sector has a positive impact on net fees compared to approximately one-fourth (27%) of all proactive firms (this groups includes the internationalized firms). However, a smaller percentage of the international firms report that the educational institutions in the area had a positive impact-47 percent of the proactive group reported a positive effect whereas less than one-fourth (22%) of the international firms report the same (Table 6.13).

Table 6.14: The Positive Effect on Net Fees of Selected Locational Factors: A Comparison Between Successfully Internationalized and Proactive Firms

Locational Factor	Successfully Internationalized	Proactive firms
Medical Industry	56%	27%
Financial Sector	33%	20%
Educational Institutions	22%	47%

Source: Dec. 1995 - Jan. 1996 Researcher's Survey

Various methods are used by the interested and successful firms to obtain the expertise required to internationalize their practice (Question #28). The most important method is to train current personnel outside the practice through professional development seminars and continuing professional education (CPE) activities (Table 6.15). Hiring personnel with formal education in the international field or training current personnel outside the firm through courses at educational institutions are given less importance. This suggests that a deficiency exists in the educational institutions in WNY for training people in accounting for international work (Table 6.15). Therefore, curricular changes are necessary to train accountants proficient in assisting small and medium-sized firms in public accounting to internationalize their practices.

Table 6.15: Methods Used to Obtain Required Expertise in Internationalizing Practices

	International Orientation	
Methods Used	**Interested**	**Successful**
Hiring Practices: Consultants		
Outside Consultants	1.60	1.14
Personnel with previous international work experience	1.40	3.14
Personnel with formal education in international field	1.30	1.71
Training current personnel through:		
In-house professional development seminars	2.50	2.57
Exposure to international work	2.60	3.86
Training current personnel outside through:		
Professional development seminars	3.30	4.14
CPE activities	3.50	4.00
Courses at educational institutions	2.30	2.43

Source: Dec. 1995 - Jan. 1996 Researcher's Survey

The locational disadvantages (the state of the WNY economy and the decline in manufacturing) in dictate a larger negative impact for the internationalized firm vis a vis the proactive group. Forty seven percent of the proactive firms reported that the state of the WNY economy has a negative impact on net fees as compared to 56 percent of the international firms. Similarly, 40 percent of the proactive firms reported the decline in manufacturing to have a negative effect on net fees compared to 67 percent of the international firms. The international firms are more susceptible because the manufacturing sector is the source of their main clients. On the other hand, the decline in manufacturing may have influenced these firms to seek international clients.

Internationalization and the Geographic Spread of Markets. Hypothesis H16 states that the geographical spread of the clients of exporting local and regional firms is wider for the firms that have joined international associations of accountant than for those that have not joined. Although the small and medium-sized public accounting firm does not establish a physical presence in a foreign country, other methods are available to obtain foreign clients. One of these methods is to join an international association of accountants that create a network of accounting firms from different parts of the world. The purpose of these associations is to refer member accounting firms to clients that are internationalizing. Therefore, a small-to-medium size public accounting firm in France may have a client that is either exporting to the WNY area or investing in the area. The French public accounting firm would refer the client to a member firm in WNY. It is expected that the local and regional public accounting firm in the WNY area that has joined an international association would have a wider geographic spread of markets.

Dividing the successfully internationalized firms into two groups- members of international associations and non members- clearly shows that the internationalized firms that have joined international associations of accountant serve a wider geographic area than firms that have not become members of these associations (Table 6.16). The clients of the successfully internationalized firms that have not joined international associations of accountants are located in either Canada (3) or United Kingdom (1). The clients of the successfully internationalized firms that have joined international associations of accountants are located in Canada, Europe, Japan, India, Laos, and Indonesia.

Table 6.16: Geographic Location of Clients of Successfully Internationalized Firms

Country	Members of International Associations	Non Members of International Associations
Canada	4	3
Europe	2	1
Japan	1	0
India	1	0
Laos	1	0
Indonesia	1	0

Source: Dec. 1995 - Jan. 1996 Researcher's Survey

Question #26 in the survey requested the firms interested in internationalization and the successfully internationalized firms to indicate their best export prospects over the next five years (Table 6.17). The number of firms listing European countries (including France, Spain, Germany, and England) equals the number choosing Canada, indicating that these firms anticipate increased business from the European Union equal to their closest geographic neighbor. In addition, the Pacific Rim (Japan, Laos, Indonesia, New Zealand) countries are also viewed as export prospects indicating that the growing importance of this region is also being recognized by the local and regional public accounting firms in the WNY area. Some of these firms also recognize the potential of India and China, and their southern neighbors of Mexico and Peru.

Table 6.17: The Best Export Prospects

Country	Number of Firms
Canada	15
European Countries	15
Pacific Rim	5
India and China	2
Mexico	1
Peru	1

Source: Dec. 1995 - Jan. 1996 Researcher's Survey

6.5 Conclusion

First, this chapter analyzed the characteristics of successfully internationalized local and regional public accounting firms in the Western New York area, and then analyzed the relationship between international orientation and proactivity. Second, the linkages between international orientation, marketing and collaboration are established. Finally, the interrelationships between international orientation, locational factors, and economic performance are determined. All respondents from WNY are grouped into three self-determined international orientations-'not interested in internationalization', 'interested, not yet successful', and 'successfully internationalized.' The findings show that the successfully internationalized firms are larger than the firms that have not internationalized, and that they have higher proactivity indices and more elements of proactivity. The results on proactivity show that the most important elements for success at internationalization is marketing and promotion strategies followed by short-range planning and personnel policies. The internationalized firms place a greater importance on all methods of promotion - media advertising, personal selling association memberships, social activities, community service and sponsorships - with the exception of board memberships. In addition, the internationalized firms are more technically advanced utilizing local and wide area networks more than the firms not successful at internationalization. The internationalized firms, similar to the proactive firms of Chapter 6, also regard the ability to provide personal attention to clients as their main source of competitive advantage. This is translated into their service delivery methods by placing increased importance on face-to-face contact with their clients. In addition, flexibility is also considered to be a major source of their competitive advantage. and the increased importance of local and wide area networks provides them with this flexibility in their service delivery. The internationalized firms also place more importance on speed of service and range of expertise than the proactive firms of Chapter 6. These two elements of competitive advantage indicate that the local and regional public accounting firms are not shying away from the threat of large multinationals; rather these advantages are allowing the local and regional firms to appeal to local clients especially clients who belong to small and medium-sized categories in their respective sectors. Their competitive advantage is based on quality rather than cost-based. The internationalized firms efforts in the promotion and delivery of services show that they are sufficiently aware of the processes necessary to market their services in a larger, geographic area, and to maintain their chief competitive advantage of providing personal attention to clients.

The barriers faced by these firms in the internationalization process include both internal and external ones. Both proactivity and experience at internationalization help the firms overcome the internal barriers which relate to size or scale economies. The external barriers such as licensing requirements, right of establishment and immigration issues cannot be controlled--therefore, these become major barriers to internationalization as soon as they overcome the internal barriers.

One method the internationalized firms utilize to overcome barriers to internationalization are through collaborative relationships which are either formal or informal. Such collaborations are excellent sources of client referrals because most clients prefer to establish a trust-based relationship with their accounting firms. Referrals indicate trust, established reputation, and dependability. Membership in international associations provide the firms with a larger geographic reach. The internationalized firms make a greater use of collaborative networks than the firms that have not internationalized. Contrary to the literature on large, accounting firms (Daniels,), the use of niches are not emphasized by these firms unless utilized in conjunction with collaborations.

The internationalized firms realize the advantages of being in a cross-border region more than the firms that have not internationalized. The declining manufacturing sector and WNY economy negatively affected the net fees of the internationalized firms more than the other location factors. This may have influenced these firms to seek international clients, or to serve their manufacturing clients who chose to internationalize. Only one-fourth of the internationalized firms reported a positive effect on their net fees due to the presence of WNY educational institutions--a similar finding was reported for the proactive firms in chapter 5. It appears that the educational institutions in WNY are not serving the needs the small and medium-sized service firm interested in diversifying their markets. These institutions need to address the needs of these small and medium-sized firms in training programs.

Chapter 7

Conclusions

This research analyzed the determinants of success for small and medium-sized public accounting firms. The analysis is based on a survey of such professional service firms in the Western New York region. The general profile of these firms closely matches the characteristics of the average firm in the Texas survey which is based on a national sample. Two questions are asked by this research. First, what are the determinants of success for these firms? Second, what is their internationalization status? To answer these two questions, several specific questions are asked. What is the relationship between proactivity and economic performance, and what is the source of competitive advantage for these public accounting firms? Are the local and regional public accounting firms in the WNY area internationalizing their practices, and, if so, what characteristics differentiate these firms from the firms that are not internationalizing? What are the true barriers (internal and external) faced by these local and regional public accounting firms in internationalizing their practices, and do these barriers change with proactivity and experience? What types of strategic networks are being used by local and regional public accounting firms? This chapter summarizes the results, and some recommendations are provided to sustain the competitive advantage of these firms in Western New York. In summary, this study focuses upon the interrelationships between proactivity, competition, collaboration, marketing (promotion, pricing, delivery), internationalization, and economic performance.

7.1 Summary

In order to determine what contributes to the success of the local and regional public accounting firm in WNY, the study develops a proactivity index composed of five elements--long-range planning, short-range planning, personnel policies, preparation of up-to-date financial statements, and marketing and promotion policies. Next, the study determines if an association exists between proactivity and economic performance. The empirical evidence shows that as proactivity increases so does the economic success of the firm. Economic success is measured using net income per owner, growth-orientation and ownership characteristics (single versus multi-owners).

The proactivity elements that are given greater importance by the successful, multi-owner, and growth-oriented firms are the short-range planning and personnel policy elements. The most important sub-element (short-range planning) differentiating between successful and less-successful firms is the consideration of specific strengths and weaknesses of the firm in making plans.

In the personnel policy category, the most important sub-elements are 'offering employees better than average or excellent benefits' and 'developing or empowering the employee.' Illeris and Philippe (1993) recognize that the competitive advantage of specialized producer services depends on the qualifications of their staff. The empirical evidence in this study supports these statements. Furthermore, the major source of competitive advantage for these firms is personal attention, therefore, proactive personnel policies are more likely to strengthen such core competencies.

The growth-oriented firms place more importance on marketing and promotion strategies than the not growth-oriented firms. 'Identifying and analyzing target markets' significantly differentiates successful firms from less-successful, multi-owner firms from single owner firms, and growth-oriented firms from not-growth-oriented. A proactive firm seeks out markets rather than waiting for the market to come to it.

The two elements in the Proactivity Index that did not significantly differentiate between groups were long-range planning and up-to-date financials. The accounting profession understands the importance of up-to-date financial statements and would likely prepare them for their own firms. Therefore, this element of proactivity may be a differential element for other types of firms but not for public accounting firms. In the case of long-range planning, the average firm in all of the groups considered it to have a moderate or very important impact on their planning procedures. Therefore, this research does not indicate that long range planning is unimportant, it is simply not an element that differed between the economic performance groupings.

Proactive or successful firms (also multi-owner and growth-oriented) do not show a preference for serving niche markets. Rather, most firms collaborate to access complementary services. One method the internationalized firms utilize to overcome barriers to internationalization are through collaborative relationships-either formal or informal. To provide firms with a larger geographic reach, international associations are used. The internationalized firms make a greater use of collaborative networks than the firms that have not internationalized, and do not emphasize the use of niches unless utilized in conjunction with collaborations.

The proactive firms are also more cognizant of their location. Proactivity helps them overcome locational disadvantages, and make use of locational advantages. Findings reveal that small and medium-sized accounting firms do internationalize. Approximately, 50 percent of the firms either had successfully internationalized or were interested in doing so. The internationalized firms were more proactive than the firms that had not internationalized. A greater importance is placed on marketing and promotion strategies in addition to short-range planning and personnel policies by the internationalized firms than by the firms that had not internationalized. In addition, the internationalized firms are larger in terms of employees and revenues, and also place greater importance on the use of information technology.

The largest barriers faced by these firms are internal barriers, although as a firm moves along the proactivity continuum, the impact of the internal barriers decreases as compared to the external barriers. Also, as the firm internationalizes, the external barriers become greater than the internal barriers. Because the local and regional public accounting firm is not interested in physically locating an office in another country, the external barriers of licensing requirements, right-of-establishment, and immigration issues are viewed as smaller barriers than cultural differences (i.e. language, legal, political and religious differences). Although the majority of these firms listed Canada as their main export market, the surveyed firms are interested in a much larger geographic market which includes European, Pacific Rim, Asian, and South American countries.

7.2 Recommendations

Based on this study, the recommendations for public accounting firms and the profession are as follows: first, the available opportunities for the small and medium-sized service firm in the global market must be studied and well-publicized. Second, the small and medium-sized service firm must be able to identify their true abilities, and determine how these abilities can be utilized for economic success in the internationalization process. Third, easier access to databanks and information should be made available to these firms.

The chief obstacle that must first be removed to promote the internationalization of local and regional public accounting firms is the lack of recognition by these firms of their own potential to embark upon international business activities. Although they may be aware of the impact of the global marketplace on other types of businesses, the visualization of themselves as "local" and "regional" may hinder their expansion into this marketplace. Many of these small and medium-sized accounting firms experience a natural resistance to internationalization. These firms feel that any such initiative will be a burden on their already limited managerial and financial resources. Any deviation of their attention from local and regional markets could be perceived as a serious mistake. Findings from this study demonstrate that small and medium-sized service firms can benefit from internationalization, and may assist other WNY firms to expand their client-base. In addition, educational institutions and professional societies, such as the AICPA and the state-level societies, may be encouraged to develop programs that will help the local and regional firm identify opportunities beyond the local and regional markets. In too many cases, programs run by the professional societies are designed by professionals whose background and experience have been shaped by their experience in large firms. These societies have to recognize that the needs of the small and medium-sized firm are both different and important.

As part of the internationalization process, the small and medium-sized firm must determine its strengths and weaknesses (United Nations, 1993). The internationalized firms in this study place greater importance on considering specific strengths and weaknesses in making plans than the firms that had not internationalized. This research, therefore, emphasizes that a firm must evaluate its potential before internationalizing. The proactivity index can be used as a starting point to determine the areas in which changes may be necessary to strengthen the competitive advantage of these firms in the international market.

Small and medium-sized enterprises usually experience difficulties in accessing information through data banks because such information may not be easily interpreted or amenable to decision-making. Furthermore, small and medium-sized enterprises have limited managerial resources and are not usually familiar with electronic data banks. These data banks are often located on the premises of governmental or private organizations that are not physically accessible and the use of such data sources may require compliance with certain regulations. In order to facilitate the availability, access, and use of such databases, efforts should be made to increase the number of focal points through which firms can approach data banks; and access procedures should be simplified. This study pointed out that only 22 percent of the firms that had successfully internationalized believed that educational institutions had a positive effect on their fees. One recommendation would be to have the area's educational institutions include seminars on the availability and use of these data banks for the small and medium-sized service firm. In addition, more educational institutions should provide access to the data banks, including the smaller private colleges. The large, state institutions should consider providing remote access to users of their data banks.

The study also indicated that collaborative relationships were important for the successful and internationalized firms. Are any mechanisms in place at various levels that would facilitate these collaborative relationships? Web sites, such as Alta Vista and Excite, are available listing trade leads for industrial companies. Perhaps establishing sites for potential service company collaborations is also necessary. The professional societies can also facilitate these collaborative relationships by holding joint meetings with Canadian accounting societies across the border, and by designating a portion of their monthly newsletter to listing opportunities for collaborative relationships. In addition, the professional accounting societies should consider holding joint meetings with societies in other fields such as the Financial Executives Institute (FEI).

7.3 Future Research

As noted earlier, proactiveness and economic performance are associated, with the successful firms more able to allocate resources to proactive strategies. It is also possible that firms allocating resources to proactive strategies may suffer if the environment changes quickly in an unanticipated direction. Those allocated resources may not be available to help effect a rapid shift in activities. Longitudinal studies would help determine if these relationships existed. In the first scenario, a longitudinal study would trace when the proactive strategies were put into place. Was it a frame of mind or priority from the start of the business, or was it established as the business gained a certain amount of success? In the second scenario, it is assumed that a firm allocating resources to proactive strategies is more likely to be positioned for change than a firm not engaging in proactive strategies. Therefore, such an organization is more likely to be able to re-tool than an organization that has not been looking forward. A longitudinal study would help determine if in times of sudden change, a proactive firm was more successful than a reactive or passive firm.

One of the methods that these local and regional public accounting firms utilized to widen their geographic reach was collaborative relationships. Future research should focus on a detailed evaluation of the economic benefits of these networking strategies, and how they evolve over time. Finally, a greater recognition of particular locational advantages existed in the proactive firms. Research should be conducted on the ways that these firms become aware of locational advantages, and proceed in making use of them. This will help provide empirical evidence for the Porter's (1990) concept of competitive advantage and contribute to Rugman's (1993) efforts to find methods to operationalize the diamond.

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APPENDIX A:

SURVEY AND ACCOMPANYING LETTERS

Note: A number of questions in the survey were based in whole or in part on the work of Dodd et al. (1995) and Beyers and Lindahl (1994). Their contribution to this study is gratefully acknowledged.

UNIVERSITY AT BUFFALO
STATE UNIVERSITY OF NEW YORK

CANADA-UNITED STATES TRADE CENTER
Alan D. MacPherson, Director
(716) 645-2299
Fax: (716) 645-2329

December 21, 1995

Dear Managing Partner,

I am studying local and regional public accounting firms in the Western New York area for my doctoral research. The role of the local and regional firms and their importance to the Accounting Profession merits more attention than previously given. Policies aiding and promoting these firms can lead to economic development in a region. It is my goal to generate the needed data to emphasize the importance of these firms to the appropriate policy making bodies in the region.

Your cooperation in filling out the enclosed questionnaire is of utmost importance to me. I assure you that in no way will I try to identify your firm, and I will not disclose any firm-level information. The whole analysis will be based on aggregation of data from over 200 questionnaires. If you are interested in the data summary, please enclose your business card or send it to my attention in a separate envelope at the above address any time before March 30, 1996, and I will forward you a copy of my results.

Enclosed is also a letter of endorsement by Peter Bellante, President of the Buffalo Chapter of the New York State Society of CPAs asking your cooperation in returning this survey. Most questions ask for rough estimates only, or yes/no answers. Skip any items that you feel uncomfortable with, and feel free to add written comments at any point. I would appreciate it if you could return the survey in the enclosed stamped, addressed envelope before January 15, 1996.

Thank you for your time and cooperation.

Sincerely,
Linda Kuechler
Linda Kuechler, CPA, CMA

Department of Geography, Wilkeson Quadrangle, Ellicott Complex, Box 610023, Buffalo, New York 14261-0023

Fiddler and Company
Certified Public Accountants

One Towne Centre
501 John James Audubon Pkwy.
Amherst, New York 14228
716-688-4343 Fax 716-688-4875

Joseph A. Fiddler, CPA
1893 - 1976

Joseph DiMatteo, CPA
John E. Peter, CPA
Peter X. Bellanti, CPA
John LaMonte, CPA
Robert R. Closs, CPA

ASSOCIATE
Joseph H. Mergler, CPA

December 15, 1995

Dear Managing Partner

I would like to urge you to take the time to fill out the enclosed survey sent by Linda Kuechler, CPA. She is presently in the process of completing her PhD, and the data gathered through this survey is of the utmost importance in enabling her to do so.

Linda has been a practitioner and academician since 1974. She is very interested in promoting the importance of the local and regional public accounting firm, and this survey will help her collect the data to do so.

Thank you.

Sincerely,

FIDDLER AND COMPANY

Peter X. Bellanti, CPA

Section A: General Business Characteristics

1. In what year did your firm first start doing business? ____________

2. Which of the following most closely describes your firm?

☐ Local ☐ Regional ☐ National ☐ International

3. Is your firm a

☐ Partnership ☐ Professional Corporation ☐ Sole Proprietorship
☐ Other *(Please specify)*____________

4. What was your firm's total revenues in 1994?

☐ Under $ 50,000
☐ $ 50,001 - $150,000
☐ $ 150,001 - $350,000
☐ $ 350,001 - $500,000
☐ $ 500,001 - $ 650,000
☐ $ 650,001 - $ 850,000
☐ $ 850,000 - $1,000,000
☐ Over $1,000,000

5. What was your firm's annual average growth rate in revenues in the last five years? ___%

6. Please indicate below the total number of personnel in each category.

NOTE: For the purposes of this survey, **professionals** mean client service professionals only, and are defined as CPAs, prospective CPAs, and others with a similar amount of academic training in a field that is part of the practice of public accounting (e.g. consulting). Partners and others in equivalent positions (such as Shareholders) should be excluded in the above definition, and be placed in own category.

	PARTNERS/ OWNERS		SUPERVISORS & MANAGERS		PROFESSIONALS		CLERICAL	
	MALE	FEMALE	MALE	FEMALE	MALE	FEMALE	MALE	FEMALE
FULL-TIME								
PART-TIME .... REGULAR								
.......AS-NEEDED								

7. For the categories below, what was the firm's 1994 amount and average five year annual growth rate?

Category	1994 Amount	Average annual growth rate
Total Net Fees	$__________	___%
Firm Net Income	$__________	___%
Earnings from internationalization *	$__________	___%

NOTE: * In the context of this survey, internationalization is defined as either rendering management advisory services that will help a domestic client internationalize their operations, or by providing tax, auditing, or other services to foreign companies that have entered the U.S. environment.

8. **Please indicate the approximate percentage breakdown of your firm's total revenues in 1994.**

Audit	_____%
Tax Preparation, Planning, Representation	_____%
Management Advisory Services	_____%
Securities Advice	_____%
Mergers & Acquisitions	_____%
Business Valuations	_____%
Litigation Support	_____%
Bankruptcy (Insolvency) Services	_____%
Market and Economic Feasibility Studies	_____%
Executive Searches	_____%
Computer Hardware Sales	_____%
Computer Software Sales	_____%
Computer Hardware Selection & Installation (Other than Sales)	_____%
Computer Software Selection & Installation (Other than Sales)	_____%
Other *(Please specify)* _________________	_____%

9. **How would you describe the following factors in giving your firm a competitive advantage? Give a number response to each of the following statements, ranging from 1 (not important) to 5 (critically important).** ***(Circle one number for each statement.)***

FACTORS	Zero	Minor	Moderate	Very Important	Critically Important
Personal attention to client's needs........................	1	2	3	4	5
Established Reputation..	1	2	3	4	5
Price of Services...	1	2	3	4	5
Specialized expertise	1	2	3	4	5
Product/service quality or design...........................	1	2	3	4	5
Range of expertise	1	2	3	4	5
Speed of Service..	1	2	3	4	5
Creativity...	1	2	3	4	5
Ability to quickly adapt to shifting client needs.....	1	2	3	4	5
Geographical proximity to clients..........................	1	2	3	4	5
Marketing activities/capabilities............................	1	2	3	4	5
Other *(Please specify)*..	1	2	3	4	5
....					

10. **What impact do you feel that your location in Western New York has had on your firm in relation to the following items:**

	Positive Impact (↑ Net Fees)	Negative Impact (↓ Net Fees)	No Impact (No Effect)
WNY Economy..	☐	☐	☐
Border Crossing......................................	☐	☐	☐
Free Trade Agreement.............................	☐	☐	☐
NAFTA..	☐	☐	☐
Proximity to Toronto...............................	☐	☐	☐
Decreasing Manufacturing Sector............	☐	☐	☐
Concentration of Medical Industry..........	☐	☐	☐
Concentration of Financial Sector...........	☐	☐	☐
Large number of Educational Institutions	☐	☐	☐

11. How would you describe your main clients? ***(Check one or more of the boxes below.)***

- ☐ manufacturing/industrial firms
- ☐ retail
- ☐ insurance, banks or finance
- ☐ travel and tourism-related firms
- ☐ utility companies (e.g. oil, gas, power)
- ☐ individuals
- ☐ government markets
- ☐ transportation companies
- ☐ medical equipment and supply firms, hospitals, or health-care facilities
- ☐ other (please specify) ______

12. Does your firm collaborate with other firms, i.e. enter into either formal arrangements (e.g. subcontracting work) or simply work as a team on particular projects or network to obtain clients?

☐**Yes** ☐**No** ***(Please go to question 13)***

If you do collaborate, from the following list, check the industries of your collaborators. Also, check boxes if the collaboration is stable (one used every year) and/or formal (involving the payment of fees or other remuneration).

Industries	Stable	Formal
☐ Legal	☐	☐
☐ Advertising & Marketing	☐	☐
☐ Other Accounting	☐	☐
☐ Insurance	☐	☐
☐ Financial Planners	☐	☐
☐ Banking	☐	☐
☐ Management Consulting	☐	☐
☐ Information Technology	☐	☐
☐ Computer Hardware/Software Co.	☐	☐
☐ Other *(Please specify)* ______	☐	☐

Check a number from 1 (not important) to 5 (critically important) indicating the impact of the collaboration on your firm's economic success. ***(Circle one number for each statement).***

INDUSTRIES	Zero	Minor	Moderate	Very Important	Critically Important
Legal	1	2	3	4	5
Advertising & Marketing	1	2	3	4	5
Other Accounting	1	2	3	4	5
Clerical/Bookkeeping	1	2	3	4	5
Insurance	1	2	3	4	5
Financial Planners	1	2	3	4	5
Banking	1	2	3	4	5
Management Consulting	1	2	3	4	5
Information Technology	1	2	3	4	5
Computer Hardware or Software Companies	1	2	3	4	5
Other *(Please specify)* ______	1	2	3	4	5

What are the reasons for your collaborations? ***Check as many as applicable.***

- ☐ Expand Range of Expertise
- ☐ Provide Access to New Foreign Markets
- ☐ Improve Finance and Market Credibility
- ☐ Assist in Management/ Staff Development
- ☐ Development of Specialist Services
- ☐ Provide Access to New Domestic Markets
- ☐ Help Retain Existing Client Base
- ☐ Share Research and Development Costs
- ☐ Other *(Please specify)* ______

Section B: Planning Procedures

13. In developing a mission statement for your firm, which of the following factors are considered? Give a number response to each of the following statements, ranging from 1 (not important) to 5 (critically important). ***(Circle one number for each statement.)***

Mission statement includes:	Zero	Minor	Moderate	Very Important	Critically Important
Basic type of product/service offered......................	1	2	3	4	5
Primary markets or customer groups served............	1	2	3	4	5
Technology used...	1	2	3	4	5
Geographic Domain...	1	2	3	4	5
Concern for survival through growth/profitability...	1	2	3	4	5
Managerial philosophy and/or public image the firms seeks..	1	2	3	4	5
Other *(Please specify)*...	1	2	3	4	5
....					

14. Describe the planning procedures your firm utilizes. Give a number response to each of the following statements, ranging from 1 (not important) to 5 (critically important). ***(Circle one number for each statement.)***

The planning procedures followed by the firm are:	Zero	Minor	Moderate	Very Important	Critically Important
Goals are set for each part of business....................................	1	2	3	4	5
Goals are set for the total firm..	1	2	3	4	5
Goals are kept in written form..	1	2	3	4	5
Specific strengths/weaknesses are considered in making plans	1	2	3	4	5
Plans are based on forecasts..	1	2	3	4	5
Alternative courses of action are considered in making plans..	1	2	3	4	5
Plans are kept in written form..	1	2	3	4	5
Budgets are prepared..	1	2	3	4	5
Plans are distributed to those responsible for execution............	1	2	3	4	5
Alternate plans are prepared for unexpected occurrences.........	1	2	3	4	5
A control system is used comparing planned & actual results..	1	2	3	4	5
Plans are reviewed and revised..	1	2	3	4	5

15. How often does your firm prepare up-to-date financial statements for itself?

☐ monthly ☐ quarterly ☐ semi-annually ☐ annually

16. Which of the following statements best describes the firm's personnel policies:

☐ No policies ☐ Informal policies ☐ Formal policies

17. Which of the following statements best describes the firm's employee benefits:

☐ No benefits ☐ Some benefits ☐ Average benefits
☐ Above average benefits ☐ Excellent benefits

18. Which of the following statements best describes the goal of the firm's personnel policies:

☐ Employee maintenance ☐ Employee development ☐ Employee empowerment

19. In your marketing efforts, which of the following factors have been considered. Give a number response to each of the following statements, ranging from 1 (not important) to 5 (critically important). ***(Circle one number for each statement.)***

Marketing efforts include:	Zero	Minor	Moderate	Very Important	Critically Important
Identifying and analyzing target markets...............................	1	2	3	4	5
Identifying demand for service/product.................................	1	2	3	4	5
Analyzing price and establishing systematic pricing policy..	1	2	3	4	5
Engaging in systematic promotion efforts.............................	1	2	3	4	5
Other *(Please specify)*...	1	2	3	4	5
....					

20. Do you believe that your firm serves a specific market? ☐**Yes** ☐ **No**

If yes, how would you describe that specific market? *Check all that are applicable*

☐ particular service (e.g. taxes) *(Please specify)* ____________________

☐ particular industry (e.g. healthcare) *(Please specify)* ____________________

☐ particular geographic location (e.g. Canada) *(Please specify)* ____________________

☐ other *(Please specify)* ____________________

21. What methods does your firm routinely use to systematically promote your services? Give a number response to each of the following statements, ranging from 1 (not important) to 5 (critically important). ***(Circle one number for each statement.)***

Promotion methods include:	Zero	Minor	Moderate	Very Important	Critically Important
Media Advertising..	1	2	3	4	5
Personal Selling..	1	2	3	4	5
Association Memberships................................	1	2	3	4	5
Social Activities..	1	2	3	4	5
Community Service...	1	2	3	4	5
Sponsorships..	1	2	3	4	5
Board Memberships...	1	2	3	4	5
Other *(Please specify)*....................................	1	2	3	4	5
....					

22. How would you describe your firm's goal concerning growth?

☐ Aggressive growth - 20.0% or more growth in revenues per year

☐ Moderate growth - 10.1% - 19.9% growth in revenues per year

☐ Modest growth - 1.0% - 10.0% growth in revenues per year

☐ Maintenance of status quo - no growth in revenues

☐ Survival - 1.0% or more decrease in revenues per year

Section C: Internationalization

23. How would you describe your firm's current position regarding internationalization, given the definition at the beginning of this survey?

☐ Not interested in internationalization ☐ Attempting to internationalize, but not yet successful
☐ Successfully internationalized. *What is your definition of success and in what year did you internationalize?* ______________________________

24. What are the largest obstacles concerning internationalization of the firm's practice? If you have actually internationalized, please answer in regard to the actual obstacles faced. If you are attempting to internationalize or are not interested in internationalization, please answer in regard to the perceived obstacles faced. Rank the following obstacles with *1 the largest and 9 the smallest.*

Obstacles:	Rank Order (1=Largest, 9=Smallest)
Size of Firm..	__________
Financial Requirements..	__________
Risk Willingness..	__________
Lack of In-House Expertise in Internationalization..	__________
Management Time Requirements............................	__________
Licensing Requirements..	__________
Right-of-Establishment..	__________
Immigration Issues...	__________
Cultural Differences (differences in language, legal and political systems)	__________

25. How do you deliver services to your clients? Give a number response to each of the following statements, ranging from 1 (never used) to 5 (always). *(Circle one number for each statement.)*

How services are delivered:	Never Used				Always Used
People Talking:					
Face-to-face Conversations (at client's office)	1	2	3	4	5
Face-to-face Conversations (at firm's office)..	1	2	3	4	5
Telephone Conversations................................	1	2	3	4	5
Video Conferencing...	1	2	3	4	5
Computer File Transfer:					
Via Modem (direct to client)..........................	1	2	3	4	5
Via Information Network (e.g., E-mail, Internet, Compuserve, Time-share mainframe)	1	2	3	4	5
Local Area Network......................................	1	2	3	4	5
Wide Area Network.......................................	1	2	3	4	5
Via Mail/Courier (mailing disks or tapes)......	1	2	3	4	5
Written/Graphical Documents:					
Face-to-Face (at clients)................................	1	2	3	4	5
Face-to-Face (at firm)....................................	1	2	3	4	5
Via Mail/Courier..	1	2	3	4	5
Via Fax..	1	2	3	4	5
Other (*Please specify*):__________	1	2	3	4	5

If you have foreign clients, do you deliver your services to your foreign clients any differently than marked above? ☐ **Yes** ☐ **No**

IF YOUR FIRM IS NOT INTERESTED IN INTERNATIONALIZING, PLEASE STOP HERE.

26. If you currently perform services for foreign entities, please specify and rank the top three countries of these entities. Also indicate where you expect to see the best export prospects over the next five years.

Current Export Markets	Best Export Prospects
1. ____________	1. ____________
2. ____________	2. ____________
3. ____________	3. ____________

27. If you are actively working to increase revenues from internationalization, please check the actions your firm has taken to accomplish this and, if appropriate, specify the particular action.

- ☐ Integrated international goals into firm's mission statements and planning procedures.
- ☐ Quantified the portion of business desired from the international arena.
  Please specify what portion of business is desired from the international arena ____________
- ☐ Identified the type of services to offer in the international arena.
  Please specify the type of services your firm will offer in the international arena ____________
- ☐ Identified the foreign origination of the entities to which to offer these services.
- ☐ Established an international division.
- ☐ Joined an International Association of Accountants. *Please specify which one* ____________
- ☐ Formally assigned personnel to develop international revenues.
  Please specify the number assigned at each level and check box if their compensation is tied into developing international revenues.

Level	*Number assigned*	*Compensation Tied In*
Partner	____________	☐
Manager	____________	☐
Supervisor	____________	☐
Senior	____________	☐

28. What methods are you using to obtain the required expertise in internationalizing your practice? Give a number response to each of the following statements, ranging from 1 (not used) to 5 (critically important). ***(Circle one number of each statement.)***

Methods Used	Zero	Minor	Moderate	Very Important	Critically Important
Hiring Outside Consultants..............................	1	2	3	4	5
Hiring Personnel with Previous International Work Experience	1	2	3	4	5
Hiring Personnel with Formal Education in the International Field (e.g. through college courses)	1	2	3	4	5
Training current personnel in-house through:					
in-house professional development seminars	1	2	3	4	5
exposure to international work..................	1	2	3	4	5
Training current personnel outside through:					
professional development seminars...........	1	2	3	4	5
CPE activities...	1	2	3	4	5
courses at educational institutions.............	1	2	3	4	5
Other *(Please specify)*..	1	2	3	4	5

THANK YOU FOR YOUR TIME AND INPUT