



The Role of the External Accountant in Small Firms

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Abstract

This paper details a second stage of a study into the use of small business computerised accounting systems (CAS), together with the role and impact of the accountant across businesses that use and do not use computerised systems. The most popular accounting software product is MYOB and the CAS was predominantly used for operational activities rather than for strategic purposes. Despite many owner-managers implementing a CAS, there was still a heavy reliance on accountants to review financial statements and to perform bookkeeping services. In fact, non-CAS users tended to utilise accountants' services less than computerised accounting businesses. The findings of this study would be useful for accountants in determining marketing strategies for their small business clients, and for small business owners in general in encouraging them to utilise a CAS to provide more cost effective accounting information.

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1.0 Introduction

There has been a renewed interest in the record keeping procedures and financial management approach taken by small firms in Australia since the introduction of the Goods and Services Tax (GST) in 2000. It is generally accepted that there is a greater level of usage of Computerised Accounting Systems (CAS) since the GST commenced.

This paper reports on a study initially designed to determine the influences that motivated the use of a CAS as well as the factors that hindered the introduction of a CAS. A secondary stage of the study considered the role of the accountant in this new post GST era.

The external accountant is a key support agent in the management of small firms and their influence on the introduction of a CAS is investigated. The tasks carried out by the external accountant in small firms that use a CAS is compared with those tasks carried out in small firms that do not use a CAS. Other issues that are investigated include the frequency of meetings with the accountant and the likely impediments to increasing the number of such visits.

The paper begins with a review of the literature on accountants' services to small business and the influence of information technology on the financial management of such firms. The methodology undertaken in the study is then described in the following section. The results section describes the sample groups and then proceeds to discuss the issues around the usage of a CAS. Then there is a report on how frequently the small firm operator meets with their accountant and the impediments to meeting more often. The paper concludes with a discussion of some of the opportunities for accountants to help their small business clients to improve the financial management of their business.

2.0 Literature Review

Sound financial management is crucial to the survival and growth of small business (McMahon and Holmes 1991; Gorton 1999). A major reason for small business failure is poor or careless financial management (Berryman 1983; Peacock 1985; Hall and Young 1993). The need to take control of financial management, coupled with improved accounting software and more powerful hardware systems appears to be the driving factors behind owner-managers' adoption of IT. It is anticipated that small business financial management practices have improved since the widespread embracement of computerised accounting packages. Research suggests, however, that accounting software is mainly used to perform basic operational functions such as the recording of sales, the payment of suppliers, the purchase of inventory, and the like (Lai 1994).

McMahon and Holmes (1991) reported that in contrast to the amount of financial information available, the actual use of financial reports by owner-managers was limited. They believed that several studies overstated the depth and quality of analysis undertaken. Gorton (1999) undertook a comparative UK study of SMEs that used financial management techniques and those that didn't. He found that just over half of the 366 SME respondents produced a financial plan. Just over two-thirds maintained a CAS although the emphasis was on operational, rather than strategic aspects. Four-in-ten respondents in Gorton's (1999) study set no annual financial targets. Overall, Gorton quantified the importance of planned financial management through the setting of financial plans and the maintenance of comprehensive accounting systems.

To ensure financial management success, small business owner-managers need to be more forward thinking and proactive in their management style; setting goals, broad strategic direction and undertaking planning and operational controls necessary to achieve targets (McMahon and Holmes, 1991). This suggests that the use of financial management data should evolve from a support function



to more strategic purposes. For a small business to become more strategically oriented, however, they need to explore ways of using the financial management information to generate business opportunities. Gorton (1999) found some relationship between the use of a CAS and strategic orientation. Firms which constructed a financial plan at start-up were more likely to be employing a CAS and were more likely to be high-growth firms. These findings are supported by Smith (1999) who found that the greater the use of IT, the higher the businesses' performance in terms of return on capital and sales per employee; and by Reid and Smith (2002) who argue that efficient information processing plays a vital role in successful firms. A further explanation for the link between SME financial reporting, performance and growth is that SME growth results in increased financial challenges. Consequently, there is a greater need for careful attention to financial management and financial reporting, if the growing SME is to succeed and prosper (McMahon 2001). This led McMahon (2001) to conclude that improved financial control in growing SMEs can and should come about through a significant upgrading of financial reporting systems.

The major benefits of implementing a CAS are to make the execution of business processes more efficient and timely, and to take control of financial management. For example, in the Burgess (1997) study, the top two ranked benefits of IT were *increased business efficiency* and *better access to information*. It could be argued that these benefits represent a time and cost saving to the small business. Nowadays, small business accounting software is relatively affordable for even the smallest of business, so why have some owner-managers chosen not to implement a computerised system given the benefits?

Research suggests that lack of time is the major reason why small business owner-managers do not implement a CAS (Proudlock et al. 1999). This lack of time is not simply due to the time required to research the market place for suitable accounting software, but also to implement the software and to input day-to-day transactions. The cost of computerising the accounting system is also an obstacle to adoption. Many small business owner-managers that do not have a CAS perceive it as a costly venture (Head 2000). Other concerns small business owners have are that the system is too complex and onerous to operate, lack of IT knowledge and the perception that IT will be of little benefit to the business (Proudlock et al. 1999). The Australian Bureau of Statistics (ABS) 1999-2000: Business Use of Information Technology noted other concerns about the adoption of IT. The ABS found that the largest barrier to using IT was the perception that the technology was not suited to the nature of the business (47% of non-user respondents) and the lack of skills and training (36% of non-user respondents). The Burgess (1997) study, which involved both IT users and non-users, indicated that the major IT problems were: inefficient use of the technology, lack of IT expertise, and lack of planning for implementation and training.

In Australia, the introduction of the Goods and Services Tax (GST) on 1st July 2000 encouraged many small businesses to upgrade their accounting systems; either by improving their existing computerised system or by replacing their manual accounting system with a computerised one. There is much anecdotal evidence in newspapers and journals as to the impact of the GST on small business record keeping practices, although we could not source any empirical studies on the impact of GST on accounting computerisation in Australia. In New Zealand, however, Lief (2000) found that many NZ small businesses computerised their accounting systems following the introduction of GST because post-GST manual accounting methods were too onerous to maintain.

The Australian Government set in place a number of mechanisms to reduce the cost burden to small business in accounting for the GST. For example, the Australian Tax Office (ATO) permitted an immediate write-off of GST related software for businesses with a turnover of less than \$10 million. In addition, the ATO produced a free software package called e-Record and made it available to small business. A further strategy was to give small businesses \$250 to assist with the transition to GST. It



was the small business owner-manager's discretion as to how they applied this income to the burden of the GST transition, however, many used the finance to purchase GST compliant accounting software. The implementation of the GST, together with the Australian Government incentives to improve GST record keeping, encouraged many small business owner-managers to implement a computerized accounting information system.

Some of the concerns regarding time constraints on the sourcing and implementation of accounting software can be overcome by the use of an external accountant. Accountants spend much of their time on compliance work (ASCPA 1992; Breen et al. 1994) because of its standardised nature and higher return (Oran 1988). On the other hand, many small business owner-managers are not aware of the additional services provided by accountants (Oran 1988; and Shannon 1986). Furthermore, many accountants are not consulted by the owner-manager until a problem arises (Holmes 1987). Accountants are uniquely placed to provide accounting software advice and support to their clients as business owners value the recommendations made by their accounting firms in choosing accounting software. Such recommendations are an efficient and effective way for small businesses to select accounting software (Wenzler 1996). Gorton (1999) found that businesses in the start-up phase were more likely to approach an external accountant for advice than more mature businesses.

3.0 Methodology

This study involved a telephone-based interview with two separate groups of small business operators. The study commenced with a review of the literature followed by a focus group discussion with a few small business operators to clarify the issues and formulate the research questions. The next step was the development of two separate questionnaires - one for CAS users and the other for non-users. The questionnaire for CAS users focussed on the motivation for using a CAS to perform the accounting function. The non-user's questionnaire concentrated on the impediments to CAS use and the incentives that would encourage CAS use. Both questionnaires also included a range of questions designed to ascertain the role of the external accountant in the financial management of the small business.

Respondents were selected from two databases. The first database (Dun & Bradstreet) consisted of a selection of two thousand small firms from their Dunsfile *Business Who's Who*. The parameters placed on the selection of firms included firm size of five employees or less and firms located in the state of Victoria. The choice of smaller firms was made on the understanding that larger firms were more likely to use a computerised accounting package and therefore would not be useful to this research.

The second database was sourced from participants of the New Enterprise Incentive Scheme (NEIS) program. Because of the confidential nature of client information, and the more recent introduction of privacy legislation, it was necessary to engage two administrators of NEIS (Business Enterprise Centres) to conduct the telephone interviews on behalf of the researchers with a selection of firms from their databases. All telephone interviewers were given a set script to follow.

As a result of this process, the data collected consisted of 221 completed questionnaires from a total of 122 firms that use a CAS and a further 99 firms that did not. The data collected from these interviews was entered into the SPSS statistical computer package for analysis.



4.0 Findings

4.1 Sample characteristics

There were some clear differences between the two groups surveyed. The non-user group tended to be smaller than the user group, with a significant group of non-employing businesses (53%) among those not using a CAS. More than one-third of CAS users (34.2%) had more than 5 employees, whereas only 6.6% of non-users had that number of employees. The non-users also involved smaller businesses with respect to their annual sales turnover. Only one firm in the non-user group had a turnover in excess of \$1 million, whereas one-in-five (19.3%) of the CAS users had that level of turnover. Almost three-quarters of non-users had turnover of less than \$50,000. The non-users were more likely to be in less information-intensive industries (such as trades and services) while the CAS users were more likely to be in information-intensive industries such as manufacturing and retail.

4.2 Use of Computerised Accounting Systems

In the total sample, 122 owner-managers (55%) used a CAS and 99 (45%) did not. This section focuses on those businesses that used a computerised accounting system. Owner-managers were asked what influenced them to use a CAS. Thirty-eight percent were influenced by the need to account for the GST and a further 26.2% indicated they were influenced by their accountant.

Table 1		Accounting Software Vendor	
Vendor			%
MYOB			54.9
Quickbooks			24.6
Cashflow Manager			2.5
Attache			2.5
Tailor-made software			4.1
Other			11.4
Total			100.0

Referring to Table 1, *MYOB* was the most popular choice of package (54.9%) followed by *Quickbooks* (24.6%). A few respondents used *Cashflow Manager* (2.5%) and *Attache* (2.5%). Only 4.1% indicated they used tailor-made software. In terms of who entered the data in the CAS, on most occasions it was completed in-house either by a member of staff (40.2%), or by the owner-manager (25.4%). Approximately one-third of owner-managers reported that data entry was performed externally, usually by the accountant.

The software is predominantly used to produce financial statements (see Table 2) such as the Balance Sheet (77.9%), the Profit and Loss statement (76.2%) and the Cash Flow statement (63.1%). About three-quarters of owner-managers (73%) use the CAS to produce BAS statements. Other uses of the CAS were for Debtors aged-analysis (59.0%), Bank reconciliations (54.1%) and Group certificates (51.6%). Less than half of the owner-managers (44.3%) used the CAS for inventory reports.

Table 2		The CAS is used to produce:	
Report			%



Balance Sheet	77.9
Profit and Loss	76.2
BAS Statements	73.0
Cash Flow Statement	63.1
Aged Debtors	59.0
Bank Reconciliation	54.1
Group Certificates	51.6
Inventory reports	44.3
	N=122

Consistent with the literature, the CAS is used mainly to perform operational functions (Table 3). Most owner-managers used the system for invoicing (87.7%), to prepare the cash book (73.8%), for payroll (68.0%) and for purchasing (66.4%). Fewer respondents used the system for more strategic decision making purposes such as budgeting (59.0%) and inventory control (56.5%). It would appear that the CAS is predominantly used to prepare financial statements, satisfy GST reporting requirements, and to perform basic operational functions. In the next section, it is evident that many CAS users, still utilise an accountant to assist with business advice (apart from the standard tax return and GST compliance work) (see Table 4).

Table 3		Tasks the CAS is used for:
Report		%
Invoicing		87.7
Cash book		73.8
Payroll		68.0
Purchasing		66.4
Budgets		59.0
Inventory control		56.5
		N=122

In relation to *who* uses the reports generated by the CAS, 71.3% were used by the owner or management, 20.5% by the accountant and 6.6% by both groups. Two owner-managers indicated that the reports were not used at all.

4.3 Use of the Accountant

The following section is based on the total sample of 221 businesses and focuses on issues relating to the owner-manager's relationship with their accountant. Wherever practical, comparisons are drawn between CAS Users and Non-Users. Overall, eighty-nine percent of the total sample used an accountant with a higher proportion of CAS-users (98%) than non-users (78%) using an accountant. Owner-managers were asked to specify the tasks performed by the accountant (Table 4).

Table 4		What tasks are performed by the accountant:		
		CAS-	CAS	Total



	users %	non-users %	%
Tax Return	86.6	89.0	87.5
Financial statements	63.0	30.1	50.5
GST compliance	52.1	24.7	41.7
General business advice	47.9	25.7	39.6
Bookkeeping	33.6	16.4	27.1
	N=119	N=73	N=192

Since accountants offer a range of services to their small business clients, there was usually more than one response to this question, consequently, the percentages do not total 100. It is interesting to note that CAS-users tended to utilise a range of accountant's services, while non-users tended to use the accountant mainly for tax return preparation. This could be a function of the sample where non-users were predominantly younger and smaller firms. While about three-quarters of CAS-users stated they used the software to generate financial statements (see Table 2), 63.0% still used the accountant to assist with financial statements. Perhaps for some, the accountant was used to check the validity of the statements prepared. Only 30.1% of non-users got their accountant to prepare their financial statements, suggesting that far fewer of this group use financial statements as part of their financial management. In terms of accounting for GST, just over half (52.1%) of CAS-users consulted the accountant while only 24.7% of non-users consulted on GST compliance. Again, this could be due to the low turnover of the non-users rendering them outside of the GST \$50,000 compliance net. It would be expected that in the future accountants would spend less of their time on GST compliance work as the small business owner became more familiar with the procedures involved. Moreover, accounting software suppliers are now marketing GST compliant software, which could extend to Business Activity Statements (BAS), much in the same way that tax return software packages are now available.

In terms of general business advice, far more CAS-users (47.9%) than non-users (25.7%) took advantage of this service. The overall results were consistent with the literature where the major service provided by accountants is tax return and compliance work. While typically, general business advice and bookkeeping represents a smaller proportion of accountant's work.

One-third of CAS-users used their accountant for bookkeeping services (Table 4). This is significant given that these small businesses have a CAS yet they still use an accountant to assist with bookkeeping. In comparison, only about one-in-six of the non-users (16.4%) used their accountant for bookkeeping services.

Overall, about one-quarter (23.3%) of owner-managers met with their accountant once per year (Table 5). A much higher proportion of CAS non-users (37.2%) met with the accountant yearly. This is clearly related to the fact that most of the non-user businesses only used the accountant for taxation matters as indicated in the previous section (see Table 4). CAS-users tended to meet with their accountant more regularly with just under one-third (32.0%) meeting weekly or monthly. Only 18.6% of CAS non-users met that often with their accountant. Overall one-in-three of the owner-managers (34.4%) met with their accountant quarterly. Given the regularity of meetings, the accountant is in a privileged position to review the computerised system and its output and make suggestions for its improvement. This is supported by the fact that one quarter of respondents (26.2%) stated that their accountant influenced their decision to use accounting software.



Table 5	How often do you meet with your accountant?		
	CAS- users %	CAS non-users %	Total %
Weekly	5.9	2.9	4.8
Monthly	26.1	15.7	22.2
Quarterly	38.7	27.1	34.4
Half yearly	14.3	17.1	15.3
Yearly	15.1	37.2	23.3
	N=119	N=70	N=189

Slightly less than one-half of non-users would hold more meetings with their accountant if not for the cost of those meetings (Table 6). The non-users, however, tended to be younger and smaller businesses, consequently they probably have not yet accumulated adequate financial resources to pay for accountant's services (other than taxation compliance work). About one-quarter (24.6%) of non-users did not yet perceive any benefit in visiting the accountant more often and a further 22.8% did not have the available time. This is not a function of CAS non-users per se, but a function of resource poverty where younger, smaller businesses tend to lack financial and available time resources (Thong 1999). The majority of CAS-users, who already visited the accountant regularly, did not perceive any impediments to holding more meetings with their accountant (58.0%).

Table 6	Impediments to holding more meetings with your accountant:		
	CAS- users %	CAS non-users %	Total %
Cost	16.8	45.6	26.1
Perceived benefit	7.6	24.6	13.1
Time	5.9	22.8	11.4
Other	11.8	0.0	8.0
No Impediment	58.0	7.0	41.5
	N=119	N=57	N=176

Owner-managers were further asked whether they believed there were additional benefits in meeting with their accountant more often. Overall, about one-in-five (21.9%) of owner-managers felt there would be benefits and 78.1% said there would be no benefit. A slightly higher proportion of non-users (29.4%) felt there would be benefits in meeting their accountant more often.

5.0 Discussion and Conclusions

The findings of this study confirm the results of earlier studies (Lai 1994) that much of the work involved in a CAS is of an operational nature rather than strategic. Given that only 59.0% of CAS Users report that they use the CAS for budgeting there is still a great deal of scope for small business operators to use their CAS for more strategic purposes.

Even though the CAS Users have their records managed with the aid of a computer, a far greater proportion of them use their accountant to provide both bookkeeping and financial management



assistance than those who are described as non-users. Furthermore they also meet with their accountant more often than the non-users group. This finding indicates that the introduction of a CAS should not be seen as a threat to the accountant, but rather an opportunity.

The CAS Users are more likely to use their accountant for a wide range of services including the preparation of financial statements and general business advice. These services tend to be higher value adding for the business and more profitable for the accountant. So clearly there are financial benefits for accountants as well as financial management benefits for the small business when a small business client migrates to a CAS.

Given the findings of Gorton (1999) that the start-up stage is the most opportune time for the accountant to discuss proposed computerised record keeping practices, and the findings of this study that accountants are a key influence in encouraging their small business clients to adopt a CAS, then accountants should be promoting the benefits of a CAS from their very first interaction with a small business client.

This study highlights the opportunities that exist for accountants to improve the financial management performance of small firms. They can influence early starters to introduce a CAS so these small businesses have better records of their financial activities. Within their client group who already have a CAS they can encourage them to make more strategic use of their financial data to improve the performance of the small business. Finally they can also provide value added services to their small business clients to help them to improve their business performance.



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