CHAPTER 3

LITERATURE REVIEW

3.1 INTRODUCTION

This chapter provides an overview of the extant outsourcing literature. The remainder of the chapter is organised as follows. Section 3.2 describes the definition of outsourcing. Section 3.3 discusses the advantages and disadvantages of outsourcing. The role of the transaction cost economics (TCE) theory on outsourcing decision is discussed in Section 3.4. Section 3.5 offers a discussion on the role resource-based view (RBV) on outsourcing. Section 3.6 provides an explanation of the role of the resource based and transaction cost economic perspectives on the relationship between outsourcing and firm performance. The association between transaction cost economics (TCE) theory and resource- based view (RBV) is provided in Section 3.7. Section 3.8 presents and discusses the role that professional accountants play in the SME environment and accounting functions that are outsourced by SMEs. The chapter concludes with Section 3.9.

3.2 DEFINITIONS OF OUTSOURCING

The term outsourcing was created at the end of the 1980s for contracting out information systems (Espino Rodríguez and Padrón-Robaina 2004; Hussey and Jenster 2003). For example, in the past, most subcontracted functions related to information systems or component manufacture, even though, in recent years, many other service functions in various sectors have been outsourced (i.e., accounting functions, administration services, human resources activities, catering services, logistics, and etc) (Espino Rodríguez and Padrón-Robaina, 2004; Espino-Rodríguez and Rodríguez-Díaz, 2008; Carey et al., 2006). Primarily the emphasis is on outsourcing support and professional activities in firms, such as accounting functions or human resources (Caniëls and Roeleveld, 2009). The word outsourcing is seen to be synonymous with the decision to externalise (Espino Rodríguez and Padrón-Robaina, 2004, 2006). For instance, many claim that outsourcing involves processing outside the firm to obtain specific activities or services that are not provided inside the firm (Hamzah et al., 2010; Espino-Rodríguez and Padrón-Robaina, 2006). Overall, outsourcing is usually explained as the contracting with an external service provider to provide a service function (Carey et al., 2006; Espino Rodríguez and Padrón-Robaina 2004). Therefore, Hamzah et al. (2010) defined outsourcing as a process of transferring the responsibility for a specific activity from an internal staff to an external service provider. However, outsourcing has different meanings for diverse business activities. For example, the process of outsourcing of accounting involves the 'external accountant,' including both the professional accountant and the accounting firm on one hand (Everaert et al., 2007). On the other hand, the process of internalising of accounting includes the 'in-house accountant' who is the business staff member carrying out the accounting functions in the firm (Everaert et al., 2007).

In general, most SMEs delegate part or all the accounting functions to professional accountants, but most LEs traditionally perform accounting functions internally (Nicholson et al., 2006; Wood, Barrar, Jones and O'Sullivan, 2001). Table 3.1 summaries the definitions of outsourcing from the different business functions perspectives.

Table 3.1: Definitions of Outsourcing in Business Functions

Activities	Definitions	Source
Manufacturing Operations	Relying on external sources to undertake manufacturing activities and other value-adding activities by manufacturing firms	Ehie (2001)
Information Technology (IT)	External vendors or suppliers supply labour and materials in handling the particular components of the IT infrastructure in the firm	Loh and Venkatraman, (1992)
Logistic	The transfer of logistic functions such as outbound transportation, inbound transportation, freight bill auditing/payment, warehousing and freight consolidation/distribution to the logistic external vendors	Cho, Ozment and Sink (2008)
Human resource management	Includes employing an external service provider to manage a firm's human resource functions such as people, processes and technologies	Pelham (2002)
Accounting	Accounting outsourcing means transferring all or part of accounting functions to an external (professional) accountant with the intention of cutting cost, get access to skills and obtain competitive advantage	Hamzah et al., (2010); Everaert et al. (2007)

3.3 ADVANTAGES AND DISADVANTAGES OF OUTSOURCING

The extant outsourcing literature evidences that outsourcing practice can significantly benefit the SMEs or can prove to be equally disastrous depending on how well it is planned and performed. Advantages and disadvantages of outsourcing practice are identified. These are discussed next.

3.3.1 Advantages of Outsourcing Practice

Five main advantages of outsourcing have been identified, namely, access to expertise; cost reduction; affords a focus on core business; enhances innovation; and alleviates time pressure (Hamzah et al., 2010; O'Connor and Martinsons, 2006). These are discussed as follows:

3.3.1.1 Access to Expertise

Most SMEs need expertise to conduct their business operations successfully (Blackburn et al., 2010). Evidently, SMEs can develop long-term strategic relationships with their external accountants (Blackburn et al., 2010). In fact, SMEs can benefit from higher capabilities, technical competence (expertise) and new investment in resources that an external service provider can provide to their firm (Jayabalan et al., 2009; CIMA, 2008). Consequently, outsourcing enhances managerial control, skill, and as well capacity, and stability in SME environment (Rittenberg and Covaleski, 2001). For example, professional accountants are often highly specialised in the provision of accounting activities, permitting them to provide at lower costs than the smaller firms could do internally due to scale economies (Hamzah et al., 2010; Jayabalan et al., 2009).

3.3.1.2 Cost Reduction

Another important advantage of outsourcing is cost reduction (Kotabe and Mol, 2009; Görg and Hanley, 2004; Rittenberg and Covaleski, 2001; Quélin and Duhamel, 2003). For instance, SMEs can lessen working capital, increase tax efficiency and reduce excessive capital expenditure by outsourcing their accounting activities (CIMA, 2008; Hamzah et al., 2010). Outsourcing reduces many types of employment and administrative costs by decreasing the capital investment required to improve processes (Rittenberg and Covaleski, 2001; Espino Rodríguez and Padrón-Robaina, 2004; Kotabe and Mol, 2009). Outsourcing may reduce overhead costs and induce short-term cost savings (Caniëls and Roeleveld, 2009; Ngwenyama and Bryson, 1999).

More importantly, the activities carried out by the external service providers represent their core competences and so those service providers are able to offer the services at a lower cost than the SME can carry out internally (Espino Rodríguez and Padrón-Robaina, 2004; Heshmati 2003; Jiang, Frazier and Prater, 2006). For example, Blumberg (1998) reported that outsourcing could generate economic advantages that may diminish costs by between 20 percent and 40 percent. Hence, outsourcing is expected to imply cost saving compared with internal service provision (Hamzah et al., 2010; Carey et al., 2006). Therefore, professional accountants can perform accounting functions far more cheaply and efficiently than when firms conduct with their own employees (Carey et al., 2006; CIMA, 2008).

3.3.1.3 Focus on Core Business

Outsourcing practice permits firms to move away from non-core business and concentrate on core business activities (Greer, Youngblood and Gary, 1999). The non-core activities in manufacturing industry include accounting, IT, human resource management, and logistics or transportation (Hsiao, Kemp, van der Vorst and Omta, 2010). Many studies evidence that outsourcing practice permits firms to concentrate on their core activities (Gilley and Rasheed 2000; Gilley et al., 2004b; Beaumont and Sohal 2004). Hence, concentrating on core business is a key attraction of outsourcing practice in SME environment (Hamzah et al., 2010; Gilley and Rasheed, 2000; Everaert et al., 2006, 2007; Jayabalan et al, 2009). For instance, when firms outsource their accounting practices and focus on producing their products, they generally move towards a business strategy, which assists them in maintaining their competitive advantage in serving customers (Hamzah et al., 2010). It is remarkable that outsourcing practice enables the smaller firms to focus on core business and access to technical competencies and expertise not available from in-house staff, and to take benefit of economies of scale enjoyed by external service providers (Jayabalan et al, 2009; Strange, 2009).

3.3.1.4 Enhanced Innovation

When non-core processes and activities are removed from the firm to an external service provider (Mahmoodzadeh et al., 2009), SMEs can release internal resources to concentrate on more strategic (core) activities to gain competitive advantage (Gooderham et al., 2004). Firms that organise an outsourcing practice can shift internal resources from operations to innovation (CIMA, 2008). Hence, outsourcing permits smaller firms to get better quality services especially from the experts (Gooderham et al., 2004; Elmuti, 2003).

3.3.1.5 Managing Time Pressure

SMEs which are unable to handle time-sensitive issues and competing demand, particularly during peak periods, may outsource with the intention of dealing with their time pressure (Jayabalan et al, 2009; Gooderham et al., 2004; Greer et al., 1999). In actual fact, SMEs simply use an external accountant to handle accounting activities because they do not have the time, and are not able to complete those functions (Hamzah et al., 2010; Jayabalan et al, 2009).

3.3.2 Disadvantages of Outsourcing practice

Five key disadvantages of outsourcing have also been identified, namely, loss of internal expertise and skills; loss of management control; doubtful cost savings; risk to succession planning; and risk to proprietary data. These are discussed next.

3.3.2.1 Loss of Internal Expertise and Skills

A key disadvantage of outsourcing practice is that it leads to a loss of opportunity to train and develop internal expertise and skill (Everaert et al., 2007; Gilley and Rasheed, 2000). Over-reliance on external service providers may lead to wear away the firms' internal expertise and skills (CIMA, 2008; Elmuti, 2003). For example, a firm that is excessively reliant on external service providers cannot emphasise sufficiently on internal skills and expertise development. This leads to loss of significant expertise and skills within the firm and the development of inappropriate skill sets (Quinn and Hilmer, 1994; Domberger, 1998). Furthermore, outsourcing practice produces the risk of becoming extremely reliant on a specific service provider, which unpredictably may diminish the quality of provided services (Quélin and Duhamel, 2003). Then, it becomes difficult to revert to insourcing and even more so for accounting activities, since performance of such accounting functions requires specific expertise and firm specific knowledge (Everaert et al., 2007).

3.3.2.2 Loss of Management Control

When firms outsource their functions to external service providers, they may lose control of the process and the outcome to an external service provider (Elmuti, 2003; CIMA, 2008). For instance, firms that rely on outside suppliers excessively for the performance of their business functions will find themselves locked into definite arrangements that wear down their internal abilities and management control to perform functions critical to competitiveness (Quinn and Hilmer, 1994; Abdul-Halim, 2009). Outsourcing practice diminishes a firm's control over how specific activities are delivered, which may possibly increase the firm's liability exposure (Elmuti, 2003). For example, over-reliance on external service providers may make it essentially difficult for the firm to maintain its competitive advantages without undertaking developmental activities that are continuously improving the design and business technologies (Elmuti, 2003; Kotabe, 1998).

3.3.2.3 Doubtful Cost Savings

The cost savings expected from an outsourcing practice may possibly be counteracted by other costs such as search cost (e.g., cost to collect information on external service providers), and contracting cost (i.e., ex-ante costs of negotiating a contract, the ex-post costs of monitoring performance and providing feedback) (Gilley and Rasheed, 2000; Bryce and Useem, 1998, Kremic, Tukel, and Rom, 2006; Elmuti, 2003). Outsourcing practice may lead to diminishing wage costs, but it does not lead to reduce the total costs (CIMA, 2008; Tomkins and Green 1988). Hence, it is important to consider the transaction costs of agreeing to a contract, monitoring the performance, and transferring documents to an external accountant (Everaert et al., 2007). Combined, these added charges may cause outsourcing practice being more costly (Everaert et al., 2007).

3.3.2.4 Risk to Succession Planning

An in-house accounts department can be a training ground for future senior accountants and SME executives (CIMA, 2008). An outsourced function may not be a source of competitive advantage in the future (Everaert et al., 2007; CIMA, 2008). For example, some SMEs which outsource their activities may suffer from low quality output by external service providers who have low knowledge of the activities and the firms' objectives (Barthelemy and Geyer, 2005; Elmuti, 2003; Barthelemy, 2003). Indeed, outsourcing practice can shift the benefits of organisational learning to the external service provider (CIMA, 2008; Elmuti, 2003).

3.3.2.5 Risk to Proprietary Data

Although outsourcing practice may minimise risks and maximise value to the firm (Ngwenyama and Bryson, 1999), but confidentiality and risk to intellectual capital are frequently cited as key reasons why some firms do not outsource to an external supplier (Everaert et al., 2007; CIMA, 2008). Firms that outsource ought to provide adequate security measures to control the risk of intellectual property theft or breaches of confidentiality (CIMA, 2008). This can affect the entire firm and can result in significant resistance to any outsourcing initiative (Elmuti, 2003).

3.3.3 Advantages and Disadvantages: Reasons for Accounting Function Outsourcing: A Summary

The above discussion of the advantages and disadvantages of outsourcing practice provides the background for the discussion of outsourcing. Outsourcing becomes a common practice among firms and it is utilised extensively in various service functions (Nelson, Richmond and Seidmann, 1996; Poppo and Zenger, 1998; Aubert et al., 2004; Barthelemy and Geyer, 2005; Alvarez-Suescun , 2010; Widener and Selto,1999; Speklé, van Elten and Kruis, 2007; Everaert et al., 2006, 2010; Dibbern and Heinzl, 2006; Lamminmaki, 2007, 2008; Hansen and Morrow, 2003; Carey et al., 2006; Dibbern and Heinzl, 2009; Wang, 2002). In fact, most studies emphasise on outsourcing of other activities and their impact on firm performance and the related advantages and disadvantages (Gilley and Rasheed, 2000; Gilley et al., 2004a; Salimath et al., 2008; Jiang et al., 2006). In the face of this trend, a limited number of academic scholars has analysed how decisions of accounting function outsourcing are formulated, the way in which these outsourcing decisions are performed and the effectiveness of such outsourcing practice (Everaert et al., 2006, 2010). However, none of them has examined the benefit of the accounting function outsourcing comprehensively. Accordingly, academic-oriented studies on issues related to accounting function outsourcing are both fragmented and inconclusive.

Furthermore, there are many reasons to embark on accounting function outsourcing at both the strategic and operational levels of firms. Particularly, demands for profitability and growth of the firms have encouraged SMEs to analyse their internal processes and human resource gaps, resulting in a shift towards strategic outsourcing of functions (Everaert et al., 2007). Moreover, reasons for accounting outsourcing are frequently a response to a demand for cost reduction (i.e., reduction in overheads) (Everaert et al., 2007; Hamzah et al., 2010), quality improvement (Elmuti, 2003), focus on core competencies (Elmuti, 2003) and access to the experts in accounting areas (Everaert et al., 2007). It enables firms to profit from the increasing comparative advantage of external accountants who have technical expertise in the areas concerned (Carey et al., 2006). Furthermore, outsourcing allows SMEs and professional accountants to cooperate with each other and collaborate their consultative and strategic roles to design and apply programs which to improve SME performance (Blackburn and Jarvis, 2010; Blackburn et al., 2010). In brief, the main reasons for accounting function outsourcing are found to be fairly consistent. Generally, the key reasons include seeking expertise and competence, enhancing the quality of the services, costs reduction and enabling professional accountants to take on a more strategic role.

3.4 THEORETICAL ARGUMENTS: TRANSACTION COST ECONOMICS (TCE)

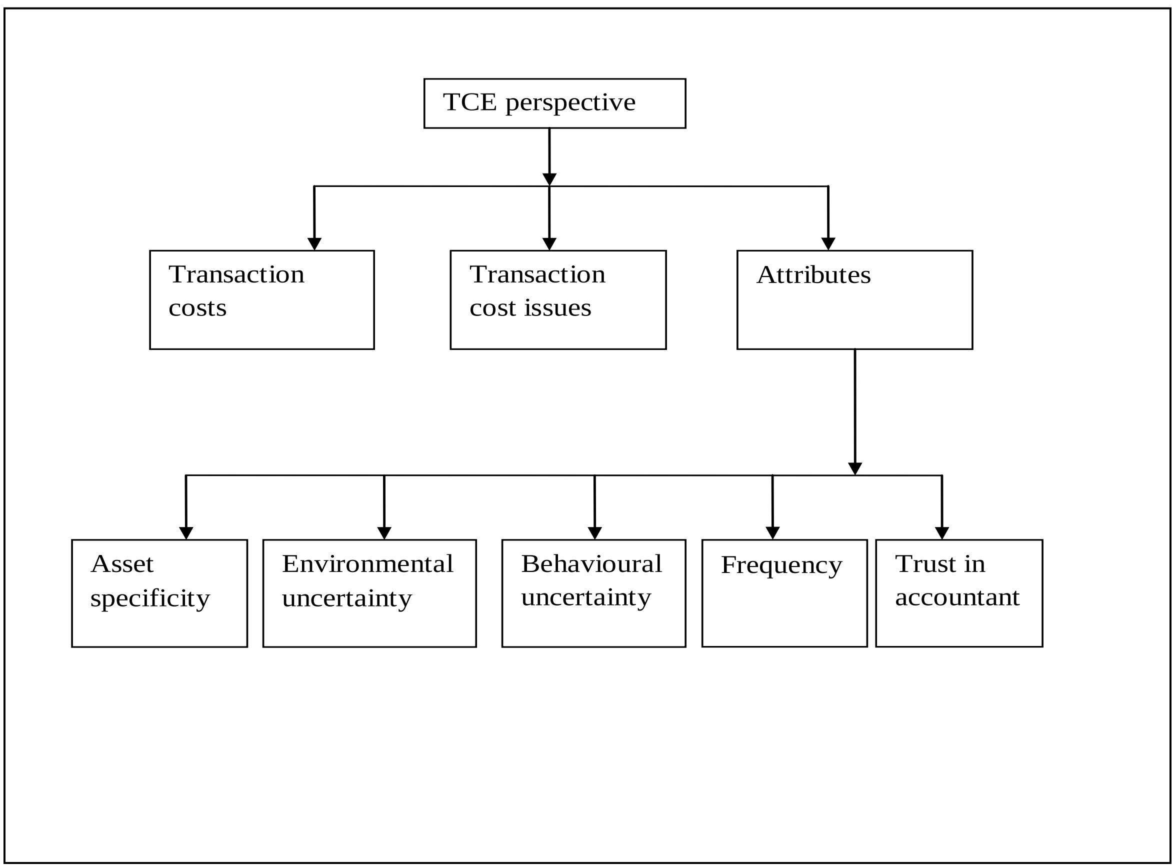
The transaction cost economics (TCE) perspective found by Coase (1937) and developed principally by Williamson (1975, 1985, 1996), posits that there are costs in using a market. TCE perspective merges economic theory with management theory to posit an ideal type of relationship a firm must possess in the marketplace (McIvor, 2000, 2009). Hence, TCE emerges as the main theory to explain outsourcing practice over the past 20 years (Espino-Rodríguez, Lai and Baum, 2008).

TCE perspective has laid the basics for the buying discipline that utilises an investigation of the factors, which establish the internal and external boundaries (e.g., insourcing or outsourcing) of the firm (McIvor, 2000, 2009). The notion of TCE is that the properties of a transaction establish what constitute the efficient governance structure market (buy=outsourcing), hierarchy (make= insourcing) or alliance (insourcing and outsourcing) (McIvor, 2000). Markets are assumed to be efficient, but efficiency requires that all information is available to all parties (i.e., firms and service providers)(Marshall et al., 2007). If this condition is not met, firms can incur costs, called transaction costs (Marshall et al., 2007).

Inevitably, TCE theory has established to be one of the more popular theoretical paradigms for investigating outsourcing practice (Reeves et al., 2010; Everaert et al., 2010; Lamminmaki, 2007; Espino-Rodríguez and Gil-Padilla, 2005; Nickerson, Hamilton and Wada, 2001; Widener and Selto, 1999). TCE perspective suggests that firms are organised in such a way that minimises transaction costs (Lamminmaki, 2007). TCE view argues a firm seeks to balance transaction and production costs in their decision to internalise (insource) or externalise (outsource) a transaction (Jiang, Belohlav and Young, 2007).

Therefore, the greater the transaction costs, the more likely that the transaction form (mode) goes to managing within the firm (i.e., insourcing) rather than buying (e.g., outsourcing) (Jiang et al., 2007). When a firm decides to outsource a service function, it suggests to the market that the cost of this new external transaction mode (form) must be lower than its former in-house transaction cost (Jiang et al., 2007). Accordingly, the TCE perspective to resulting TCE variables are shown in the Figure 3.1. These variables are discussed next.

Figure 3.1: TCE Variables



3.4.1 Transaction Costs

The direct and indirect costs of negotiating, monitoring, and enforcing explicit and implicit contracts between firms and suppliers (service providers) are defined as transaction costs (Tiwana and Bush, 2007). TCE perspective argues that the question of internalising or externalising an activity is based on cost comparisons which take into account the sum of transaction and production costs (Williamson 1975, 1985, 1991; Dibbern and Heinzl, 2009; Arnold, 2000; Marshall et al., 2007). In effect, the idea of transaction costs is that some firms choose to "make" functions or activities and others "purchase" such activities (Thouin, Hoffman and Ford, 2009). Thus, the cost for a firm to provide an activity internally is captured by the production cost while the cost of purchasing an activity is captured as a transaction cost (Thouin et al, 2009). Indeed, firms provide a service function internally when it is economically more cost effective than purchasing the same service function on the open market (Thouin et al, 2009). Accordingly, outsourcing decision is based on production and transaction cost considerations (i.e., a cost comparison, which considers the sum of transaction and production costs) (Caniëls and Roeleveld, 2009; Ngwenyama and Bryson, 1999).

TCE view provides a set of principles for analysing client-external service provider transactions and determining the most efficient mode of building up and handling them (Ngwenyama and Bryson, 1999). According to TCE, transactional relationships (costs) have three stages, including contact, contract, and control (Carmel and Nicholson, 2005). Contact cost includes cost of the information processing service, which is assessed from the market (Ngwenyama and Bryson, 1999). Contract costs comprise recognising potential impending contingencies, negotiation and investment in assets specific to the transactional relationship and design of safeguards (Greenberg et al., 2008). Contracting cost, which include search cost to find a service provider, negotiation fees (i.e., the ex-ante costs of negotiating a contract), legal fees, and other labor costs incurred to institutionalise the relationship (Alvarez-Suescun, 2010; Gulbrandsen, Sandvik and Haugland, 2009; Holcomb and Hitt, 2007). Control costs include the costs of monitoring (e.g., ex-post costs of monitoring performance and providing feedback), settling disputes, renegotiation, coordinating related to the activities of the service providers including labor and equipment and potential loss of investment because of the relationship breaking up (Greenberg et al., 2008; Ngwenyama and Bryson, 1999). In addition, switching cost is the cost to substitute a service provider in circumstances of under-performance (Alvarez-Suescun, 2010; Ngwenyama and Bryson, 1999).

According to the TCE view, the firms should perform the activities within the firms when costs of processing activities by external service providers are (e.g., external governance costs) larger than the costs of performing such activities in-house and using an internal governance structure (insourcing) (Gulbrandsen et al., 2009). In other words, the firm should outsource activities if to process those functions internally would require excessive investment to get the lowest unit cost (McIvor, 2000). Consequently, when internal transaction costs (e.g., cost of processing an activity internally or insourcing) equal the cost of purchasing (outsourcing) the same activity on the open market, the firm will have a tendency to stop providing internally and buy from the open market (Lilly et al., 2005). The main aim of a firm's manager making outsourcing decisions is to minimise total cost (i.e. production and transaction costs) and maximise total value to the firm (Ngwenyama and Bryson, 1999). Therefore, attributes of activities that lower transaction costs are likely to raise the likelihood that firms' managers will choose to outsource activities (Tiwana and Bush, 2007).

Overall, TCE perspective has become a standard framework to explain why some firms choose to process some service functions internally, while other firms decide to outsource such functions to an external service provider (Everaert et al., 2010). TCE asserts that sourcing decisions are based on characteristics related to the effectiveness of the firm's governance (Espino-Rodríguez et al., 2008). Accordingly, cost economies due to effective governance structures represent important criteria in outsourcing decision (Holcomb and Hitt, 2007). By considering the relative cost of transactions utilising their staff on the one hand and external providers on the other hand, TCE perspective tries to explain how firms are organised (Everaert et al., 2010). In fact, transaction cost is a major issue in the sourcing decisions and this highlights the potentially significant role for accounting functions in facilitating decisions whether to outsource or insource (Everaert et al., 2006; Lamminmaki, 2007, 2009). For example, the decision to outsource or internalise accounting activities in a specified condition depends upon comparative transaction costs (Everaert et al., 2010; Lamminmaki, 2007, 2009).

3.4.2 Transaction Cost Issues

TCE perspective indicates that the most important factors producing transactional difficulties, including bounded rationality, opportunism, small numbers bargaining and information asymmetry (McIvor, 2000, 2009; Thouin et al, 2009; Holcomb and Hitt, 2007). Bounded rationality and opportunism signify behavioural assumptions (McIvor, 2009). In addition, bounded rationality signifies the cognitive limitations of the human mind, which expands the difficulties of perceiving entirely the complexities of all feasible decisions (Aubert et al., 2004; Marshall et al., 2007; McIvor, 2000, 2009). Opportunism relates to decision makers behaving with guile, in addition to acting out of self-interest (McIvor, 2000). This assumption is that some people engage in opportunistic behavior and it is necessary for a firm to monitor the other party (service provider)'s performance – adding to the cost of conducting a transaction (Thouin et al, 2009). Small numbers bargaining refers to the extent to which the firm (buyer) has substitute sources to meet its requirements (McIvor, 2009). Information asymmetries refers to the presence of information asymmetries between the firm and external service provider (e.g., buyer and vendor), which implies that either party may possibly have more knowledge than the other (McIvor, 2000, 2009).

3.4.3 Transaction Attributes

The transaction costs associated with any activity or function depend on key attributes (factors) of the activity such as (1) asset specificity, (2) environmental uncertainty, (3) behavioral uncertainty, (4) frequency (Williamson, 1979, 1985, 1996; McIvor, 2000, 2009; Dibbern and Heinzl, 2009; Lamminmaki, 2007), and (5) trust in service provider (Hansen and Morrow, 2003; Verwaal et al., 2008). Asset specificity refers to transactions that need high investments, which are specific to the prerequisites of a specific exchange relationship (McIvor, 2000, 2009; Dibbern and Heinzl, 2009). For example, "asset specificity refers to the degree to which an asset is valuable in the context of a specific transaction; this is relevant because of its interplay with opportunism" (Rieple and Helm, 2008, p. 281). Environmental uncertainty turns to the stability and predictability of a service function that are a consequence of the firm condition (i.e., adaptations by firm and volatility of business activity) (Lamminmaki, 2007; Widener and Selto, 1999). Behavioral uncertainty turns to ambiguity (uncertainty) as to transaction definition and performance (Rieple and Helm, 2008; McIvor, 2000). Transaction frequency involves occasional and recurrent transactions (Watjatrakul, 2005; Murray, 2001). For example, frequency of transaction; because of the long-term, repeated, stable, and high volume transactions, a large number of transaction costs have been emerged (Lamminmaki, 2007). Trust turns to a situation where one party (firm) relies on the other party (service provider) based on the economic indication that the other party would carry out the commitment and act in a predictable way (Lee, Huynh and Hirschheim, 2008). Those factors identify whether a function or activity is most efficiently performed internally or outsourced (Rieple and Helm, 2008).

As observed by Marshall et al. (2007):

> "the presence of high asset specific investments can lead to contracting problems as the contracting parties need to safeguard specific investments against the threat of opportunism" (p. 246).

In other words, high asset specificity and environmental uncertainty and behavioural uncertainty lead to transactional difficulties such as supplier opportunism, with the transaction held internally within the firm hierarchical governance (i.e., insourcing) (Marshall et al., 2007). For example, the activities are likely performed in-house while transactions requiring specific assets will bear higher transaction costs (Aubert et al., 2004; Arnold, 2000). Outsourcing is appropriate in conditions in which markets are competitive (Everaert et al., 2010). Market pressures reduce the need to monitor service provider's behaviour (Hennart, 1994). Accordingly, when markets fail, the firms can decrease the transaction costs by using their own staff because they can monitor and control their own staff' behaviour more efficiently (Reeves et al., 2010; Hennart, 1994)). As a result, an activity is performed within the firm under conditions of high asset specificity and high uncertainty, because transaction costs (e.g., the costs of writing, monitoring and enforcing contracts) are expected to be high (Gottschalk and Solli-Sæther, 2005; Ang and Straub, 1998). For instance, when transaction costs are high, outsourcing is considered to be rather inefficient compared with insourcing (Reeves et al., 2010; Gulbrandsen et al., 2009; Gottschalk and Solli-Sæther, 2005; Marshall et al., 2007; Aubert et al., 2004; Arnold, 2000). However, it indicates that the higher the frequency of transactions, the more likely insourcing will be utilised (Reeves et al., 2010). TCE perspective also extends personal characteristics such as management's trust in its service provider as critical factor in outsourcing (Brouthers and Brouthers, 2003; Hansen and Morrow, 2003; Verwaal et al., 2008).

Trust is as an expectation that another party (supplier) does not act in an opportunistic manner (Gainey and Klaas, 2005). According to TCE theory, the parties are related to two characteristics including, bounded rationality and opportunism (McIvor, 2009; Greenberg et al., 2008). The goal alignment of different parties (buyer and supplier) significantly lessens the degree of opportunism (Aubert et al., 2004). For example, TCE perspective indicates when trust develops, both parties (firm and external service provider) feel confident in their relationship and the opportunism will be decreased due to reliance in their ability to perform a function (Greenberg et al., 2008; Bozzurro, Costa and Zhang, 2008). However, one of the key characteristics of TCE is the threat of opportunistic behavior by the outside supplier (Tiwana and Bush, 2007; Lane and Bachmann, 2001). Therefore, an imperative element of outsourcing is the firm's exposure to the service provider (supplier) opportunism (Wuyts and Geyskens, 2005). Such opportunistic behavior may display itself in the form of the external service provider taking advantage of the firm after the outsourcing decision is made (Tiwana and Bush, 2007). Threat of opportunism is indicative of a lack of trust that an outside service provider will honestly fulfill task or project obligations (Ghoshal and Moran, 1996). The greater this threat, the greater the degree to which a firm (client) has to employ complex and costly governance mechanisms to safeguard its interests in its transactions with an external service provider (Dyer, 1996). Accordingly, the managements of the firms are expected to outsource activities only if they understand ex ante that they are sufficiently protected from the service provider's opportunistic behavior (Tiwana and Bush, 2007). Therefore, trust of a firm in its external service provider reduces transaction costs by reducing the perceived threat of opportunism (Dyer and Chu, 2003). Such trust in an external service provider is a project-specific feature that may arise from external service provider’s reputation (Sabherwal, 1999). Therefore, trust in the service provider was suggested to be the central mechanism which is consistent with the TCE model of economic interaction which takes on specific forms and is employed in specific relationships to each other (Bachmann, 2001; Gainey and Klaas, 2005). Thus, based on TCE perspective, trust has been recognised as a tremendously important mechanism in outsourcing decisions (Bachmann, 2001; Hansen and Morrow, 2003; Tiwana and Bush, 2007; Greenberg et al., 2008; Verwaal et al., 2008). TCE attributes (factors) are discussed next.

3.4.3.1 Asset Specificity

According to TCE theory, asset specificity is one of the critical factors affecting outsourcing intensity of accounting functions (Reeves et al., 2010; Everaert et al., 2006, 2010; Williamson, 1999). There are two general types of specific assets, namely physical (tangible) assets (i.e. specific equipment and machinery) and (intangible) human assets (e.g. human capital) (Williamson, 1985; Greenberg et al., 2008; McIvor 2009). Indeed, asset specificity (physical and human assets) describes the nature of the transaction (Nicholson et al., 2006; Reeves et al., 2010). Asset specificity refers to the degree of idiosyncrasy (customisation), of the assets necessitated by buyers (firms) and suppliers (external service providers) to complete the transaction (Nicholson et al., 2006; Reeves et al., 2010). Highly asset-specific investments signify costs that do not have value outside the transaction (i.e., insourcing is more appropriate) (McIvor, 2009). The costs can be in the form of physical asset specificity (e.g., level of product customisation) and human asset specificity (i.e., level of specialised knowledge involved in the transaction) (Reeves et al., 2010; McIvor, 2009). Asset specificity can be specific or idiosyncratic (e.g., highly customised to the firm) and non-specific (i.e., highly standardised) or mixed (i.e., both standardised and customised elements in the transaction) (McIvor, 2009). Lamminmaki (2005) noted that:

> "Human asset specificity encompasses any unique knowledge or skill that an employee develops through training, and represents specialised know-how or experience specific to a particular employer/employee relationship, i.e. the knowledge or skill is not transferable as it has limited relevance to other job situations" (p. 517-518).

Asset specificity (specific physical and human assets) turns to the extent to which an asset is important in the circumstance of a specific transaction; this is applicable because of its interaction with opportunism (Rieple and Helm, 2008; Dibbern and Heinzl, 2009). Therefore, the major reason for market failure relates to the presence of specific assets (Williamson 1985, 1986; Klein, Frazier and Roth, 1990). As a general rule, specific assets are not re-deployable for alternative uses (Vita, Tekaya and Wang, 2010; Dibbern and Heinzl, 2009; Espino-Rodríguez et al., 2008). When investments in these types of assets are made, a service provider and client are 'locked into' a transaction, because the assets are specialised to that transaction and do not have value elsewhere (Williamson, 1985). Specific assets make it expensive to shift to a new relationship (John and Weitz, 1988). Hence, TCE premises that specialised assets have lower transaction costs inside the firm because the firm has the ability to gauge and reward behavior of the internal staff (Everaert et al., 2010). In such conditions, with high asset specificity, firms would rather insource than outsource (Everaert et al., 2010).

Generally, assets are specific if their value is to a large extent higher in the particular exchange relationship than in their next best, alternative use (Nicholson et al., 2006). The level of specificity determines the form of governance (sourcing decisions) (Nicholson et al., 2006; Reeves et al., 2010). In other words, the degree of asset specificity of accounting functions depends on the nature of the accounting functions (Speklé et al., 2007). For example, non-specific transactions, such as accounts payables do not need dedicated assets for particular firms, and therefore can be processed using standard equipment and non-specialised knowledge (Nicholson et al., 2006). Conversely, idiosyncratic transactions such as management accounting (product costing) and financial planning or financial management services involve specialised knowledge of accounting processes and the associated environment (Nicholson et al., 2006). Consequently, the degree of asset specificity depends on the role that the accounting functions play in managing the firm (Speklé et al., 2007). In fact, outsourcing is efficient at low levels of asset specificity (e.g., low transaction cost), while high levels favour provision within the firm and insourcing is managed (e.g., hierarchical governance of the transaction) (Nicholson et al., 2006).

In the accounting context, physical assets refer to the accounting software used in the firm and human asset refer to information and knowledge which may be acquired from the market (Dibbern and Heinzl, 2009; Everaert et al., 2010). For instance, physical and human assets are specific when accountants require specialised knowledge of the certain characteristics of the enterprise so as to process a specific accounting practice (Everaert et al., 2010). However, accounting functions is inclined to be more people-intensive and less capital-intensive (Brouthers and Brouthers 2003; Everaert et al., 2010). For example, accounting functions are mainly people-intensive and asset specificity focuses primarily on human asset specificity (Everaert et al., 2010). Overall, asset specificity has a major factor impact on sourcing decisions (Watjatrakul, 2005). For example, according to TCE, when asset specificity (i.e., physical asset and human capital) is low, and transactions are relatively frequent, outsourcing will be used (Jiang et al., 2007; Chang et al., 2009). In other words, high asset specificity leads to transactional difficulties, and insourcing is utilised (Jiang et al., 2007). For example, the TCE posits that when the accounting functions involve high levels of asset specificity, the search for external accountants might be longer and the contractual negotiations more debatable (Espino-Rodríguez et al., 2008; Thouin et al., 2009). Faced with those conditions, it is suggested that insourcing provides a means of preventing high transaction costs and allows more frequent adaptations (Espino-Rodríguez et al., 2008; Thouin et al., 2009). On the other hand, low-accounting functions may be governed with an outsourcing design (Espino-Rodríguez et al., 2008). When accounting practices become more customised to a firm and more specialised, asset specificity intensifies and, therefore, transferring these functions to an accounting firm may be prolonged, complex , incomplete and costly (Everaert et al., 2010). Conversely, when asset specificity decreases, transferring accounting functions to external accountant is more appropriate (Everaert et al., 2010). Taken as a whole, TCE perspective argues that in the presence of high asset specificity, accounting practices have a tendency to be internalised as a consequence of the opportunistic behavior that may otherwise result (Lamminmaki, 2007).

3.4.3.2 Environmental Uncertainty

Many researchers distinguished between environmental uncertainty (variation in activity demand) and behavioural uncertainty (difficulty in monitoring activities) (Everaert et al., 2010; Wang, 2002; John and Weitz, 1988; Widener and Selto, 1999; Williamson, 1979). Environmental uncertainty argues about the degree to which ex-ante contractual costs and behavioural uncertainty argues about ex-post monitoring and enforcing costs (Vita et al., 2010). Environmental uncertainty and behavioural uncertainty are key factors influencing outsourcing that have been discussed by TCE perspective (Klein, 2005; Wang, 2002; John and Weitz, 1988; Widener and Selto, 1999). Environmental uncertainty makes it difficult to write and implement contingency claims contracts (Williamson, 1979). According to TCE, environmental uncertainty relates to the intrinsic incompleteness of contracts (Lamminmaki, 2007). The harder it is to predict what events may impose on a buyer and supplier relationship, the higher the uncertainty and the higher the potential for imperfect contracting and opportunistic behaviour (Lamminmaki, 2007).

Environment uncertainty comprises the cost related to searching for information in the market and signifies an important portion of general transaction cost as complete information on all prices and products at any specified time is impracticable (Thouin et al., 2009; Greenberg et al., 2008). Indeed, information processing is essential because firms' ability to handle information is tied to environment uncertainty (Lilly et al., 2005). If the environmental uncertainty intensifies, information processing will become more difficult, then it is expected that a firm will attempt to develop better ways for processing information to obtain a competitive advantage (Lilly et al., 2005).

According to TCE, one of most essential determinant in sourcing decisions is environmental uncertainty (Reeves et al., 2010; Dibbern and Heinzl, 2009; Kotabe and Mole, 2009). For instance, if a firm is faced with environmental uncertainty, the firm may choose to process an activity internally because doing so retains control of unanticipated benefits and costs (Ellram et al., 2008; Kaufmann and Carter, 2006; Williamson, 1975, 1985). TCE perspective indicates a higher environmental uncertainty will lead to internalise due to the potential for imperfect contracting and opportunistic behavior (Lamminmaki, 2007). In effect, the TCE theory premises that a firm will substitute the market when the costs of processing within the firm (i.e., internal provision costs) are less than the costs of transacting (e.g., external transaction costs) through the market (Lamminmaki, 2005). Overall, high environmental uncertainty is a deterrent for firms trying to outsource a function (Aubert et al., 2004).

Some studies incorporated the effect of environmental uncertainty on the decision to use governance structures (insourcing or outsourcing) (Aubert et al., 2004). However, in internal audit activities, Speklé (2001, p.105) indicated that “Uncertainty refers to the degree of specifiability of intended performance and predictability of the environment within which the contract is to be executed (environmental uncertainty), and to the problems contracting parties may experience in monitoring performance (behavioural uncertainty)”. In professional services, Ellram et al. (2008) asserted that environmental uncertainty deals with the degree of volatility and unpredictability in the market place in connection with changes in availability, technology, price, and any other significant disruptions to the market. Widener and Selto (1999, p. 48) stated that environmental uncertainty turns to “expected variation in the demand for audit activities”. Similarly, in the context of accounting, Everaert et al. (2010) stated that:

> “Environmental uncertainty concerns the stability and predictability of the workload related to accounting tasks, as a consequence of the volatility of business activities. If business activities are volatile (e.g., unstable number of purchase and sales invoices because of seasonal trends; unstable period-end tasks because of mergers, acquisitions or plant closures), the workload related to sequential accounting tasks also becomes unstable and unpredictable. If firms can predict and schedule the workload related to their accounting tasks accurately, the costs of contracting should be low, and firms may outsource their accounting tasks, while accruing low transactions costs”(p. 97).

3.4.3.3 Behavioural Uncertainty

Transaction costs are also determined by the degree of behavioural uncertainty (Dibbern and Heinzl, 2009; Everaert et al., 2006). As discussed earlier, TCE view identified the primary factors creating transactional difficulties such as information asymmetry and opportunism (Dibbern and Heinzl, 2009; McIvor, 2009; Aubert, Rivard and Patry, 1996). As noted earlier, information asymmetry is as a derivative condition that arises primarily from uncertainty and opportunism (Williamson, 1975). Uncertainty is rooted transactional difficulties (Alvarez-Suescun, 2010; Aubert et al., 1996). Therefore, behavioural uncertainty reflects the potential of opportunistic behavior of an external service provider (Alvarez-Suescun, 2010; Dibbern and Heinzl, 2009; McIvor, 2009). For instance, behavioural uncertainty creates problems for performance evaluation (Watjatrakul, 2005). As a result, behavioural uncertainty indicates difficulties in monitoring suppliers’ (service providers’) performance and human tendency toward opportunism (e.g., shirking of responsibilities, distortion of information, cheating, and other forms of untruthful behavior)

(Williamson, 1985; Hill, 1990). If the firm is concerned about high levels of uncertainty and the possibilities for opportunism from an external service provider, the separation across time and the long distance between a firm and an external service provider raise the costs of transaction of processing a function (Nicholson et al., 2006). A service provider and firm should organise mechanisms to communicate effectively and transfer knowledge in order to determine and monitor performance, plan for future contingencies and build-in scope for flexibility and the fine-tuning of long-term service agreements (Nicholson et al., 2006).

In the context of a service function, behavioural uncertainty was evaluated by appraising the difficulty of measuring whether a function is effectively carried out, whether a service provider has accomplished the function in accordance with contractual obligations (Lamminmaki, 2007; Widener and Selto, 1999), and the extent to which an outsourcing contract provides the same extent of control as if the function is performed internally (Lamminmaki, 2007). Similarly, in the accounting context, "behavioral uncertainty can be interpreted as the difficulty of evaluating whether the accountant did the job accurately and to the best of his or her ability" (Everaert et al. 2010, p.97). They concluded that "high behavioural uncertainty causes high transaction costs, due to writing, negotiating, monitoring, and enforcing contracts, all done to prevent opportunistic behaviour"(P.97). When measurement difficulties exist, firms have a tendency to internalise accounting functions (Alvarez-Suescun, 2010). For instance, hierarchy (insourcing) permits them to reduce the threat of opportunism because the firm can measure behaviour better than outcome in addition to utilising the hierarchical (insourcing) control to ascertain work procedures and rules, and sanction any deviation in the external service provider's behaviour (Alvarez-Suescun, 2010). Conversely, when the appropriate behaviour of an external accountant can be specified earlier and/or its performance can be easily measured, outsourcing the accounting activities will be the most efficient alternative (Alvarez-Suescun, 2010).

3.4.3.4 Frequency

Another important dimension for describing transactions in TCE theory is frequency (Greenberg et al., 2008; Wang, 2002; Williamson, 1985). According to TCE, a main driver of a firm's decision to use markets (buy) versus hierarchies (make) is the transaction cost. Williamson (1985) indicated that transaction frequency has been considered as the number of transactions, where the number of transactions is a proxy for the total cost of transactions (i.e., more transactions means higher cost). For example, fourth "TCE transaction attribute, relates to the repetitiveness and volume of similar transactions" (Lamminmaki, 2007, p.75). For example, the frequency of the transaction is how often a firm needs the transaction completed (Greenberg et al., 2008; Ellram et al., 2008). Overall, transaction frequency relates to occasional and recurrent transactions (Watjatrakul, 2005; Murray, 2001; Colbert and Spicer, 1995).

Frequent or recurrent activities (functions) can produce benefits of economies of scale, which allow the improvement of setup costs (Widener and Selto, 1999). The TCE perspective seeks to economise on transactions and production costs (Reeves et al., 2010). TCE suggests that governance structures (i.e., sourcing decisions) are arranged in a line with transactions in a distinguishing, transaction cost economising approach (Speklé et al., 2007). Therefore, TCE promises that frequent or recurrent activities are expected to be processed internally (insourcing) (Williamson, 1985).

Frequency of accounting functions is realised in two ways (Everaert et al., 2006, 2010; Widener and Selto, 1999). First, frequency is recognised as the periodicity of the accounting activities (Everaert et al., 2010; Widener and Selto, 1999). Specifically, "each of the accounting tasks can be performed every day, week, month, quarter, semester, or year" (Everaert et al., 2010, p.98). Although accounting laws oblige that some accounting activities such as financial statements are provided once a year, many enterprises organise financial statements more often (Everaert et al., 2006). Furthermore, some accounting service providers may use standard payroll packages and also trained staff is available in the market, but providing of payroll accounting services is a non-specific function that occurs frequently (Nicholson et al., 2006). More importantly, many accounting functions (i.e., management accounting, financial planning, financial management services, etc) are idiosyncratic activities that are difficult to standardise because of the particularities of each firm and its environment (Nicholson et al., 2006). Therefore, those accounting activities affect outsourcing decisions in most firms (Nicholson et al., 2004, 2006). In this case, the availability of economies of scale favours market provision (Nicholson et al., 2004, 2006). In essence, TCE suggests that market (externalising) are more helpful than hierarchies (internalising) on condition that the level of idiosyncrasy is low (Nicholson et al., 2006). Second, frequency also is realised in terms of the size of the activity (Everaert et al., 2006, 2010; Widener and Selto, 1999). For instance, Everaert et al. (2010) noted that "for the entry of invoices, the size of the activity is important, representing the number of resources invested (in this case, employee(s) needed to enter the invoices)" (p. 98). For example, a firm that performs processing of one-hundred invoices every week has a lower frequency of 'invoice entry' than a firm that conducts processing of two-thousand invoices every week (Everaert et al., 2010). The former firm will more likely to outsource their accounting functions to a professional accountant than the latter (Everaert et al., 2010).

More importantly, smaller firms have an effect on transaction costs due to economies of scale whereby they are perceived to have lower frequency of accounting activities than larger firms (Carey et al., 2006). Accordingly, smaller firms have greater difficulty in producing economies of scale, which in turn is expected to limit the justification for employing in-house facilities and enhance accounting function outsourcing alternatives (Carey et al., 2006). TCE promises that “the greater the extent of a transaction (i.e., for large and recurring transactions), the more likely the transaction will be internally managed due to the production economies that can be obtained” (Lamminmaki, 2007, p. 75).

3.4.3.5 Trust in the Professional Accountant

Many researchers have studied the notion of trust from different areas, and each one emphasises different aspects (Siakas and Siakas, 2008; Lee et al., 2008; Greenberg et al., 2008; Gainey and Klaas, 2005; Bachmann, 2001; Tiwana and Bush, 2007). Trust can be defined as social phenomenon which is viewed as a characteristic of the social structure that facilitates interactions among parties (i.e., client and external service provider), takes into account interpersonal behaviours, communication channels and interpersonal trust ties (Lewicki, McAllister and Bies, 1998; Tyler and Stanley, 2007). Lee et al. (2008) define the notion of trust as one party (firm)'s willingness to believe the other party (external service provider) based on the economic and cognitive cues that the other party (service provider) would fulfill the commitment and behave in a predictable way. On one hand, Mayer, Davis and Schoorman (1995) argued that:

"Trust is the willingness of a party to be vulnerable to the actions of another party based on the expectation that the other will perform a particular action important to the trustor, irrespective of the ability to monitor or control that other party" (p.712).

On the other hand, (Hansen and Morrow, 2003) said:

"While many scholars may agree on a fundamental definition of trust and the conditions necessary for trust to arise, a variety of conceptualizations of trust have been offered, particularly in terms of the nature of trust and its dimensionality" (p. 44).

In context of accounting, Everaert et al. (2010) defined:

"Trust in the external accountant as the expectation of the executive that the accountant (1) can be relied upon to fulfil legal obligations, (2) will behave in a predictable manner, and (3) will act and negotiate fairly when the possibility for opportunism is present"(p.101).

This definition of trust entails that the SME owner-managers expect that (1) professional accountants are expert and capable, (2) professional accountants will behave in a consistent way and (3) professional accountant will charge fairly for accounting activities provided (Everaert et al., 2006). Gainey and Klaas (2005) maintained that trust is as an expectation that outside supplier do not act in an opportunistic manner. In line with TCE, Greenberg et al. (2008) stated the parties include bounded rationality, and opportunism. Wang (2002) maintained that:

"Opportunism describes a condition of self-interest seeking with guile that includes propensities to disseminate, distort, fail to disclose, and otherwise act in an untrustworthy and even fraudulent manner for purposes of the transactor's own gain" (p.161-162).

Bounded rationality influences on outsourcing intensity because it indicates that all contingencies concerning the transactional relationship may not be predicted (Greenberg et al., 2008). In outsourcing relationship, this means that a comprehensive (complete) contract will not be written (Greenberg et al., 2008). Opportunism implies that client and supplier will take advantage of the relationship even to the point of misrepresentation (Greenberg et al., 2008). Therefore, the main purpose of different parties is to lessen the degree of opportunism (Bozzurro et al., 2008). TCE argues when trust is enhanced and both parties feel confident in their relationship, the opportunism will be diminished (Bozzurro et al., 2008). Transaction costs and firm's exposure to the external service provider's opportunism are critical elements in outsourcing decisions (Wuyts and Geyskens, 2005). Hence, threat of opportunism means a lack of trust that an external service provider will honestly fulfill a function (Ghoshal and Moran, 1996). Therefore, Dyer and Chu (2000, 2003) mentioned that trust between the firm and external service provider reduces the costs of transaction by diminishing threat of opportunism. Overall, the lower the perceived trust in external accountants, the lower is the likelihood that the owner-managers of SMEs will choose to outsource their service functions (Everaert et al., 2006, 2010; Tiwana and Bush, 2007). Conversely, a high level of trust in professional (external) accountants tends to be outsourced more activities (Lee et al., 2008).

According to the TCE framework, transaction costs will increase when there is a smaller amount of trust in supplier, and decrease when there is a higher amount of trust (Bachmann, 2001; Gainey and Klaas, 2005; Eriksson, 2007). Accordingly, the TCE model helps to explain how firms gain their competitive advantages through governance of transactions (Eriksson, 2007; Williamson, 1996). For instance, outsourcing relationships based on trust in the service provider can generate a competitive advantage by way of the strategic sharing of the external service providers' key information and knowledge (Konsynski and McFarlan, 1990). By sharing knowledge between the firms and their external service providers, they are able to maintain a more useful outsourcing relationship over time (Lee et al., 2008). Thus, based on TCE perspective, trust in the external service provider has been recognised as an extremely important factor in outsourcing decision (Bachmann, 2001; Adler, 2001; Tiwana and Bush, 2007). Consequently, there is increasing evidence reported in the literature confirming the importance of trust in outsourcing intensity (Greenberg et al., 2008; Verwaal et al., 2008; Kim, So and Lee, 2007; Oza, Hall, Rainer and Grey, 2006; Hansen and Morrow, 2003). Overall, SMEs should be confident that the external accountants are trustworthy and sufficiently capable, before they outsource (Everaert et al., 2006, 2010; Verwaal et al., 2008; Hansen and Morrow, 2003).

3.4.4 Review of Empirical Studies Employing TCE Framework

Although there are a number of empirical studies that utilised TCE perspective to examine TCE attributes on outsourcing intensity (Lamminmaki, 2009), most of those prior studies have focused solely on the asset specificity variable (see, Nickerson et al., 2001; David and Han, 2004; Carter and Hodgson, 2006). Only a limited of empirical research has examined the TCE attribute such as asset specificity, environmental uncertainty, behavioral uncertainty and frequency (John and Weitz, 1988; Widener and Selto, 1999; Lamminmaki, 2007; Everaert et al., 2006, 2010). Additionally, empirical research to investigate the role of trust in outsourcing decision is scarce (Hansen and Morrow, 2003; Verwaal et al., 2008). To ignore trust on outsourcing decision, shows only a partial investigation of the TCE model, and indicates that the results are uncertain and limiting (Verwaal et al., 2008). Table 3.2 shows a number of empirical studies that have tested the direct effect of outsourcing based on TCE Framework.

Table 3.2: Empirical Evidence on the Determinants of Service Function Outsourcing Decisions

Researchers	Functions	Variables	Finding
Poppo and Zenger (1998); Aubert et al. (2004); Nelson et al. (1996); Barthelemy and Geyer (2005)	IT	Asset specificity	Supported
Nam et al. (1996)	IT	Asset specificity	Not supported
Everaert et al. (2006, 2010)	Accounting	Asset specificity and frequency Environmental uncertainty, behavioral uncertainty	Supported Not supported
Widener and Selto (1999); Spekle et al. (2007)	Internal audit	Asset specificity and frequency	Supported
Dibbern and Heinzl (2006)	IT	Environmental uncertainty and behavioral uncertainty	Partially supported
Alvarez-Suescun (2010)	IT	Asset specificity Behavioral uncertainty	Supported Not supported
Widener and Selto (1999)	Internal audit	Environmental uncertainty and behavioral uncertainty	Not supported
Dibbern and Heinzl (2009) and Wang(2002)	Information System (IS)	Asset specificity	Not supported
Dibbern and Heinzl (2009)	Information System (IS)	Behavioral uncertainty and environmental uncertainty	Partially supported
Lamminmaki (2007)	different Activities	Asset specificity, environmental uncertainty, behavioral uncertainty and frequency	Not supported For frequency supported
Wang (2002)	Information System	Behavioral uncertainty and environmental uncertainty	Supported
Hansen and Morrow(2003)	Business functions	Trust in service provider	Not supported
Verwaal et al. (2008)	Supply chain logistics	Asset specificity, trust in service provider and frequency	Asset specificity and trust supported Frequency was not supported

However, the findings of studies that have examined the relative significance of the asset specificity, uncertainty and frequency attributes on outsourcing are also somewhat unclear (John and Weitz, 1988; Widener and Selto, 1999; Lamminmaki, 2007; Everaert et al., 2006, 2010). For example, Widener and Selto (1999), using regression analysis, found support for their hypothesis relating to asset specificity, mixed support for frequency, and no support for uncertainty. Lamminmaki (2007), also using regression analysis, found support for frequency, no support for asset specificity, environmental uncertainty and behavioral uncertainty, Using regression analysis, Everaert et al.(2006, 2010) found support for asset specificity and frequency, and they did find not any support for behavioural and environmental uncertainty.

Besides, Verwaal et al. (2008) examined the role of asset specificity, frequency and trust in external service provider on outsourcing, so they found support for asset specificity and trust, no support for frequency. Hansen and Morrow (2003) examined the role of trust in outsourcing intensity. The role of trust in external service provider did not find any support in their study. Overall, the empirical studies discussed above, have been conducted in developed countries, a research to examine those factors impacting outsourcing of accounting practices is absent in developing countries.

3.4.5 The importance of the Utilisation of the TCE Perspective in Accounting Outsourcing

This study draws on TCE for two reasons: (1) the TCE has been utilised as a basis for examining outsourcing intensity (McIvor, 2000, 2009; Dibbern and Heinzl, 2009; Rieple and Helm, 2008; Lamminmaki, 2007; Aubert et al., 2004). Secondly, prior studies have utilised TCE perspective in a limited manner to describe outsourcing of accounting activities. For example, Everaert et al., (2006, 2010) only refer to one construct, ie. …whereas Nicholson… yield results that do not support…. (Everaert et al., 2006, 2010; Nicholson et al., 2006; Widener and Selto, 1999). (2) Whilst the use of TCE theory has been popular in explaining the outsourcing decision in many service functions in areas such as information technology (Beaumont and Costa, 2002), human resource management (Gilley et al., 2004a), internal audit activities (Widener and Selto 1999), and accounting functions (Everaert et al., 2006, 2010; Nicholson et al., 2006), its applicability in accounting outsourcing has not been conclusive. This calls for examining other theoretical perspectives as well.

3.5 THEORETICAL ARGUMENTS: RESOURCE-BASED VIEW (RBV)

Resource Based View (RBV) originated by Penrose (1959, p. 7), and has been employed for outsourcing decisions, shifting the attention from transaction costs and opportunism to firm performance and competitive advantage (Wernerfelt, 1984; Barney, 1991; Grant, 1991). The RBV argues that firms should carry out the activities or functions internally for which they have resources and capabilities because this approach will allow them to go one better than competitors, and thus obtain greater rents (Quinn and Hilmer, 1994). Alternatively, the RBV also promises that activities should be outsourced when firms lack sufficient resources to obtain the expected performance (Alvarez-Suescun, 2010). Taken as a whole, the RBV rests on two key points (Gottschalk and Solli-Sæther, 2005). Firstly, a resource with the potential to generate competitive advantage should meet a number of criteria, including value, rarity (scarce), imitability (ease to imitate) and organisation

(Barney (1991), and secondly, that resources are the determinants of firm performance (McIvor, 2009; Gottschalk and Solli-Sæther, 2005).

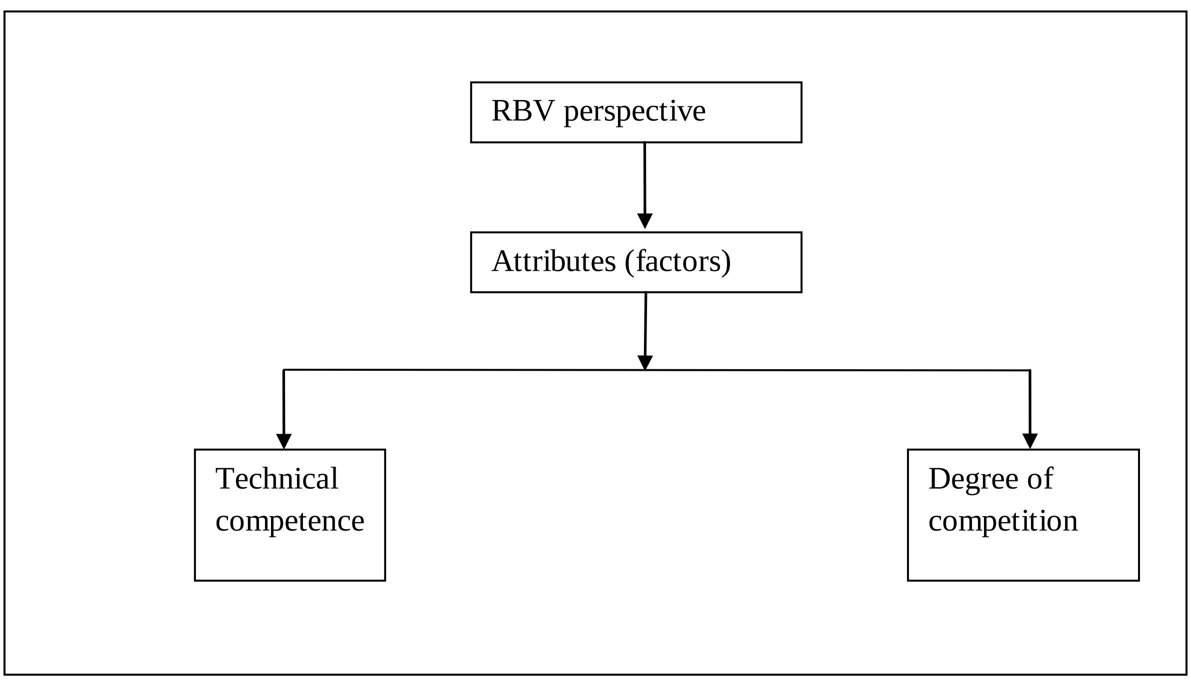
Resources include assets, capabilities, processes, knowledge and competence that a firm possess or obtain from external sources, and that should be applied to formulate and implement competitive strategies (Rivard, Raymond and Verreaul, 2006). Therefore, a valuable resource that is unique amongst both current and probable competitors is expected to be a source of competitive advantage (Marshall et al., 2007). For example, resources and capabilities are taken into account valuable if they allow a firm to take advantage of opportunities and cope with threats in the competitive environment (McIvor, 2009; Marshall et al., 2007; Barney, 1991). The rarity criterion turns to the number of competitors that have a valuable resource (McIvor, 2009; Marshall et al., 2007). Evidently, where a number of competitors have a valuable resource then it is not expected to be a source of competitive advantage (McIvor, 2009; Marshall et al., 2007). For example, if a firm possesses a resource and several of its competitors also have that resource, this resource cannot generate competitive advantage (Rivard et al., 2006). The imitability criterion (ease to imitate) is related to considerations of the ease with which competitors can replicate a valuable and rare resource possessed by a firm (Marshall et al., 2007). In effect, evaluating the imitability criterion includes determining the sustainability of the competitive advantage in the resource (McIvor, 2009; Marshall et al., 2007). In fact, a firm must organise to take advantage of its resources and capabilities (Barney, 1991). Finally, the organisation criterion comprises a number of elements such as management control systems, reporting structure and compensation policies (McIvor, 2009). If a resource provides competitive advantage, it will maintain its value in decision-making by resisting wearing away that launched by competitors (Hafeez, Malak and Zhang, 2007). Hence, competitive advantages are the competences that firms have to acquire competitive advantage (Espino Rodríguez and Padrón-Robaina, 2004). Accordingly, the competitive advantage of firms relies on their ability to incorporate, develop and reconfigure internal and external competences to deal with rapid changing environments (Teece, Pisano and Shuen, 1997).

Hafeez et al. (2007) categorised resources into three sub-categories, that is, physical assets, intellectual assets and cultural assets. Physical assets (i.e., inventories, plant and equipment) are easily recognisable due to their tangible existence or visible (Hafeez et al., 2007). The physical assets are readily priced in balance sheets of the firm and accounting system (Hafeez et al., 2007). Intellectual assets (e.g., human resource) include tacit knowledge, employee expertise and skills and competence which are intangible (Hafeez et al., 2007). Cultural assets are a firm's unique history and legacy (Hafeez et al., 2007). However, the central tenet in RBV is that unique organisational resources of both tangible and intangible nature are the real source of competitive advantage (Gottschalk and Solli-Sæther, 2006). In the accounting context, resources primarily relates to knowledge, skill and competence (Everaert et al., 2006; Jayabalan et al., 2009). For instance, explicit knowledge (expertise and technical competence) in accounting functions is knowledge of generally- accepted accounting principles (Everaert et al., 2006). However, employing those accounting principles in a business environment needs tacit knowledge (Everaert et al., 2006). For professional accountants, tacit knowledge predominantly is obtained through practice, which makes it almost impossible to transfer (Hafeez et al., 2007).

The RBV declares that core activities should be performed in-house, while non-core activities (i.e. accounting tasks) should be outsourced (Caniëls and Roeleveld, 2009; Espino-Rodriguez and Padron-Robaina, 2006). Therefore, the RBV concentrates on the extent to which a firm seeks to obtain competitive advantage through enhancing strategic knowledge and competences from internal and external sources (Johnson, Webber and Thomas, 2007). However, one important characteristic of smaller firms is that they seldom have the resource to permit accounting practices to be carried out internally (Døving and Gooderham, 2005; Holmes and Nicholls, 1988). For instance, many claim Accounting Information Systems in smaller firms tended to be undeveloped and that as a result little management accounting and financial management information was available to the management (McMahon and Holmes, 1991). Lack of utilisation and understanding of accounting and financial information lead SMEs not to make effective decisions and this may cause low performance (Sarapaivanich, 2003). Hence, one major cause of SMEs' failure is the inefficient use of accounting information (Peacock, 1988; Sarapaivanich, 2003). This has led SMEs to outsource accounting activities traditionally carried out in-house (Marshall et al., 2007; Everaert et al., 2006; Jayabalan et al., 2009; Devi and Samujh, 2010). In effect, activities in which SMEs lack the necessary resources (expertise and competence) internally can be outsourced (McIvor, 2009; Jayabalan et al., 2009; Devi and Samujh, 2010; Hamzah et al., 2010). Therefore, the RBV explains the firms that encounter insufficient resources to perform accounting tasks internally should utilise professional accountants (Døving and Gooderham, 2008). Hence, the RBV explains successfully a number of respects of accounting functions by external accountants (Døving and Gooderham, 2008).

SMEs may not be able to operate in the financial market like LEs, mainly because of their small size and limited knowledge and expertise (Jayabalan et al., 2009; Sarapaivanich, 2003). According to RBV, SMEs need accounting information more than larger firms to cope with competitive pressures and market demand conditions (Døving and Gooderham, 2008; Jayabalan et al., 2009). For example, LEs use comprehensive accounting information; they are generally profitable and are more likely to grow (Lignier, 2008). However, accounting information too provides useful information to assist owner/managers to make sound decisions, and this leads to improved SME performance (Sarapaivanich and Kotey, 2006). However, SMEs lack qualified people or knowledge to fulfill the accounting functions (Jayabalan et al., 2009; Devi and Samujh, 2010; Hamzah et al., 2010). Interestingly, consistent with the RBV theorisation, SMEs outsource accounting functions to fill up their internal resource gaps (Everaert et al., 2006; Gooderham et al. 2004; Døving and Gooderham, 2008; Marriott, Marriott, Collis and Son, 2008). Effectively, the RBV can assist with analysing a firm's resources, which can link outsourcing to firm performance and to provide competitive advantage (Shang et al., 2008; Marshall et al., 2007). Consequently, the RBV variables are shown in the Figure 3.2 and these variables are discussed next.

Figure 3.2: RBV Variables



3.5.1 Resource-Based Attributes

Smaller firms can access complementary resources (e.g., human capital or competence) from external sources when they can gain no human capital to perform their activities internally (McIvor, 2009). Hence, the RBV discusses a view that if firms are to grow they should be open and have adaptive systems where knowledge is gained from outside the firm (Worrall, 2007). Therefore, the RBV argues SME owner/ managers should learn to exploit the resources available outside the firm in competitive environment (Worrall, 2007; Gooderham et al., 2004).

A key prerequisite for the SME clients is an understanding of how to manage resources that the firm does not own (Everaert et al., 2006; Gottschalk and Solli-Sæther, 2006). From a service provider's perspective, there are many potential opportunities and benefits for the SME clients to utilise professional accountants while they are confronted with limited resources in a competitive business environment (Blackburn et al., 2010; Gottschalk and Solli-Sæther, 2006). These opportunities and benefits can be derived from outsourcing of accounting functions to a professional accountant especially, those requiring technical competence and expertise or skill (Døving and Gooderham, 2008; Carey et al., 2006; Gottschalk and Solli-Sæther, 2006). Additionally, internal provision of accounting practices requires SMEs to invest in accounting expertise and in training and development to keep this expertise up-to-date (Speklé et al., 2007).

From the professional accountants' perspective, as the scope of accounting practices is expanding and internal accountants have to deal with increasing demands on their technical competence and expertise, these investments become substantial for SMEs (Speklé et al., 2007). By their nature, such investments bring economies of scale, and the demand for accounting activities need to be adequately large to be able to recover the investments (Speklé et al., 2007). In fact, it is expected that only the largest firms are able fully to internalise the accounting functions if they want to provide internally (Everaert et al., 2010). The reason being accounting practices are becoming increasingly more advanced and specialised in terms of expertise and technical competence, so that only the larger firms can afford to keep the necessary specialists as employees (Speklé et al., 2007).

The resource-based view (RBV) is probably the most popular framework that supports SMEs' use of professional accountants (Everaert et al., 2006; Blackburn et al., 2010; Gooderham et al., 2004). In this context, the RBV explains that the technical competence of a professional accountant and degree of competition are vital factors affecting a firm's decision to use external accountants' services (Blackburn et al., 2010; Gooderham et al., 2004). By identifying the source of a firm's success, the RBV literature provides a framework for developing an understanding of the potential role for the external accountant in helping the SME achieve competitive advantage (Blackburn et al., 2010; Gooderham et al., 2004). Small accounting practitioners can encapsulate a range of technical competencies that sustain the SME's intangible resources, providing a potential source of competitive advantage (Gooderham et al., 2004). The professional accountants may also maintain the competitive advantage of a firm by providing accounting and professional services on market competitive forces approach though it is in the areas of financial management and with systems and processes that the external accountant has long-standing expertise (Blackburn et al., 2010). However, the relationship between the degree of competition and outsourcing intensity has been examined using contingency theory in the hotel sector (Lamminmaki, 2007). In this SME context, resource-based theory is more appropriate for the role of degree of competition in outsourcing of accounting activities because most SMEs face resource gaps that professional accountants can fill (Gooderham et al., 2004; Blackburn et al., 2010). RBV attributes (factors) are discussed next.

3.5.1.1 Technical Competence

The RBV examines the ability of a firm to develop the scope of its products or services enabling it to go into new markets which is being dependent on its possession of superior resources (Døving and Gooderham, 2008). According to RBV, a firm’s possession of valuable resources such as competencies is the important determinant of a firm’s capability to pursue economies of scope (Barney, 1986; Penrose, 1959; Wernerfelt, 1984). The concept of the competence derived by Hamel and Prahalad (1994) which has developed from the RBV – has influenced significantly outsourcing decisions. One of the objectives of the RBV is to help owner/managers to realise why competence is perceived as a firms’ most valuable asset, and to understand how those assets can be used to improve firm performance (Caldeira and Ward, 2003). Competencies are skills, knowledge, and technological expertise that a firm needs to possess or obtain from external sources (McIvor, 2000). However, in the accounting context, technical competence of external accountant ascribes to suitable qualifications, experience, essential specialised skills, industry specialisation and technological expertise (Carey et al., 2006). Indeed, majority of SME owner/managers have no professional, management or other formal qualifications (Stanworth and Gray, 1992). For example, many of SME managements lack financial skills or technical competence of how accounting information might be used to aid decision-making (Deakins, Logan and Steele, 2001; Collis and Jarvis, 2002; Marriott and Marriott, 2000; Breen, Sciulli and Calvert, 2003; Devi and Samujh, 2010). According to RBV, critical competencies are necessary for competitive advantage, so SMEs should develop internally or access through the accounting firms in order to transfer best practices across firms (Gooderham et al., 2004). However, smaller firms often have difficulties to employ competent persons due to their incapability to offer competitive salaries and benefits (Jennings and Beaver, 1997).

Many of smaller firms lack resources (i.e., accounting knowledge and competence) to perform accounting functions internally (Everaert et al., 2006, 2007; Jayabalan et al., 2009). However, the employing of full-time employees (internal accountants) is not always a speedy process and there are obvious problems associated with terminating staff if they are no longer needed (Carey, 2008). While larger firms may be able to employ specialised full-time staff as the need arises, SMEs will not be able to employ specialised full-time staff due to resource constraints (Carey, 2008; Carey et al., 2006). One possible way for a smaller firm to obtain competencies is to utilise qualified persons (Gooderham et al., 2004). For instance, SMEs experience from the deficiency of managerial competence, which can be complemented by professional accountants that provide accounting activities to the SME managements when and where they need (Everaert et al., 2006, 2007; Jayabalan et al., 2009). For example, professional accountants' services to their small firms can encapsulate a range of competencies providing an important source of competitive advantage (Gooderham et al., 2004). Therefore, by relying on outsourcing, smaller firms can obtain the competence they need from small accounting firms (Gooderham et al., 2004). Moreover, SMEs rely on professional accountants because they perceive that professional accountants are competent and proficient to provide a value-for money in the provision of accounting functions (Leung, Raar and Tangey, 2008). Thus, the presence of accounting outsourcing practices has provided the best option for SME survival (Jayabalan et al., 2009). This is more significant for Iranian SMEs (Naderian, 2010). In fact, the involvement of a professional accountant is seen as a positive indication and contribution in addressing asymmetric information issues (Naderian, 2010; Marlow and Carter, 2005).

3.5.1.2 Degree of Competition

In the present day, business environments are unstable and unpredictable as a consequence of economic globalisation, technological change, market maturity, the need to respond to the customers' increasing demands and fiercer competition (Espino Rodríguez and Padrón-Robaina, 2004). This indicates that the new competitive environment is harder to predict, which makes business management more complicated (Espino Rodríguez and Padrón-Robaina, 2004). Consequently, as competitive pressures intensify, smaller firms have to find ways of improving business performance (McIvor et al., 2009). In a more competitive business environment, there is heightened risk that many smaller firms (SMEs) will not survive (Blackburn et al., 2010). Therefore, SMEs have to think new ways of managing firms (Blackburn et al., 2010; Kotabe and Mol, 2009; Jiang and Qureshi, 2006). Therefore, the RBV identified a number of dimensions that make smaller firms more vulnerable than larger firms (Blackburn et al., 2010; Gooderham et al., 2004). Those dimensions are competitive pressures and insufficient competencies for survival (Blackburn et al., 2010; Gooderham et al., 2004). In response to these concerns, smaller firms should choose to outsource their activities by shifting what they traditionally handled in-house to external service providers (Kotabe and Mol, 2009; Lamminmaki, 2007, 2008). For instance, competitive pressure leads to outsource some functions or activities that can be improved by specialist service providers, in other words, turning to external sources to accomplish the desired objective (Espino Rodríguez and Padrón-Robaina, 2004; Quinn and Hilmer, 1994). Hence, outsourcing practice may cause hollowing out and an accompanying loss of competitive distinction (Kotabe and Mol, 2009; Kotabe, Mol, Murray, 2008; Bettis et al., 1992). Now, outsourcing practice is one of the vital strategies to meet demands for more well-organised ways to address organisational competitiveness (Jiang and Qureshi, 2006; Delmotte and Sels, 2008). In effect, the competitive environment in which SMEs operate are unstable and unpredictable (Blackburn et al., 2010; Gooderham et al., 2004), these mean that they should consider outsourcing as important tool to improve their performance (Lamminmaki, 2007, 2008; Espino-Rodríguez and Padrón-Robaina, 2005). However, the resource-based view (RBV) would also lead to suppose that SMEs utilise external accountants when they face competitive pressures as a function of the resources at the disposal of the firm (Blackburn et al., 2010; Gooderham et al., 2004).

3.5.2 Review of Empirical Studies Using RBV Framework

Gooderham et al. (2004) investigated the association between technical competence and the use of professional accountants' advisory services in RBV Model. Furthermore, Carey et al. (2006) examined the relationship between technical competence and outsourcing of internal audit activities. Technical competence was supported in both studies. Besides, Gooderham et al. (2004) examined the relationship between degree of competition and the use of external accountants in their RBV model. In addition, Lamminmaki (2007, 2008) used contingency theory in examining the relationship between the degree of competition and outsourcing of other service functions in the hotel sector. Degree of competition was not supported in both studies. Table 3.3 provides a summary of empirical studies that have tested the direct effect of technical competence and degree of competition on outsourcing based on resource-based view and other perspectives.

Table 3.3: Empirical Evidence on the Determinants of Service Function Outsourcing Decisions

Researchers	Function	Variables	Finding
Carey et al.(2006)	Internal audit	Technical competence	Supported
Gooderham et al. (2004)	Professional accountants' advisory services	Degree of competition	Not Supported
Gooderham et al. (2004)	Professional accountants' advisory services	Technical competence	Supported
Lamminmaki (2007)	Different Activities (i.e., Housekeeping, General Maintenance)	Degree of Competition	Not supported
Lamminmaki (2008)	Degree of accounting department involvement in outsourcing	Degree of Competition	Not supported

However, while the literature has considered competence and degree of competition in general, evidence of the importance of competence and degree of competition in relation to accounting function outsourcing within the SME context is both scarce and underdeveloped (Blackburn et al., 2010; Carey et al., 2006; Gooderham et al., 2004). More importantly, the studies discussed above, have been conducted in the developed countries, and a study to examine those factors impacting outsourcing of accounting practices is absent in developing countries.

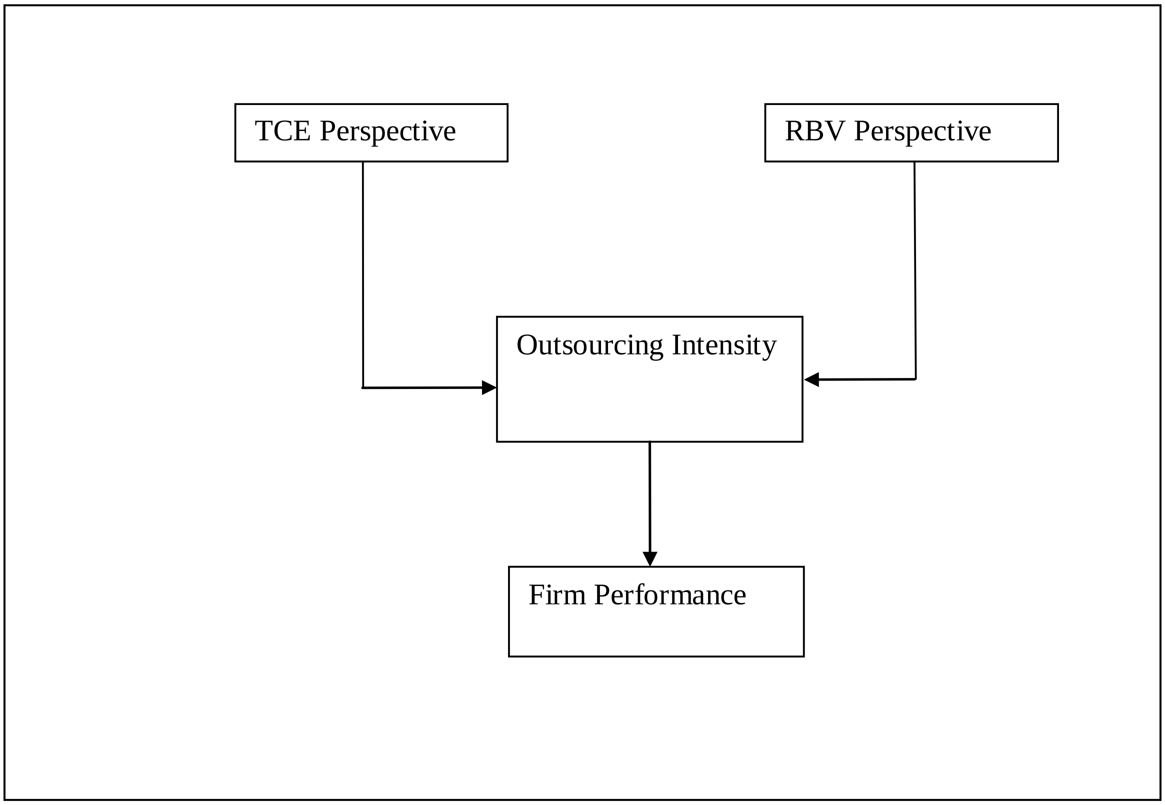
3.6 THE USE OF THE RESOURCE BASED VIEW AND TRANSACTION COST ECONOMIC PERSPECTIVE TO EXPLAIN FIRM PERFORMANCE

A major concern of the RBV is how a firm's resources develop and impact its performance (Gainey and Klaas, 2003). SMEs might use external accountants to provide services (i.e., financial planning) which directly improve their performance (Blackburn et al., 2010).

Therefore, the external accountants can help SME sector to achieve competitive advantage with their long-standing expertise in accounting such as systems and matters of finance and planning (Blackburn et al., 2010). In addition, the RBV argues that SME performance can be improved by obtaining knowledge and information skill from external sources (Bennett and Robson, 2004). As a result, the RBV of the firm, on one hand, provides a theoretical basis for the assessment of outsourcing that is potentially affect the firm performance (Irwin et al., 1998). Indeed, outsourcing gives a SME access to resources in the accounting firm as the external accountant processes accounting functions for the client (Everaert et al., 2006; Gottschalk and Solli-Sæther, 2006). Consequently, RBV perspective maintains outsourcing is a powerful vehicle for improving a firm performance (Marshall et al., 2007).

On the other hand, TCE provides a framework for understanding the firm and thus similarly helps identify a potential role for the small accounting firms in aiding SME performance (Carey, 2008). The TCE theory is concerned with the choice of firm structure; implicit in this literature is the assumption that minimising transaction costs is central to business success (Carey, 2008). Therefore, the accounting firm offer services such as financial statement preparation, payroll, and product costing to the SME sector and reduce their internal transaction costs (Carey et al., 2006; Carey, 2008; Everaert et al., 2010). In both instances, the professional accountants might contribute to firm performance by aiding in cost control (Carey et al., 2006; Carey, 2008; Everaert et al., 2010). Besides, according to TCE view, Lilly et al. (2005) argues that outsourcing practice is appealing to firms' managements since it develops some of the metrics used to improve firm performance. For instance, firms that outsource any function do so with the idea that the firm performance will increase (Lilly et al., 2005). Figure 3.3 shows the link between outsourcing and firm performance based on RBV and TCE perspectives.

Figure 3.3: Linking Outsourcing and Firm Performance: TCE and RBV perspectives



3.6.1 Firm Performance

Consistent with the RBV of the firm, the firm's fundamental purpose is to improve firm performance by obtaining resources and defending competitive positions which are critical to production, service and distribution (Wernerfelt, 1984; Barney, 1986; Conner, 1991). The RBV premises that firms will achieve competitive advantage by developing higher performance positions in activities that are valued them (Espino Rodríguez and Padrón-Robaina, 2004; Barney, 1991). In fact, the RBV indicates that firms can maximise their profits through outsourcing (Jiang and Qureshi, 2006; Yasuda, 2005; Gilley et al., 2004a). The RBV also argues that outsourcing enhance firm performance in the firm that is facing with limited capabilities and resources (McIvor, 2009; Han, Lee and Seo, 2008). Firms should build capabilities in areas that bring competitive advantage (Bustinza, Arias-Aranda and Gutierrez-Gutierrez, 2010; McIvor, 2009). This is more significant for smaller firms because they are facing with internal resource gaps (Gooderham et al., 2004; Blackburn and Jarvis, 2010). Therefore, smaller firms must consider outsourcing as a strategy to access resources, for garnering unavailable competitive advantages to improve their performance (Yasuda, 2005). For instance, outsourcing allows smaller firms to increase return on assets, minimise fixed costs, and increase profitability (Koudal, 2005).

TCE theory is another perspective to explain that outsourcing has a critical role in firm performance (Kroes and Ghosh, 2010; McIvor, 2009; Jiang and Qureshi, 2006; Espino Rodríguez and Padrón-Robaina, 2004; Yasuda, 2005; Bettis et al., 1992). Accordingly, Vita et al. (2010) claimed that:

> "The main tenets of TCT relate to the effect of governance choice on firm performance given the influence these transaction characteristics exert on the transaction cost- minimising tendency of the firm"(p. 2).

Consequently, possible benefits to the firm undertaking the outsourcing include higher profitability and the possible gains from access to the technical competence and expertise of the external service providers and overall firm performance (Strange, 2009; Gilley et al., 2004a; Espino Rodríguez and Padrón-Robaina, 2004). Accordingly, by outsourcing to external service providers, firms may achieve superior levels of performance of their staff, thus achieving improved firm performance (Gilley et al., 2004a). For example, by outsourcing activities, the firm will be better able to focus on the value-creating activities that take competitive benefit (Gilley et al., 2004a; Shang et al, 2008). Furthermore, Jiang et al., (2006) indicated that many firms get benefits from outsourcing by reducing costs, improving speed and responsiveness, reducing cycle times, improving innovativeness, increasing flexibility, and improving overall firm performance. For example, Jiang and Qureshi (2006) claim outsourcing (activities are not specified) will increase profitability (overall performance) of a firm in many ways as follows:

> "Staffing – the use of independent contractors provides employers the flexibility to hire help only when they need it and only for as long as they need it. Outsourcing allows firms to avoid costly benefits" (p. 51).
>
> "Capabilities – outsourcing enables even the smallest firms to have a specialist on staff. While it may not pay for them to own that person, firms can rent their expertise without adding to their payroll" (p. 51).
>
> "Facilities – while firms may need additional facilities to serve short-term needs, pouring cash into buildings may not match their long-term plans. When possible, focus on reducing inventory, another cash drain, to minimize the need for additional facilities. When more space is needed, firms may lease and still avoid long-term investment obligations" (p. 51).
>
> "Services – some services may be cheaper or easier to handle outside. Specific functions, such as accounting, recruiting or payroll management may be handled outside as well" (p. 51).
>
> "Payroll – salaries are a high proportion of a business's costs, particularly in service industries. Independent contractors are a direct way to outsource – hire for the task. When firms need staff in-house, another approach is to focus on incentive-based compensation rather than boost salaries across the board. Thus, when sales are up, revenue is available to cover the higher salaries. When sales are down, firms are not tied to unrealistic salary costs" (p. 51).

Taken as a whole, outsourcing will allow firms to achieve greater performance gains via obtaining specialised expertise and capabilities by firms (Han et al., 2008; Holcomb and Hitt, 2007).

3.6.2 Empirical studies- Association between Outsourcing and Firm Performance Based on RBV and TCE perspectives

There are several studies, which have examined the relationship between outsourcing and firm performance, although in combination with other activities. These empirical studies are discussed next.

Gilley and Rasheed (2000) examined the association between outsourcing (core and peripheral functions) and firm performance. They collected subjective data on firm performance in relation to outsourcing intensity from 94 manufacturing large firms in the United States (US). They measure performance with overall financial performance (return on assets, return on sales) and non-financial performance (innovation performance, stakeholder performance) based on subject data. The results of this study show no direct impact of outsourcing on overall firm performance.

Görzig and Stephan (2002) investigated the effect of outsourcing on firm performance of German manufacturing large firms utilising a large dataset of 43,000 firm-year observations. They utilised three proxies to capture the degree of outsourcing of the firms, namely, “material inputs over labour cost, representing the “make or buy”-type of outsourcing, external contract work over labour costs as proxy for the outsourcing of production functions, and external services over labour costs”. It can be shown that all three types of outsourcing lead to improved firm performance in terms of return per employee. Overall, only increased material input is significantly positively associated with overall firm performance (return over sales).

Benson and Littler (2002) compared the effects of outsourcing of core and support functions of large Australian firms using a survey among 1222 firms. The main objective is to examine the effect outsourcing on firm performance (reduction of labor costs and an increase in labor productivity). However, they could not find support for the relationship between outsourcing and firm performance.

In general outsourcing (i.e. activities were not specified), Jiang et al. (2006) provided empirical evidence of the difference between the performance of firms that outsource and firms that do not outsource (i.e. comparing outsourcing firms' performance with that of their non-outsourcing competitors). They examined the effects of outsourcing on the firm level performance of 51 large US firms based on audited accounting data. Indeed, they directly measured the impacts of outsourcing after the transactions were completed. They obtained the exact dates of the outsourcing by searching the press for outsourcing announcements and measured the profitability of the firm, cost efficiency and productivity involved within one year after the outsourcing, based on quarterly accounting data. Observing the absolute change of the performance measures and the development compared with a control group without outsourcing they did not find any change in the productivity and profitability of the outsourcing firms, but outsourcing improved cost efficiency.

Kroes and Ghosh (2010) evaluated the impact of outsourcing on business performance and supply chain performance, using empirical data collected from large manufacturing enterprises units operating in the US. They found that outsourcing significantly related to supply chain performance. The measurement indicators were applied for supply chain performance, including cycle times, delivery accuracy, delivery timeliness and return costs, and the measurement indicator for business performance comprises several key financial indicators, such as profit margin, return on sales, return on assets, and sales over asset. Taken together, the key findings of this study show the outsourcing is positively associated with supply chain and business performance.

Also in the US, Salimath et al. (2008) examined the effect of outsourcing (activities were not specified) on financial performance (profitability, sales revenue, net profit, growth in profits and in sales revenue). They found that outsourcing has a positive effect on financial performance.

Gilley et al. (2004a) examined the association between outsourcing (i.e. payroll and training) and firm performance. Their sample consists of 94 USA large manufacturing firms representing 16 two-digit SIC code industries. They measure performance with overall financial performance (Return on assets, return on sales) and non-financial performance (innovation performance, stakeholder performance) based on subject data. They concluded that outsourcing activities had a significant positive influence on non-financial performance. They concluded that outsourcing was not associated with firm financial performance.

In Canary Islands (Spain), Espino Rodríguez and Padrón-Robaina (2004) examined outsourcing of service operations (i.e. reception, administration and accounting, housekeeping, food and beverage, maintenance, leisure activities, security and surveillance) on financial and non-financial performance of a sample of 50 hotels. They found that outsourcing has a positive influence on the financial and non-financial performance.

The significance of the role of external accountants, reported in most studies reviewed by Bennett and Robson (1999), Berry et al. (2006) in the UK, was examined in the context of the advisory services of an external accountant and SME performance. For example, Bennett and Robson (1999) demonstrated an association between SMEs that obtained the advisory services of an external accountant and employment growth. In their study, SME respondents were placed into three growth categories: (i) declining/stable, (ii) medium growth, and (iii) fast growth. The percentage of SMEs that use an accountant was higher in the fast growth category than in the medium growth category and the declining/stable growth category. Hence, this study supports that the use of accountant’s services is associated with SME growth.

Berry, Sweeting and Goto (2006) explored the relationship between the four types of advisory services (e.g. business advice, emergency advice, financial management support and statutory advice) provided by an external accountant and SME performance (growth). This study revealed that the average growth of users of the services of an external accountant was significantly higher than the average growth of non-users. Consequently, Berry et al. (2006) concluded that utilisation of accountants' advisory services was positively associated SME performance. Therefore, the above discussions are summarised in Table 3.4.

Table 3.4: Empirical Research on the Relationship between Outsourcing of ServiceFunctions and Performance

Outsourcing	Source	Performance	Result	Theory
Human resource	Gilley et al. (2004a)	Financial performance (Return on assets and Return on sales) Non- financial performance (innovation performance and stakeholder performance)	Positive effect: innovation performance	RBV and TCE
Not specified	Gilley and Rasheed (2000)	Financial performance (return on assets and return on sales) innovation performance, stakeholder performance	No direct effect	RBV
Not specified	Jiang et al. (2006)	Cost efficiency, productivity, profitability	Not support for Productivity and profitability	TCE
Not specified	Salimath et al. (2008)	Profitability, sales revenue, net profit, growth in profits and sales revenue	Positive effect on all	RBV
material inputs over labor cost	Görzig and Stephan (2002)	return over sales	Supported	-
Core and support functions	Benson and Littler (2002)	labour cost reductions labor productivity	Not supported	-
Not specified	Kroes and Ghosh (2010)	Supply chain performance (cycle times, delivery accuracy, delivery timeliness, and return costs) Business performance (financial indicators such as profit margin, return on sales, return on assets, and sales over asset)	All Supported	RBV and TCE
Service operations	Espino Rodríguez and Padrón-Robaina (2004)	Financial and non-financial performance (indicators were not specified)	Supported	RBV
External accountants' advisory services	Bennett and Robson (1999)	SME performance: employment growth: (a)declining/stable, (b) medium growth, and (c) fast growth	Supported	-
External accountants' advisory services	Berry et al. (2006)	SME performance (growth)	Supported	-

To sum up, whilst prior research has examined the association between outsourcing and firm performance in general (see, Gilley and Rasheed, 2000; Görzig and Stephan, 2002; Benson and Littler, 2002; Jiang et al. 2006; Kroes and Ghosh, 2010; Salimath et al., 2008; Gilley et al., 2004a; Espino Rodríguez and Padrón-Robaina, 2004), no empirical study has specifically investigated the relationship between outsourcing of accounting functions and SME performance. Consequently, motivated by the benefits to outsourcing claimed by some researchers and the corresponding lack of any direct evidence as to the truth behind these assertions, this study aims to determine whether there is a relationship between outsourcing of accounting functions and SME performance. In general, despite the growing interest in accounting outsourcing, a study to examine the outsourcing accounting functions is missing.

More importantly, prior studies have measured performance based on financial and non-financial performance (Görzig and Stephan; 2002; Görg and Hanley; 2004; Jiang et al., 2006; Espino Rodríguez and Padrón-Robaina; 2004), but those measurements of firm performance in terms of financial and non-financial performance are not suitable for SMEs because SME performance should be evaluated in terms of the SME management goals (Blackwood and Mowl 2000; Jarvis, Kitching, Curran, Lightfoot, 1996). Therefore, the key financial goals pursued by SME executives include profitability, growth in sales, return on assets, and cash flow (Dyer and Ross, 2008: Sarapaivanich and Kotey, 2006; Jarvis et al. 1996) and non-financial goals comprise lifestyle, independence and job security (Sarapaivanich and Kotey, 2006; Fielden, Davidson and Makin, 2000; Akande, 1994; Glancey, 1998; Kuratko, Hornsby and Naffziger, 1997).

3.7 THE ASSOCIATION BETWEEN TRANSACTION COST ECONOMICS (TCE) THEORY AND RESOURCE- BASED VIEW (RBV)

So far, the discussion has treated transaction cost economics and the resource- based views as independent approaches, there are a number of studies supporting the need for both perspectives in outsourcing decisions (Ellram et al., 2008; Holcomb and Hitt, 2007; Jacobides and Winter, 2005; McNally and Griffin, 2004; Madhok, 2002; Poppo and Zenger, 1998). In fact, the prescriptions proposed by each theoretical perspective is complementary, and each theoretical perspective by itself cannot describe outsourcing decision completely (McIvor, 2009; Marshall et al., 2007). Although the TCE and the RBV are concentrating on two different issues, (1) TCE premises on why firms exist and (2) the RBV premises on why firms differ in performance, these two issues are very applicable to the outsourcing decision (McIvor, 2009; Marshall et al., 2007). The RBV focuses on developing definite capabilities and resources, which have significant implications for which functions should be conducted within the firm which functions should be performed by external service providers or outsourced (McIvor, 2009; Marshall et al., 2007). The RBV also help to analyse capabilities and resources of the firms, which can connect outsourcing with firm performance and the competitive priorities of the firm (McIvor, 2009). TCE will improve our perception of whether it is more suitable to outsource or insource a service function (Stratman, 2008). TCE emphasises the existence of firms as a means of reducing the opportunistic behaviour (Conner, 1991). Furthermore, the RBV examines the enterprise as a bundle of valuable capabilities and resources that produce competitive advantage and enhance firm performance, whilst TCE considers the firm as an avoider of negative opportunism (Conner, 1991). For example, in a case where a firm has sufficient resources to develop a difficult-to imitate capability and the potential for opportunism is high, their activities should be performed internally (Marshall et al., 2007).

The RBV concentrates on achieving competitive advantage via analysing organisational resources and capabilities and link outsourcing with firm performance (Marshall et al., 2007), whilst TCE explains firms as institutions for developing economic activity or concentrates on the role of efficient governance via transaction costs in determining the boundary of the firm (Bahli and Rivard, 2005)

More importantly, asset specificity as a critical factor in sourcing decisions should be analysed from both theories (TCE and RBV), particularly when firm performance is being studied (Watjatrakul, 2005; Espino-Rodríguez et al., 2008). For instance, the RBV demonstrates that the asset specificity, mainly the human assets embodied in firm-specific routines such as knowledge and expertise, are significant to firm performance (Barney, 1991). While RBV concentrates on the opportunity to produce and sustain competitive advantage, TCE perspective emphasises the relationship between characteristics of transaction costs and the likelihood of ex post opportunistic behavior (Espino-Rodríguez et al., 2008; Leiblein and Miller, 2003). In effect, the RBV theory indicates that market failings and opportunism solely do not determine outsourcing decisions, it is, however, the positive impact that the non-outsourcing of specific functions may have (Espino-Rodríguez et al., 2008). Effectively, the RBV focuses predominantly on production skills whilst TCE is focusing principally on governance skills (Marshall et al., 2007). For instance, utilisation of the two theoretical perspectives enhances our comprehension of the relationships and transactions among factors that affect management decisions on the subject of insourcing and outsourcing (Gulbrandsen et al., 2009). Taken as a whole, in practice, outsourcing practice is being influenced by both RBV and TCE predictions (Everaert et al., 2006, 2010; McIvor, 2009; Marshall et al., 2007; Carey et al., 2006; McNally and Griffin, 2004; Madhok, 2002).

3.8 OUTSOURCING OF ACCOUNTING FUNCTIONS IN SME ENVIRONMENT

In the 1980s, many firms outsourced their activities that traditionally had been carried out internally (Caplan, Janvrin and Kurtenbach, 2007). Even before 1990, some firms had outsourced internal audit activities to accounting firms for reasons that seemed compelling (Caplan et al., 2007). Up till now the implications of outsourcing practice go beyond internal audit activities (Ellram et al., 2008; Caplan et al., 2007). However, it is argued that small accounting practitioners (external accountants) are more competent than internal accountants as they are able to develop technological efficiencies and gain economies of scale (Carey et al., 2006; Everaert et al., 2006). Consequently, the empirical evidence on the role of the professional accountants and accounting function outsourcing in the SME context is discussed next.

3.8.1 The Role of Professional (External) Accountants in SMEs

"Over one half of the 2.5 million professional accountants who are members of the member bodies of IFAC work in business, many of them in roles which are critical to the success of the enterprise"(IFAC, 2005, p.1). The professional accountants play very diverse role in whichever sector of the economy they work (Devi and Samujh, 2010; IFAC, 2007). For example, professional accountants provide accounting practices to SME sector, such as taxation, information systems, financial reporting, business intelligence and corporate finance (IFAC, 2007). "They also work as internal or independent external auditors or as consultants across a range of specialist areas" (IFAC, 2007, p.1). Nonetheless, there is no governmental restriction on the joint provision of compliance (statutory) and non- compliance services in the SME environment (Blackburn et al., 2010). This is because in the SME environment,firms experience greater alignment between owners and managers and therefore less agency conflict than in large private and publicly listed enterprises (Blackburn et al., 2010). In fact, the role of the professional accountant or small accounting firm is moving towards more involvement in financial management and strategic planning, financial and management accounting beyond routine transaction work (Naderian, 2010; Devi and Samujh, 2010; Hasle et al., 2010; Ong, Azmi, Isa, Jusoh, Kamarulzaman, 2008; Burns and Scapens, 2000).

The role of small accounting practitioners is emerging, as they are seen as the most important provider of accounting and support services for SMEs. This has also been noticed by academic scholars and public authorities looking for means to help SMEs (Hasle et al., 2010; Blackburn and Jarvis, 2010). Most professional accountants not only offer support services on matters related to finance and economy but are also expanding into broader fields such as management accounting, financial planning, business strategy and planning, risk management and performance management (Naderian, 2010; Ong et al., 2008). For instance, in a Norwegian Survey approximately one quarter of the professional accountants provided services in financial management and human resource management, which demonstrates that a significant number of professional accountants offer services outside a narrow scope of traditional financial accounting to their SME clients (Døving and Gooderham, 2008).

Professional accountants often give emotional support to their SME clients, who are often facing traumatic changes in lifestyles and relationships with their clients during succession processes (Martin, 2005; Hasle et al., 2010). For example, Naderian (2010) argues Iranian small accounting firms not only attest to the credibility of financial information used to monitor performance, but can also provide services such as design and installation of reporting and control systems, budgeting, customer profitability analysis and financial management. Hence, small accounting practitioners possess legitimate expert power linked to the requirements for SMEs to perform accounting tasks and need to develop value-adding support services relationships requiring different technical expertise and skills (Devi and Samujh, 2010; Martin, 2005). In fact, the professional accountant is a critical source of information and competitive advantage for SME owner-managers in many of their decision-making and financial planning processes (Naderian, 2010; Breen et al., 2003). Interestingly, small accounting firms provide support on computer accounting system factors such as customisation of the software to suit the businesses needs, available software, the businesses reporting requirements, implementation, and the ability to interface with other software to SME sector (Breen et al., 2003). Professional accountants not only prepare financial statements but also they provide functions such as decision making, internal management planning, control and strategic planning to small firms (Chittenden, McConnel and Risner, 1990; Deakins et al., 2001). The role of the external accountant is extremely important to the growth/survival of smaller firms, especially where the SME owner-managers do not have sufficient financial and management skills (Brown, Saunders, and Bresford, 2006).

Small accounting firms are noteworthy help to the SME management in managing the firm especially when it comes to the introduction and implementation of changes (Gooderham et al., 2004). Moreover, the role of the external accountant is perceived by SMEs as helping them to cope with tax requirements, even though empirical evidence suggests that they provide activities such as management accounting (product costing) and financial management services beyond compliance work (Evans, Ritchie, Tran-Nam and Walpole, 1996; Marriott and Marriott, 2000). For instance, small accounting firms have provided much of the financial management and taxation services for the SMEs and they are as the preferred professional adviser to SMEs (Leung et al., 2008).

Small accounting firms were evolving into larger, more broad-based strategy and business consulting practices focusing on niche industries (Farrell, 1998). Therefore, small accounting firms and sole practitioners are likely to play a significant role in the multidisciplinary practice arena in SME environment (Ong et al., 2008; Jayabalan et al., 2009; Amani and Davani, 2010; Blackburn and Jarvis, 2010). Although small accountancy practices provide advisory works to their SME clients, the provision of accountancy activities remained the core of their activities (Ong et al., 2008; Jayabalan et al., 2009; Blackburn and Jarvis, 2010; Martin, 2005). For example, Martin, (2005) argue that professional accountants not only provide support services on a wider range of issues but also offer accountancy activities such as management accounting and financial planning to their SME clients (Ong et al., 2008; Martin, 2005). Hence, small accounting practitioners need to be able to empathise and relate to SMEs' situations when providing accounting functions, as well as combining rational, generalist approaches with an ability to draw in specialist competence and expertise where required (Devi and Samujh, 2010; Blackburn and Jarvis, 2010; Martin, 2005; IFAC, 2007). It is clear that external accountants can play an important role in improving awareness and in development of SME growth (Martin and Hartley, 2006). This can result in a close personal relationship between professional accountants and SMEs, but equally it means that the extent to which SME owner-managers obtain a valued source from professional accountants (Perry and Coetzer, 2009; Lewis, Massey, Ashby, Coetzer, and Harris, 2007). Consequently, "professional accountants contribute to the growth of economies and ultimately to the well being of society" (IFAC, 2007, p. 2).

3.8.2 Empirical Evidence- Accounting Functions are outsourced by SMEs

In an empirical study of small firms in UK, Sian and Roberts (2009) found 57.2 percent of small owner/managers outsource accounting activities to professional accountants, mainly to provide tax or VAT information (30.8%), to prepare financial statements (51.1%), or even to run the accounting system (18.1%). Often these professional accountants provided some additional services (86.3%), written (36.9%) explanation or analysis of the accounts or the most common being a verbal (61.1%).

In an empirical in 121 Belgian SMEs, Everaert et al. (2007) distinguished financial accounting tasks into two categorizations routine and non-routine tasks. Functions such as period end accounting, preparation of financial statements, VAT compliance and corporate tax compliance were considered as non-routine tasks, whereas routine tasks included the entry of invoices and preparation of interim reports. They revealed that more than half of SMEs utilise a combination of outsourcing and insourcing of accounting services, while 35 percent of the SMEs use only in-house accountants' services and 12 percent use total outsourcing of accounting services.

In 126 Belgium SMEs, Everaert et al. (2006, 2010) examined the association between outsourcing of financial accounting tasks as dependent variable and four independent variables such as asset specificity, environmental uncertainty, behavioral uncertainty and frequency of transaction. They found that asset specificity and frequency of transaction is significant driver in outsourcing of accounting practices.

Devi and Samujh (2010) identified 34 types of service currently offered to SMEs based on views of 174 Malaysian small and medium-sized practices (SMPs). The respondents identified traditional types of services dominate the non-compliance offerings by small accounting firms, such as bookkeeping, cash flow forecasting and tax planning. A wide range of other services are offered, including business coaching, grant application, and strategic planning. Some firms are offering support in the relatively ‘newer’ areas of forensic accounting and ISO standards. However, small accounting practitioners spend 60 percent of their time on compliance tasks – principally tax filing, auditing and secretarial services – that are not deemed to be part of business advisory services. Some of small accounting planned to extend their services (54.4%) appeared to favour areas such as: business planning, business coaching, internal controls, liquidations or corporate recovery, and internal audit.

In an empirical study of 164 Malaysian SMEs, Jayabalan et al. (2009) found that 70 percent of the SMEs appeared to outsource certain accounting functions (e.g. financial reporting, management reporting and tax filing, bookkeeping, accounts receivable and accounts payable).

Earlier in a survey of 145 Malaysian SMEs, Ong et al. (2008) identified 11 types of accounting functions that SMEs use. Of these, the most widely used were accounting, market research, tax, legal, corporate services and assurance services. Those generally outsourced were accounting (32%), corporate services (68%), legal services (89%), tax (86%), assurance services (85%), and market research services (8%).

In a questionnaire survey of 336 micro and small businesses in the UK, Kirby, Najak and Greene (1998) distinguished statutory services from non-statutory services in the SME environment and found that external accountants were the most likely source of non-statutory services.

In a survey of 100 SMEs in Ireland, Doran (2006) distinguished also statutory accounting services from non-statutory services. He concluded that the services outsourced by SMEs included tax compliance (77%), firm secretarial(69%), statutory audit (63%), statutory accounts preparation (77%), payroll services (20%), and limited SME respondents pointed out that they outsourced non-statutory services comprising management accounting (9%), succession planning (11%), management consultancy and IT consultancy (9%), business advice (46%), tax consultancy(43%), financing advice(31%) and non- statutory audit (17%).

Using semi-structured interviews with the owner-managers of 15 small firms in the UK, Marriott and Marriott (2000) concluded "there appears to be significant potential for accountants to expand the management accounting services they provide to smaller firms" (p475). They found that the potential role of the professional accountant as a provider of any service beyond statutory financial reporting compliance is not well recognised by respondent small businesses.

Again in the UK context, in a survey on the use of financial information by small firms, Collis and Jarvis (2002) noted that three sources of financial information were utilised in the small firms; cash flows, monthly/quarterly management accounts and bank statements. In their view these financial management practices were rather sophisticated and that the role of the professional (external) accountants in provision of accounting activities provides the opportunity for the support services.

In an empirical study of SMEs in Australia, Holmes and Nicholls (1989) found that small firm owner/managers typically outsource for statutory services, but rarely for other services. The main statutory services outsourced from an external accountant were preparation of tax returns (88.8%) and balance sheet and profit/loss statements (69.3%). Other than budgeted information (e.g., profit and loss statements (26.6%) and cash flow statements (16.3%), less than 5% of respondents purchased other “non-statutory” services from their external accountant.

DeThomas and Fredenberger’s (1985) survey of 360 small businesses in Georgia, USA found that 81 percent of the small enterprises regularly outsource summary financial information (traditional financial statements, bank reconciliation and operating summaries). Furthermore, this study revealed that over 50 percent of small firms used an internal accountant for recording transactions whereas external accountants carried out preparation of financial statements. In addition, this study shows that external accountant were responsibility for the bookkeeping (25%) and other accounting tasks (53%).

In Australia, Leung et al. (2008) examined accounting services that SMEs outsource to external accountant. They reported that external accountants provide many accounting services to SMEs such as financial management and taxation support, and they have long been seen as the preferred professional adviser to SME firms.

In brief, whilst these studies discussed above have been conducted in developed countries, literature outsourcing accounting activities in emerging economies or lesser developed economies such as Iran is absent except a limited research conducted in Malaysia (Devi and Samujh, 2010; Jayabalan et al., 2009; Ong et al., 2008). Furthermore, a study to examine the association between factors such as asset specificity, behavioural and environmental uncertainty, frequency, trust, technical competence, and degree of competition and outsourcing of accounting practices is missing in developing economies.

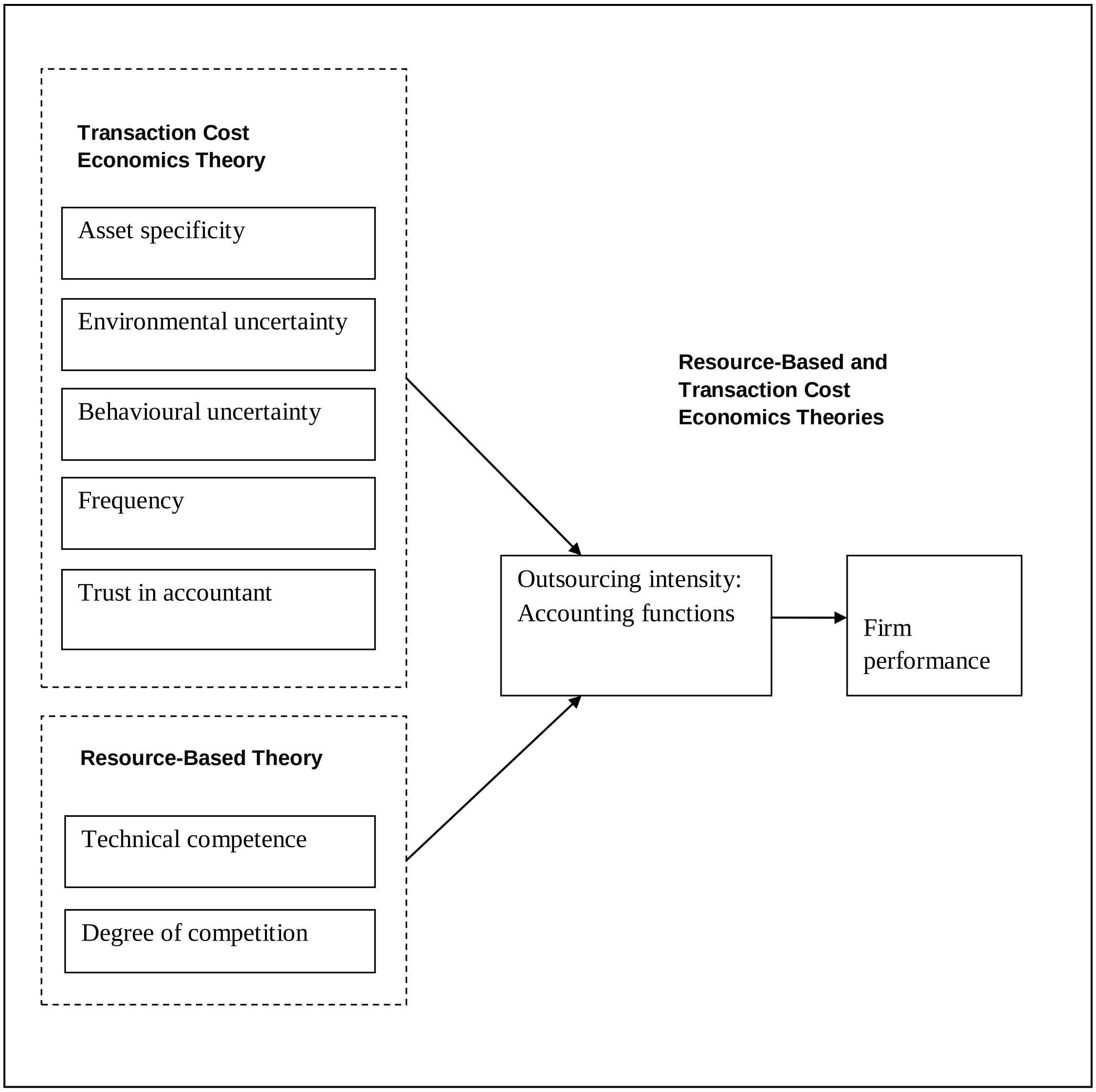
Based on the above discussions, Table 3.5 summarises the types of services that SMEs outsource to external accountants.

Table 3.5: The Services that SMEs Outsource to Professional Accountants

Sources	Accounting Service functions
Everaert et al. (2006, 2007, 2010)	Period-end accounting, preparation of financial statements, preparation of interim profit and loss accounts, VAT compliance and corporate tax compliance and entry of invoices and financial transactions
Devi and Samujh (2010)	Bookkeeping, business coaching, business formation/start-up, business plans, business valuation, cash flow forecasting, firm listing, compliance filing tax returns, design/review internal control systems, due diligence, grant applications, IT system implementation, internal audit, ISO standard compliance, liquidations and/or corporate recovery, loan applications, mergers and acquisitions, negotiations with inland revenue board, payroll services, profit improvement programmes, recruitment/head hunting/sourcing staff, secretarial services, sourcing grants/incentives, statutory audit, strategic planning, taxation planning, GST, loan monitoring, forensic accounting, and financing arrangement and rearrangement
Doran (2006)	Statutory accounts preparation, tax compliance, firm secretarial services, statutory audit, payroll, business advice, tax consultancy, financing advice, non- statutory audit, management accounting (product costing), succession planning, management consultancy and information technology consultancy
Jayabalan et al., (2009)	Account payable, account receivable, general ledger, internal audit services, lease administration, payroll, property accounting, and sales audit to tax
Hamzah et al (2010) and Reddy and Ramachandran (2008)	Preparation of financial statements, financial reporting, management information system, management accounting, and financial planning and analysis, bookkeeping, general ledger accounting, accounts payable, fixed assets accounting, inventory management, reconciliations, payroll accounting, tax strategy; accounts receivable and internal controls.
Ong et al. (2008)	Accounting (e.g., bookkeeping, financial statement compliance, budgeting/forecasting, product/service costing, costumer profitability analysis and financial planning); Taxation (i.e., tax compliance, tax planning, tax dispute resolution and tax incentives application); Assurance (i.e., financial audit, internal audit, internal control review and financial due diligence); Corporate(e.g., mergers & acquisition and firm secretarial services); Corporate finance (i.e., funding raising, financial management services and business restructuring); Business consulting services (i.e., business strategy and planning, insolvency and receivership, HR consulting, risk management, performance management and control systems)

Figure 3.4 draws together the discussion in this chapter to summarise a diagrammatical representation of the theoretical model that underlies the research investigation in this study.

Figure 3.4: Theoretical Model



3.9 SUMMARY AND CONCLUSION

The objective of this chapter has been to provide an overview of the theories and critically evaluate the extant outsourcing literature to identify the research gaps. The theories described are transaction cost economics (TCE) and resource- based theories. These two theories were chosen as they were all seen as having significant relevance to the sourcing decisions. However, this is not to infer that other theories may not also inform an understanding of sourcing decisions. TCE theory is the main theory drawn on in this study and thus has dominated the bulk of the chapter's discussion. TCE model discusses the significance of main transaction attributes, such as asset specificity, environmental and behavioral uncertainty, frequency and trust. In addition, resource-based model focuses competence and competition. Above and beyond, both theories link outsourcing to firm performance as discussed in this chapter.

In spite of considerable evidence that asset specificity, environmental uncertainty, behavioral uncertainty, frequency and trust are significant factors influencing outsourcing intensity, empirical evidence on the role of trust on outsourcing decision is scant. Furthermore, empirical research investigating factors impacting outsourcing of accounting practices is also limited. Additionally, although a limited number of studies examined the factors, such as degree of competition, technical competence on outsourcing in general (i.e., housekeeping, internal audit functions), an empirical study to examine those factors on accounting function outsourcing is missing.

While there have been empirical studies of other service function outsourcing effects on firm performance, no empirical research has specifically addressed the impact of outsourcing of accounting practices on SME performance. Besides, there is no study in the accounting literature that investigates outsourcing based on combination of RBV and TCE perspectives. Additionally, the literature evidences that there is no research that examines the mediating role of accounting outsourcing empirically.

Drawing the discussion in this chapter, the next chapter develops the specific hypotheses based on the theoretical model developed in this chapter. The theoretical model is further refined and discussed in the next chapter.