



DEFICIENCIES OF TURKISH SMEs WITH REGARD TO SUSTAINABILITY, CORPORATE GOVERNANCE AND ACCOUNTING POLICIES *

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ABSTRACT

Today's ever-growing challenges in local and global economies pose threats for the sustainability of Small and Medium-sized Enterprises (SME). As multinational companies invade local markets, local businesses continually suffer. In addition to financial distress, internal dynamics such as fraud, transparency matters, and business ethics play principal roles for jeopardizing the sustainable life spans of SMEs as well. By the same token, violating going concern by employing manipulative accounting methods to adjust financial statements merely act as a palliative measure. The aim of this paper is to investigate the deficiencies of SMEs and propose remedies to cure these areas. Data is collected from 104 Turkish accounting professionals by means of survey method. Findings of the study uncover an imperative implication that if Turkish SMEs wish to have sustainable life spans, they need to allocate the most extent of emphasis on the variables that make up the *internal information systems* factor some of which are efficiently functioning reporting and accounting system, effective organizational structure in addition to effective politics and procedures. Results of this study will be fruitful for not only academics but also for the industry in terms of pointing out what specific areas need improvements in the name of sustaining the survival of SMEs.

1. INTRODUCTION

External factors pose threat for the sustainability of SMEs at all times. Enterprises have very limited control, if any, over these external factors. Rapid changes in technology, vulnerable economies with fluctuating interest rates and parities, all play important roles in the sustainability of SMEs. There are limited proactive measures to be taken for these external factors since some of these factors may even strike an economy overnight. Imperative weight lies on the internal actions taken by the decision makers in the name of avoiding failure. Factors that can be attributed to the failure SMEs need to be clearly identified. When unwise decisions are made, consequences may be fatal for the entity.

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Therefore it is of the essence to formulate what areas is deficient pertaining to SMEs so that failure can be prevented. The purpose of this study is to investigate and define the deficient areas of Turkish SMEs. In doing so, SMEs themselves have not been directly taken into consideration since feedback gathered from these entities is expected to be biased simply to the extent that an average business will never admit evading tax. However, accounting professionals whose foremost work is to undertake the bookkeeping and consulting of these entities are expected to provide the most objective and unbiased feedback for this research. The results of the research are intended to construct guidelines for SMEs for empowering sustainability, since the most significant deficient areas will be identified.

The paper provides a comprehensive literature review highlighting the definition of SMEs, their occupancy and weight in Turkey and Turkish economy, relationship between sustainability and SMEs, and last but not the least, underlining the significance of business ethics in terms of sustainability. Literature review is followed methodology where sample, research design, and measurement instruments are clearly presented. Results of the research are conducted by a reliability analysis and finally examined under discussion and conclusion.

2. LITERATURE REVIEW

2.1 Small and Medium-sized Enterprises Definition

Although there is not one generally accepted definition for SMEs, on fact is certain: They are crucial to the economies in which they exist. International Accounting Standards Board (IASB) defines an SME as an entity holding no public accountability. Because of the fact that do they not issue debt or equity securities, nor they hold assets as a fiduciary for a broad group of outsiders and that they are not entrusted with public resources, they do not have public accountability (www.fei.org, 2007). Official Journal of the European Union (2003) defines SMEs as business entities made up of enterprises which employ fewer than 250 persons and which have an annual turnover not exceeding 50 million Euros, and/or an annual balance sheet total not exceeding 43 million Euros”.

Threatening nature of harsh competition in the market acts as a triggering force to push SMEs to always innovate to remain in the contest. The presence of SMEs have significant subsidy to the welfare of the economy, simply to the extent that they do create jobs. Some significant percentages of SMEs around the globe demonstrate how important they are to the well being of their economies: 96 percent in England, with a high percentage of 99.9 percent in France, 99.8 percent in Germany, 98.6 percent in India, 97 percent in Italy, 99.4 percent in Japan, 97.8 percent in South Korea, and 97.2 percent in the United States of America (Deloitte Touche Tohmatsu, 2007). Considering the fact that SMEs constitute 97.2 percent in the United States, it is fair to state that the American economy is reliant on SMEs.

In addition to financial enhancement within the economy due to endeavors of SMEs, jobs are fueled for women, minorities, and many other interest groups in the community (Ferrel et al., 2011). They are a chief source of entrepreneurial skills, innovation and employment. Micro, small and medium-sized enterprises play a central role in the European economy. Within the European Union of 25 countries, there are over 23 million SMEs, which provide approximately 75 million jobs and represent 99 percent of all business (Verheugen. 2005)

2.2 Turkish SMEs

SMEs constitute 98 percent of all enterprises, 76.7 percent of actual employment, 26.5 percent of investments, 38 percent of value added, and 10 percent of all exports in Turkey. Additionally they make up 99.32 percent of the total number of enterprises is in the manufacturing sector, which are well over 250,000 enterprises in total (Kaya, 2011).

By early 1980s, with heavy deregulation in many areas in Turkey, a new texture of marketplace was born where there were much more room for entrepreneurs when compared to pre-1980 era. This new entrepreneur-encouraged transformation has created great deal of opportunities for those entrepreneurs to establish their own businesses. With deregulation come liberal economy; and this new synthesis with freed policies provided bases for transforming the economic structure from a state-oriented economy to the free market (Uygur, 2009).

Even with the newly set free market and its contributions to encourage SMEs, it is well accepted that SMEs are disproportionately impacted by stringent regulation compared to large firms, and therefore some researchers recommend that legislation appropriately be written towards SMEs (Agan et al., 2013).

However, SMEs have limited resources, capability, competency, flexibility, skills, and knowledge. They lack technologies and capital in order to enter new markets, meet new strong competitive challenges, increase competitive forces, and have a leading edge over competitors. Thus, it is indispensable that SMEs need to innovate, look for potential strategies, develop new skills, acquire critical resources, gain market access, develop new technologies, attain important scale economies, and enhance firm reputation through delivering quality good and/services at competitive prices (Lohrke et al., 2006 cited in Ussahawanitchakit, 2008).

2.3 Sustainability and SMEs

“Change. Change. Change. We must learn to deal with it, thrive on it. That’s today’s relentless refrain. But it’s incorrect. Astoundingly, we must move beyond change and embrace nothing else than literal abandonment of the conversations that brought us to this point. Eradicate ‘change’ from your vocabulary. Substitute with ‘abandonment’ or ‘revolution’ instead (Peters, 1994).

Within this context, to enhance the endurance of survival skills of SMEs, one proposed method from the literature is a sustainability report, which aims at clarifying myopic sight of SMEs, which well may hinder these financially inflexible entities to sustain their existences. This report briefly aims at improving the following areas of SMEs:

- Focusing on the customers where the sustainability report could be exploited as a *marketing and commercial tool*, even if the consequent benefits will be clearly quantified in the medium– long term,
- Setting up and improving relationship with public authorities and the community where the sustainability report could be a way to better inform and involve them, establishing an *extremely transparent dialogue*,
- Paying a great deal of attention on the relationship with employees, where the sustainability report is a good way to make them aware of their responsibilities and to involve them even more in the company’s activities, thus *improving the quality of the workplace*,
- Last but not the least, since the suppliers’ choice is linked exclusively to the *quality of raw materials*; the sustainability report could be considered only as a tool for spreading the culture of the corporate social responsibility issues. (Borga et al., 2009).

Numerical balance sheet values, which show performances of enterprises in today’s world, are not sufficient indicators of real performances and values of enterprises alone. What is important is the sustainability of these performances and indicators of success. In order to provide sustainability in enterprises, it is necessary to succeed in the creation of a chain of values on all of the social stakeholders starting from the supply chain. And this becomes possible by the adoption of environmental and social elements within the framework of a principle of corporate governance and management structure and by minimization of the probable risks and costs that may be encountered within the process. For this reason, corporate enterprises that have adopted transparent, responsible, and accountable governance and management principles endeavor to attain to fundamental and environmental targets within an application of a sustainable environmental management structure as well as within the framework of a target of zero waste, ‘carbon neutral’ production and with an approach of life cycle for the products. At the same time, such enterprises aim at managing, as a part of their sustainability, such social values as establishment of workers’ health and occupational safety, provision of social rights and equality of opportunities, presentation of possibilities of education and training, and freedom of getting organized. The approach which encourages the enterprises in the market to operate for a sustainable development also ensures that enterprises see their probable environmental and social effects as one of the basic items in their accounting system, therefore they define such matters as part of their fundamental work processes. For this reason, understanding corporate sustainability encourages enterprises to have a more innovatory nature by planning the probable risks and costs beforehand.

From late 20th century until today, business entities are forced to modify their objectives due to constant changes in many areas from technology to know how. Since enterprises are profit oriented entities, the understanding that accepts all kinds of activities to increase accounting profits are true and real has been superseded by an understanding which accepts such an organization of activities to increase economic profits and which promotes economic profits. Expectations with financial contents have been superseded by expectations with social contents. In reality, financial expectations increased the opportunities to compete in the new order for enterprises, which apply implementations that have social contents and protect social values with high social responsibility. (Kuşat, 2012) Even though sustainable development is accepted to be a concept, which contains both ethical and social and technological issues in the modern world, it is seldom evaluated to be a corporate issue. (Hoverstadt and Bowling, 2005).

Literature focusing on the relationships between enterprises and competition revolves around two fundamental questions:

- Why do some enterprises compete more successfully in comparison to other enterprises?
- What can enterprises do in order to make their competition advantages sustainable? (Teece et al., 1997)

In order to understand the success of enterprises in competition, emphasis is made on benefiting from introverted organizational advantage models, which propose internally focused behaviors instead of externally focused propositions. As a concept, sustainability contains the themes of economic development, social development, and protection of the environment. The fact that sustainability is habitually associated with economic development is actually directly related to the activities of the decision-making units. It is not sufficient for commercial entities to be enterprises that merely manufacture products and that create values; while carrying on with these ordinary activities of theirs, it is necessary that they should abolish and eliminate or at least minimize their negative external effects (Hahn and Scheermesser, 2006). Unless they successfully manage to identify and prepare themselves for awaiting risks, they may not be eligible to cope with challenges and sustain their operations.

According to the results of a research carried out by the United Nations Global Principles Agreement on the CEO's of 766 enterprises in the year 2010 which operate in various countries, the most effective and influential factors, which encourage enterprises in the field of corporate sustainability, are as follows;

1. The fact that the increasing brand value, reliability, and esteem increase the profitability of the enterprise,
2. The fact that increasing the motivation of the personnel also increases the profits of the enterprise,
3. The fact that employment of qualified personnel becomes easier with the increase in the profits of the enterprise,

4. The fact that as a result of the legitimacy in the eyes of the society a competitive advantage is obtained against the competitors,
5. The fact that the possibilities of obtaining financial support from internationally responsible investment companies become easier;
6. Finally the changing enterprise demands of the consumers whose level of consciousness has increased (Istanbul Stock Exchange, 2011).

It is possible to evaluate the internal elements of corporate sustainability under the subtitles of corporate citizenship, corporate management, corporate social responsibility (CSR), corporate learning, corporate information management and transfer, corporate esteem, corporate social capital, corporate value, and last but not the least corporate happiness. Enterprises are expected to share their financial successes that they generate on a quantitative basis with their employees, customers, and other social stakeholders such as their suppliers, public establishments and organizations, media, and related non-governmental organizations through sustainability and corporate social responsibility reports that they have prepared. These positive studies do not only increase the loyalty of the customers and employees to the enterprise but also they contribute to the brand value of the enterprise. In today's world, brand value of many global corporations has a worth much higher than their remaining assets including fixed assets as well.

It is clear that sustainability is vitally important for enterprises to the extent that corporate sustainability performances of the enterprises are used as investment criteria as well since many individual investors, portfolio managers, and various responsible investment funds make investments in sustainable enterprises. The most important reason for this is that the value of the shares of the enterprises whose managers can plan and manage the social and environmental risks by adopting an understanding of management which involves transparent and responsible management style increase very steadily in the long-run. For this reason, within the framework of such neutral and objective and specific criteria as 'Dow Jones Sustainability Index' the structures, which determine and grade the sustainability of enterprises shows us the fact that the importance of corporate sustainability is a fundamental standard for enterprises whose shares are purchased and sold in stock exchanges. Financial crises and ecological changes are few of many indicators that short-term myopic strategies not in accordance with sustainability will not last for long. Especially in the Western European Countries and in the United States, there are many examples that show us the fact that those enterprises which have internalized sustainable applications are not adversely and negatively affected by the ongoing economic crisis. The enterprises in Turkey are also obliged to put the new applications into practice within the framework of sustainability. For this reason, for a sustainable development, the enterprises are obliged to develop business and work models which will help them compete in the low carbon production in the future in a creative and responsible manner.

All and all, SMEs are seeking for a relatively simple, effortlessly adaptable, flexible sustainable management systems, expressing sustainable development aspects through financial indicators. Sustainability management accounting and composite sustainable development index methodologies fill this gap, being very promising tools for sustainable decision making in SMEs (Laurinkeviciute and Stasiskien, 2011).

2.4. Significance of Business Ethics for Sustainability

Accounting information must be reliable, understandable, comparable, and last but not the least, be able to meet the requirements of users. These are the essential conditions of financial reporting of the current state of the accounting world (Akdoğan, 2010). However, the validity of this statement for the Turkish SMEs is debatable. Decision makers within the business are required to effectively understand, manage, utilize, and pass on down to all levels of the business, not only ethical values in general; but also business ethics to improve earnings quality, sustainability, and succeed in the present and future operations (Ussahawanitchakit, 2008). Ethical depletion within the decision making process create the basis for fraudulent conduct of business. Such behavior can very well turn into an internal epidemic for the business entity. Preventing such hazardous business conduct requires the top-level management to have faith in remedial abilities of corporate governance, business ethics, and transparency. Findings of Imoniana et al., (2011) suggest that, because a good number of the entrepreneurs are conservative and so reluctant in accepting consulting activities, showing that trust is low, rescuing the situation of the SMEs is a case that does not only need institutional decisions but governance reframing. On the same token, framing corporate governance is a challenging task and in the name of ultimate success, the essence of such system should be constructed upon fairness, transparency, accountability, and responsibility (Capital Market Boards of Turkey, 2005). SMEs are constantly surrounded by risk, which can be best described as the uncertainty of an outcome or an event (Lipczynski, 2008), derived both from internal and external forces. According to Aksoy and Bozkuş (2008), adoption of corporate governance and enterprise risk management is a necessity for SMEs in order to prevent financial burden. Additionally, within the context of sustainable growth and sustainability in general, SMEs in Turkey are entailed to be alert for the changing business world with intense caution to be able to survive in the competitive business environment. In the name of surviving and growing, SMEs are to devise the correct strategies to achieve specific and attainable and goals. Business ethics as one of the most crucial ingredient is seemingly not well comprehended by the broad-spectrum of the economy. However, in order to allocate the required emphasis in business ethics, initially the decision makers are expected to grasp the magnitude of its efficacy. Only then passing this crucial and valuable message down to all levels of the entity can be achieved. Concurrently, they should expand their other strategies to include advanced business wisdom in order to continuously maintain and increase the levels of business excellence, competitive advantage, and competitiveness. (Ussahawanitchakit, 2008). Sustainability, as a challenging concern, requires a great deal of effort from SMEs to perform. Much of research reveals that such aspiration depends on a number of elements.

SMEs, due to their vulnerable financial conditions, are boundlessly threatened by external factors ranging from interest rates to changing regulations.

On top of external factors, internal factors pose substantial threat to the wellbeing of SMEs as well. It has been noted that lack of corporate governance with weak weight allocation on business ethics, accountability, and reliable reporting establish the perfect ground for SMEs' insolvencies.

3. METHODOLOGY

Data were collected from 104 accounting professionals in Istanbul. Convenience sampling method, which is a type of nonprobability sampling where people are sampled simply because they are "convenient" sources of data for researchers was used (Battaglia, 2008). Of the 104 questionnaires, eight were left out of the analysis because of missing data. This research is descriptive and cross-sectional. There are 21 items measuring sustainability and three demographic questions measuring job title, experience, and education level. Six point Likert scale is used ranging from "fully agree" (6) to "fully disagree" (1).

Descriptive statistics was employed. Results are tabulated in Table 1.

Table 1: Descriptive Statistics of the Sample

Variable	N	Percentage
Gender		
Male	90	93.75
Female	6	6.25
Title		
Intern	29	30
CPA	55	57
Sworn-In	12	13
Education Level		
High School	5	5
University	63	67
Post Graduate	25	26
Experience		
1-5	30	31
6-10	19	20
11-15	22	23
16-20	7	7
20+	18	19

Of the 96 respondents, 55 are Certified Public Accountants, 29 are interns, and 12 are Sworn-in Accountants. 23 percent of the respondents' work experience is between 11-15 years, 31 percent of the respondents' work experience is between 1-5 years, 20 percent of the respondents' work experience is between 5-10 years, and last but not the least 19 percent of the respondents' work experience is 20+ years.

Majority of the respondents have an undergraduate degree, 30 percent hold graduate degrees, and 5 percent are high school graduates. Factor analysis using principle components solution with varimax rotation was employed in order to find the factor structure of sustainability. The 21 questions measuring sustainability are subject to factor analysis to observe the factor structure of the scale. One item was left out of the analysis because of a factor loading less than .50. Factors with Eigenvalues 1.00 or more were taken into consideration in total variance explained. Kaise-Meyer-Olkin (KMO) value was found as .913 which is well above the accepted value. This result marked the homogenous structure of the variables and the result of Bartlett test, which resulted in .000 (chi-square: 1383.656, df: .190) showed that the variables were suitable for factor analysis. The remaining 20 questions loaded on three factors explaining 65.124 percent of the total variance. The factors were named as *transparency and accountability, internal information systems, and sustainability*. Results are shown in Table 2.

Table 2: Results of the Factor Analysis of Sustainability Scale

Factor 1: Transparency & Accountability	%variance:32.25	Factor Loadings
Self-interest of company 's benefit		.796
Family relations in management structure		.784
There is no conflict of interest between owners of capital		.762
Top management's fair treatment to the personnel		.736
Transparency management in SME's		.701
There is no fraud and corruption		.698
Financial decision and company's going concern		.683
Healthy tax consciousness		.659
Vision & mission		.629
Accountability in SME's		.622
Importance of code of ethics for SME's management		.500
Factor 2: Internal Information System	% variance: 22.52	.
Efficient reporting system		.742
Efficient accounting system		.737
Effective organizational structure		.715
Effective politics and procedures		.689
Sustainability in SME's		.665
Corporate sustainability depending on social and environmental		.575
Factor 3: Sustainability	% variance: 10.36	.
Sustainability in SMEs only concerns company shareholders		.762
Relationship between working conditions and corporate sustainability		.728
Risky decision making		.563
KMO: .913	df: 190	
Bartlett Significance Value: .000	Chi-Square Value: 1383.656	

Reliability Analysis

Reliability analysis was conducted for all factors of sustainability scale. Cronbach's Alpha is above .70 since all the subscales and the inter-correlations among test questions have fairly high internal consistency. Reliability coefficients quantify the consistency among the multiple measurements on a scale from 0 to 1 (Webb et al., 2006). The reliability coefficients, means and standard deviations for factors of sustainability are represented in Table 3.

Table 3: Means, Standard Deviations and Reliability Coefficients of Subscales of Sustainability

Scale	Mean	Standard Deviation	Cronbach's Alpha
Transparency and Accountability	2.61	.91157	.940
Internal Information Systems	3.11	.90745	.877
Sustainability	2.97	1.04545	.689

Within the scope of social sciences, any Cronbach's Alpha value scoring above .90 is considered to be excellent, values between .70 and .90 are considered to be good, and values between .60 and .70 as acceptable (Santos, 1999). Consequently, reliability of each subscale is considered to be adequate even though the Cronbach's Alpha of *sustainability* is just below .70.

4. CONCLUSION

Accounting professionals, whose primary work is to undertake bookkeeping and consulting functions for business entities are a valuable source for evaluating the current state Turkish SMEs. With their experienced observations and insights, our findings expose some valuable evidence about the general characteristics of Turkish SMEs.

When sustainability scale was subjected to factor analysis, three factors were found; *transparency and accountability*, *internal information systems*, and *sustainability*. This states the fact that the questions prompted to the accounting professionals in our research loaded on three factors explaining 65.124 percent of the total variance. Among the three factors, *internal information systems* as a factor has received the highest mean asserting that the accountants "agreed more" on the questions that make up this factor with an overall mean value of 3.11/6 on the Likert scale. Following the first factor, *sustainability* as a factor has received an overall mean value of 2.97/6 on the Likert scale asserting that the accountants agreed less on the questions that make up this factor. As for the *transparency and accountability* factor, a relatively lower overall mean of 2.61/6 was delivered.

Findings of this research uncover an important implication that, if Turkish SMEs wish to have sustainable life spans, they need to allocate the most extent of emphasis on the variables that make up the *internal information systems* factor some of which are efficiently functioning reporting and accounting system, effective organizational structure in addition to effective politics and procedures. In addition to being fruitful for academics, findings of this study will shed light on SMEs in terms of identifying which areas are perceived as the most deficient ones by the Turkish accounting professionals who have access to internal practices of countless SMEs operating in a wide range of industries.

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