

Is the level of literacy of small business owners important for cash flow management: An experts' perspective.

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1. Introduction

The life cycle of many small businesses in Australia is less than five years.² This has been attributed to their struggle to maintain consistent cash levels. Cash flow management appears to be difficult for many small business owners (SBO); however it is unclear why SBO find it so problematic. The obligation to collect and pay tax has been suggested as being one factor that may negatively impact the ability of SBO to maintain consistent cash levels. This project seeks to uncover whether the cash flow crisis is a direct result of taxation or whether there are other underlying issues that conflict with the cash flow and taxation relationship. In particular to this research, the level of SBO literacy in terms of business taxation, computer accounting software (CAS) and professional financial literacy is explored.

Preliminary results of a multiple case study³ suggest that SBO are not particularly concerned with the impact of Fringe Benefit Tax (FBT),⁴ Superannuation Guarantee (SG)⁵ and Income Tax⁶ on their cash flow. In fact a number of businesses identified benefits for cash flow as a

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² Australian Bureau of Statistics. 2017. *Counts of Australian Businesses including Entries and Exits (Jun 2012 to Jun 2016)*. Cat No 8165.0. Canberra: ABS. The survival rate of small business increases as annual turnover increases. Those generating less than \$200,000 per annum have a lower chance of survival than those earning over \$200,000.

³ The case study was the first stage of the PhD project that this research forms part of. The case study engaged small business owners from service related businesses in Australia. see: Belle Isle, M., B. Freudenberg and T. Sarker. *The Small Business Cash Flow Struggle: Should taxation be held accountable?* (Working Paper, Griffith University, 2017); Belle Isle, M., B. Freudenberg and T. Sarker. *The Small Business Cash Flow Struggle: What role does owner literacy play?* (Working Paper, Griffith University, 2017).

⁴ *Fringe Benefits Tax Assessment Act 1986 (Cth)*

⁵ *Superannuation Guarantee (Administration) Act 1992*

⁶ *Income Tax Assessment Act 1936 (Cth); Income Tax Assessment Act 1997 (Cth)*

result of paying instalments in advance when complying with FBT and Income Tax. Whereas when discussing Goods and Services Tax (GST)⁷ and Pay As You Go (PAYG)⁸ Withholding, there appeared to be some apprehension about the effect these taxes have on small businesses. A number of SBO suggested that these tax systems restrict the growth of their business and the unpredictability of the tax liability makes cash management difficult.

The level of literacy of SBO was examined. A high proportion of SBO identify that increased literacy would be beneficial to their cash flow management. When investigating the level of literacy held it was found that only 12% of SBO implemented systematic cash flow management practices in their business and only those educated in accounting made use of financial statements. Twelve and half percent of SBO were not aware that they could prepare financial reports in their CAS and 56% had limited knowledge on what financial reports were available to be produced in their CAS. In relation to business tax literacy it appears that 25% of SBO see little benefit in being tax literate and see taxation literacy to be the role of their accountant or advisor. The remaining SBO believe that literacy in tax would be beneficial to their cash flow.

As a result of these findings, interviews with small business experts were conducted in an attempt to identify whether experts in various fields had similar views about the relationship between cash flow, taxation and owner literacy as participating SBO. Experts involved included accountants, academics, advocates and Government/ATO employees. The purpose of the interviews was to determine whether experts believe that there is a minimum level of literacy or concepts that SBO should possess in order to sustain cash flow levels in their business and in turn remain successful. It was also hoped that taxation concerns for small

⁷ *A New Tax System (Goods and Services Tax) Act 1999 (Cth).*

⁸ *A New Tax System (Pay As You Go) Act 1999 (Cth)*

businesses from a professional perspective could be highlighted. This paper presents the outcome of the data collected from a small business expert using a Delphi technique.⁹

2. Small business cash flow concerns

A critical issue for all businesses is maintaining a consistent cash flow, this can especially acute for small businesses due to restricted access to finance. Cash flow is the extent of cash or near cash assets available for use, along with any inflow or outflow of cash related to these assets.¹⁰ Therefore cash flow is any business activity that alters the balance of the cash accounts. Previous research in Australia suggests that SBO have recognised that cash flow is of particular importance to their ongoing survival,¹¹ although it can be difficult for them to manage.¹²

Cash flow management has been identified as one of the most important problems for businesses in the UK, USA and Australia.¹³ Effective cash management is important to business survival irrespective of the size of the business.¹⁴ When assessing small business liquidity it has been suggested that small business are less liquid and exhibit more volatility

⁹ The Delphi technique is a systematic, repetitive process of collecting opinions or views of a group of experts: see Evans, C. (2007). Unravelling the mysteries of the oracle: using the Delphi methodology to inform the personal tax reform debate in Australia. *eJournal of Tax Research*, 5(1), 105-134: 107; Landeta, J. (2006). Current validity of the Delphi method in social sciences. *Technological forecasting and social change*, 73(5), 467-482: 468-69.

¹⁰ Ekanem, I. (2010). Liquidity management in small firms: a learning perspective. *Journal of Small Business and Enterprise Development*, 17(1), 123-138.

¹¹ Belle Isle, M., Freudenberg, B., & Copp, R. (2014). Cash flow benefit from GST: is it realised by small businesses in Australia? *Australian Tax Forum*, 29(3), 417-454; Wallschutzky, I. G., & Gibson, B. (1993). Small business cost of tax compliance. *Australian Tax Forum*, 10(4), 511-543: 527.

¹² Belle Isle, M., & Freudenberg, B. (2015). Calm Waters: GST and Cash Flow Stability for Small Businesses in Australia. *eJournal of Tax Research*, 13(2), 492-532.

¹³ Holmes, S., & Nicholls, D. (1988). An analysis of the use of accounting information by Australian small business. *Journal of Small Business Management*, 26(2), 57-68: 57; Peel, M. J., Wilson, N., & Howorth, C. (2000). Late payment and credit management in the small firm sector: some empirical evidence. *International Small Business Journal*, 18(2), 17-37: 19.

¹⁴ DeThomas, A. R., & Fredenberger, W. B. (1985). Accounting needs of very small business. *The CPA Journal*, 55(10), 14-24.

with cash flow and profit than their larger competitors.¹⁵ SBO should try to avoid extended cash shortages, as supply constraints effect the ongoing operations of the business.¹⁶ In order to reduce cash constraints and achieve better control of cash flow SBO need to implement effective liquidity management practices.¹⁷

Effective liquidity management consists of keeping financial accounts, maintaining a business plan and cash budget, keeping records of revenue, expenses, creditor and debtor invoicing and maintaining an inventory schedule.¹⁸ Previous research in Australia and the UK suggests that SBO are not actively involved in systematic liquidity management practices.¹⁹ While day-to-day recording of activities involving cash inflow and outflow may be undertaken, the process involved in receiving and making payment for those activities or managing cash once received may not be actively conducted.²⁰

Skill strengths of SBO at commencement of their business revolve around the technical skill set that the owner possesses.²¹ Research suggests that small businesses are lacking financial management skills at start-up of their business (with the exception of businesses related to

¹⁵ Peel, M. J., Wilson, N., & Howorth, C. (2000). Late payment and credit management in the small firm sector: some empirical evidence. *International Small Business Journal*, 18(2), 17-37: 19.

¹⁶ Ekanem, I. (2010). Liquidity management in small firms: a learning perspective. *Journal of Small Business and Enterprise Development*, 17(1), 123-138: 124-25.

¹⁷ Peel, M. J., Wilson, N., & Howorth, C. (2000). Late payment and credit management in the small firm sector: some empirical evidence. *International Small Business Journal*, 18(2), 17-37: 19-24.

¹⁸ Drexler, A., Fischer, G., & Schoar, A. (2014). Keeping it simple: Financial literacy and rules of thumb. *American Economic Journal: Applied Economics*, 6(2), 1-31: 13; Ekanem, I. (2010). Liquidity management in small firms: a learning perspective. *Journal of Small Business and Enterprise Development*, 17(1), 123-138: 125.

¹⁹ Belle Isle, M., & Freudenberg, B. (2015). Calm Waters: GST and Cash Flow Stability for Small Businesses in Australia. *eJournal of Tax Research*, 13(2), 492-532: 514; Peel, M. J., Wilson, N., & Howorth, C. (2000). Late payment and credit management in the small firm sector: some empirical evidence. *International Small Business Journal*, 18(2), 17-37: 19.

²⁰ Belle Isle, M., & Freudenberg, B. (2015). Calm Waters: GST and Cash Flow Stability for Small Businesses in Australia. *eJournal of Tax Research*, 13(2), 492-532: 514; Peel, M. J., Wilson, N., & Howorth, C. (2000). Late payment and credit management in the small firm sector: some empirical evidence. *International Small Business Journal*, 18(2), 17-37: 19.

²¹ DeThomas, A. R., & Fredenberger, W. B. (1985). Accounting needs of very small business. *The CPA Journal*, 55(10), 14-24.

finance or accounting).²² Research proposes that liquidity management should be regarded as important at the start and throughout the growth of the business.²³ Advances or procurement of new liquidity management skills are adopted with time and business development.²⁴ This often occurs as a result of external events or stakeholders that force SBO to learn new procedures and routines.²⁵ For those who never have to prepare a cash budget or business plan for an external party this may result in some SBO never becoming aware of effective and efficient cash flow management practices.²⁶

The level of proficiency of the SBO in relation to cash flow management is not solely reflective of the owners' abilities and capacity.²⁷ Cash flow management practices can be influenced by the SBO attitude or the value they place on having effective procedures within their business.²⁸ Results from previous research advocates that the majority of SBO undervalue the importance of cash flow management practices in their business decision making, with more value placed on information gathered from market research.²⁹ Management of cash and credit was rated second last of all management functions and only a minority of business owners identified any benefit from acquiring any form of cash

²² Peel, M. J., Wilson, N., & Howorth, C. (2000). Late payment and credit management in the small firm sector: some empirical evidence. *International Small Business Journal*, 18(2), 17-37: 19.

²³ Peel, M. J., Wilson, N., & Howorth, C. (2000). Late payment and credit management in the small firm sector: some empirical evidence. *International Small Business Journal*, 18(2), 17-37: 19.

²⁴ Deakins, D., Morrison, A., & Galloway, L. (2002). Evolution, financial management and learning in the small firm. *Journal of small Business and Enterprise development*, 9(1), 7-16: 9.

²⁵ Deakins, D., Morrison, A., & Galloway, L. (2002). Evolution, financial management and learning in the small firm. *Journal of small Business and Enterprise development*, 9(1), 7-16: 15-16.

²⁶ Deakins, D., Morrison, A., & Galloway, L. (2002). Evolution, financial management and learning in the small firm. *Journal of small Business and Enterprise development*, 9(1), 7-16: 15-16.

²⁷ Halabi, A. K., Barrett, R., & Dyt, R. (2010). Understanding financial information used to assess small firm performance: An Australian qualitative study. *Qualitative Research in Accounting & Management*, 7(2), 163-179:169.

²⁸ Halabi, A. K., Barrett, R., & Dyt, R. (2010). Understanding financial information used to assess small firm performance: An Australian qualitative study. *Qualitative Research in Accounting & Management*, 7(2), 163-179: 169.

²⁹ Holmes, S., & Nicholls, D. (1988). An analysis of the use of accounting information by Australian small business. *Journal of Small Business Management*, 26(2) 57-68: 59; Peel, M. J., Wilson, N., & Howorth, C. (2000). Late payment and credit management in the small firm sector: some empirical evidence. *International Small Business Journal*, 18(2), 17-37: 24.

management training.³⁰ SBO appear to adopt a minimum standard rather than attempting to achieve a level of best practice.³¹ This may be a result of SBO being naïve about the benefits of having an effective cash flow management system in place and how it can be achieved.³²

3. Small business owner literacy

Professional Financial Literacy

Business owners have been identified as having greater financial literacy than other groups of individuals. This includes SBO, who have a higher level of financial awareness in comparison to other individuals.³³ However, the financial literacy required for individual success is not as comprehensive as what is required to operate a small business. Previous research suggests that owners of small businesses lack the required level of financial literacy to make important financial decisions for their business.³⁴

The level of financial literacy required can depend upon someone's role. For example the financial literacy expected of directors has been identified as professional financial literacy and includes having an understanding of financial statements, cash flow management, internal control mechanisms and corporate governance.³⁵ The solvency of small business is a critical part of small business management and is dependent on the level of professional

³⁰ Peel, M. J., Wilson, N., & Howorth, C. (2000). Late payment and credit management in the small firm sector: some empirical evidence. *International Small Business Journal*, 18(2), 17-37: 31-32.

³¹ Deakins, D., Morrison, A., & Galloway, L. (2002). Evolution, financial management and learning in the small firm. *Journal of Small Business and Enterprise Development*, 9(1), 7-16: 9; Ekanem, I. (2010). Liquidity management in small firms: a learning perspective. *Journal of Small Business and Enterprise Development*, 17(1), 123-138: 135.

³² Deakins, D., Morrison, A., & Galloway, L. (2002). Evolution, financial management and learning in the small firm. *Journal of Small Business and Enterprise Development*, 9(1), 7-16: 11.

³³ Brown, R. B., Saunders, M. N., & Beresford, R. (2006). You owe it to yourself: The financially literate manager. *Accounting Forum*, 30(2), 179-191: 188.

³⁴ Drexler, A., Fischer, G., & Schoar, A. (2014). Keeping it simple: Financial literacy and rules of thumb. *American Economic Journal: Applied Economics*, 6(2), 1-31: 1-2.

³⁵ Worthington, A. (2004). *The distribution of financial literacy in Australia* (No. 185). School of Economics and Finance, Queensland University of Technology: 5.

financial literacy that the business owner possesses.³⁶ Solvency is achieved through careful cash planning and control which requires the owner to understand the financial position and activities of the organisation.³⁷ Financial literacy of SBO can impact firm growth and productivity and those with higher levels of financial literacy have been known to be more effective when using financial products and are more engaged in using and offering trade credit.³⁸

Adequate financial literacy for SBO can assist with everyday functions in the workplace. This can enable SBO to evaluate financial information in order to make decisions while understanding the consequences of those decisions.³⁹ Professional financial literacy includes reading and understanding Balance Sheets, Income Statements, Cash Flow statements and preparing a Cash Budget.⁴⁰

Preparation and use of financial statements can assist business owners to make more informed decisions and facilitates improved performance. Information from financial statements can illustrate the consequences of the business operations and the impact of previous financial decisions.⁴¹ Financial statements can be used to measure profitability, perform ratio analysis and assist with providing information to external stakeholders including financial institutions.⁴² An important advantage of use of financial statements for

³⁶ Brown, R. B., Saunders, M. N., & Beresford, R. (2006). You owe it to yourself: The financially literate manager. *Accounting Forum*, 30(2), 179-191: 179-80.

³⁷ DeThomas, A. R., & Fredenberger, W. B. (1985). Accounting needs of very small business. *The CPA Journal*, 55(10), 14-24: 21.

³⁸ Bruhn, M., & Zia, B. (2013). Stimulating managerial capital in emerging markets: the impact of business training for young entrepreneurs. *Journal of Development Effectiveness*, 5(2), 232-266: 234 and 238.

³⁹ Brown, R. B., Saunders, M. N., & Beresford, R. (2006). You owe it to yourself: The financially literate manager. *Accounting Forum*, 30(2), 179-191: 179-80.

⁴⁰ Brown, R. B., Saunders, M. N., & Beresford, R. (2006). You owe it to yourself: The financially literate manager. *Accounting Forum*, 30(2), 179-191: 188.

⁴¹ Bruhn, M., & Zia, B. (2013). Stimulating managerial capital in emerging markets: the impact of business training for young entrepreneurs. *Journal of Development Effectiveness*, 5(2), 232-266: 234 and 248.

⁴² Dyt, R., & Halabi, A. K. (2007). Empirical evidence examining the accounting information systems and accounting reports of small and micro business in Australia. *Small Enterprise Research*, 15(2), 1-9: 5; Halabi, A.

small business is to provide up to date cash flow information. Cash flow records can have greater usefulness to small business than accrual information when determining solvency, as preparation of reports relevant to cash flow provides a more accurate assessment of the present status of the business and assists with implementing strategies to overcome any cash flow problems.⁴³

Regardless of the abundance of research that suggests that use of financial statements is valuable to the ongoing success of small business, it appears that small businesses in Australia and overseas make limited use of financial statements to assist them in managing their business.⁴⁴ Although a large proportion of SBO believe that evaluation and use of financial statements is their responsibility, previous research in Australia suggests that only 20% of SBO perform any form of ratio analysis, 30% use reports for decision making, 11% use the information to evaluate business performance and 10% use current financial information for future plans or budgets.⁴⁵ DeThomas and Fredenberger⁴⁶ suggested the limited use in Australia to be a result of owners' lack of understanding of how to analyse the

K., Barrett, R., & Dyt, R. (2010). Understanding financial information used to assess small firm performance: An Australian qualitative study. *Qualitative Research in Accounting & Management*, 7(2), 163-179: 167.

⁴³ Sharma, D. S., & Iselin, E. R. (2003). The decision usefulness of reported cash flow and accrual information in a behavioural field experiment. *Accounting and Business Research*, 33(2), 123-135.

⁴⁴ DeThomas, A. R., & Fredenberger, W. B. (1985). Accounting needs of very small business. *The CPA Journal*, 55(10), 14-24; Dyt, R., & Halabi, A. K. (2007). Empirical evidence examining the accounting information systems and accounting reports of small and micro business in Australia. *Small Enterprise Research*, 15(2), 1-9; Halabi, A. K., Barrett, R., & Dyt, R. (2010). Understanding financial information used to assess small firm performance: An Australian qualitative study. *Qualitative Research in Accounting & Management*, 7(2), 163-179; Peel, M. J., Wilson, N., & Howorth, C. (2000). Late payment and credit management in the small firm sector: some empirical evidence. *International Small Business Journal*, 18(2), 17-37; Sharma, D. S., & Iselin, E. R. (2003). The decision usefulness of reported cash flow and accrual information in a behavioural field experiment. *Accounting and Business Research*, 33(2), 123-135.

⁴⁵ Dyt, R., & Halabi, A. K. (2007). Empirical evidence examining the accounting information systems and accounting reports of small and micro business in Australia. *Small Enterprise Research*, 15(2), 1-9: 5; Halabi, A. K., Barrett, R., & Dyt, R. (2010). Understanding financial information used to assess small firm performance: An Australian qualitative study. *Qualitative Research in Accounting & Management*, 7(2), 163-179: 167.

Note: Limitation of Australian research is that the number of participants were only 10.

⁴⁶ DeThomas, A. R., & Fredenberger, W. B. (1985). Accounting needs of very small business. *The CPA Journal*. 55(10), 14-24: 20

figures within the statements and their reluctance to seek help to do so from their accountant.⁴⁷

Responses from SBO indicate that the limited use of financial reports was a result of owners placing minimal significance on the information provided in the statement especially with regard to Income statements and Balance Sheets.⁴⁸ They believed that the main purpose of record keeping and producing reports was for tax compliance requirements.⁴⁹ That is there is a lack of managerial benefit of the accounting records, let alone the tax records/returns. Prior compliance cost research has highlighted how compliance cost can be miscategorised as a tax cost when it is more a cost about basic record keeping for a business.⁵⁰ More importance was placed on remaining up-to-date with the cash at bank balance and this figure was perceived to be a more accurate measure of performance.⁵¹ Although SBO identified that cash was essential for survival of their business, research suggests that they still did not see the importance of using financial reports like a cash flow budget or cash flow statement to provide cash related information.⁵²

⁴⁷ DeThomas, A. R., & Fredenberger, W. B. (1985). Accounting needs of very small business. *The CPA Journal*, 55(10), 14-24: 20; Halabi, A. K., Barrett, R., & Dyt, R. (2010). Understanding financial information used to assess small firm performance: An Australian qualitative study. *Qualitative Research in Accounting & Management*, 7(2), 163-179: 171-74.

⁴⁸ Halabi, A. K., Barrett, R., & Dyt, R. (2010). Understanding financial information used to assess small firm performance: An Australian qualitative study. *Qualitative Research in Accounting & Management*, 7(2), 163-179: 171.

⁴⁹ Halabi, A. K., Barrett, R., & Dyt, R. (2010). Understanding financial information used to assess small firm performance: An Australian qualitative study. *Qualitative Research in Accounting & Management*, 7(2), 163-179: 168.

⁵⁰ Evans, C., Ritchie, K., Tan-Nam, B., & Walpole, M. (1998). Taxation compliance costs: some recent empirical work and international comparisons. *Australian Tax Forum* 14, 93-122; Lignier, P., & Evans, C. (2012). The rise and rise of tax compliance costs for the small business sector in Australia. *Australian Tax Forum* 27 (3) 615-672.

⁵¹ Halabi, A. K., Barrett, R., & Dyt, R. (2010). Understanding financial information used to assess small firm performance: An Australian qualitative study. *Qualitative Research in Accounting & Management*, 7(2), 163-179: 167-74.

⁵² DeThomas, A. R., & Fredenberger, W. B. (1985). Accounting needs of very small business. *The CPA Journal*, 55(10), 14-24: 18-19.

Computer Accounting Software Literacy

CAS has been advocated as being of great importance to small business success. Since the introduction of the GST in 2000 and increases in the personal use of information technology it is posited that the majority of small businesses in Australia use a CAS for record keeping in their business.⁵³

For a CAS to be effective to small business it should be simple to maintain by the owner.⁵⁴ This is because the owner is likely to be active in the record keeping rather than having a delegated employee. This allows the owner to gain a greater understanding of the financial strengths and weaknesses of the business. A CAS allows SBO to collect and collate information from transactions for use in a timely manner without having to request this information from accountants.⁵⁵

Australian research suggests that small businesses do not use their CAS to its full potential.⁵⁶ Indeed, the majority of small business owners do not produce financial reports from their CAS.⁵⁷ The reasoning for non-generation of reports was that SBO do not understand accounting language, conventions or terms and therefore see limited value in generating a

⁵³ Lignier, P. (2008). Identification and evaluation of the managerial benefits derived by small businesses as a result of complying with the Australian tax system. PhD University of New South Wales: 25; Lignier, P., & Evans, C. (2012). The rise and rise of tax compliance costs for the small business sector in Australia. *Australian Tax Forum*, 27(3), 615-672.

⁵⁴ DeThomas, A. R., & Fredenberger, W. B. (1985). Accounting needs of very small business. *The CPA Journal*, 55(10), 14-24: 21.

⁵⁵ Halabi, A. K., Barrett, R., & Dyt, R. (2010). Understanding financial information used to assess small firm performance: An Australian qualitative study. *Qualitative Research in Accounting & Management*, 7(2), 163-17: 166.

⁵⁶ Halabi, A. K., Barrett, R., & Dyt, R. (2010). Understanding financial information used to assess small firm performance: An Australian qualitative study. *Qualitative Research in Accounting & Management*, 7(2), 163-179: 166.

⁵⁷ Halabi, A. K., Barrett, R., & Dyt, R. (2010). Understanding financial information used to assess small firm performance: An Australian qualitative study. *Qualitative Research in Accounting & Management*, 7(2), 163-179: 166.

report that they do not understand.⁵⁸ It was suggested that 10% of SBO were unaware that they could produce financial reports from their CAS.⁵⁹

Recent Australian research indicates that the CAS is not being used effectively to assist with management of cash flow, as there was low engagement in the use of CAS reporting options.⁶⁰ As a result participants were spending considerable time arranging finances for payment of liabilities. It is argued that this may be a result of limited knowledge about the use and benefits that a CAS can create for small businesses.

Business Taxation Literacy

Recent research by Chardon, Freudenberg and Brimble⁶¹ suggests that understanding of tax systems is beneficial to a persons' overall financial position. The level of knowledge that an individual possess of tax systems is posited to have a relationship with their ability to budget, communicate with advisors, make decisions and appropriate choices and understand their rights and obligations.⁶² It is proposed that there is a base level of taxation and superannuation literacy or knowledge required in order to be financial literate.

Recent Australian research found that individuals that are involved in business are more literate in regard to individual taxation requirements than those who are not.⁶³ However the level of tax literacy in relation to business tax systems does not appear to be adequate for

⁵⁸ DeThomas, A. R., & Fredenberger, W. B. (1985). Accounting needs of very small business. *The CPA Journal*, 55(10), 14-24 : 22-23; Halabi, A. K., Barrett, R., & Dyt, R. (2010). Understanding financial information used to assess small firm performance: An Australian qualitative study. *Qualitative Research in Accounting & Management*, 7(2), 163-179: 168.

⁵⁹ Halabi, A. K., Barrett, R., & Dyt, R. (2010). Understanding financial information used to assess small firm performance: An Australian qualitative study. *Qualitative Research in Accounting & Management*, 7(2), 163-179: 171.

⁶⁰ Belle Isle, M., & Freudenberg, B. (2015). Calm Waters: GST and Cash Flow Stability for Small Businesses in Australia. *eJournal of Tax Research*, 13(2), 492-532.

⁶¹ Chardon, T., Freudenberg, B. and Brimble, R. Tax literacy in Australia: not knowing your deduction from your offset. (2016) 31 *Australian Tax Forum* (2), 321–362.

⁶² Chardon, T., Freudenberg, B. and Brimble, R. Tax literacy in Australia: not knowing your deduction from your offset. (2016) 31 *Australian Tax Forum* (2), 321–362.

⁶³ Chardon, T., Freudenberg, B. and Brimble, R. Tax literacy in Australia: not knowing your deduction from your offset. (2016) 31 *Australian Tax Forum* (2), 321–362..

management of their tax requirements.⁶⁴ Research in the 1990's suggests that SBO needed to spend more time improving their level of tax knowledge. McKerchar⁶⁵ suggests that SBO experience difficulty with understanding SG, Income Tax, Provisional Tax⁶⁶ and FBT. McKerchar⁶⁷ found there was difficulty when determining what deductions are allowable, which benefits are classified as a fringe benefit and which employees attracted SG. Complexity was also experienced in determining the correct dates for lodgement and payment of the tax liability.⁶⁸ A significant number of SBO had a limited understanding of Provisional Tax. SBO had difficulty comprehending that a payment of Provisional Tax decreased the overall amount of tax liability due at the end of the financial year.⁶⁹

While research found that more than 90% of SBO suggested that they pursued tax information from various sources including advisors and the ATO, this rarely occurred on a regular basis.⁷⁰ Evidence suggests that SBO are not proactive in improving their tax knowledge. This was substantiated during prior studies when researchers provided information of taxes that were identified as being complex to the respondents. The participants within the research did not make use of the information during the time that the research was conducted.⁷¹ It was suggested that lack of uptake of the tax information was primarily related to two arguments. Firstly, tax obligations were a low priority for SBO, with

⁶⁴ McKerchar, M. (1995). Understanding small business taxpayers: Their sources of information and level of knowledge of taxation. *Australian Tax Forum*, (12) 25-41: 40.

⁶⁵ McKerchar, M. (1995). Understanding small business taxpayers: Their sources of information and level of knowledge of taxation. *Australian Tax Forum*, (12) 25-41: 32-35.

⁶⁶ Provisional tax was replaced and the new system is known as PAYG instalments covered under *A New Tax System (Pay As You Go) Act 1999 (Cth)*.

⁶⁷ McKerchar, M. (1995). Understanding small business taxpayers: Their sources of information and level of knowledge of taxation. *Australian Tax Forum*, (12) 25-41: 34.

⁶⁸ McKerchar, M. (1995). Understanding small business taxpayers: Their sources of information and level of knowledge of taxation. *Australian Tax Forum*, (12) 25-41: 34.

⁶⁹ McKerchar, M. (1995). Understanding small business taxpayers: Their sources of information and level of knowledge of taxation. *Australian Tax Forum*, (12) 25-41: 34.

⁷⁰ McKerchar, M. (1995). Understanding small business taxpayers: Their sources of information and level of knowledge of taxation. *Australian Tax Forum*, (12) 25-41: 30.

⁷¹ McKerchar, M. (1995). Understanding small business taxpayers: Their sources of information and level of knowledge of taxation. *Australian Tax Forum*, (12) 25-41: 32; Wallschutzky, I. G., & Gibson, B. (1993). Small business cost of tax compliance. *Australian Tax Forum*, 10(4), 511-543: 528.

greater importance placed on income earning activities.⁷² An opposing argument by McKerchar is that SBO perceived that they were knowledgeable about business tax matters.⁷³ Once business owners believed that they were knowledgeable about a specific tax matter they did not review or revise their tax management practices at a later date. As a result SBO were oblivious to any changes to legislation or misrepresentations of tax law that occurred at a later time.⁷⁴

Further reasoning for limited tax knowledge was determined to relate to expert advisors. SBO placed great reliance on their accountant to carry out and understand all tax matters relevant to their business.⁷⁵ McKerchar indicated that there was need to improve tax knowledge of SBO, however if they themselves did not believe there was any shortfall in the tax information they possessed then any attempt at educating them would be futile.⁷⁶ Considering recent research into literacy of trustees of Self-Managed Super Fund (SMSF) suggests that literacy has a positive association with fund compliance, it would be advantageous for SBO to remain at a level of taxation literacy to ensure that they are compliant with relevant tax systems.

Consequently; it can be appreciated that SBO need literacy in a number of areas including professional financial, CAS and business taxation literacy. However, findings suggest that while SBO may have improved literacy compared to the broader public, it is questionable as

⁷² McKerchar, M. (1995). Understanding small business taxpayers: Their sources of information and level of knowledge of taxation. *Australian Tax Forum*, (12) 25-41: 36; Wallschutzky, I. G., & Gibson, B. (1993). Small business cost of tax compliance. *Australian Tax Forum*, 10(4), 511-543: 528.

⁷³ McKerchar, M. (1995). Understanding small business taxpayers: Their sources of information and level of knowledge of taxation. *Australian Tax Forum*, (12) 25-41.

⁷⁴ McKerchar, M. (1995). Understanding small business taxpayers: Their sources of information and level of knowledge of taxation. *Australian Tax Forum*, (12) 25-41: 35.

⁷⁵ McKerchar, M. (1995). Understanding small business taxpayers: Their sources of information and level of knowledge of taxation. *Australian Tax Forum*, (12) 25-41: 36.

⁷⁶ McKerchar, M. (1995). Understanding small business taxpayers: Their sources of information and level of knowledge of taxation. *Australian Tax Forum*, (12) 25-41: 40.

to whether it is sufficient to operate a business and it is not clear whether it influences cash flow management.

4. Methodology

This paper examines one part of a larger project into the cash flow concerns of small businesses as a result of taxation and owner literacy. This section of the research involved the collection of data from small business experts in an attempt to determine what level of literacy in terms of business taxation, CAS and professional financial literacy is necessary in order for SBO to successfully manage their business cash flow.

The primary research question being addressed is: How is the cash flow of Australian - business influenced by tax obligations? However this research compliments the sub-research question two: Is cash flow management practices in small business influenced by literacy of small business owners?

The strategy of inquiry implemented for this part of the project involved first stage (of two) of a Delphi technique.⁷⁷ The data collection instruments employed included a semi-structured interview and a series of quick response questions. The purpose of the collection of data was to explore the importance that experts place on SBO literacy and whether literacy levels have any influence on cash flow management. Experts represented four groups including academia, Government, advocacy and advisory. Twenty-three experts participate in the project with five experts representing the groups of academia, Government and advocacy and eight experts involved in advisory positions in the small business arena.

An overview of participant years of experience and roles held can be found in

⁷⁷ The Delphi technique was briefly mentioned above, see n 9. It is anticipate that future publications for this research, once both stages are completed will discuss the application of the Delphi to the research in more depth including strengths and weaknesses that were recognised.

Table 1 below. Twenty participants had been involved in the small business landscape for more than 5 years. The remaining three participants were involved in assisting small business between 3-5 years (2 participants) or less than 3 years (1 participant). Sixteen of the participants had been involved in more than one expert role over their years of experience and six participants had previously owned a small business.

Table 1 An overview of participant expertise in relation to small businesses.

Expert	Years of experience	Field of expertise	Prior roles held as an expert
ACC8	Over 10 years	Small business advocate	Small business advisor other than an accountant Government/ATO employee Small business owner
ACA1	Over 10 years	Academic	No other role held
GOV1	Over 10 years	Government/ATO employee	No other role held
GOV6	Over 10 years	Government/ATO employee	Accountant Small business advisor other than an accountant Government/ATO employee Small business advocate Small business owner
GOV8	3-5 years	Government/ATO employee	Accountant
ACA6	Over 10 years	Academic	Government/ATO employee
ADV6	Over 10 years	Small business advocate	Academic Small business owner
ACC12	5-10 years	Accountant	Small business advisor other than an accountant Small business advocate
ADV5	Over 10 years	Small business advocate	Accountant Small business advisor other than an accountant
ACC10	Over 10 years	Accountant	Small business owner Board member of non for profit agencies
GOV7	Over 10 years	Government/ATO employee	No other role held
ACA4	Over 10 years	Academic	Accountant
ACC13	Over 10 years	Accountant	Small business advisor other than an accountant Government/ATO employee Small business advocate
ACA5	5-10 years	Academic	Government/ATO employee
ACC4	3-5 years	Accountant	No other role held
ADV4	Over 10 years	Small business advocate	Government/ATO employee
ACC5	Over 10 years	Small business advisor other than an accountant	Accountant
ADV1	Over 10 years	Small business advisor other than an accountant	Small business owner
GOV2	5-10 years	Government/ATO employee	Small business advisor other than an accountant
ACC11	< 3 years	Small business advisor other than an accountant	Involved in advising ASBFEO on cash flow management practices.
ACC6	Over 10 years	Small business advisor other than an accountant	Small business owner
ACA2	Over 10 years	Academic	Accountant
ADV3	5-10 years	Small business advocate	Government/ATO employee

5. Findings

Expert perception was explored to address two important questions for each of the areas of literacy addressed in this project. Expert feedback was sought on whether they believed there are essential concepts or a base level of literacy that SBO require in relation to use and understanding of financial statements, computer accounting software and business taxation systems. The second question posed was whether the level of literacy that SBO possess has an influence on their ability to manage cash flow in their business. The responses are discussed below under each literacy area.

Professional Financial Literacy

As previously discussed Professional Financial Literacy includes having an understanding of financial statements, cash flow management, internal control mechanisms and corporate governance.⁷⁸ Two components of Professional financial literacy are investigated in this project. These include the understanding of financial statements and the ability to implement cash flow management processes within a business situation. Prior research suggests that SBO are better equipped to operate their business if their literacy in these areas is adequate.⁷⁹

Expert perception of cash flow management processes implemented by small business owners

Previous research suggests that effective cash flow management includes keeping financial accounts, maintaining a business plan and a cash budget, keeping records of revenue, expenses, creditor and debtor invoicing.⁸⁰ The research explored contemporary views of the

⁷⁸ Worthington, A. (2004). *The distribution of financial literacy in Australia* (No. 185). School of Economics and Finance, Queensland University of Technology: 5.

⁷⁹ Brown, R. B., Saunders, M. N., & Beresford, R. (2006). You owe it to yourself: The financially literate manager. *Accounting Forum*, 30(2), 179-191: 179-80.

⁸⁰ Drexler, A., Fischer, G., & Schoar, A. (2014). Keeping it simple: Financial literacy and rules of thumb. *American Economic Journal: Applied Economics*, 6(2), 1-31: 13; Ekanem, I. (2010). Liquidity management in small firms: a learning perspective. *Journal of Small Business and Enterprise Development*, 17(1), 123-138: 125.

expert participants and the importance they place on the concepts of effective cash flow management. The semi-structured interview identified that understanding of cash flow and liquidity were considered significant for SBO literacy. The largest number of responses recorded related to liquidity and cash flow. Examples of participant responses are detailed below and highlight concerns that experts have in terms of SBO cash flow literacy;

Definitely you need to understand the principles behind identifying debtors, identifying aged payables, identifying what's profit, what's a loss, identifying those indicators of liquidity. Having that planning ahead of what's coming up in terms of your business debts and what your cash flow's going to be (ADV3).

They need to determine short, long term viability. They should also have some idea about managing cash flow. That's why a lot of small businesses end up in trouble, because they don't understand the cash flow. (ACA5).

I think they need to do some education around cash flow management because it doesn't come naturally to those that aren't financially inclined. Therefore it is important, if not critical, for them to get their mind around numbers and cash flow versus profit in particular because there is a significant difference and a lot of owners just don't understand it (ACC13).

Probably the difference between what's profit and what is actual cash inflow and outflow. We find that a lot of small business owners don't understand the interaction between the profit and loss and the actual cash flow (ACC12).

To investigate cash flow management literacy further experts were asked to indicate their thoughts in the quick response questions to this statement: 'Small business owners have a good understanding of their cash flow.' Seven participants (30.44%) agreed, five participants

were neutral in their response and eleven participants (47.83%) disagreed that SBO have a good understanding of their cash flow. This indicates that experts have concerns about whether SBO are capable of determining their business liquidity which could explain the high response rate in the interview discussions.

The quick response questions explored further whether experts had witnessed or believed that: 'Small business owners have procedures in place to manage their cash flow.' The number of experts that disagreed increased from the previous question to three strongly disagreeing and ten disagreeing with this statement. This represents 56.52% who believe that SBO are not implementing procedures to manage cash flow. Of the responses only 17.39% agreed with the statement and the remaining 26.09% gave a neutral answer. The semi-structured interview and quick response questions were then utilised to determine what concepts of effective cash flow management experts deemed to be important for small business.

Participants were asked to express whether they believed that SBO should prepare a business plan to assist with management of cash flow. Fourteen participants agreed in the quick response questions that a business plan should be prepared for managing cash flow and only four participants disagreed (5 were neutral). This suggests that experts consider a business plan to be a worthy instrument for effective cash flow management. The responses in the semi-structured interview contradict these results however as none of the participants suggested that a business plan was a necessary concept that SBO should possess in order to be considered as having effective cash flow management practices in place.

Experts were asked to indicate whether they believed that preparation of a cash budget would assist SBO to manage their cash flow. The discussion in the interviews gave minimal support for preparation of a cash budget as being effective for cash flow management. One

participant did suggest that budgeting and cash flow were important. Participant ACC6 made the following comment;

I mean theoretically, they need to understand basic sorts of things like budgeting and cash flow (ACC6).

In contrast the short response questions showed that 60.87% strongly agreed (14 participants) and 30.43% agreed (7 participants) that SBO should prepare a cash budget in order to effectively manage cash. The remaining two participants responded with a neutral answer. This demonstrates that experts believe that a cash budget is a worthy tool for effective cash flow management as there were no opposing responses despite the lack of feedback in the interview discussion.

The responses in the semi-structured interview in relation to understanding of necessary concepts for professional financial literacy gave considerable support to SBO having a thorough understanding of their debtors and creditors and what effect these concepts have on their cash flow. Collectively there were 15 responses in the interviews relating to treatment of debtors and creditors (or aged payable or receivable). Predominantly this was discussed in concert with a misunderstanding of what these figures represent in the financial statements (this will be discussed further in the next section) and how credit transactions can give a false indication of the immediate cash flow situation of the business.

The influence of credit vastly changes situations so that a person can go broke making a profit (ACA2).

Cash flow and debtors and creditors, that's got to be the two most critical things (ADV1).

Understanding of the concepts of debtor, creditors especially accounts payable and accounts receivable is probably another one that's really important (ACC8).

In terms of the requirement to keep financial accounts including a record of revenue and expenses, minimal discussion (if any) was directed specifically at these concepts. However the discussions in the interviews appeared to suggest that keeping these records are a necessary component of operating any business. This is particularly evident where experts believed there are specific financial statements that need to be maintained and understood. Without accurate and up to date records of transactions these financial statements would not be a true representation of the financial status of the business.

Base level or concepts of financial statement literacy that should be acquired by small business owners

In relation to financial statements, professional financial literacy includes reading and understanding Balance Sheets, Income Statements, Statement of Cash Flows and preparing a Cash Budget.⁸¹ Preparation and use of financial statements has been advocated as being effective in helping SBO to make more informed decisions. Information from financial statements can illustrate the consequences of the business operations and the impact of previous financial decisions.⁸² An important advantage of use of financial statements for small business is to provide up to date cash flow information. Regardless of the abundance of research that suggests that use of financial statements is valuable to the ongoing success of

⁸¹ Brown, R. B., Saunders, M. N., & Beresford, R. (2006). You owe it to yourself: The financially literate manager. *Accounting Forum*, 30(2), 179-191: 188.

⁸² Bruhn, M., & Zia, B. (2013). Stimulating managerial capital in emerging markets: the impact of business training for young entrepreneurs. *Journal of Development Effectiveness*, 5(2), 232-266: 234 and 248.

small business, it appears that small businesses in Australia and overseas make limited use of financial statements to assist them in managing their business.⁸³

The quick response questions explored whether experts have witnessed SBO making use of financial statements for cash flow management. Experts were firstly posed with the statement: Small business owners make use of financial statements to manage their cash flow. Only two participants agreed with this statement. In comparison 16 participants or 69.56% of participants disagreed/strongly disagreed (5 participants answered a neutral response).

In comparison to the use of financial statements, the quick response questions also explored the reliance on the bank account balance. This was included due to prior research indicating that SBO place more importance on being up to date with the cash at bank balance as a cash flow and performance measure than the use and understanding of financial statements.⁸⁴ Experts were asked to indicate their thoughts on SBO use of the bank statement or bank account and were posed the following proposition: Small business owners rely on the bank account to manage their cash flow. Responses in agreeance to this statement were 82.9% (19 participants) in comparison to 8.7% disagreeing. This suggests that experts believe that SBO are relying heavily on their bank statement or bank balance as an indicator of cash flow.

In order to determine whether small business experts perceived that there are specific concepts that SBO should hold to have financial statement literacy, the semi-structured interview addressed the question: 'In your opinion what is the base level or concepts of literacy required by small business owners in relation to use and understanding of financial

⁸³ DeThomas, A. R., & Fredenberger, W. B. (1985). Accounting needs of very small business. *The CPA Journal*, 55(10), 14-24; Dyt, R., & Halabi, A. K. (2007). Empirical evidence examining the accounting information systems and accounting reports of small and micro business in Australia. *Small Enterprise Research*, 15(2), 1-9; Halabi, A. K., Barrett, R., & Dyt, R. (2010). Understanding financial information used to assess small firm performance: An Australian qualitative study. *Qualitative Research in Accounting & Management*, 7(2), 163-179; Peel, M. J., Wilson, N., & Howorth, C. (2000). Late payment and credit management in the small firm sector: some empirical evidence. *International Small Business Journal*, 18(2), 17-37; Sharma, D. S., & Iselin, E. R. (2003). The decision usefulness of reported cash flow and accrual information in a behavioural field experiment. *Accounting and Business Research*, 33(2), 123-135.

⁸⁴ Halabi, A. K., Barrett, R., & Dyt, R. (2010). Understanding financial information used to assess small firm performance: An Australian qualitative study. *Qualitative Research in Accounting & Management*, 7(2), 163-179: 167-74.

statements.’ Since it was anticipated that experts may have some difficulty articulating an immediate, well informed response, participants were supplied with a list of possible concepts that might be considered when determining financial statement literacy (see

Appendix 1).

As already discussed in the section prior there were a large number of responses that related to aged payables and receivables and liquidity and cash flow. In terms of financial statement literacy however, there were varying views on which concepts and financial statements were necessary to be considered literate. Only one participant mentioned the need to understand accounting ratios. This suggests that accounting ratios may not be considered a necessary part of professional financial literacy for SBO.

For a person starting off in business they should actually understand the different ratios (ACC12).

An attempt was made to determine whether experts believed that certain financial statements were better suited or gave more value to a SBO for cash flow management. The semi-structured interviews and the quick response questions explored the importance experts place on use of financial statements for cash flow management. The interviews gave varying feedback regarding the necessity to understand financial statements.

I think the base level concepts is around, I guess, the difference between assets and liabilities - at that basic level. How much equity they have; I guess, fundamentally the difference between like a balance sheet and a profit and loss statement and what they can be used for. I suppose flowing on from that it's probably more about what financial statements can be used for in terms of running their business; so whether there's things that they can use themselves or whether they're for the bank or other people. A cash flow statement and what it can tell them (ACA6).

The interview provided varying feedback on specific financial statements. The largest number of responses in the interviews related to the Profit and Loss Statement followed by

the Balance Sheet and the Statement of Cash Flows receiving equal feedback. The outcome of the quick response questions however placed the Statement of Cash Flows as the most important financial statement to assist with management of cash flow. Feedback from the quick response questions relating to the Profit and Loss Statement suggested that just over half (52.17%) of the expert participants believe it to be useful for cash flow management. Thirty percent disagree that it is a cash flow management tool and the remaining experts were either unsure or gave a neutral response about its purpose for cash flow management. The interview responses however were more supportive of the Profit and Loss Statement. Participants gave the following feedback;

Well I think they need to understand where they're making a profit, so profit and loss and they need to determine short, long term viability (ACA 5).

The problem with the profit and loss statement is that it involves credit transactions. If it's a cash only basis, then you've got an idea. But if it's got credit involved in it, and quite often it does, then it's not going to help you because it's going to show you making a profit when in point of fact, you don't have any money (ACA2).

So probably the base level of using financial statements should be the ability to read the profit and loss, and in terms of understanding probably - the big thing we try and get people to focus on is their gross profit margin (ACC10).

For a business starting out they should understand financial statements and difference between revenue and profit and loss (ACC12).

Only one participant that discussed the profit and loss statement suggested that it was not as effective at helping with cash flow management.

Not so much profit and loss (GOV2).

The Balance Sheet was determined the least useful statement to assist with management of cash flow in the quick response questions. Fifty percent of participants agreed/strongly agreed that it was effective whereas 31.82% disagreed and 18.18% gave a neutral response. These results are supported by the lack of responses from the interviews. Two experts gave positive feedback about the necessity for SBO to understand the Balance Sheet in order to have professional financial literacy.

They need to look at and understand the balance sheet, again to help them work out whether they're viable or not (ACA5).

I think they need to understand their balance sheet (GOV 2).

The remaining comment suggested that the Balance Sheet is not necessary for professional financial literacy especially in terms of cash flow management because it includes a large amount of non-cash items. Participant ACA2 made the following comment;

Balance sheets NO – they have got so many non-cash items involved in them (ACA2).

The quick response questions expressed significant support for the understanding of the Statement of Cash Flows as a tool for cash flow management. Participants were asked to respond to the statement: The Statement of Cash Flows should assist small business to manage their cash flow. An overwhelming response of 87% (20 people) of participants agreed that this is a useful statement for cash flow management. Only one participant disagreed and the remaining two experts gave a neutral response. As mentioned the interview comments were not as supportive of the Statement of Cash Flows as a necessary component of professional financial literacy. Comments relating to the Statement of Cash Flows were:

So obviously the statement of cash flows would be probably the most important; and the profit and loss; and the balance sheet, I guess would be the next (ACA2).

Cash flow statement is necessary but they don't read it (ACA2).

We try and encourage clients to do annual forecasting but probably get them more to focus on a 12 week cash flow forecast, which is more probably dynamic and continuing. So in terms of using financial statements, the cash flow statement is the most important (ACC10).

That's why a lot of small businesses end up in trouble, because they don't understand the cash flow statement (ACA5).

Although understanding and use of the Statement of Cash flows was not well discussed in the interviews, cash inflow and outflow and the distinction between cash and profit was given substantial consideration overall in terms of cash flow literacy (see previous comments). This suggests that knowledge and understanding of liquidity is an essential part of professional financial literacy.

In summary, experts suggest that SBO do not currently make use of or understand their financial statements. The results demonstrate that experts have observed that SBO place more significance on the information obtained from the bank account as an indicator of cash flow stability than any other source.

In contrast small business experts propose that the most influential financial statements that SBO should make use of and understand in order to be professional financial literate include the statement of cash flows and the profit and loss statement. Preparing a cash budget and a business plan have also been given strong support by experts as necessary components for cash flow management and in turn professional financial literacy. Financial concepts that

have been implied by experts as being essential for SBO include identifying indicators of liquidity or recognising cash flow issues include understanding the effect of aged payables and receivables on cash flow, determining the difference between profit and cash and having some ability to prepare and maintain a cash budget or forecast.

Does the level of small business owner professional financial literacy influence their ability to manage cash flow?

DeThomas and Fredenberger⁸⁵ suggest that solvency is dependent on careful control of cash and the ability to understand the financial position and activities of the organisation. Considering that solvency is a critical part of cash flow management,⁸⁶ the views of experts were examined to determine whether experts believe that the level of professional financial literacy of SBO has any impact on their ability to manage cash flow.⁸⁷

The data collected in the semi-structured interview was used to explore the thoughts of small business experts in terms of the impact of literacy levels on cash flow management. Participants were asked to respond to the question: ‘In your opinion, does the level of understanding of financial statements influence SBO ability to manage cash flow?’ Only one participant suggested that literacy levels have no bearing on cash flow management from a financial statement literacy perspective. Participant ACC6 suggested that financial statements only provide SBO with historical data and are of no use for cash flow management. The respondent’s comments are illustrated below;

Most of them don't understand their financial statements and I don't think that influences their ability to manage cash flow. Basically nobody uses financial

⁸⁵ DeThomas, A. R., & Fredenberger, W. B. (1985). Accounting needs of very small business. *The CPA Journal*, 55(10), 14-24: 21.

⁸⁶ Brown, R. B., Saunders, M. N., & Beresford, R. (2006). You owe it to yourself: The financially literate manager. *Accounting Forum*, 30(2), 179-191: 179-80.

⁸⁷ Brown, R. B., Saunders, M. N., & Beresford, R. (2006). You owe it to yourself: The financially literate manager. *Accounting Forum*, 30(2), 179-191: 179-80.

statements produced by their accountant, you're onto the next financial year before you get them (ACC6).

However this statement appears to be more in terms of end of year reporting including balance sheets and profit and loss statements. This participant argues that end of year reporting is redundant for cash flow management due to the statements containing historical data. This suggests that the level of SBO literacy is irrelevant because these financial statements are not useful for cash flow management.

The remaining feedback from experts all confirmed that the level of literacy has some impact on management of cash flow. The responses from participants revolved around four main themes. Experts suggested that literacy levels influence the SBO ability to succeed by allowing them to understand the principles in the financial statements, to identify cash flow issues in advance, to illustrate the effects of previous decisions and to have more informed conversations with external stakeholders. The expert feedback reinforces the existing literature suggesting that adequate professional financial literacy supports SBO with everyday functions in the workplace and allows them to make more informed and strategic decisions.⁸⁸

Firstly, responses indicate that without adequate literacy SBO are not equipped to interpret what important information the financial statements are notifying them of in terms of cash flow. Misunderstanding of the concepts and principles required to read financial statements can leave SBO in a vulnerable situation in terms of their cash flow. Experts expressed their concerns about inadequate ability to understand these concepts in the financial statements.

If you don't understand the principles behind those financial statements - if you don't even think about I've got to not only pay this month but I've got to think about what

⁸⁸ Brown, R. B., Saunders, M. N., & Beresford, R. (2006). You owe it to yourself: The financially literate manager. *Accounting Forum*, 30(2), 179-191: 179-80.

I've ordered, what's coming up in the month ahead, you can't manage your cash flow (ADV3).

A lot of small businesses don't succeed because they don't understand the financial statements. If they don't create them or don't understand them, then that causes cash flow problems. So yes, a very strong relationship between the literacy and managing cash flow (ACA5).

The level of literacy that they hold in many ways can influence the success of the business because they need to understand how to manage their revenues and their expenses. They can pay an accountant to do that but it's expensive and they tend to shy away from that and they tend to do it themselves. Therefore, especially in those initial stages of owning a business, the higher their level of literacy around financial numbers the greater the chances of them succeeding in managing their business (ACC13).

Similar to research by Bruhn and Zia⁸⁹ experts expressed their views on how increases in literacy of financial statements can improve SBO cash flow effectiveness. Being more literate allows SBO to be more informed in discussions with external stakeholders and reduces expenditure when engaging advisors.

A higher level of literacy also helps them to contain advisor costs because it means that they have the capability to put together briefs and statements and information in a way in which it saves advisors time in terms of getting on top of and understanding what their business is (ACC13).

⁸⁹ Bruhn, M., & Zia, B. (2013). Stimulating managerial capital in emerging markets: the impact of business training for young entrepreneurs. *Journal of Development Effectiveness*, 5(2), 232-266: 234 and 238.

Having adequate professional financial literacy has been advocated as being influential in helping SBO to make more informed decisions which in turn facilitates improved performance.⁹⁰ Expert responses support prior research by implying that increased literacy in financial statements assists SBO to identify the consequences of business operations and the impact of previous financial decisions. Comments of two expert advisors are expressed below;

The higher the level of literacy, the better the understanding of financial statements. They can then see and recognise the early warnings including any variances and react and respond to make it favourable to them. If their literacy is low, then their understanding of it is low and therefore they may not even be able to read the signals even if they do get the information (ADV1).

So you need to be able to compare your financial statements. You need to compare it to a budget, or a benchmark, or to a prior period so you get some relativity. So unless you're capable of doing those things, you're not able to compare and measure performance (ACC10).

Previous research indicates that cash flow understanding is critical in determining solvency and therefore limitations in literacy is likely to cause detrimental effects to ongoing business viability.⁹¹ Higher levels of cash flow and profitability literacy has been advocated in allowing SBO to make more accurate assessment of the present status of their business and assist with implementing strategies to overcome any cash flow problems.⁹² Some experts

⁹⁰ Bruhn, M., & Zia, B. (2013). Stimulating managerial capital in emerging markets: the impact of business training for young entrepreneurs. *Journal of Development Effectiveness*, 5(2), 232-266: 234 and 248.

⁹¹ Sharma, D. S., & Iselin, E. R. (2003). The decision usefulness of reported cash flow and accrual information in a behavioural field experiment. *Accounting and Business Research*, 33(2), 123-135.

⁹² Sharma, D. S., & Iselin, E. R. (2003). The decision usefulness of reported cash flow and accrual information in a behavioural field experiment. *Accounting and Business Research*, 33(2), 123-135.

expressed their concerns about SBO misunderstanding of profitability and cash flow and the implications that can result from a lack of knowledge in relation to these concepts.

If they don't understand their cash flow, they don't know whether they can purchase anything new. They don't actually know whether they're making a profit or not, so they might be a restaurant and they might have their doors open and their tables filled, but they don't actually realise how much it's actually costing them to produce that meal, they might actually be running at a loss. So it's really important, I thought, that they actually understand cash flow and basic financial literacy (ADV4).

It does influence their ability to manage their cash flow because if they don't understand how the cash that they spend impacts on their finances then they can have cash issues. We find that a lot of people say that they don't make a profit because they've got no money which is not necessarily true. They just spend all of the money, they just don't realise how it's been flowing through the financial statements (ACC12).

Overall it appears that the majority of experts in the research perceive that the level of SBO literacy has an impact on their ability to manage their business cash flow. Concerns were expressed about limitations in professional financial literacy having negative impact on the ability of SBO to identify early warning signs of cash flow issues. Experts suggested that in order to support cash flow SBO should have a level of literacy that allows them to compare current financials with prior figures, determine the consequences of previous decisions in order to be more informed about decisions in the future and have increased awareness of financial status in order to have more educated conversations with advisors and external parties.

Computer Accounting Software Literacy

Recent research Belle Isle and Freudenberg⁹³ indicates that the CAS is not being used effectively to assist with management of cash flow, as there was low engagement in the use of CAS reporting options. Considering that CAS literacy is a relatively new concept this project relies on two areas of professional financial literacy including cash flow management and understanding of financial statements to determine CAS literacy. The research investigates the use of a CAS for cash flow management activities including preparing a cash budget, keeping records of revenue, expenses, creditor and debtor invoicing and generation and use of financial reports.

Base level or concepts of CAS literacy that should be acquired by small business owners

The results from a related project involving small business owners⁹⁴ and recent research Belle Isle and Freudenberg⁹⁵ indicate that the CAS is not being used effectively to assist with management of cash flow, as there was low engagement in the use of CAS reporting options. Experts were therefore engaged to determine if there are specific functions in the CAS that SBO should be capable of performing.

Firstly, the quick response questions explored whether experts have observed that record keeping is accurate as a result of the use of CAS by SBO. Experts were posed with the statement: ‘Small businesses have reliable records as a result of their accounting software.’ As illustrated Table 2 in twelve participants agreed that small business records are more accurate as a result of CAS in comparison to 17.39% who disagreed and 30.43% who gave a neutral response.

Table 2 Small businesses have reliable records as a result of their computer accounting software

⁹³ Belle Isle, M., & Freudenberg, B. (2015). Calm Waters: GST and Cash Flow Stability for Small Businesses in Australia. *eJournal of Tax Research*, 13(2), 492-532.

⁹⁴ Belle Isle, M., B. Freudenberg and T. Sarker. The Small Business Cash Flow Struggle: What role does owner literacy play? (Working Paper, Griffith University, 2017).

⁹⁵ Belle Isle, M., & Freudenberg, B. (2015). Calm Waters: GST and Cash Flow Stability for Small Businesses in Australia. *eJournal of Tax Research*, 13(2), 492-532.

Answer Choices	Response Rate	Respondents
Strongly Disagree	4.35%	1
Disagree	13.04%	3
Neutral	30.43%	7
Agree	47.83%	11
Strongly Agree	4.35%	1
Not Sure	0.00%	0
Not Applicable	0.00%	0

The large number of neutral responses might be explained by the data given in the semi-structured interviews. Experts were asked to respond to the question: ‘In your opinion, what is the base level or concepts in terms of operating a CAS that is required by SBO for cash flow management?’ Participants were provided with a list of possible CAS concepts that they could refer to in order to determine CAS literacy requirements (see

Appendix 1). One discussion that presented a number of times related to the incorrect coding of transactions and how that could result in inaccurate recording of records. Expert concerns can be seen in the following comments;

As we all know, data output is only as good as the data in. If the data's been classified or incorrect, then it's not that useful to them. They have to have a base understanding of how to code the transactions themselves so that they can generate the output that they need. (GOV1).

It's knowing how to code things, where they go, identifying what is an expense, what is capital, what is income, what is not core business activities, and that type of stuff they need a little bit more education on I think (GOV6) .

Half the time I think their struggling because of errors that come up in the accounting software from incorrect entering of data (ADV3).

Some people don't even know how their accounting software is set up and what might need to change in the set up based on changes in their business or changes in other factors which impact on their data entry and the reporting that they get out of it (GOV7).

This argument is strengthened by the feedback given in the quick response question: 'The initial set up of computer accounting software should be carried out by the accountant or advisor.' See Table 3 below;

Table 3 The initial set up of computer accounting software should be carried out by an accountant or adviser

Answer Choices	Response Rate	Respondents
Strongly Disagree	0.00%	0
Disagree	4.35%	1
Neutral	13.04%	3

Agree	34.78%	8
Strongly Agree	47.83%	11
Not Sure	0.00%	0
Not Applicable	0.00%	0

Those experts agreeing that the CAS initial set up should be the role of the accountant or advisor represent 82.61% or 19 of the 23 participants. This indicates that experts perceive that there may be a relationship between coding errors and incorrect set up of the software. Participant GOV1 discussed the requirement to have the initial set up carried out by an expert if their literacy is lacking in that area.

I think it depends on the software. One of the keys in that is setting it up. I don't know that the business owner necessarily has to understand how it all works if they can set it up properly or they can get someone to set it up properly for them (GOV1).

The purpose of the semi-structured interview was to determine what concepts and functions of the CAS the SBO should be capable of in to be considered CAS literate for cash flow management. The responses from the participants were varied. One participant suggested that they didn't believe that CAS would be very helpful for cash flow management. Participant ACC10 made the following comment:

Most do have a computerised accounting system of some degree is what we find. How they use that to manage cash flow, I would probably suggest their actual accounting software probably doesn't help them in terms of cash flow. I think generally they will be doing it in spreadsheets for that (ACC10).

Another participant suggested that CAS was detrimental to educating and increasing knowledge of accounting concepts for SBO as basic accounting was now conducted by a

computer preventing SBO from undertaking fundamental accounting procedures on a regular basis.

The reliance on electronic data processing has overcome good basic sound accounting knowledge because everybody now is an expert because they can hit a key on the computer. They simply don't understand what's happening in their business because they don't use a handwritten journal which would give them a running balance of your cash flow at any point in time. Provided it's kept up, it forms a far better superior system than the computerised accounting system in my opinion (ACA2).

Three participants suggested that SBO require a level of literacy that allows them to produce and understand financial reports available in their CAS.

The small business owner needs not just to know how it works, but he should be the day to day person working it. Absolutely they should create financial statements in their accounting software (ACA2).

Definitely they do need to know which reports to print, how often to print them. So you want to keep your eye out on your cash flow regularly; profit and loss statement, you want to do at least monthly, and balance sheet that can be done a less frequent basis, I suppose, because with the assets [unclear] you should, kind of generally they would know where they're at and what they have. But cash flow, profit and loss statement, their debtors and creditors - yes, absolutely, they must keep an eye out on that (GOV6).

They should be using it as a management tool. I try to get my clients to do a monthly profit and loss, and aging debtors and aging creditors, because then you can see how their cash flow is going (ACC11).

The remaining experts believe that a thorough understanding of how the CAS functions is necessary to be considered as having adequate CAS literacy.

Ideally, they should be able to produce reports and understand what those reports are telling them. So they need basic digital literacy, then they need to understand their actual accounting software, what it will do and what it won't do for them. They need to know how to use it, and they need to know how to get value out of it relevant to running their business effectively. They don't need to be experts but they do need to have a level of ability to use the software to actually help them run the business (GOV7).

They definitely need a very solid understanding of that whole accounting software to be able to generate invoices correctly and accurately and to monitor the cash flow and action payments. Then be able to track and report on it as well (ACC11).

A good basic understanding of the software is essential to the success of small business. They need to know how to enter in the information and, to some degree, get that back out in a way that's useful to them, that they can understand (ADV1).

Overall the majority of experts believed that CAS literacy of SBO should at minimum allow them to produce and understand financial reports. However some experts extended their literacy requirement to suggest that a thorough understanding of how the CAS functions is necessary in order to be considered CAS literate. In contrast the majority of experts agree that the initial set up of a CAS system does not form part of SBO CAS literacy. In order to prevent incorrect recording and coding of transactions in the future, experts believe that set up should be carried out by the expert or advisor.

Does the level of SBO CAS literacy influence their ability to manage cash flow?

The semi structured interviews explored whether experts believed that SBO CAS literacy influenced their ability to manage their cash flow. Three participants agreed that literacy levels were important for cash flow management. Their responses suggest that without CAS knowledge the reports and data available will be worthless and serve little purpose for cash flow management.

Certainly with the accounting software, if you don't understand how to use it, you're just going to produce erroneous data that don't help you manage your cash flow (ADV3).

Looking at your financial statements and having good accounting software and knowledge helps to analyse cash flow. It helps you to look forward, thinking about your tax liabilities and other debts and planning for those (ACC8).

The more they know about their CAS, the better their business will be (ACC11).

The remaining comments from experts revolved around SBO knowledge of accounting concepts. It appears from the data analysis that participants perceive that management of cash flow using CAS is reliant on SBO understanding of basic accounting concepts:

Behind this computer accounting software - you've got to have accounting knowledge. It gets complicated when you're looking at your reports out of your accounting software. You'll have some debtors that are on account and some debtors like your sub-contractor that wants to be paid weekly, they're almost dealt with like a cash cycle. That makes it very tricky to use those financial statements that are coming out of that reporting system (ADV3).

If you have a good standard in understanding bookkeeping and basic accounting, the methods used i.e. electronic data processing as opposed to any other system, it becomes irrelevant (ACA2).

It's not literacy of the computer accounting software, it's literacy of debits and credits or what's a profit and loss or what's a balance sheet that influences their ability to manage cash flow when using their software (ACC12).

A review of the data suggests that it is not solely the level of literacy of CAS that influences SBO ability to manage cash flow. It appears that knowledge and understanding of basic accounting concepts compliments SBO CAS literacy levels. This is concerning when taking into account the views of participant ACA2. As discussed above, this participant suggested that reliance on electronic data systems for recording of business transactions has eroded basic financial and accounting knowledge of SBO. This is a result of SBO never having to determine the treatment of the transactions that they process through the accounting system.

Business Taxation Literacy

As previously discussed SBO have been identified as being broadly tax literate in relation to individual tax systems, however this level of literacy does not appear to extend to business tax systems. Prior research suggests that the level of tax knowledge of SBO is not sufficient for management of their ongoing business tax obligations. This research explores the perception of experts in regard to the level of business tax literacy required by SBO in order to manage cash flow and in turn a successful business.

Base level or concepts of business tax literacy that should be acquired by small business owners

In a related case study project small business participants were asked if they believed that their understanding of tax systems affected their cash flow.⁹⁶ Twelve participants confirmed that having an increased understanding of tax systems would be beneficial to effectively managing their cash flow. Increased business tax literacy was identified as being advantageous for planning for the tax liability, useful when making tax related decisions and recording tax related transactions accurately. Four of the SBO however did not see any benefit to cash flow from being literate in business tax systems. They believed that taxation literacy was the role of their accountant or advisor. This is comparable to research by McKerchar⁹⁷ who found that SBO rely heavily on their accountant at the detriment of their own tax literacy. Experts were engaged to determine if they consider that there is a base level of literacy or certain taxation concepts that SBO should possess in order to be considered as having business tax literacy.

Initially the quick response questions were utilised to determine whether experts believed that record keeping for taxation purposes assisted SBO in managing their cash flow. This question was included to determine if experts believed that SBO realise a managerial benefit from keeping records for taxation purposes. Seventeen of the experts agreed/strongly agreed that tax recording is beneficial for cash flow management. Only two participants disagreed/strongly disagreed. Responses are displayed in Table 4.

Table 4 The records and information generated for tax obligations assist small businesses with managing their cash flow

Answer Choices	Response Rate	Respondents
Strongly Disagree	4.35%	1
Disagree	4.35%	1

⁹⁶ Belle Isle, M., B. Freudenberg and T. Sarker. The Small Business Cash Flow Struggle: What role does owner literacy play? (Working Paper, Griffith University, 2017).

⁹⁷ McKerchar, M. (1995). Understanding small business taxpayers: Their sources of information and level of knowledge of taxation. *Australian Tax Forum*, (12) 25-41: 40.

Neutral	8.70%	2
Agree	47.83%	11
Strongly Agree	26.09%	6
Not Sure	4.35%	1
Not Applicable	4.35%	1

Semi-structured interviews were conducted to determine expert views on what the minimum literacy requirements would be for SBO in relation to business tax systems. Participants were asked, ‘In your opinion, what is the base level of literacy or concepts of business taxation required by SBO to be considered literate?’ There were two common themes that emerged from the data collection. The most prevalent responses were focused on being aware of their obligations and realising that the tax liability is a business expense. Research by McKerchar⁹⁸ in 1995 showed that determining correct payment and lodgement dates for taxation was a complex issue for SBO. Experts today appear to suggest that this may still be any issue considering that a large number of responses relate to this subject. Comments from the interviews are presented below:

They definitely need to have a good understanding of when those payments need to be made so they can manage their cash flow appropriately (ACC11).

They should know how often they have to report in their tax returns and they should know what dates they have to pay the tax, if there's any - the base level. They can get advice in terms of accounting adviser as far as doing the tax returns, but they should know the dates that they have to fill in those reports and should be able to communicate with their advisers (ACA5).

⁹⁸ McKerchar, M. (1995). Understanding small business taxpayers: Their sources of information and level of knowledge of taxation. *Australian Tax Forum*, (12) 25-41: 34.

Well of course, they need to have a basic understanding of how the tax and superannuation systems work. What the requirements are on them. They need to be able to plan to meet those requirements. They also need to understand how to engage with the tax and super systems, either directly or through their accountant or bookkeeper (GOV 7).

If you're a micro to small business person, you should actually definitely have an understanding of what the tax office needs you to record (ADV6).

The other common response related to taxation being a business expense and businesses needing to be aware of the impact of the tax portion when planning for cash flow. Participants suggested that SBO are confused about what portion of the money that they hold in their account is the tax liability and what portion is their business cash:

Well I think the bottom line is you really have to have an idea because in a nutshell I think they basically need to know the difference between my money and the money of others, that's what it comes down to (ACA1).

Tax is one of the biggest expenses - you have your rent, you have your wages and then you have your tax - so tax is a large portion of their profits, it takes a large [gross proportion] of their profits. When they come to invest, they have to take that money and pay it to the tax office. So it takes it out of their business and that has an impact, especially today, when things are a bit hard (GOV6).

A number of participants gave feedback about specific tax systems and necessary concepts in those tax systems that SBO should be aware of. The most frequently discussed tax system was GST. The feedback from experts related to rules about taxable supplies and credits,

understanding what goods are subject to GST and determining if your business is required to be registered:

I think they have to understand things that impact them on a day to day basis. I think some basic understanding of like you mentioned, GST, that determines whether they charge or collect GST on which products. I think if they're not understanding the concept that they claim most of it back and it's the net cost that becomes relevant, not the inclusive (ACC5).

With GST, which goods or services have GST and which ones don't and how that affects cash flow. I think GST from what I believe, or my view, is GST is more about cash flow (ACA 6).

GST on a base level, I think people understand there are taxable [supplies], and there are credits coming back. I think they need to have a base understanding of those concepts, and then how that fits into preparing a BAS (ACC10).

Minimal feedback was given in relation to literacy required for the other business tax systems relevant to this research. Experts made comments regarding Income tax, PAYG Instalments and FBT however the feedback was scarce. Responses for income tax concentrated on understanding depreciation and determining the deductions available to the individual business.

My view is that there are basic things like, basic concepts around what's kind of deductible and what's not. What's a deduction and what's depreciation (ACA6).

Income tax is a bit different. Income tax, because of the way that it operates, you probably have to have less of a knowledge of it, but it is always good to understand

what concessions are available to you so that you can make the best use of those, that are available (GOV1).

One expert discussed the importance of SBO literacy for PAYG instalments,⁹⁹ particularly in the first year of trading. This participant suggested that without the required level of business tax literacy, SBO could experience significant cash flow problems if they have not forecasted or set aside funds to satisfy their income tax liability for the first year. Subsequent years will incur a PAYG instalment that is required to be paid throughout the year based on the previous years' income.¹⁰⁰ However considering that there is no prior trading in the first year the Income Tax liability will be due as a lump sum once the return is lodged with the ATO.

Pay as you go instalments will, as a matter of course, be a negative to your cash flow because of what it does. Essentially, it's a provision towards your income tax liability for that particular year, so you're actually paying it earlier than you otherwise should have. Particularly for small businesses that are starting out - because of the way pay as you go instalments operate - they can get themselves into quite a bit of trouble because they haven't actually been making provision for their income tax liability throughout the year, so when they lodge that first return that has a tax liability on it, there's nothing to offset that liability, with a lump sum amount that they have to then find the cash for. Unless they've actually been putting the money aside - we call it pay as you go instalment lag or pay as you go instalment shock because the return comes in, it's probably nine months after the end of the relevant income year, they're going okay (GOV1).

⁹⁹ *A New Tax System (Pay As You Go) Act 1999 (Cth)*.

¹⁰⁰ *A New Tax System (Pay As You Go) Act 1999 pt 2-10 sub-div 45-C*.

This feedback differs to the results of the research in 1995 relating to Provisional Tax. McKerchar¹⁰¹ suggested that SBO experienced complexity with understanding that a Provisional Tax payment decreased the overall amount of tax liability owed at the end of the reporting period. Current expert feedback in comparison suggests that the most significant issue for cash flow is not identifying the implications of not paying an instalment in the first year of trade and the possible restrictions to cash that SBO could face when the tax liability is due in the subsequent year. This supports the responses in a recent related case study project of small business participants.¹⁰² Two business owners suggested that more education is required at the start-up of a business in relation to the likely tax liability that will be owing at the end of the first year of trade.

In regard to FBT literacy expert ACC5 supported research by McKerchar¹⁰³ suggesting that SBO literacy needs to be improved. Lack of understanding by SBO about what is classified as a Fringe Benefit is still prevalent in today's small business environment.

A lot of small businesses don't pay FBT. But they should be. A lot of them have got exposures and they don't even know they've got an exposure (ACC5).

In summary, expert feedback indicates that record keeping for tax obligations is still regarded as being beneficial for cash flow management. Concepts identified as being essential for SBO literacy with respect to business tax systems include the need to be aware of ongoing tax obligations and determination of correct lodgement and payment dates for the tax systems that are relevant to their business. SBO should also be capable of identifying that tax

¹⁰¹ McKerchar, M. (1995). Understanding small business taxpayers: Their sources of information and level of knowledge of taxation. *Australian Tax Forum*, (12) 25-41.

¹⁰² Belle Isle, M., B. Freudenberg and T. Sarker. The Small Business Cash Flow Struggle: Should taxation be held accountable? (Working Paper, Griffith University, 2017).

¹⁰³ McKerchar, M. (1995). Understanding small business taxpayers: Their sources of information and level of knowledge of taxation. *Australian Tax Forum*, (12) 25-41.

liabilities are a business expense and should be able to differentiate between the money allocated to tax liabilities and cash available for business trade.

In regard to specific tax systems, the largest number of participants identified GST concepts as being necessary for SBO tax literacy. In particular, concepts highlighted as critical were rules relating to taxable supplies and credits, determination of goods subject to GST and understanding the GST registration requirements and thresholds. Other tax concepts that are considered crucial for SBO literacy include determination of what is considered a fringe benefit, identifying available deductions and concessions, understanding depreciation and forecasting for income tax liability in the first year of trade before PAYG instalments become part of business tax obligations.

Does the level of SBO business tax literacy influence their ability to manage cash flow?

The collection of data then focused on the perception of experts about the effect of SBO business tax literacy on cash flow management. The semi-structured interviews were used to explore whether experts believed SBO business tax literacy had any implications on their ability to manage cash flow. One expert expressed their concerns about SBO ability to manage cash flow, however they suggested that the relationship between business tax literacy and cash flow management is irrelevant. Their response implies that the understanding of business tax concepts is excessive and SBO should have simple understanding of tax where calculation of the tax liability as part of cash flow should be predicted as 1/3 of net profit.

Participant ACA2 made the following comment:

I see cash flow management as a vastly superior problem to taxation. If a small business is making a good profit, tax is an irrelevance. Quite simply, all the business proprietor has to understand that it's roughly a third of his net profit, that's his

depreciation costs. So I've never had the situation yet where anybody has ever complained about an overestimation of tax liability (ACA2).

In comparison the remaining participants suggested that the level of SBO business tax literacy would likely influence their ability to manage cash flow. One participant suggested that taxation was more complicated for SBO than any of the other requirement of running a business and therefore their business tax literacy would have some bearing on their ability to manage cash flow.

I think it probably is more in relation to the taxation, the GST, PAYG withholding and super guarantee side of things. Because the tax obligations, I think, do have an impact on their ability to manage cash flow. My view is that they probably have less literacy in relation to the taxation obligation, than they do in relation to their general business (ACA6).

Two participants highlighted the importance of business tax literacy and its relationship with cash management, particularly in relation to forecasting for the tax liability.

They absolutely need to understand taxation obligations. Again, because in my view it impacts cash flow directly. You have to have the cash flow to pay the tax when due (GOV2).

I mean just the basic issue of GST, you know, to be able to account for that and budget for that, so that when it does become due, that it is there and can be paid on time without them spending it and having it included into their day to day cash thing. They look, they think their cash flow is good but it's not because part of it is their tax liabilities (ADV1).

The remaining feedback proposed that the impact of business tax literacy on cash flow management revolved around the level of literacy held in financial statements and CAS. Experts indicate that insufficient literacy in the other two areas would have negative consequences on the level of business tax literacy held and in turn the ability to manage cash flow. This suggests that in order to have business tax literacy SBO need to be literate in financial statements and CAS. These outcomes broadly contradict the proposition by Chardon et al¹⁰⁴ that a base level of literacy in taxation and superannuation is required in order to be financially literate. Alternatively the results may not oppose Chardon et al¹⁰⁵ but may suggest that taxation, superannuation, financial statement and CAS literacy work in concert with each other and having a high level of literacy in any of these areas is in turn beneficial to your individual understanding of other concepts especially when considering the ability to manage cash flow. Comments of experts are highlighted below:

Literacy has consequences on their cash flow. So if they're not fully understanding tax, financial statements and computer accounting software then it will influence negatively if they're not sure how these interplay with their cash flow. If you don't know what the tax consequences are then you're not going to be able to project the cash correctly (ACC5).

They've got to make sure that they put aside the tax, whether it be the GST or the income tax or even the Pay as You Go, that they're not using it as part of their cash flow, that they've actually set it aside otherwise they're going to get themselves in to trouble at the end of the year (ACC5).

¹⁰⁴ Chardon, T., Freudenberg, B. and Brimble, R. Tax literacy in Australia: not knowing your deduction from your offset. (2016) 31 *Australian Tax Forum* (2), 321–362.

¹⁰⁵ Chardon, T., Freudenberg, B. and Brimble, R. Tax literacy in Australia: not knowing your deduction from your offset. (2016) 31 *Australian Tax Forum* (2), 321–362.

What I would say is that there are a proportion, well less than half of small businesses who start out with the required literacy and capability to actually effectively manage their finances, their business planning, and their tax and superannuation. Therefore, the remaining small business owners can't manage their cash flow because they don't have those capabilities. They simply can't do it. They don't understand basic things like the difference between their business income and their personal income. Business expenses, personal expenses. Their level of understanding is very low. Consequently, they get into financial strife or under financial stress very quickly (GOV7).

I guess my view is that if they're on top of their books and they're able to comply with their tax obligations, it also has the benefit of them being able to manage their cash flow and their understanding of how well their business is going (GOV8).

In summary, analysis of the data in the semi-structured interviews indicates that the majority of experts believe that the level of business tax literacy held by SBO influences their ability to perform effective cash flow management. The capacity to forecast the remaining cash available after taking the tax liability into consideration seemed to be an area that experts were concerned about for SBO literacy. The remaining responses from experts emphasized that management of cash flow when considering business taxation literacy may have a relationship with literacy in the other areas investigated in this research. Experts perceived that the level of business tax literacy of SBO is supported by their level of financial statement and CAS literacy when taking cash flow management into consideration.

6. Conclusion and recommendations

Overall it appears that in order to be professionally financial literate, experts believe that SBO should make use of a cash budget, business plan, profit and loss statement and cash flow

statement. However a critical part of using these documents in the management of cash flow is the ability to extract meaningful information in order to understand their cash flow situation. Essential information includes how to interpret the difference between cash and profit and the effect of cash receipts in comparison to aged receivables and payables.

For CAS literacy SBO should ideally have a thorough understanding of how the CAS functions and at minimum be capable of producing financial reports and comprehending the information contained in those reports. With regard to the effect of CAS literacy on management of cash flow, experts consider comprehension of basic accounting concepts as a requisite to CAS literacy concepts.

When assessing business taxation literacy, experts believe that SBO should be aware of their ongoing tax obligations and determination of correct lodgement and payment dates for the tax systems that are relevant to their business. In regard to specific tax systems, identification of goods attracting GST and rules relating to registration, thresholds, taxable supplies and credits were considered essential for GST. For Income Tax, necessary concepts highlighted were identification of allowable deductions and concessions, comprehension of depreciation rules and understanding of the impact of the tax liability after the first year of trade.

Experts expressed concerns that SBO business tax literacy could impact cash flow management if SBO were incapable of differentiating between the money allocated to tax liabilities and cash available for business trade. Experts propose that to effectively manage cash flow SBO business taxation literacy needs the support of adequate levels of professional financial literacy and CAS literacy.

Appendix 1

Base level literacy could include some or all of the following concepts.

<u>Financial statements</u>	<u>Computer Accounting Software (CAS)</u>	<u>Small business taxation</u>
Understanding of liquidity ratio	Perform original set up of accounts in CAS	Reporting and payment dates for taxes
Understanding of indicators of insolvency	Input data for creditor and debtor invoicing	Preparation of income tax returns, business activity statement, Instalment activity statement, Superannuation reports.
Determine profitability in Income Statement	Maintain bank reconciliation in CAS	Superannuation guarantee and Superannuation contribution
Understand Net value in balance sheet	Preform set up of employees including tax and superannuation obligations	Fringe benefit determination
Understand the difference and effect of current and long term debt	Prepare superannuation reporting and payment	Treatment of dividends, dividend imputation credit, factoring accounts.
Be able to analyse comparative data in: Cash, accounts payable/receivable, equity, inventory and retained earnings.	Prepare IAS and BAS in CAS	Understanding of: Income Business income Revenue vs capital receipt Immediate deduction Small business CGT Repairs Depreciation Small business immediate deductions Marginal tax rates Medicare levy
Understand the difference between operational costs, asset investments and finance in the cash flow statement.	Determine tax treatment of transactions in CAS	Ability to effectively communicate with financial and tax advisers
Compare the Income statement and cash flow statement to determine if there are non-essential expenses.	Produce financial reports from CAS including Balance Sheet, Income Statement, Statement of Cash Flow.	Understanding of GST terminology: GST free, non-reportable, GST inclusive/exclusive, Taxable supplies, input tax credits.
Understanding the concepts of debtors, creditors, assets, liabilities and equity.	Prepare a financial budget in CAS	Capital gains tax, 50% CGT discount, Small business CGT concessions.
Ability to make use of information in financial statements to support preparation of a business plan or budget.	Moderate level of proficiency in business related software including Excel.	Treatment of offsets, deductions, write-offs, concessions, tax rates.