



A reflective analysis of the “new audit” and the public interest

The revolutionary innovation that never came

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Abstract

Purpose – Prior to the sudden collapse of large companies following the turn of the century and the implication that the auditing of these enterprises had failed, the large public accounting firms sought to re-engineer the audit. A comprehension attempt to convert that which had been designed as a social good into one more aligned with a commercial logic was halted by the legislative response to this departure from classic professionalism. Recent developments suggest that change in this direction is regrouping. The purpose of this paper is to provide a reflective analysis of the thoughts of the authors on the early development of the new audit approach.

Design/methodology/approach – Most of the information in the piece was garnered from conversations with public accounting partners during the era in question. Logical argumentation derived from the academic and theoretical literature is the primary method.

Findings – Attributes of the firms’ strategies during this period are outlined. Features of the new audit are developed, especially as they vary from the traditional audit. These techniques and approaches are analyzed in terms of their ability to serve the public interest. This paper argues that motivating factors of the new audit will continue to be a force even in the more hostile regulatory environment of today.

Practical implications – An appreciation of the findings of the study is useful in maintaining a level of skepticism about changes to the audit that are advocated by audit firms. Users of audit services, regulators, and legislators would benefit from an appreciation of the recent past. The motivating factors underlying these changes to audit environment continue to operate over time as the social purposes of the audit are less likely to be converted by the firms to ones that can be commercially exploited.

Originality/value – The study contributes insights into the origins of the new business audit approach and related strengths and limitations. These factors should be considered as the approach is developed and moves forward into the future in order for the audit approach to be effective in performing its social functions.

Keywords Auditing, Innovation, Public sector accounting

Paper type General review



1. Introduction

The audit approach used by the large accounting firms has frequently changed over the last 25 years (Solomon and Trotman, 2003). A new audit approach emerged in the 1990s that was qualitatively different from the auditing described in textbooks and codified in authoritative standards. This audit method, which evolved into business

risk auditing (BRA), was not just the result of capturing the efficiency gains made possible by information technology and other technical enhancements, but represented a more complete merger of the business of accounting practice and its professional aspirations. Strongly motivated by the promise of heightened growth and profits, and developed during a period of time when the firms were relatively free to innovate and apply the new method without outside interference, it represented a dramatic shift in the purpose of the audit and the interests that it served, as the firms acquired a firmer understanding of their place in the financial and economic globalization of the world[1].

This paper provides a reflective analysis of the thoughts of the authors on the early development of the new audit approach, which represents the culmination of many changes in the accounting profession. Throughout the twentieth century, the value of auditing has been closely connected with the existence of independence and the ethical states that are closely associated with such a posture. The publication of Mautz and Sharf's *The Philosophy of Auditing* in 1961 represents an apex of the normative expectations of the profession. Since then three major problems the profession has had to deal with are:

- (1) heightened competitive pressure on audit fees (Tonge and Wootton, 1991; Humphrey and Moizer, 1990);
- (2) a litigious environment (Curtis and Turley, 2007; Palmrose, 1988); and
- (3) persistent negative stereotypes (Silvers, 2007; Willmott and Sikka, 1997).

The new audit approach could also be seen as a partial reaction to the continuing problematics and ambiguities of more established audit methods, such as the internal control audit, the structured audit, and the audit risk model (Knechel, 2007; Francis, 1994; Power, 1995) and their inability to overcome these deep-rooted problems within the auditing profession[2], [3].

The decline of the traditional audit was matched by the ascendancy of other services sold by audit organizations. The ability to “cross sell” to audit clients a host of other consulting services increased organizational profitability and allowed audit organizations to compete for the “best and brightest” recruits from universities and corporations. This juxtaposition also allowed audit organizations to demonstrate to their clients that they were providing value added, even though the audit itself was perceived to be little more than regulatory compliance.

The new audit approach fits well with the development of the firms into world-wide diversified professional services firms, as they walked away from being called accounting and auditing firms, and suited the deregulated, free market philosophy of the times (Windsor and Warming-Rasmussen, 2009; Zeff, 2003a, b). Doing this under the rubric of BRA[4] provided theoretical justification for the firms in converting the audit from a cost-cutting commodity to value-added services, blending consulting and auditing. A broad array of services could be brought within their legitimate borders and conceptual justifications developed to bring along the social, economic, and cultural environments (Robson *et al.*, 2007; Power, 2003).

The firms also stepped away from the “social trustee” value set of professionalism, with a public duty obligation, to a “professional expertise” value set of professionalism, based on market value of knowledge and expertise (Suddaby *et al.*, 2009; Brint, 1994), as they outgrew professional and national boundaries and regulatory authorities and their interests and those of their clients changed (Suddaby *et al.*, 2007; Greenwood

and Suddaby, 2006; Cooper *et al.*, 1998). During this period, there was a power imbalance in favor of the large accounting firms over the federal and state regulators and professional organizations (Greenwood and Suddaby, 2006), that they sought to take advantage of to change the legitimate institutional face of the world-wide accounting profession as well as its functional processes of getting the work done[5]. The firms wanted to establish the legitimacy of these institutional and functional changes between the profession and professionalism, the state and important constituencies with clients, fellow practitioners, regulatory authorities, and others because successful core institutional and technological changes requires the development of sufficient allies to overcome resistance (Robson *et al.*, 2007).

Their success in transforming themselves into top-flight business consulting operations, though, gradually fell victim to its own success. In the USA, SEC inquiries in 2000 into the conflict of interest between consulting and auditing work for the same client suggested that the “foot in the door” strategy (wherein the audit could be *post facto* leveraged into other work) was externally suspicious. Internally, as the reputation for consulting excellence continued to be decoupled for the audit (Covaleski *et al.*, 2003), the latter seemed to be unnecessary for the acquisition of the former, reducing the prestige of the audit segment of the business among auditors.

Among the many revelations that came out in conjunction with the government’s case against Andersen was that this firm had used Enron as a place to roll out what it called an “integrated audit.” At this point in time, the new audit approach had progressed quite far with some clients. Even so, the new audit was nascent in its wide-spread adoption prior to the Sarbanes-Oxley Act of 2002 in the USA that changed the rules of the game. The transition that it called for could not be accomplished overnight, and it may never have totally usurped the traditional audit. Fischer (1996) indicates that in these initial years of audit transformations that there was a subterranean continuation of the old by those that were uncomfortable with the new. Curtis and Turley (2007) found similar results and suggest the discomfort and resistance was caused by practitioners’ lack of perceived linkage between audit work performed on business risks and the opinion rendered on the financial statement. One result was that the methodology underwent successive versions. The new audit was largely a product sold only by the large international firms for their larger audit clients, and may have also been predicated upon the audit firm gaining unusual degrees of confidence with the client through multiple years of traditional audits. Left to itself to evolve, the new audit may have taken years to filter down to a large base of clients.

The passage of regulatory acts in the USA and around the world (e.g. the US’s Sarbanes-Oxley in 2002 and Australia’s Corporate Law Reform Program Act[6] in 2004), has altered the circumstances of world-wide auditing practice in ways that are not yet clear. As part of the legislation, accounting firms cannot provide consulting services to the publicly traded firms that they audit. Has the new international regulations, however, halted the conversion process to the new audit and the dissolution of a boundary between auditing and consulting? In complex social and economic transformation of struggle and competition, both within the firms and with other firms, matters rarely develop linearly or in a straight-forward manner (Power, 2007). A more complicated picture is needed to be reflective of reality.

The purpose of this paper is to outline the attributes of the erstwhile strategy of the large auditing organizations during this transitional period. The features of what

can be called the new audit will be developed, especially as they vary from the traditional audit. This serves as a prelude to an analysis of the ability of the new audit to serve the public interest. In the final section, we discuss the transformation of the new audit and its potential to morph under a different set of regulatory regimes.

The “new audit”
and public
interest

2. Recalibration of the audit

The new BRA that developed in the 1990s[7] represents the retooling of a service that had been primarily directed towards external parties interested in the financial statements of the client into a consulting engagement. As such, it could be considered as an internal leveraging of business advisory services in the name of auditing, and therefore reflected a logical end game of the scope of services. The diversification away from the traditional audit by the large firms had run its course. A diversification within the audit then occurred, creating space for the new audit as a viable service segment.

Firms offering the new audit promised to deliver a large degree of value added for clients. Accordingly, it flipped the conventional value proposition, attending to the public interest dimensions of attestation only as a by-product (Jeppesen, 1998; Zeff, 2003b). The new audit provided nominal compliance with authoritative standards, and therefore continued to be a means of evaluating the possibility of material misstatement in the financial statement. However, this was no longer the center of the engagement.

Unlike the old audit, the new audit was planned with the client (Jeppesen, 1998; Humphrey and Moizer, 1990). This co-development of the audit designated service levels, focus objectives, and measurement dimensions. This mixed responsibility created a radical departure from the traditional audit that had prided itself on being unilaterally determined by the auditor, as guided by professional standards. The new audit also was clearly designed to produce high levels of satisfaction for client management. The production of a positive contribution to the client’s share price now was being offered as the reason for the audit experience.

The new BRA relied heavily upon benchmarking and best practices techniques. The purpose of these methods was to identify conditions, in the financial statements and elsewhere, where the client departed materially from industry averages or was not employing a proven practice of the industry (Lemon *et al.*, 2000; Bell *et al.*, 1997). In short, the new audit approach did not content itself with traditional “what is” questions, but launched from such a point to investigate unprecedented “what should be,” inquiries.

The new audit deepened the need to do work that featured auditor industry specialization. Since it was predicated on the belief that the auditors knew the industry better than the client did, the new audit had to be run by a highly focused staff to be credible. The new audit extended the logic that investing heavily in a narrow industry experience would yield heterogeneous returns.

In a world in which unprecedented market pressures had led to market saturation, commodity pricing, and great pressures to reduce substantive testing, the traditional financial statement audit was losing value in the 1990s (Robson *et al.*, 2007; Eilifsen *et al.*, 2001). Firms struggled to establish that their work was of higher quality than that of their competitors and to overcome the powerful homogenizing influences of the market. The new audit allowed firm reputation for high quality to come to the foreground.

It was designed to be highly differentiated, and therefore very resistant to commodification. If the critical dimension of success is the ability of auditors to deliver upon the expectations they allow their clients to have, firm success would translate into a clearer notion of audit quality.

2.1 *The new audit engagement*

The business aspects of auditing have gained broader recognition over the last several decades, leading to the commercialization of the audit (Windsor and Warming-Rasmussen, 2009; Zeff, 2003a, b; Willmott and Sikka, 1997). Instead of demonstrating loyalty to their auditor, many corporations have realized significant cost savings by regularly seeking bids from firms for their audit work. In order to win these competitions, audit firms had to reduce the prices they charged. This necessitated increased pressure to conduct the audit on a schedule that would preserve its profitability for the audit organizations. The pursuit of these time efficiencies is believed to be associated with diminished audit quality and increased potential for malpractice liability (McNair, 1991; Knechel, 2007).

In establishing a new institutional face for the international accounting profession[8], the new audit began with a more explicit coupling of the business aspects of the market and the work that would be done (Power, 2003; Hopwood, 1998; Jeppesen, 1998). Instead of attempting to provide a public good at the diminishing prices that the private sector was willing to pay, the new audit was unabashedly sold as a private sector good. The price that was charged primarily reflected the value for the purchasing company that can be associated with the work, and therefore would not necessarily be in perpetual decline.

For some time, auditing firms have poured resources into the task of obtaining business, starting with the effort to make their “pitch” unique and engaging. The new audit represented the continuation and exacerbation of these efforts. While this can be seen as a natural reaction to a competitive jungle, these efforts also had the potential to change how the work itself was conceived and provided over time. In order to succeed, the solicitation of the engagement had to be based upon the values held by clients and be grounded in the language that was privileged in their discourse (Khalifa *et al.*, 2007). Whereas the traditional audit was sold as an audit in the terms that its suppliers understood, the new audit in the 1990s was couched in terms of what its demanders appreciated, i.e. “business value.”

The new audit was a process of continuous risk assessment (Robson *et al.*, 2007) and necessitated that the concern about securing the engagement be a continuous one. The management of this relationship was more of a priority than it was in the old audit. Clients, even smaller ones, have to be convinced that they were valued by the auditors as if there were no more important engagements. Increasingly, auditors realized that a successful long-term engagement is built upon the need to demonstrate short-run tangible benefits to the client throughout the process. Every relationship was deemed to be more or less “at risk,” as the firm strove to meet the expectations created by fostering the notion that it stood perpetually on call for the client.

The qualitatively different attention to the relationship required that firms that provided the new audit appreciated and embraced the mission and goals of their clients. This, however, begged the question about who the client was in the new audit environment. While the ultimate client, are the investors and creditors for whom

the audit is conducted[9], the only acceptable answer is that the client was the corporation (Jeppesen, 1998; Humphrey and Moizer, 1990), as firms targeted economic growth by broadening and expanding their client base. The new audit was designed to increase the probability that the financial objectives of corporations would be achieved, which was explicitly acknowledged as part of the engagement solicitation. The clients of the new audit also included the managers of the corporation. Thus, the new audit enveloped the auditor within the political dimensions of the auditee.

Whether the corporation (or its managers) was the true client, the new audit called for a reconsideration of the critical points of contact between the auditor and the client organization. The focus of the old audit upon the financial statements promoted the idea that the CFO and other mid-level staff managers were the key points of client contact. As part of its focus on internal controls, the old audit would also engage the attention of internal auditing personnel, as well as the lower level employees that enacted the various parts of the control environment. These relationships were no longer adequate for the type of involvement sought by the new audit. The new audit, reflecting its aspirations to improve the business as a whole, required contact with higher level managers with more responsibility for strategic direction (Knechel, 2007; Lemon *et al.*, 2000; Bell *et al.*, 1997). Lower level managers possessed inadequate degrees of discretion to respond to the wide ranging advice promised by the new audit. Likewise, managers with responsibilities indirectly connected to the business operations (e.g. CFO, and tax director), were not in a position to respond to it. Accordingly, audit firms sought contact with CEOs to secure the authority to commit the firm on a wider horizon.

2.2 New audit objectives

The audit has historically been understood as a means to test the reliability of management’s financial statement assertions[10], while the responsibility to report on the possibility of business failures has been much more ambiguous (Lee, 1993). The audit has been an exercise in opining on the historical record, even if this meant bearing silent witness to the questionable stewardship of management. Only through the going concern issue was the future viability of the client considered to be within the duties of the auditor. Even there, the concern was obliquely translated into its impact upon financial statement estimates and prortions. Contrariwise, in equating the costs, risks, and values of an audit, the new audit was explicitly about the enablement and extension of client fortunes (Jeppesen, 1998) and its customization for their needs. Risks were evaluated and auditors then provided managerial insight not bound by the financial statements and less fettered by the spirit of neutrality. An audit that failed to add value to the client (e.g. help them more profitable), could no longer be defined as a good one.

A primary objective of the old audit was the measurement and control of risk. As a public good, the purpose of this audit was to report upon the risk that the financial statements were materially misstated (Boynton *et al.*, 2001). Risk continued to matter in the new audit, but it was a different type of risk and evaluated differently. The old audit focused upon detection risk and control risk, and was very much about the imperfections of search for those factors that might lead to an accounting balance being misstated. Although the new audit did not jettison these concerns, those particular objectives were seriously diminished (Eililfsen *et al.*, 2001). Within the trinity of costs, risks, and values, the new audit was designed to give as much of value as possible, constrained by the costs of doing such, with risk more equally weighted. Moreover, risk reduces value

and increases cost, but by itself was not an orthogonal element of importance for the new audit. When audit risk becomes indistinguishable from business risk (Robson *et al.*, 2007), and auditors worry about issues such as competitive positioning, changes in input prices, and inadequate cost control, the focus changed from the fairness of last year's financial statements to what next year's statements would look like. That clients need advice on what they should be worried about on a going forward basis, blurred the risk element into the value element.

The commitment to provide a high level of value could only be met with the delivery on such a promise. Relative to risk, value is highly idiosyncratic even across members of an industry. Although traditional auditing required sufficient client knowledge to refine the methods used, the audit objective itself was not negotiable. Since clients will vary greatly in their perceptions, value achievement must require an audit whose very rationale will be customized to the situation. In such a setting, the letter of generally accepted auditing standards (GAAS) may be seen as an obstacle to efficiency and limits on the desire to provide higher degrees of uniqueness in the service mix. Audit firms are likely to press for a de-emphasis of a unified GAAS through the desire of new audit providers to open more degrees of freedom with fewer mandatory procedures, more optional paths, and a general liberalization of process. If GAAS reflects antiquated thinking that presumes an excessive similarity between audit clients, the success of this advocacy merely sweeps away a nuisance. On the other hand, if GAAS reflects a minimum set of procedures needed to protect the public interest, customization of this magnitude is a retrograde influence.

In resolving the costs, risks, and values equation of the audit process, some writers have cynically observed that the real objective of auditing is the avoidance of legal liability, at least since the large-scale emergence of this litigation in the USA during the 1970s (Fogarty *et al.*, 1991)[11]. If auditors were sued only when auditing was inadequate, a rational response would be to work towards better auditing. However, when auditors are sued whenever clients fail, it is irrational to continue to invest in the traditional audit model. To strike at the heart of the problem, audit firms should work more directly to avoid client failures. To the extent that it promises such a solution, the new audit paralleled the thinking that placed the projected legal consequences at the heart of matters. Understandable as this might be, such a strategy evades the substantive reasons why audit firms were held liable. That auditors had a social duty to investors and creditors that they were not performing, would continue to be true through the new audit. Instead of insisting upon the performance of this duty, the new audit reduced the chances that their supplier would be called to account for malfeasance.

The new audit did not immunize the audit organization from the consequences of association with a risky client. Clients that fail, despite their new audit, would have resulted in litigation against audit firms. The fact that the new audit would have provided less of a defense for auditors should not matter since settlements would continue to be the preferred means of resolution. In fact, the claims made on behalf of the new audit, if internally believed, suggest that audit firms would have been willing to take on additional risk in emphasizing the value portion of the equation. The aggressive sales effort that was an important element of the new audit suggested a balance tipped increasingly toward practice development. In this regard, the new audit would have been greatly facilitated by more "reform" that mitigated the legal liability of audit organizations for client failure.

2.3 New audit planning

In the old audit, audit planning was approached in terms of materiality levels, evaluation of internal controls, choice of audit tests, and ratio assessments (Boynton *et al.*, 2001). That the audit should be responsive to these circumstances had a strong logical appeal. Nonetheless, audit planning never realized its potential as a critical process that could adequately change the resulting audit. This can be attributed to a variety of factors including loss of paper trail, the non-transparency of transaction processing (Knechel, 2007) or the inertia of the audit itself and the power of the previous year’s working papers as a template (Bedard, 1989). As a result, the audit was not adequately responsive to the unique circumstances of companies, industries, and economic conditions. The new audit, in its pre-engagement planning, specifically attempted to find a more correct pivot points between cost, risks, and value for this particular client. Rather than a focus on the trial balance, first-order strategic attention was directed toward the industry (Lemon *et al.*, 2000; Bell *et al.*, 1997). The correctly planned new audit was one that established the appropriate external benchmarks for the client. In this way, audit planning took on a new and much more important function. Whereas this information was no more than a passing road sign in the old audit, the new audit puts industry data about both financial and non-financial matters squarely in its center. Dictated by industry course, the new audit therefore promised a higher level of customization.

To plan the new audit, auditors required additional degrees of flexibility. In important ways, this necessitated finding a congruent perspective on the business with the client. Seeing the business like the key managers of that business required the ability to alter initial ideas that may have been constructed by an auditor’s socialization. Although this includes some familiar factual grounding in discovering critical facts, the new audit also entails a willingness to imagine what could be. Towards this end, the auditor’s value resided in juxtaposing objective industry knowledge upon this task; a purely retrospective vantage, epitomized by the current financial statements, became unacceptable (Knechel, 2007; Curtis and Turley, 2007).

The key component of planning the new audit was the definition and discovery of what constitutes value for the client in achieving strategic objectives (Bell *et al.*, 1997). For example, one large accounting firm during this period claimed that it had “challenged all aspects of the traditional audit” and emphasized in an advertisement how they “now help clients to gain value through new business insights and ideas for addressing business risk more effectively” (Hopwood, 1998, p. 515). As far as possible, the realization of this value had to be measured in the course of the work. Value did not “happen” on its own accord, as may have been the implication of the old audit procedures. Therefore, audit resource deployments had to be strategically focused on work that would succeed in these novel terms. In essence, the new audit plan was co developed with the client (Jeppesen, 1998; Humphrey and Moizer, 1990). Since a successful audit now was defined in terms of client objectives and priorities, only the auditor that knew how to listen could produce a plan poised toward success.

Assurance in the new audit was not exactly planned. Instead, it is “mapped.” This term evinces how the fuzzy edges of an already very imprecise idea grew more pronounced in the new audit. As a result, exactly what constituted an audit became more obscure in its application than normal, and the auditors’ comfort with the numbers could become stressed (Power, 1997, 2003; Pentland, 1993). The old audit had a fairly standard set of tests that could be anticipated and a relatively knowable

conception about the central tradeoffs (e.g. between substantive tests and internal control reliance). The old audit's structure provided a baseline around which special adjustments could be made. This level of comfort did not emerge during the 1990s with the new audit (Curtis and Turley, 2007; Fischer, 1996). Since each firm's plan to find value within the audit varied considerably, how this should have dovetailed with nominal adherence to the discovery of financial statement misstatement would have varied considerably. In the new audit, where the consideration of GAAS was a necessary but not a sufficient requisite, it would have been even more difficult to predict what the auditor needed to know to say that the audit was done. In that the cost, risk, value triad could not be reduced to an analytical specification, the seemingly hard edges of the relationship of audit planning to field procedures were in a state of flux.

Audit planning in the new audit leaned heavily upon the relative success and trajectory of an industry, pushing the firm itself into an almost secondary position. Vast amounts of business intelligence data needed to be accumulated, aggregated, and communicated in meaningful ways to make this new level of analysis work. Plans in place included the development of "dummy" financial statements and disclosures that were expected in any particular industry. This approach prioritizes the development of deep knowledge about industries. As such, it changed the focus of auditing from a check on the reliability of managerial assertions about what has happened, to a projection of ideas about the balances that should have been realized through transactions (Lemon *et al.*, 2000; Bell *et al.*, 1997). The audit was then planned centered around deviations from "normal" balances.

A full-scale mandate of industry specialization for audit personnel was also complicit with the planning around the new audit. Since knowing the client became less important than knowing the industry, industry knowledge was the essential prerequisite to developing an effective audit plan. This created different possibilities for the enhancement of human capital, as well as for the ability to deploy it across engagements.

The new audit could have been seen as a reinvigoration of the spirit of audit planning (Knechel, 2007). In that it extends well beyond the financial statements, planning could not have been faulted for an excessively narrow scope. The new audit may have been more capable than the traditional audit in identifying situations that were unique or out of proportion. However, the issue would more likely have been that this form of planning does not necessarily connect to activities that resemble auditing practice. The audit planning of the new audit might not have led to proportionate changes in levels of substantive testing and follow-up procedures. Although this lack of articulation may also be a problem with the conventional audit (Wright and Wright, 1997), such a result is not a product of design.

2.4 New audit evidence

The evidence that supported the audit opinion has included many different work products including statistical sampling, tests of attributes, testaments of client personnel, and external party transactional confirmations (Boynton *et al.*, 2001). The assembly of this audit work into the work papers of the engagement drew a bright line around the audit that separated it from any other work done for the client. The new audit broke through this functional silo by no longer honoring the distinction between auditing and consulting, and emphasizing analytical procedures rather than the direct testing of account balances and underlying transactions (Cullinan and Sutton, 2002;

Jepperson, 1998)[12]. To deliver value and to manage all sorts of business risk in a coordinated way, efforts were made to bring elements of assurance, consulting and tax services seamlessly together[13]. In this process, that which is evidentiary took on an expanded domain since it reflects more aspects of a client’s business. The evidence that was sought had to be more ambitious and more integrative because it promised to inform the client’s CEO about no less than the hidden truths about the business.

At the same time, that the scope of audit evidence has been greatly expanded, the means of its acquisition were sharpened. Auditors continued to envision the prospects of the full-electronic, and completely off-site audit. This would be possible if much more complete data could be captured from the client’s information systems. In this sense, every audit would have to be a continuous one and one that would be internet based (Elliott and Jacobson, 1997). As deviations between client data and industry data (also being constantly updated on thousands of databases and synthesized for this comparison) become apparent, audit protocols would be triggered. For the most part, the collection of new audit evidence would lie outside the hands of engagement-specific human auditors. Expert systems would be used to “make decisions” based on causal connections that partially reflect industry templates and partially incorporate client idiosyncrasies “learned” through past data assimilations. As economics had changed what the audit needed to be about, technology was changing how it would be performed.

Another evidentiary question that the modern new audit sought to answer pertains to the duplication of audit evidence. The traditional audit involves a good deal of “reinvention of the wheel” for each client. For the most part, the known similarities between clients are not used to achieve higher efficiencies. Instead, many traditional exercises such as the production of the management letter are continued as audit ceremonies. The new audit stripped away the ritual of individual production in the name of efficiency. Prototypes were constructed in the effort to produce audit evidence that would come close to describing client situations. This machine-generated evidence would reduce the need for the handiwork of human auditors in the field and therefore bypass the source of the most expensive duplication. The hope was that suites of products developed in one industry could be effectively implemented in others. These efficiencies in the production of audit evidence were expected to grow as the audit firm deepened its appreciation for an industry. This approach implies that the audit evidence needed for one engagement may have been collected, at least in part, in a previous one.

At the same time, other sources of audit evidence were materializing for the new audit. The construction of very large databases on firms, industries, and the economy led to the codification of knowledge and the leveraging of the knowledge base across staff (Morris and Empson, 1998). This made possible searches independent of a priori theories drawn from audit experience and based on an audit plan. Ongoing monitoring of seemingly unrelated data produced a body of knowledge about normal operating conditions. “Data mining” of this nature could allow for a continuous and unobstructive audit presence. Exceptional variations would trigger additional, more selective inquiry.

The collection of audit evidence has traditionally been subject to materiality thresholds. Although it has defied precise depiction, materiality has been linked to financial statement levels (e.g. percentage of net income) in most operationalizations. The new audit proposed a new approach linking materiality to the purposes of the new audit. If the new audit aimed at elevating the share price of the client, that which does not have the potential to effect this valuation would not be material. Whereas the old audit

presumed that account balances on the financial statements mattered, the new audit was less insistent about the importance of accounting (Eilifsen *et al.*, 2001), shifting to strategic risks, processes and performance indicators. Thus, the mechanism of materiality would vary from industry to industry depending upon something like the earnings responsiveness coefficients. Taken to its extreme, the meaning of materiality in the new audit required accounting itself to rejustify itself as material. The ability of the new audit to look elsewhere for the standard of relevance could only be accomplished if more and more that the old audit would have produced could be considered unimportant.

For the most part, the audit occurred apart from equity market reactions. News, even of the dramatic sort such as going concern opinions, tended to have already been impounded into share prices. The purpose of the new audit, and its materiality standard, more closely entwines it in the maddening effort of companies to meet analyst expectations (Levitt, 1998). This heightening of consequences does not seem consistent with the need for independent professional judgment driven by conservatism and skepticism.

The transition of the materiality threshold called for in the new audit had to be understood as a statement that the financial statements were an opaque way to understand the auditee. If over time, more and more that the old audit would have produced can be classified as irrelevant, a migration would be appropriate. However, there does not seem to be solid empirical evidence on this issue. Moreover, the explicit linkage of materiality to the equity markets creates heavy handed symbolism about the ghettoization of other users of accounting information.

2.5 Internal control

Internal control seeks to ensure that a system is in place to ensure that the transactions aggregated in the financial statements are reliable. As such, good internal controls enable the audit to compensate for the inability to test a large percentage of individual transactions. However, if the risks faced by a business do not appear primarily as threats to the integrity of the financial statements, internal control is less important (Eilifsen *et al.*, 2001; Lemon *et al.*, 2000; Bell *et al.*, 1997).

Internal control evaluation provides a good field of comparison between the new and the old audit approaches. Assessments of internal control serve as a fulcrum in the traditional audit, in which the degree of substantive testing is determined (Boynton *et al.*, 2001). Internal control is so important to justify a separate report to management on the subject. In the new audit, the auditors purposed to do less with internal control at least on any explicit basis. The new auditors seem more willing to assume that adequate levels of control existed. Unless evidence to the contrary appeared, this assumption became a starting point for the engagement. Since the new audit was targeted to the larger companies, such a presumption may not have been widely inappropriate. Years of past audit suggestions on how to improve internal control could have been interpreted as having reached the inevitable point of diminishing returns. Not only did the new audit not focus upon internal control, it did not offer traditional substantive tests in its place (Curtis and Turley, 2007; Eilifsen *et al.*, 2001).

The diminishment of internal control by the new audit was facilitated by changes occurring to corporate clients. The reengineering of business has been largely accomplished at the expense of internal control. By investing more responsibility

in fewer hands for larger pieces of processing, internal control is often violated insofar as less separation of duties and other interpersonal checks are possible. Increasingly, internal control has been transferred to the information system, and therefore has become mostly invisible in the conduct of routine business. The new audit furthered the hope that technology could replace the control achieved by the more obvious duplications that had been largely built in response to the old audit.

The appropriateness of business processes consumes much of the energy previously devoted to the documentation of internal control in a traditional audit (Lemon *et al.*, 2000; Bell *et al.*, 1997). The new audit required auditors to go further into the design issues. Processes were to be identified, flowcharted, and critically scrutinized by auditors. Inputs and outputs were decomposed and key performance indicators were weighted. In the new audit, separate processes were arranged into meta-processes, which are rank ordered by auditors according to their importance. While controls were part of this effort, they no longer are the primary objective. In fact, controls would not normally be allowed to change the logic of the processes. In the pursuit of efficiency, these processes were more often made to conform to that which currently could be done via automated instruction.

2.6 New audit communications

A great deal of attention has been paid to the audit opinion (Boynton *et al.*, 2001). This communication addresses the external constituents of the audit and provides a categorical classification that summarizes the results of the audit work. The traditional audit is also accompanied by a report on internal control and conversations with the company's audit committee.

The communication of interest to the new audit was that which occurred with the key managers of clients. In sharp contrast to the old audit, the new audit required communications that were convincing and persuasive regarding the value that had been delivered. Much effort would have been needed to actually customize these reports and to close the gap between the work that was done and the descriptions of it.

The profession-wide consensus regarding the method and content of an audit facilitated the use of various levels of monitoring as a means of ensuring audit quality. The new audit proposed work that was much less reviewable because much of it stemmed from proprietary models and customized beliefs in causal effects, e.g. Bell *et al.* (1997). The new audit did not depend upon the standards generated by the collective profession for its value in the marketplace and therefore provides little basis, beyond competence inputs, for its review.

Reviews of new audit work within the firm would have been less related to the search for inadequate documentation or for unsubstantiated judgment. These reviews might be valuable in identifying new sources of value that could have been offered to the client with the evidence that had been assembled (Eilifsen *et al.*, 2001; Lemon *et al.*, 2000). Unlike second partner traditional audit reviews, substantial learning potential would have been available for the reviewer.

3. The new audit and the public interest

Although a complete consensus is difficult to establish, the public interest can be defined as that which provides the greatest utility to society as a whole. Whereas private interest behavior is that which furthers the well-being of a narrow range

of people, public interest objectives made wide contributions to the betterment of a diverse population.

The traditional audit has often been described as a public interest service (Lee, 1993; Flint, 1988; Mautz and Sharaf, 1961), a critical part of corporate financial stewardship for the economy. The purpose of restricting auditing to a dedicated class of licensed professionals has been to avoid the injury to many that would be experienced in the face of inadequate skill and improper motivation. The integrity of financial information requires an attestation function to provide a disinterested opinion on disclosure and approximate accuracy (Boynton *et al.*, 2001).

The new audit presented greatly revised thinking about the public interest objectives of audits, both in the absolute and relative to the pursuit of private welfare[14]. These issues range across all auditing dimensions and adhere to the objectives, methods, and consequences of this enterprise.

The very goals of the new audit displaced the public interest purposes of auditing as it has been understood. Advocating a "value-added" audit to increase in the wealth of shareholders (Khalifa *et al.*, 2007; Eilifsen *et al.*, 2001; Bell *et al.*, 1997) is fundamentally different than contributing to the efficiency of the distribution of resources in equity markets. The latter, often given as a rationale of the traditional audit, entails the possibility that, as a result of auditor action, investors should be given information that would suggest that their capital go elsewhere. The new audit worked towards the preservation and expansion of a particularized claim on these resources.

The new audit engaged in much more "invisible hand" reasoning. The achievement of assurance about accounting information has long since been believed to require sustained work and particularized expertise. The new audit did not challenge this directly, but does not stress it either. The efficiency of capital markets and the ability of investors/creditors to access high-quality information about companies just happen as byproducts of self-interested behavior. The conflating of the public interest in belief that there is a mutuality of interests between corporate management, service providers, and shareholders was offered to us by the new audit as the distinction between auditing and consulting was occluded (Robson *et al.*, 2007; Bell *et al.*, 1997). In other words, the new audit was likely to add more substance to the branding that the firms have sought and achieved, in other areas of their work.

3.1 Human resources

The new audit also worked changes to auditing organizations that would have had public interest dimensions. The new audit was seen as a way for accounting firms to make progress on their continuing struggle to recruit the high caliber staff (Greenwood and Suddaby, 2006). Distancing themselves from the "tic and tally" stereotype of the old audit, the firms found themselves being able to recruit seasoned people in mid-career with the realistic prospect of work that was challenging, novel, and well-compensated. The new audit promised sufficiently robust to employ people with different types of skills ranging from backroom technicians to smooth salespersons. The new audit, with these lateral infusions of staff capable of prodigious "billability," should make the idea of an auditing career much more complex and less subrogated to ideas about the integrity of the capital markets for its *raison d'être*.

Performance in the new audit environment would be more difficult to operationalize. The smaller team size and the new value equation translated into less emphasis upon

minimizing the inputs (e.g. “being within budget”) and more on securing high levels of client satisfaction. Whereas the pressure to do the former inadvertently compromised audit quality, the latter creates more purposeful incentives to subvert it.

The new audit threatened to implode the very idea of the general auditor in favor of the industry-specific consultant-auditor. In this vein, the generalized techniques of auditing were not as highly prized as they once were. By hiring talented people working in industry to be these experts, audit firms thought they could bypass the continued tendency of educational organizations to produce generalist auditors. This also minimized the extent that employees had to have a commitment to, or even knowledge of, the pure form of auditing. The new audit would have been possible not by convincing existing auditors to behave differently than their formal training may have suggested, but by hiring people that never knew any different.

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3.2 Independence

The public interest dimensions of the new audit require a consideration of the interaction between the audit and consulting services. Whether or not the provision of consulting service to audit clients erodes the independence of the audit has been keenly debated since the 1970s because of its growing importance to the firms as a revenue source. For many years the struggle was generally being won by the auditing organizations, who attempted to establish that there was either no harmful conflict in expanding the professional services or that the additional services could be appropriately managed. Normally, these arguments were sufficient to dampen down the debate until the next scandal occurred (Humphrey and Moizer, 1990). Over these years, though, the institutional logic supporting the accounting profession was undergoing a profound change. Rather than seeing professionalism as a social space counter to the market and the state and autonomous of them, i.e. as a “social trustee,” there was a fundamental shift in core institutional values to viewing professional work in technocratic terms rooted in the market value of the knowledge and expertise, i.e. “professional expertise” (Suddaby *et al.*, 2009). As part of this process of expanding professional services and redefining professionalism in market terms, systemic attempts were made to redefine what was the public interest (Willmott, 1990), reinterpret the meaning of independence (Reiter and Williams, 2004), and to redefine the professional requirements of independence (Citron, 2003). The issue came full circle in the aftermath of the accounting scandals at the beginning of this century, with governmental organizations acting to prevent the provision of suddenly incompatible services, e.g. The Sarbanes-Oxley Act of 2002 and Corporate Law Reform Program Act of Australia in 2004. For some, this ended the conflict of interest problem. However, the new audit is a more subtle approach to the problem. If the audit could be changed from within, incompatibility of auditing and consulting would be more difficult to allege. Whereas two separate engagements easily can be prevented by regulatory edict, a single engagement with a single fee would prove difficult to disentangle.

The new audit represented a short-lived but bold assertion for the modification of auditor accountability. As professionals, auditors have been held responsible in a variety of ways. With the idea of independence prominently embedded in a code of ethics, auditors implicitly promised allegiance to a social welfare that transcended the interests of their clientele (Lee, 1993; Flint, 1988). The new audit threatened to reduce a complex professionalism covenant into a simplistic insistence upon competence.

In other words, accountability would matter only when an auditor failed to provide good advice or to possess the skills that were promised to the client.

One of the most consequential independence problems that the new audit posed was that it was “co-developed” with the client (Jeppesen, 1998). If this were to be the guiding ethos, whether the auditor could have sufficiency separation from the client to provide even a semblance of an audit is an open question. The cognitive demands of independence, heavy enough in the traditional audit (Braun, 2000) would no doubt magnify in this new environment of client service. If one were to presume the absence of fraud and a very tight system of internal control, the lack of reasoned skepticism on behalf of the auditor could be seen as an acceptable condition. However, this reasoning would also question the importance of having any audit and be inconsistent with reoccurring revelations that indicate the need to have a rein on management.

In the new audit during this time period, the auditor promised to work toward the same goals that motivated the client (i.e. profitability, growth, and market share). This advocacy existed in sharp contrast to those that believe the audit should represent a social space separate from the market and the state and that the auditor should work toward increasing the efficiency of the capital markets. Knechel (2007, p. 402) suggests that the breakdown of rituals and traditions that accompanied the introduction of business risk methods may have “inadvertently provided a highly fertile ground upon which the worst cases of client aggrandizement may have sprouted in the name of providing value to the client.” Although all business can be made better with the correct mix of external services, the advocate’s role is filled with a higher degree of temptation to make things appear better than they really are. Efficiency in the allocation of capital requires the identification of the firms that merit a higher cost. This may not be possible for auditors that see themselves as advocates of clients’ objectives.

The traditional audit provided value to external parties because of their inherent suspicion cast upon managers. The obligation of managers to faithfully account the transactions that they have conducted was only believed to the extent that it could be verified by the auditors. The new audit was predicated on a belief that there should be no rational basis for thinking that the interests of the corporation and its managers depart from those of shareholders (Robson *et al.*, 2007; Suddaby *et al.*, 2007; Bell *et al.*, 1997). The new audit was focused upon the common enemy of both groups, excess costs and less than optimal methods of seeking revenues. The magnitude of this common interest was believed to dwarf the size of the traditional moral hazard concern. Thus, the new audit tended to deny any tension between private interests and public ones. After all, is not what is good for corporations also good for the country?

In that the new audit reduced our need to consider the special public interest role of auditors, it amounts to a deprofessionalization of its providers. The special competencies involved in performing the traditional audit have served as the cornerstone of the professional claims of auditors. The rationale for the licensure of accountants and the scrutiny over their post-admission conduct is closely connected with the special duty of auditing. As auditing has gravitated toward consulting, auditors become less distinctive. If auditors align with the private interests they work for, their commitment to the public good becomes sufficiently suspect to call into question their monopoly privileges over auditing (Abbott, 1988).

4. Conclusions and implications

Some observers might react to the new audit with, “That’s not auditing, that’s consulting.” They would not only be right, but would have also seized upon the basic point. The large firms were not content to use the audit as a loss leader for the subsequent sale of high-margin consulting work. They also grew weary of defending the apparent conflict of interest that existed when these two separate engagements are juxtaposed.

In the new audit of the 1990s, major changes in the core values of the audit profession and in audit methodology supported blurring the differences between auditing and consulting (Robson *et al.*, 2007) as the commercial orientation of the audit profession was extended to its logical conclusion. Positively, while the new audit approach further weakened the profession’s image for independence, it revitalized the abstract knowledge base of the profession with a new conceptual basis for the audit process. Its innovative risk conceptualization returned ambiguity and value to the audit, reviving the audit process from the commodity that it had become (Knechel, 2007; Curtis and Turley, 2007). The new audit approach suited the professional logic espoused by the firms, as they continued to evolve from the “social trustee” value set of professional elitism to that of “professional expertise” based on the market.

The reconceptualization of the audit and of the audit profession’s responsibilities also fitted in well with the globalization process that accounting and auditing standards and the profession were going through, as the firms developed into international professional services firms. They fought wars with their regulators[15] (DeFond and Francis, 2005). And, with the dramatic shift in power from nation-states to the global economic-political system, the firms developed and implemented a strategy for international expansion providing political power and control of pivotal positions in international economic and political agencies (Caramanis, 2002). The traditional regulatory bargain between the nation-state and the profession was being superseded by a new agreement between these transnational trade organizations and the large accounting firms in which “professional services, like any other economic good, are to be governed by ‘laws’ of supply and demand” (Suddaby *et al.*, 2007, p. 346).

With the Sarbanes-Oxley Act in 2002, and other laws and regulations around the world enacted in response to major corporate failures and bankruptcies, there was a rejection of the extent of changes to core professional values and the degree of commercialization proposed for the audit profession. Self-regulation of the audit profession was reversed in the USA and the question raised of the possible need for greater governmental regulation of accounting and auditing practices around the world, as the sufficiency of self-regulation to protect the public’s interest was increasingly being challenged (Cooper and Robson, 2006; Willmott *et al.*, 1993; Baker, 1993). Laws and regulations were passed directly affecting the audit profession’s standard making and oversight function (Herwitz and Barrett, 2004). Power and resources were poured into oversight regulatory agencies and the scrutiny of the firms increased, as the nation-state reasserted its authority and power over the audit profession. With the regulatory change, the firms shifted gears from a dominate audit discourse on “business value” to one of “audit quality” (Khalifa *et al.*, 2007).

Because of the changes wrought to the new audit method from The Sarbanes-Oxley Act, and other laws and regulations around the world, the revised BRA method is now integrated into the plethora of legitimate audit methods, reviving the credibility

of the audit. The revised BRA took place within a framework that required significant rigor in risk assessment at all levels of inquiry, not just the high level and clear linkages between audit procedures and risk assessments. The Sarbanes-Oxley Act in Section 404 also required an additional report by the auditors, in addition to the audit report, assessing the effectiveness of internal controls over financial reporting. There was a clear and definite emphasis and return to auditing practices of a previous era with increased levels of examination and documentation. Rather than being viewed as constraining the methodologies and practices of audit firms, professional regulation can be viewed positively as providing significant public legitimacy to the audit process (Robson *et al.*, 2007). The power of the client is neutralized to some extent and with the greater regulatory scrutiny, the auditor acts with greater circumspection.

The Sarbanes-Oxley Act and other regulatory changes that bore upon the BRA were sufficient to bring life back to the “logic of confidence and good faith” in the appropriate functioning of the world-wide financial reporting and auditing system (Meyer and Rowan, 1991). There has however, been a material loss of trust in the audit profession (Windsor and Warming-Rasmussen, 2009; O’Connell, 2004) and serious questions still remain (Robson *et al.*, 2007)[16], [17].

The audit profession’s image and its logic of confidence based upon a system of mutual trust with world-wide public constituencies has not been helped as much as it might have with the revised BRA method because of its close association with changes in professional ideology implemented by the firms over the last two decades. The firms sought to shift the ideation boundary and dominate institutional logic defining characteristics of professionalism from “trusteeship” to “commercial exchange of expertise” as they grew their markets and worked with transnational trade associations to dismantle regulatory trade barriers to investment and trade in developing an integrated global market (Suddaby *et al.*, 2007; Arnold, 2005). Alternative market-based conceptualizations of the “global public interests” supporting a unified world-wide professional series market are offered in the place of the “public interest.” The “public interest” as a legitimate objective of regulation was actually rejected by the World Trade Organization (WTO) as too broad and imprecise; “consumer protection” was advocated in its place (Arnold, 2005).

Similarly, the government’s direct intervention in the audit profession has not improved the audit profession’s image and its logic of confidence with world-wide public constituencies as much as it might have because the use of laws as a regulatory device is limited and costly and much skepticism remains[18]. For example, the superstructure of national and international accounting and auditing standards are suppose to provide transparency and reliability of financial data in the global markets; yet many of the manipulative accounting techniques used by clients to manage earnings in the 1990s, and which eventually resulted in misleading financial statements and ultimately business fraud and failure, were encouraged and developed by the audit firms themselves (McMillan, 2004). While increased professional regulation and scrutiny has dampened down that competition between the firms for the present, it is likely only a matter of time before firms’ skills in helping clients circumvent rules and laws will return enforce in an intensely competitive environment. Laws such as The Sarbanes-Oxley Act do not “actually deal with the causes of the systematic failure of that trust, and so does not ensure the prevention of future failures of that trust” p. 947). The Sarbanes-Oxley Act also does not eliminate the conflict of interest of auditors

between serving the public interest and private interests, or does it mitigate their economic dependency upon the client. Windsor and Warming-Rasmussen (2009, p. 269) argue that “the commercialization of audit has exacerbated the inherent regulatory flaw of the auditor economically depending upon the auditee client company and management.” The essential auditor-client conflict has not been resolved, only moved forward to the next major financial disaster. Currently, the firms appear to be looking around for a new knowledge revolution to drive the audit profession forward for the next ten years (Hopwood, 2009). Addressing this deepening skepticism of the audit profession should be a significant part of this next new conceptualization.

An important touted benefit of the BRA method is its potential ability to identify litigation (Knechel, 2007). Auditors are responsible to provide “reasonable assurance” of detecting material misstatements in the financial statements of publicly traded corporations. With most of the lawsuits arising out of financial statements audits the result of bankruptcy and fraud (Curtis and Turley, 2007), Francis (2004) indicates that while the number of lawsuits on an annual basis given the population of audits is fairly small (less than 100 per year in a population of 10,000)[19], the potential magnitude of the lawsuits threaten the very existence of the firms. And historically, the firms are not very successful in predicting bankruptcy. Among an average of 40 bankruptcies a year of publicly traded companies just 30 percent had a going concern modification by the auditor (Carcello and Palmrose, 1994). With the cataclysmic meltdown of the financial section world-wide, the failure rate of banks and financial institutions has significantly increased. Such audit failures create very serious litigation risk for the large accounting firms.

Crises are a time when “the raw edges of practice are most apparent” and they clearly reveal “the negotiated nature of auditor responsibilities” (Humphrey *et al.*, 2009, p. 822). For example, for many years the large accounting firms response to expanded litigation risk has been an increase in defensive auditing, rather than promoting higher audit standards (Chandler and Edwards, 1996). Fogarty *et al.* (1991) suggest that the firms usually operate in a rational manner in relation to audit failure and litigation costs[20]. With the very low audit failure rate and the ambiguous relationship between audit procedures and audit quality[21] and the need to control costs in a highly competitive environment, the audit firms have tended to embrace growth as a means to outrun their legal liabilities. Settling lawsuits with lawyers instead of taking them to court has become a policy used by most of the firms for many years. As part of this defensive strategy, the firms have also sought to limit their liability for the escalation of lawsuits against them by supporting laws that restrict their liability, e.g. the US Private Securities Litigation Reform Act of 1995 dealing with joint/several liability (Zeff, 2003b), or state laws allowing accounting firms to become a limited liability company (Chandler and Edwards, 1996). For several decades before The Sarbanes-Oxley Act in 2002 audit fees went down drastically because of “lowballing” and increased competitive bidding (Zeff, 2003a, b), thus the firms have needed to build slack into the system and finesse their litigation risks to the extent that the system will allow[22].

Currently, the large accounting firms are dealing with world-wide estimated liability of US\$50 billion in claims (Windsor and Warming-Rasmussen, 2009), and KPMG has a single lawsuit of \$1 billion by the liquidators of the sub-prime lender New Century for failing to disclose the extent of the lender’s financial problems (Humphrey *et al.*, 2009). If this was the extent of lawsuits against the large accounting firms, then one could

argue, as Hopwood (2009) mentions, that BRA had come through the financial meltdown fairly well, since the firms have largely not been blamed for their client's business failures. Unfortunately, billions of dollars in lawsuits yet may be filed against the Big 4 accounting firms as a result of the financial meltdown of banks and other financial institutions in recent years (Mathiason, 2009). The use of the BRA method does not appear to have had the intended effect of better managing and reducing auditor's legal liabilities risks. The revised BRA approach with greater regulatory inspection of the firms has helped restore ambiguity and move the knowledge base of the profession forward, but it is not the silver bullet that kills the werewolves of cost, litigation risk, and professional image. As Chandler and Edwards (1996) mention, the problems of yesterday continue to be the problems of today.

Auditing is not only a technical practice, such as BRA method, but it is also a social process. While at the practice-level purification rituals are required within the firm and the profession (Pentland, 1993), externally the legitimacy of the audit is co-constructed and maintained within its social, economic, and cultural environments (Robson *et al.*, 2007; Power, 2003) in "a fragile and negotiated process of network building" (Free *et al.*, 2009, p. 120) with society, regulators, significant users, and others.

The meaning of professionalism within the globalized financial information system may have changed. Within that broader transition, a shifting ideological discourse is being used in shaping ideation boundaries and institutional norms involving the very meaning of auditing. Khalifa *et al.* (2007) indicates that rather than a primary technical phenomenon, auditing emerges as a highly discursive practice that enables and reflects institutional (regulatory, cultural, and normative) and competitive changes in the audit field and prevailing conceptualizations of the role of the audit. Robson *et al.* (1994) state that the terms of discourse of this professional ideology both enable and constrain the practice of accounting and occupational change, where the instability and ambiguity of meaning[23] are conditions of this possibility. To change a professional discourse that has become taken for granted and widely accepted requires that the discourse be redefined "in a way that reduces or at least muffles dissonance between public expectations and 'professional' activities" (p. 551). The relations between the profession (and the large firms) with the state and regulatory agencies and users of financial information have changed with the events of the last several decades. In this new international regulatory regime, rather than a hierarchy of state power, the relationship is best understood as a network of interacting bodies (Richardson, 2009)[24]. Suddaby *et al.* (2007) indicate that a shift is involved from hard actors with coercive powers (e.g. nation-states) to soft, transnational actors that use normative power and the capability to shape identities and interests. Power is exercised through networks of cooperative, interdependent relationships where "members become embedded in a web of mutual economic dependence" (p. 355)[25]. Under the threat of economic backwardness, marginalization and exclusion of the society, market logics and discipline are voluntarily accepted by countries in order to be included in international trade agreements (Caramanis, 2002).

The large accounting firms have become influential players in the newly developing global regulatory system (Suddaby *et al.*, 2009; Cooper and Robson, 2006). They have sought to strongly influence and work with international regulatory bodies and, as a result, have been important sites and mediators of the development of new concepts of professionalism and regulation (Cooper and Robson, 2006). The firms also are influential

in renegotiating auditing as a social and technical practice with its significant constituencies as accounting and auditing have become more of a global practice. The firms have worked proactively with nation-states, international economic institutions, and others to bring about a global market for accounting and auditing professional services using a common economic logic (Arnold, 2005) of deregulation and opening of global professional services markets. International agreements are used to purge domestic regulations that are seen as barriers to commerce.

In the international arena, the large accounting firms have enjoyed the growth of a “shared (public-private) system” regulating and setting standards in the global public interest (Humphrey *et al.*, 2009). Self-regulation is “re-emerging in a modified form of regulatory partnership between the firms, public oversight boards, and the larger national accountancy bodies” (p. 821). This shared system[26] is apparent in both in the actions of professional oversight agencies, as well as in the regulatory involvement of the firms.

Within this global system, there has been an amazing transfer of power to the international regulatory system and its agencies from nation-states in recent years (Caramanis, 2002). The move to a global, unitary market under the General Agreement on Trade in Services and the WTO has the potential to limit the ability of nations to regulate their own economic activities[27] (Arnold, 2005). Accounting and auditing, within the professional services area, was selected by the WTO as the first profession to come under review and to serve as a model for the other professions. The effect of this process cannot be easily judged in the short term, since it is “a more complex and gradual process involving forces beyond the WTO” (p. 325), with changes that only, happen gradually within the market. However, they are unidirectional. The strength and influence of the international regulatory agencies over accounting and auditing standards and regulation in an increasingly global economy are expected to grow significantly with time.

Claims of the WTO and other global bodies to serving the public interests used to create legitimacy within the complexity of global governance should be kept under review with competing, alternative conceptualizations. In a study of the International Federation of Accountants (IFAC), Loft *et al.* (2006) found that public interest explanations are now rationalized by reference to free market concepts and terminology. This has led to the dismantling of regulatory trade barriers to investments and trade, rather than to a public interest conceptualization of broader social application. A new governance system is used that is increasingly reliant upon “professional experts” from financial market regulatory interests instead of representatives of the more general public in evaluating the legitimacy and public interestedness of their actions[28].

There are numerous very real parallels between the globalization of international accounting and auditing standards and regulation and the process leading to the new audit approach of the 1990s. In both scenarios, the firms are powerful players within the institutional and regulatory settings that are trying to move the social norms and institutional understandings from a traditional perspective to a more innovative one. There is an increasing commercialization of the audit process and moving away from a dominant social logic of professional trusteeship to a dominant economic logic based upon the commercial exchange of expertise. The client and the market occupy the center of the professional universe rather than the social role of the auditor serving the public interests as an arbitrator[29]. Though there is appropriate conflagration of public

interest and private interests, the process operates for the benefit of private interests and the auditing profession “is more than ever economically dependent upon the client” (Windsor and Warming-Rasmussen, 2009, p. 272). While there has been an increasing withdrawal of trust and rising skepticism of the audit process, in coordination with the interests of numerous transnational trade organizations and others the firms have the ability to carry the commercialization logic and dismantling of the global professional services market forward for years in the face of significant opposition.

The large accounting firms are important mediators of professionalism and accounting regulation matters (Cooper and Robson, 2006) and are influential in producing and reproducing the way “economic and social life is to be conceived, managed and changed” (p. 436), already having had a major effect upon the boundary between the regulated and the regulator. For example, the narrowing of differences between “managerialism” and “professionalism” has been brought about by profound alterations in the institutional structure of professional work, and the concept of professionalism now mixes public duties and commercialism (Suddaby *et al.*, 2009). Gill (2009) performed an ethnographic study of practicing accountants in the UK and found the ethics, professionalism, and the audit process itself all permeated by this commercialized reconceptualization of the audit.

The ideological discourses used by auditors are important because in helping establish acceptable ways of speaking about a topic, they can change institutional ideation boundaries by which actors and constituents in a field define, create, and sustain their realities (Khalifa *et al.*, 2007). Suddaby *et al.* (2009, p. 425) indicate that the logic of professionalism is important as rationalized myths because they establish widespread understanding of “how professionals *ought* to act, how professions *should* be organized and how professional norms are *best* enforced,” determining the legitimacy of institutional structures and professional practices that enable and also constrains professional behavior.

One of the most fundamental reconceptualization of the commercialization of the role of the audit and the auditor is the focus upon the client, rather than the public or investor. Auditors have always had a dual focus, serving the needs of their client and also as an arbiter for the public. With the traditional trusteeship view of the profession, the stewardship of the public interest is a basic focus of the audit process and serving the clients’ needs a crucial aspect. The reconceptualization does not just juxtapose them, but drops the public interest significantly out of the equation. Cooper and Robson (2006, p. 435) go so far as to say that “no longer are the actions of professionals and regulators rationalized by reference to public interests explanations.” Basic conceptualization of legitimate and appropriate action by the auditor is revised under the new perspective. The increasing status of corporate clients, the expanding intimacy between firms and their clients, and the power asymmetry between them arising from an increasingly interdependent relationships results in a situation called “client capture” (Suddaby *et al.*, 2007, p. 342), where the need to grow revenues trumps the public interest and the traditional professional values of the firms. Thus, the conceptualization of the audit and the public interest can be morphed over time from the primary perspective on trusteeship and general welfare through many different sets of regulatory regimes to that of expertise and market efficiency.

While there are similarities in discourse used by the firms between the new audit approach of the late 1990s and the globalization process of today, there are also

real differences. The main difference was that the new audit approach of the 1990s was nominally subject to the hard, coercive authority of the nation-state. That resulted in its severe modification to come more into line with laws and regulations and broadly accepted social norms using a trustee conceptualization of professionalism based upon the “creation of a social space that is independent of both the state and the market” (Suddaby *et al.*, 2009, p. 410). The reconceptualization under the globalization process using softer cooperative, interdependent powers of transnational organizations, and trade agreements that are supportive of an economic approach to professional services and the elimination of domestic trade barriers provides new life to revised discursive ideology of professionalism. There is significant assurance that the classical concept of professionalism discussed by Friedson (2001) and Abbott (1988) will see more modifications as commercialism makes further inroads into the underlying, generally accepted and taken-for-granted conceptualizations and discursive practices.

Because of concerns about the breakdown of the logic of professionalism or even its demise with the inroads of commercialism, studies have examined the level of professionalism in the audit profession. Suddaby *et al.* (2009) examined Canadian accountants across traditional and non-traditional work arrangements. They found though evidence of the increasing influence of commercialism, a lower commitment to independence enforcement among public accountants, particularly among Big 4 firms. Gill (2009) conducted in-depth interviews with 20 Big 4 chartered accountants in the UK. He found commercialism to permeate the audit socialization and practice process.

While the concept and discursive ideology of professionalism is changing and evolving, converting that into taken-for-granted understandings among broader constituencies, and financial information structures anytime soon is questionable. Hechter (2008) indicates that changing norms is problematic and happens gradually in numerous stages. The globalization process will increase the number and variety of financial information stakeholders whose competing perspectives, tensions, and interests are greatly expanded, and appealing to “global public interests” by transnational organizations is not going to eliminate governance powers and varying perspectives at the national and regional levels or competing regulatory and oversight desires among other organizations (Raar, 2009; Loft *et al.*, 2006). Whatever role develops for the firms is likely to include a push for greater transparency and visibility by the firms themselves (Humphrey *et al.*, 2009). The evolution of the concept and discursive ideology of professionalism is likely to be long and protracted with input from large numbers of diverse global constituencies. While the firms have shown themselves to be highly influential, the final resolution may rest with its broad constituencies, that may still be willing to extend the logic of trust (Raar, 2009; McMillan, 2004).

Litigation remains the Achilles’ heel of the audit profession and accounting firms association with failed clients or fraudulent financial statements. The failures of World Com and Enron brought about the end of the new audit approach and ushered in the revised BRA approach. New audit technologies and methodologies developed to provide an adequate audit and meet the purification and ritualization requirements of the practitioners and firm performing the audit, the profession, regulators, and users of financial statements. We are already in the process of looking for the next new thing that can move the abstraction and conceptualization of the audit and its application into the future. This process is likely to continue to be both messy and jerky even if it is accompanied by a clear view of its history.

Notes

1. Other parts for the initiation of a revised and commercialized approach to the accounting profession that developed during this period included: first, a new unit of practice, the multi-disciplinary practice, converting the firms into diversified, professional services firms able to meet all the needs of their clients around the globe (Greenwood and Suddaby, 2006; Powell *et al.*, 1999); second, a new global certification administered by the profession and not by governments (Suddaby *et al.*, 2007; Fogarty *et al.*, 2006; Shafer and Gendron, 2005); and third, a shift in the key structural boundaries of the professional service field from the state to the transnational level (Humphrey *et al.*, 2009; Richardson, 2009; Suddaby *et al.*, 2007; Loft *et al.*, 2006; Cooper and Robson, 2006).
2. Regarding the first, auditor's costs potentially can be reduced by conducting a high-level strategic and analytic approach to the audit, rather than gathering evidence on all the assertions in the financial statements. As a secondary effect, the close analysis and understanding of the client's business risks has the potential to reduce litigation costs to minimal amounts. The effectiveness and efficiency of audits can be maintained in the face of tremendous fee pressure. The profession's image problem, though, is worsened, because of the need for closer working relationships with management.
3. Subsequently, Curtis and Turley (2007) indicate the potential for no cost savings or increased cost with the new method. Power (2003) suggests an incentive to increase revenue rather than decrease costs was motivational for the change in audit method.
4. The beginning of a new broader view of risk that included more than just the correction of accounting errors started with the issuance of the report *Internal Control – Integrated Framework* by the Committee of Sponsoring Organizations (1992) (Knechel, 2007). Theoretically, BRA provides a different conceptual approach to an effective audit, i.e. concentrate and gather evidence on the risk drivers of a business that directly affect audit risk, rather than gather evidence broadly across assertions in the financial statements based upon assessment of control risks.
5. See Lounsbury (2008) and Dillard *et al.* (2004) for a discussion of the use of institutional theory in understanding transformative changes in institutional face and internal function in establishing organizational legitimacy.
6. Houghton and Jubb (2003) provide some background to its development in Australia.
7. Arthur Andersen & Co. (business audit), KPMG (business measurement process), PricewaterhouseCooper (PWC audit approach), and Ernst & Young (audit innovation) each developed proprietary audit methodology during the 1990s focused on client business risk as the key element of the new audit approach (Khalifa *et al.*, 2007; Robson *et al.*, 2007; Lemon *et al.*, 2000).
8. We define the face of the international accounting profession in terms of: professionalism, ambiguity; and power. The first deals with what is brought by practitioners, firms, and professional organizations to the audit process, e.g. the knowledge, judgment, prestige, space. The second deals with the audit process itself and the usefulness of ambiguity in establishing value/power/prestige of the process (Power, 1997, 2003). The third factor deals with relationships with clients, regulators, and others and depends to a great deal upon the first two factors. The amount of power of the practitioner and firms versus clients, state, and others depends upon space, prestige, and other resources developed by practitioners, firms, and professional organizations as well, as the legal structure of the country. All of these factors together establish the face of the international profession and of individual countries and firms and the level of legitimacy that each brings to the financial reporting process (Suddaby *et al.*, 2009).
9. Shareholders are the legal client in Australia (Corporations Act 2001).

10. McNair (1991) indicates that the functional form of the audit process is driven by: costs and quality, and suggests a conflict between them. The quality function of an audit can be further broken down into a consideration of risks and values as elements motivating the audit process. As such the functional form of the audit process can be evaluated in terms of: costs, risks and (3) values. These factors are highly interrelated and interdependent and change over time in response to numerous external and internal matters (Knechel, 2007; Zeff, 2003a, b).
11. A study found that between 1991 and 1995 the Big 5 firms paid \$1.7 billion in cases that allege securities fraud and other wrongdoings. During this period, Deloitte and Touche paid \$312 million to settle claims by federal regulator of flawed audits of a number of banks and savings and loans. Ernst & Young agreed to pay a \$400 million settlement with federal banking regulators arising from several failed audits with financial institutions. KPMG agreed to paid \$186.5 million to settle claims brought by the Federal Deposit Insurance Corp., the Resolution Trust Corp., and the Office of Thrift Supervision against the firm. In 1998, KPMG agreed to pay \$75 million to settle four lawsuits with claims of \$3.5 billion from the Orange County bankruptcy. The Big 4 firms are estimated by industry sources to spend each year more than 10 percent of accounting and auditing revenues on defending and settling lawsuits (Herwitz and Barrett, 2004).
12. The nature of audit testing was to be changed “from large volume tests of details to testing of high-level monitoring of supervisory controls, supported by high precision analytical work” (Curtis and Turley, 2007, p. 444).
13. Jeffrey Skilling, President of Enron at the time, in an Andersen video tapes developed to market the integrated audit said: “I think over time we and Arthur Andersen will probably mesh our systems and processes even more so that they are seamless between the two organizations” (Herwitz and Barrett, 2004, p. 63).
14. Willmott and Sikka (1997, p. 832) quote a comment by Hanlon (1994, p. 150) that: “Today, in contrast to a decade or so ago, the emphasis is very firmly on being commercial and on performing a service for the customer rather than being public spirited on behalf of either the public or the state.”
15. Greenwood and Suddaby (2006, p. 27) indicate that by the 1990s the Big 5 had outgrown their institutional moorings and became “immune to coercive and normative processes because their market activities expand(ed) beyond the jurisdiction of field-level regulations.” As the Big 5 became “institutional entrepreneurs” on a global scale, they suggest that the firms became more receptive to alternative, commercial logics; the object of national and regional regulation became more powerful than their regulators and consequently less constrained by institutional processes. As a result, the firms were willing to become spokesmen for powerful clients (Cooper and Robson, 2006) and to do battle with their regulators and those of their clients.
16. The BRA approach joins many previous audit innovations that have found it difficult to crack the nut of the audit profession’s three continuing problems: intense competitive fee pressure, litigious environment and independent image.
17. Hopwood (2009), for example, suggests that the efficacy of risk management mechanisms in evaluating risks is being questioned by some of the firms since the risk methodology did not catch significant bankruptcies and failures. The BRA approach has never dealt well with maintaining the profession’s image of independence. Its proposed strengths were reducing costs, increasing revenues, anticipating and controlling litigation, and converting auditing to a new conceptual basis thereby adding ambiguity and power back into the auditing process.
18. For example, Malsch and Gendron (2009, p. 736) performed a sample of in-depth interviews with financial practitioners and found: “(1) a firm tendency to favour the quality of

management over the content of financial statements in investment decisions and recommendation processes; and (2) a fundamental skepticism and lack of comfort regarding the work of auditors.” They suggest that financial practitioners trust in auditors consist of a “mythical representation” that functions to generate order and reproduce the status quo in the financial system. Macintosh and Shearer (2000, p. 618) argue that the audit profession has no contract with society and no professional obligation and that the profession “only plays at being an appearance.” There appears to be a high level of skepticism of the public interest of the audit profession among many of its publics.

19. Psaros (1987) in Australia estimated a less than 1 percent rate of material fraud in audit engagements. The results of both studies indicate a very low rate of audit failure.
20. McNair (1991) suggests that the cost/quality tradeoff creates a dilemma for accounting firms. They try to operate within an ambiguous “zone of compromise” given severe cost constraints, targeted toward keeping individual behavior in the gray zone between efficiency and effectiveness.
21. Because of that obscurity, McNair (1991) indicates that auditors have difficulty in evaluating audit quality and usually rely upon two proxies: what was done last year and the firm’s proprietary technologies and audit practice manuals. Power (2003, pp. 385-8) similarly, indicates that good auditing is “equated with process” and the “relentless application and effort,” with the working papers becoming the representation of the auditor’s discernment and judgment. Both McNair and Power imply that it is good judgment that makes a good audit. It is good audit documentation, though, that has come to indicate audit quality, particularly to address litigation risks that auditors must potentially face.
22. Thus, costs, litigation risks, and maintaining audit quality (both in fact within the firms and the profession and in appearance with their publics) have been the three crucial elements in the audit equation driving the function of the audit and the face of the profession as new audit technologies are developed and implemented.
23. Suddaby *et al.* (2007) indicate that institutional logics are reflective of mythologies built upon contradictions, and that the skillful manipulation of the contradictions inherent in those logics are useful in effecting institutional change.
24. Loft *et al.* (2006) suggest that the global regulation network is complex and multilayered, with three different levels of infrastructure, i.e. supranational, transnational, and national, and that this regulatory arena has numerous competing perspectives, tensions, and interests. It is still in its formative years (Humphrey *et al.*, 2009).
25. Rather than simply displacing them, the new international actors are superimposed on the older actors with coercive power, e.g. nation-states and professions, and instead of reducing their coercive powers the new transnational actors depend upon the traditional power structure (Suddaby *et al.*, 2007).
26. For example, the IFAC speaks about an important role for the large accounting firms in regulating the profession and balancing self-regulation with external oversight with external regulation (Humphrey *et al.*, 2009, p. 817).
27. When political and economic governance are decoupled it is called “fragmentation of sovereignty” (Arnold, 2005, p. 304). Smaller, less hegemonic states are more susceptible, but advanced states are at risk also (Caramanis, 2002).
28. Windsor and Warming-Rasmussen (2009, p. 284) calls reliance upon experts in developing and administering policies for international regulatory bodies “second-level indirect representative democracy” at best, and one that ignores the fundamentals of democracy at worst.

29. Stevens (1991, p. 18) calls the logic of the traditional trusteeship professionalism the “shroud of invisibility that camouflages and covers the true nature of their work.” Without it the people will see that the king is naked, working for private and market interests even though their institutional role involves the acceptance of public responsibility to large numbers of constituents within the global financial information system.

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