

The London School of Economics and Political Science

The Changing Constellations of Audit Quality

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Abstract

This thesis examines the emergence and rise of audit quality as an object of concern from the post-war period onwards, as manifested in the discourse of regulators, practitioners and academics primarily in the US and the UK. By drawing upon Burchell et al's (1985) notions of the arena and the constellation, this thesis seeks to investigate the changing nature of the audit quality 'problem' and in so doing, reconceptualises the constellation as being dynamic in nature. It puts forward the notions of the *emergent* constellation, when an altogether new arena becomes formulated through the emergence of a new event or object and the *reformation* constellation, when an existing field of operations becomes further delineated or differentiated into more distinct arenas. Central to this dynamism is the notion of linkages, and the precise nature of the linking work entailed, which connect together disparate ideas and attach these to the audit quality discourse. Together, this thesis aims to contribute to our understanding of audit quality, the interrelationship between the three arenas of regulation, practice and academia, and of accounting change. Ultimately, this thesis will show that audit quality, a topic of profound and resilient interest, should be understood primarily, and merely, as a basis through which very particular sets of historically contingent concerns and practices are articulated, and that efforts to measure and improve audit quality are fraught with difficulties. Indeed, the attempts to do so play a role in shifting the conceptualisation of the audit quality problem and are consequently, and in this sense, susceptible to continual failure. An alternate interpretation of the importance and meaning of this rise of audit quality, beyond and irrespective of the large scale failures and crises, is an alignment with the trend of economization in society.

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Abbreviations used

AICPA	American Institute of Certified Public Accountants
APB	Auditing Practices Board
Big N	Denotes the largest global accounting firms at the time, where N has variously ranged from 8 to 4
CC	Competition Commission
CMA	Competition and Markets Authority
EC	European Commission
EU	European Union
FRC	Financial Reporting Council
FTC	Federal Trade Commission
IAASB	International Auditing and Assurance Standards Board
ICAEW	Institute of Chartered Accountants of England and Wales
IFAC	International Federation of Accountants
IFIAR	International Forum of Independent Audit Regulators
ISB	Independence Standards Board
PCAOB	Public Company Accounting Oversight Board
POB	Public Oversight Board
US	United States of America
UEC	Union Européenne des Experts Comptables Economiques et Financiers
UK	United Kingdom
SEC	Securities and Exchange Commission

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Chapter one

Introduction

1.0 The rise of audit quality

The term “audit quality” is frequently used in debates among stakeholders, in communications of regulators, standard setters, audit firms and others, and in research and policy setting. Audit quality is a complex subject and ... there is no definition or analysis of it that has achieved universal recognition.

- IAASB Audit Quality Framework, 18 Feb 2014

Concerns about the efficacy, role and objectives of the external audit¹ have plagued the accounting profession from its outset. In the UK, Humphrey et al (1992) and several others (see Lee et al, 1996; Brown, 2006) have noted that calls for the accounting profession to defend the adequacy of its own work have occurred from as early as the late 1800s, corresponding with when the accounting profession was first formalised. In the US, congressional interest in the work of auditors has occurred since the early 1900s with various committees and investigations being established following large scale, public business failures (e.g., McKesson & Robbins, 1938). Since then, concerns about the work of auditors have only continued. These concerns have variously ranged from issues of independence, objectivity, the responsibility for fraud detection, professional scepticism, the ‘expectations gap’ of the public (Porter, 1993), auditor litigation levels, the inadequacy of the audit report to many others. They are ongoing, escalating and currently have a global reach.

This wide-ranging concern has both triggered and been demonstrated by an intense discourse surrounding the ‘problems’ of the audit, produced by a range of actors in the field including regulators, practitioners and academics. In addition, beyond the discourse, these concerns have manifested themselves in an escalating trajectory of regulatory efforts and pressures for the profession to demonstrate a response. New institutional structures for external oversight of audit firms have been erected to oversee extensive programmes of audit firm inspections, organisational changes within the audit firms have been extended to cope with these inspections and periodic inquiries into the roles and responsibilities of the audit have provided some of the ongoing pressures for reform.

¹ As Power (1997) has argued, the term ‘audit’ now encompasses a wide range of activities in spaces outside the traditional financial audit. Notwithstanding this, references to ‘the audit’ within this research remains on the external financial audit conducted on corporate financial reports by audit firms and as required by legislation.

Despite these efforts and pressures, however, an observation which has been made (Chandler and Edwards, 1996; Humphrey et al, 1992), with the passage of some time, is that the on-going discourse is proving profoundly resilient. Many of the concerns with the audit, such as the responsibility for fraud detection or independence, and the underlying arguments and debates which underpin these concerns, are simply recurring. A question therefore arises as to whether or not the escalating regulatory scrutiny and audit firm activity to date, which have been deployed to address some of these wide-ranging concerns, are successfully addressing the underlying complexities.

Central to the discourse regarding the efficacy of the audit during this last half century has been the rise of the notion known as ‘audit quality’. The debates have been extensive and audit quality has within this contemporary period become established as a widely accepted concern of the external audit. Intricately linked to the concern of audit quality is the role that high profile failures, scandals, economic downturns and financial crises have had in sustaining the discourse. Indeed, much of the motivation for the interest in and ensuing discourse on audit quality has often been tied to these failures and crises, positioned as irrefutable evidence of both the significance and substance of the problem. Failures and crises have served as the clear justification for the concern. Statements such as the following can typically be found at the start of regulatory consultative documents in support of the need to investigate and improve upon audit quality:

Recent financial conditions have highlighted the critical importance of credible, high-quality financial reporting in all sectors of the world economy, including the capital markets, small companies, not-for-profit and government organizations. They have also reinforced the need, in the public interest, for continual improvement to audit quality (IAASB, 2014, emphases added).

These have not just been restricted to regulatory bodies. Similar statements can also be seen in contemporary auditing textbooks, such as: ‘In the aftermath of recent scandals, there have been calls for enhanced corporate governance and risk management, as well as increasing quality and scrutiny in auditing’ (Soltani, 2007, p. 2). Academic articles have also adopted a similar stance such as the opening sentence of Ghosh and Moon’s (2005) study on the relationship between auditor tenure and audit quality: ‘The recent rise in accounting irregularities has reopened questions about auditor tenure, independence, and audit quality (Bricker, 2002).’ In these ways, the *need* for the concern of audit quality has attained an almost taken for granted status such that the motivation for its continued pursuit is no longer even questioned.

Whilst failures and crises have perhaps contributed to the taken for granted need for concern, it remains so that the interest with audit quality has nonetheless over the course of this past half century steadily risen to far-reaching levels. References to audit quality in mainstream press articles provide an indication of the reach of the issue². The three key taglines on the PCAOB's current website are protecting investors, applying professionalism and *improving audit quality*. New institutional structures, within this past decade, have been formed in the name of quality, such as the Centre for Audit Quality in the US and the ICAEW's Audit Quality Forum in the UK. A central focus of the IFIAR is on providing a platform for dialogue on issues relating to audit quality³.

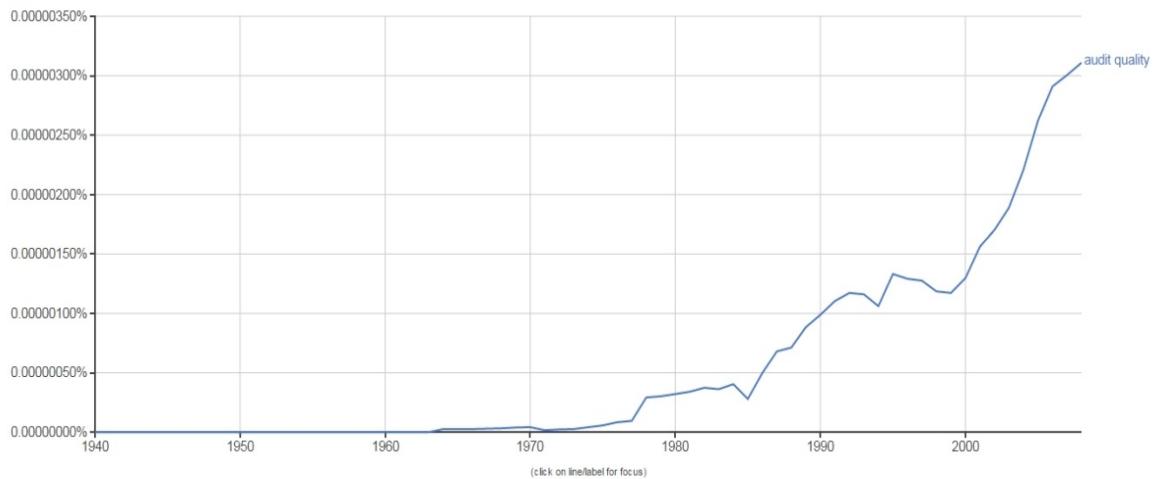
Beyond the discourse, attendant changes in the name of quality can also be seen within key domains of activity within the field. Khalifa et al (2007) analyse how the pursuit of practice change in auditing, especially in relation to audit methodologies, is being conveyed through the discourse of audit quality. Francis (2004) and Knechel et al (2012) have both provided a synthesis of the academic literature on audit quality, providing an indication of the quantum of academic research which has been generated on the subject. Few efforts in the area of contemporary audit regulation, particularly so for that which pertains to externally conducted inspections, can be seen which are *not* explicitly articulated as being related to the objective of improving audit quality in some way.

The interest in and rise of audit quality as an object of concern, within this past half century, has therefore been intense, with a breadth and depth of reach which is increasing. A Google Books Ngram Viewer graph extracted on 7 April 2016 indicatively supports this rise:

² For just one recent example, see *Accountants PwC, Deloitte, KPMG and EY face taming moves* (2014) available on www.ft.com

³ See www.ifiar.org/About-Us.aspx item number three.

Figure 1.1: Google Books Ngram Viewer chart on ‘audit quality’



Whilst the limitations of Google Books Ngram Viewer are acknowledged⁴, it nonetheless highlights the period within which the rising trend of audit quality as an object of concern can be seen and supports the observation that it has now become firmly established within the discourse. It further shows that audit quality emerges as an object of concern just prior to the mid-1960s, becoming established by approximately 1977 - 1978 and highlights the particular periods when interest has accelerated and intensified (e.g., mid 1980s and again late 1990s). Mostly, it shows an ever increasing interest with audit quality without any abatement of this concern. Viewed in isolation, the trajectory of this graph might suggest a serious issue with the efficacy of the audit currently exists, and is, despite multiple attempts at regulatory intervention, getting worse.

Yet the parallel rise in quality concerns outside of the audit field - the quality ‘explosion’ (c.f. Power, 1994) in traditionally public sectors such as healthcare (Pfluegler, 2013) and education (Ruben, 1995), the wider management for quality phenomenon (Juran, 1995), along with spheres closer to audit such as audit committee, financial reporting, earnings and disclosure quality, all suggest wider social and institutional factors in force, outside just the efficacy of the audit⁵. And whilst the most memorable of failures such as Enron in 2001 may

⁴ The parameters loaded to generate this analysis were the timeframe of 1940 – 2016, the corpus of ‘English’ (being the inclusion of books predominantly in the English language published in any country), and with a smoothing factor of 3 (the number of years’ raw data on either side of the result year which are averaged in order to generate a ‘moving average’ results graph. For example, a smoothing of 1 means that the data shown for 1950 will be an average of the raw count for 1950 plus 1 value on either side). Google Ngram Viewer only includes books within its analysis but normalises its results by the number of books published in each year (in general, this is rising).

⁵ A similar Google Books Ngram Viewer chart to Figure 1.1 run with just ‘quality’ from 1800 to 2010 indicates a rising trend which commences at the start of the 20th century. Juran himself, known widely as one of the forefathers of the total quality management movement, has even questioned

have catalysed interest in audit quality, Figure 1.1 suggests, as this thesis will continue to examine, that the start of even that particular period of intensification of the discourse *preceded* this failure, thereby challenging the commonly held view of the causal link between failures and quality concerns. Likewise, Figure 1.1 further suggests that quality had already started to permeate the audit field sometime in the early 1960s, a time which similarly preceded some of the more high profile of failures which occurred in the late 1960s and early 1970s.

Together, these observations therefore start to question the oft assumed causal relationship between failures and quality concerns. Specifically, they start to question the commonly held, and even taken for granted view, that large scale failures have served as irrefutable proof of the deficiency of the audit, and that multiple episodes of failures have only served as further evidence that this deficiency persists. However, even a cursory review of the history of auditing shows that the underlying concerns surrounding the audit are perennial, such as the ambiguity surrounding the role and objectives of an audit and the independence of auditors. And that these tensions continue to sit uncomfortably around the audit *irrespective* of, or at the very least in addition to, the failures, albeit becoming particularly heightened in times of crisis.

Whilst much of the academic research on audit quality takes a positivist, empirical archival approach, this research suggests that audit quality, particularly when viewed amongst a wider societal shift of quality concerns, cannot be thus fully understood in isolation. As Power (2003) has argued, the ‘audit quality problem’ is only in part an individual auditor judgment issue - it is also ‘a function of what gets accepted, stabilized, and institutionalized as a way of doing things’ (p. 389). He calls for a ‘deeper institutional understanding of the sources of that stability, and ideas of audit quality’ (*ibid*). With much of the extant literature on audit quality adopting a positivist approach, using observable proxies to represent and investigate audit quality, questions of this particular nature are perhaps not best suited to being addressed by such an approach. The inherently reductive nature of adopting singular proxies to stand in for audit quality implicitly denies the possibility of investigating some of the wider social, political or institutional forces which have together shaped that notion. Defining quality upfront via a proxy rules out any analysis of the social processes through which ‘quality’ may be socially defined (c.f. Atkinson, 1978 as cited in Silverman, 2015, p. 276). Holding the proxies constant also does not readily allow for the study of how the notion has come to be changed over time. Indeed, how academic conceptions of audit

whether or not, given this rise of quality, the twenty-first century will in time come to be known by historians as the ‘Century of Quality’ (Juran, 1995, p. xii).

quality itself have come to shape and influence the audit quality problem forms part of the aspirations for this research.

Given the current levels and rising intensity of concern, this research suggests that perhaps taking a new approach might be warranted. This study seeks to increase our understanding of the notion and nature of audit quality along with some of the implications and meaning of its emergence and rise, by adopting a new approach of investigation. This research also attempts to question and unpack the relationship between failures and the audit quality discourse. Before this study is positioned, however, two further matters of relevance, being some of these aforementioned underlying concerns of the audit and their shifting relationship with the audit quality discourse, are first considered.

1.1 The problems of audit (quality)

The AICPA defines the audit in terms of its overall purpose, currently specified as follows:

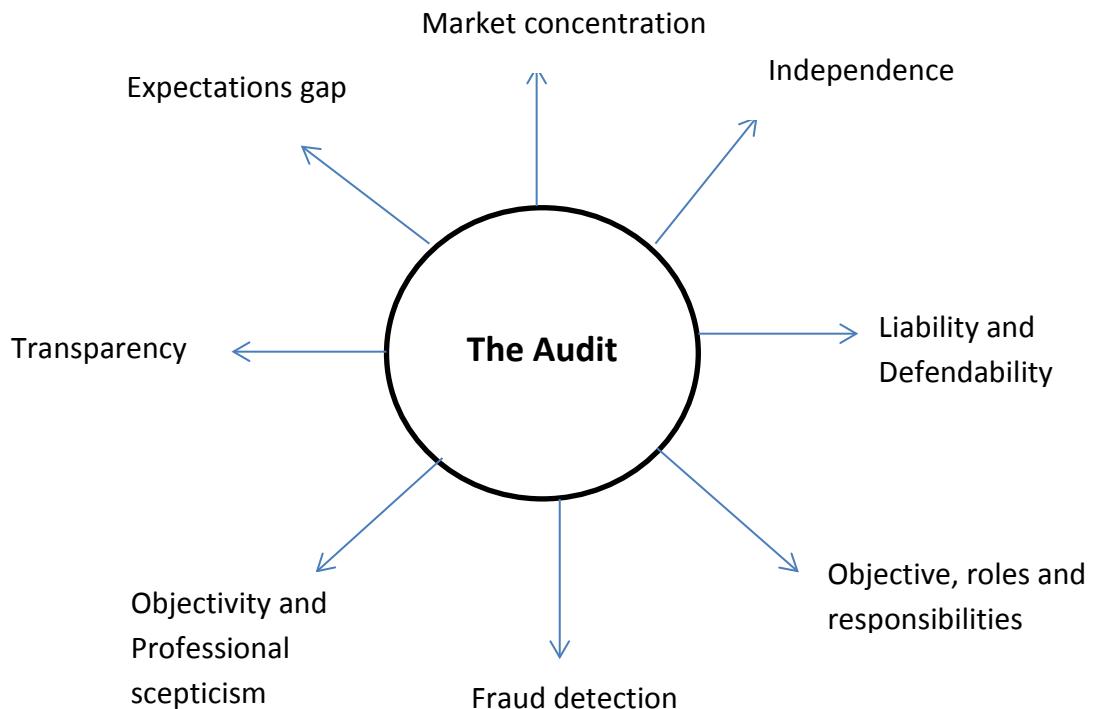
... to provide financial statement users with an opinion by the auditor on whether the financial statements are presented fairly, in all material respects, in accordance with an applicable financial reporting framework, which enhances the degree of confidence that intended users can place in the financial statements (AICPA, 2015, p. 77).

The audit is a legislative requirement, and whilst auditors act on behalf of shareholders, they are remunerated by the companies they audit. Historically, very few outputs from the audit, apart from a fairly standardised audit report are publicly available thus shrouding the entire process, at least in the public's eyes, in a veil of secrecy. Together, these two structural aspects of the audit have been, at least in part, the root of many of the ensuing difficulties. Accusations of the lack of independence, and adjacent issues such as the lack of objectivity or professional scepticism, are at least in part rooted in the inherent conflict of interest generated by the remuneration structure of the audit relationship. The commercial nature of the audit firm enterprise and historic expansions into areas such as consultancy and tax services, have exacerbated perceptions of the lack of independence. Concerns regarding the dominance of the Big N audit firms are also rooted within the potential lack of independence this concentration may come with. The unobservable nature of the audit process has contributed to the lack of understanding in what an audit actually entails. This in itself has generated a whole host of other issues such as the prevalence of an 'expectations gap' between what the public believes an audit does (or should be doing) and what it actually achieves (Porter, 1993). In part, this difference in understanding has also contributed further

to the difficulties surrounding the roles and responsibilities of auditors, especially that with respect to fraud detection. A perceived failure to meet these expectations contributes to the litigation against audit firms, in turn creating an issue for audit firms as to the defendability of its audit procedures. The lack of observability of the process also creates tensions with being able to meet satisfactorily the increasing calls for transparency of the audit and more widely in general. There are no doubt others.

These problems surrounding the audit, many of which are intricately linked, have all individually had histories of their own within the debates and discourse – some perhaps longer than others. However, despite multiple episodes of regulatory efforts, these concerns and tensions are never really ‘resolved’ to the extent that they disappear completely from the discourse. Instead, they linger uncomfortably in the background and variably come to the forefront from time to time, particularly in times of crises, perhaps becoming subsumed within another concern, or triggering new ones altogether. It is to these shifting concerns also, which have *all* at some point during the past, intriguingly become attached to the rise of audit quality discussed in the opening section which forms one of the key focuses of this study. It is not only to the questions of how and why these concerns become attached to the notion of audit quality, but also the implications, through the corresponding predisposition of specific solutions, of conceptualising quality in these very particular ways which forms part of the current study’s research interests. These opening research questions regarding the shifting nature of the audit quality ‘problem’ and more will be discussed further in section 1.3. Figure 1.2 below summarises some of these tensions which pervade the audit.

Figure 1.2: Some tensions which pervade the audit



1.2 The changing nature of the audit quality problem

Quality is an idea; it changes with time.

- Butman (1997) from *Juran: A lifetime of influence*

As Knechel et al (2012) have concluded, and as the quote at the start of this chapter also suggests, there has yet been developed a universally agreed definition of the term 'audit quality'. Whilst DeAngelo (1981) was the first to develop a definition⁶ which would 'set the benchmark' (Francis, 2004), this definition has since been superseded by challenges to the binary nature of her definition and how quality could instead be conceptualised as a continuum (*ibid*). In addition, further inroads have been made by adopting framework approaches (e.g., FRC, 2008; IAASB, 2014) which acknowledge some of the complexities and more of the interdependency of issues which drive audit quality. Notwithstanding these

⁶ The full definition is: "the market-assessed joint probability that a given auditor will both (a) discover a breach in the client's accounting system, and (b) report the breach." (DeAngelo, 1981, p. 186). This research paper specifically and the implications arising from its publication on the audit quality discourse will be examined in greater detail in chapter four.

developments, a new definition which captures these aspects has yet to be constructed. This implies underlying complexities which are yet to be ascertained.

Taking inspiration from Daston and Galison (1992), it is postulated here that part of this complexity is due to the nature, uses and meanings of audit quality not being stable over time. However, beyond just an etymological analysis of the term itself, or a general argument regarding the subjectivity of interpretation, the observation of interest here is how conceptualisations of audit quality and in particular, the ‘problem’ of audit quality, differs amongst stakeholders *and* changes over time. Whilst particular themes and concerns become central to the discourse from time to time, these concerns can variably become less pronounced, morph into new concerns, subsume others or become particularly intensified within the debates, which on the whole become heightened after moments of crisis. Beyond underlying concerns, however, further shifts are apparent as each problematization⁷ becomes stabilised. Quality takes on differing attributes and most notably changes in terms of whose property is the quality problem (i.e., the individual auditor, the audit firm or the audit services market). Together, these shifts form a new conceptualisation of the problem, which is significant as the solutions which then emerge are predicated on those conceptualisations. Attendant changes which then ensue are also not without implications.

Coupled with this observation is the significance of the wider network⁸ within which the audit quality discourse is embedded and the role of this network in contributing to this shifting discourse. In addition to the wider social movements which penetrate debates, key stakeholders, the spheres of activity in which they operate, and the relationships between them, all contribute to shaping this shifting notion of audit quality. The spheres of activity which contribute most to the audit quality discourse, and of most interest in the current study include that of regulation, audit practice and academia itself. The position of this research is that it is within the interrelationships of these networks and their interactions which together shape the notion of audit quality at different moments in time. Therefore, in order to make

⁷ The term ‘problematization’ is used generally within this thesis to refer to the process by which particular problems come to be identified and stabilised as central to audit quality. Whilst applied in a different context of examining calculative technologies and regimes, most similar to this use of the term can be found within Miller (1991) who defined it as ‘the moment at which such problems come to be identified as intrinsic to a particular calculative regime, when these difficulties come to be endowed with a wider meaning and significance than that of their deployment in particular organizations, and when an alternative technology can be appealed to as resolving these difficulties in a manner congruent with their wider perceived significance’ (p. 737).

⁸ The use of the term ‘network’ in this thesis refers not just to social networks, but to the wider interrelations between heterogeneous elements within which audit quality is embedded. This has been used elsewhere as, for example, the ‘assemblage’, the ‘complex’, the ‘apparatus’, and the ‘constellation’. This concept is central to this thesis and will be discussed in detail in chapter two. References to ‘network’ are predominantly limited to this introductory chapter until the discussion presented in chapter two, after which the term ‘constellation’ is used for the remainder of this thesis.

further inroads into its complexity, this network must also be considered and encapsulated within audit quality as opposed to its study in isolation. Audit quality has thus been positioned here as a multi-faceted notion, shaped by a genealogy of historic events, decisions, wider discourses, and linkages between them which need to be attended to in order to fully unpack its ‘contemporarily received’ meaning (Miller and O’Leary, 1987). The aspiration of unpacking quality in this way is to reveal further insights as to its taken for granted, enduring and protracted nature.

Thus, whilst it is perhaps this shifting nature of audit quality which contributes in part to the difficulty in definition, it is this shifting nature also which forms the research object for this study. Beyond just quality and its broad intersections with wider social movements (e.g., the general rise of neo-liberalism), however, at stake is the close examination of quality’s precise intersections with the social, and the mechanisms therein, with a view to ultimately furthering our understanding of accounting change. Change, it is put forward, is grounded within these dynamics.

A very high level summary of these changing conceptualisations, which also forms the three core chapters of this thesis to come, is set out below. Section 1.4 will summarise some of the main arguments within each of those chapters in further detail.

Table 1.1: Summary of changing conceptualisations of the audit quality problem

Chapter	Conceptualisation of the problem	Quality as a property of:	Solution
-	Professionalism	Individual	Ethics and training
3	Objectivity and defendability	Technique	Statistical sampling
4	Quality control	Firm	Peer review
5	Independence and competition	Market	Mandatory rotation

1.3 The research study and questions

This study examines the notion of quality within the audit field and examines how its uses, meanings, and nature, as manifested within the discourse produced by regulators, practitioners and academics, have come to change over time. By drawing upon Burchell et al’s (1985) concepts of ‘arenas’ and ‘constellations’ as the primary mode of analysis, this

study seeks to draw attention to those ideas, ideologies, and institutions (amongst others) which have intersected with underlying concerns of key stakeholder groups, influencing not only the conceptualisation of the audit quality ‘problem’ but also the means which then emerge to tackle the issue. This study aims to show that audit quality – as a problem, as a solution, as a notion constituted by the dynamics of the constellation is not stable. It reformulates in different ways, creating new patterns and forming new constellations from time to time. Specifically, this study will build upon the mode of analysis put forward by Burchell et al (1985) by examining further the constellation over time. This will be attended to through a particular focus on the co-constitutive nature of the constellation in shaping the arenas upon which it is constituted and the specific mechanisms, or linkages, which connect ideas together and attach them to the audit quality discourse.

The questions this particular focus seeks to address are many and are at different levels of inquiry. First, whilst the idea that accounting is interrelated with the social is well established and widely accepted, there are few studies which have examined the exact means by which this interrelationship occurs. Attending to the actual linkages, and the more precise nature of the linking work, which carry ideas, connect them to each another and attach these ideas to the notion of audit quality can help make inroads into understanding the mechanisms of this interrelationship. Second, whilst networks of activity can together shape social change and action, the interrelationship between different stakeholders, their own fields of activity, and the role this interrelationship has on shaping the object of interest has also not been examined. In this way, this research aspires to draw attention to the significance of networks *within* networks in shaping change and how these smaller networks, or arenas, are in themselves co-constituted or reformed within this process. The constellation, drawn centrally within this thesis, can therefore also be conceptualised as a wider network *of* networks (c.f. intertwined and multiple social networks, Padgett and Powell (2012)).

Together, these questions are examined to unpack the nature, notion and constitution of audit quality, the debates of which to date have proven intractable and persistent. By then examining some of the implications of the constellation being formed in these ways, it seeks to contribute to our understanding of how we can understand and think of audit quality – a topic of profound and resilient interest. It seeks to challenge taken for granted notions regarding quality and to also understand further the meaning and implications of its rise. This thesis will seek to show how audit quality, in one sense, has come to be primarily, and merely, a basis through which very particular sets of historically contingent concerns and practices within the audit field have come to be articulated.

Finally, notwithstanding the above, this examination of quality also seeks to draw wider contributions to theories of accounting change through the focus on the linkages and the precise nature of the linking work which take place in order for connections of ideas to stabilise and action to obtain. The theoretical and methodological approaches, alluded to above and adopted to help investigate these questions are explored in more detail in chapter two.

1.4 Thesis structure

The remainder of this thesis is structured as follows:

Chapter two, Research design: theoretical and methodological approach discusses the overarching theoretical and methodological approach taken which underpins this thesis. The research will draw upon a constructivist underpinning, followed by a genealogical approach with a data collection focus on the changing conceptualisations of the audit quality problem (and their wider contexts), as predominantly manifested within the discourse by academics, regulators and practitioners. The chapter justifies this overall approach taken along with the selection of the three key episodes within the evolution of the discourse which are examined in further detail in the following chapters. The chapter sets out the data sources examined and the data analyses performed. It presents the theoretical framework and developments being proposed which will be empirically examined further in the following chapters.

Chapter three, The pre-quality constellation of statistical sampling (mid-1940s – mid-1970s) traces some of the origins of quality ideas within the audit field in the period just prior to quality emerging as an object of concern within the discourse of practice, regulation and academia. It investigates the historically specific and contingent conditions which enabled the emergence of statistical sampling as a technique within audit practice and in so doing shows how ideas of quality were able to first become established in the audit field. This chapter seeks to develop the notion of the *emergent constellation* by attending to the key moments wherein an arena, as a particular and separate ‘field of operations’ (Burchell et al, 1985, p. 390) becomes constituted. Specifically, this chapter shows that the emergence of a more distinct academia arena around the field of auditing research became co-constituted with the advent of statistical sampling thereby introducing a dynamic element to the constellation. Further, this chapter will examine some of the key linkages, and the specific nature of the work that linking entails, upon which this dynamism is dependent. Specifically, key linkages in the form of people and documents were required in order for the very early ideas of quality, through statistics, came to be attached to the audit field. It is

through this lens which can help increase our understanding of the changing nature of audit quality. Seen this way, and as the next two chapters will continue to examine, the audit quality constellation is constantly in motion.

Chapter four, Constellation two: The emergence of quality and the rise of peer review (1970s to 1988) examines the emergence and rise of quality within the audit field, and how the confluence of events, ideologies, and wider discourses led to the problematization of ‘quality control’, which came hand in hand with a solution in the form of peer review. As in the rise of statistical sampling examined in chapter three, the advent of peer review, however, was not in itself a neutral technology and its emergence concurrently re-configured the arenas upon which the constellation is constituted. Specifically, the practice arena became reshaped as a self-regulatory model of peer review and the separation of regulatory activities from that of professional practice as a more distinct arena of operations became further reified. In this way, this chapter will empirically develop the notion of the *reformation constellation*. Furthermore, the key linkages and the nature of the linking work upon which the advent of peer review was dependent are again examined. Within this episode, a further emergent constellation nested within this wider one became formulated through the emergence of audit quality within the academia arena. The conditions which led to this emergence are also examined.

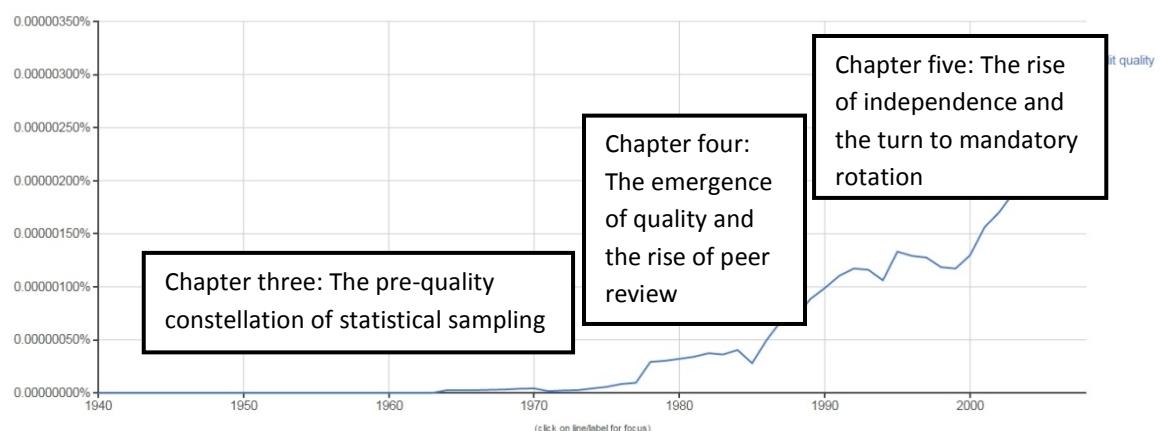
Thereafter, this chapter identifies some of the key transformations which occurred with the quality discourse within this period – most notably that of the making of its visibility within each of the three arenas, albeit in different ways, and its transformation from a property of the individual auditor to that of the firm. This chapter will examine how the making of the visibility of quality was a critical turn within each of the arenas, enabling the discourse to intensify. Consideration will be given to the relationship between this ‘empirical reductionism’ (Fogarty, 1996, p. 252) across the arenas, and the underlying quality which it purports to represent.

Chapter five, Constellation three: The rise of independence and the turn to mandatory rotation (1990s – 2014) traces the intensification of independence concerns within the audit quality discourse, from the 1990s onwards. The chapter examines how the ideology of the free markets, the stability of the capital markets, further crises and failures and the EU single markets project converged to problematize a lack of competition within the audit firm market which became particularly pronounced within the EU and the UK from the 2000s onwards. The combined and interlinked concerns of independence and competition

manifested itself into an investigation by the UK Competition Commission⁹ of audit firm market structure which resulted in the legislation of mandatory audit firm rotation in the UK, paralleling EU legislation of the same. This chapter again traces the linkages which were required in order to connect disparate ideas to that of audit quality and develops a further argument that a chain of linkages is required in order for successful action to obtain. Within this chapter, quality transforms once again – this time, into a property of the market and its underlying ideals.

Chapters three, four and five serve as the substantive chapters to this thesis and whilst somewhat overlapping are nonetheless relatively discrete episodes within the development of the quality discourse. Mapped onto Figure 1.1, the approximately timelines of these chapters follow the trajectory of the rise of audit quality in this way:

Figure 1.3: Map of substantive chapters overlaid onto Figure 1.1



Chapter six, The changing constellations of audit quality is the concluding chapter of this thesis. The chapter looks across the three preceding chapters and assesses the significance of some of the key shifts which have occurred with quality over the course of this history. It summarises the changing constellations and assesses what this analysis has informed us in terms of our understanding of accounting change, audit quality itself and the interrelationship between the arenas. It provides one interpretation of the meaning and importance of this emergence and rise of audit quality. It presents some of the key contributions, limitations and avenues for future research, along with some concluding remarks for the thesis.

⁹ Renamed the Competition and Market Authority ('CMA') following its merger with the Office of Fair Trading on 1 April 2014.

Chapter two

Research design: theoretical and methodological approach

2.0 Overarching approach

This research draws upon two well established and complementary research traditions. First, it adopts an overarching constructivist approach, drawing upon Hacking (1999) and others. Here, the underlying premise is one which focuses on the understanding of specific objects as the ‘product of historical events, social forces and ideology’ (Hacking, 1999, p. 2). Within such an approach, the premise is that the meanings of specific objects are neither fixed and inevitable, nor a product of nature. The ideas, classifications, concepts and goals used in everyday life are shaped and not found (Rorty, 1986 as cited in Young, 1996) and Young (1996) goes on to highlight the liberating potential to think of questions which might otherwise remain unthought of within such an approach. This approach also enables us, additionally, to pay closer attention to the construction process itself. With a constant object of inquiry over a timespan of over 50 years, the opportunity exists to study not only how notions of audit quality are constructed, but then also the means by which they are continuously re-constructed over time. This makes it particularly helpful in attempting to unpack notions, such as audit quality presently, which may have assumed elements of a taken for granted nature (see chapter one), where the discourse is profoundly resilient, and where meanings are also not necessarily stable over time. The construction process itself, whilst historically contingent, may also take on different forms. Attending to the specific ways which distinguishes these forms over time, such as the key mechanisms by which ideas are connected to the notion of audit quality, is one of the aims of this research.

Building on this overarching approach, this research also draws upon the ‘new accounting history’ (Miller et al, 1991) by adopting a genealogy of calculation approach (Miller and Napier, 1993). Within this approach, the focus is on ‘the outcomes of the past, rather than looking for the origins of the present.’ (p. 632). In particular, the approach helps ‘draw attention to the different meanings that have been attached to practices at different moments in time, rather than taking contemporary practices and the meanings currently attached to them as historical constants’ (*ibid*). The focus of this approach therefore makes it particularly well suited for and aligned to a study of changing meanings.

In performing a genealogy of calculation, Miller and Napier (1993) further demarcate three areas of particular emphases which distinguish this approach from traditional histories. It is put forward that all of these, being the focuses on the historical contingency of contemporary practices, the discursive nature of calculation and finally the ensembles of practices and

rationales that are assembled at collective levels are particularly useful for this study. The emphasis on the historical contingency of contemporary practices is helpful in challenging the apparent inevitability of practices as neither necessary nor self-evident. For example, whilst the contemporary discourse of audit quality, centred on mandatory rotation, has come to be inextricably linked to a problematization of the lack of competition within the audit market, adopting a genealogical approach reminds us of the historical contingency of such contemporary meanings thereby helping us to unpack this relationship as a given. In so doing, we are thus able to start making inroads into a notion and a debate which has proved intractable.

This focus on the discursive nature of calculation, being the language and vocabulary and the ways in which meaning and significance are attributed to a particular practice, is helpful in ascertaining the underlying ideals and rationales which have become implicated within the audit quality debates. These allow not just the emergence of solutions to particular problems but also for these solutions to become established. Paying careful attention to the ways in which the discourse is articulated can reveal these underlying ideals, rationales and programmatic (Miller and Rose, 1990) ambitions which underscore the discourse. This, in turn, allows us to trace the key connections which become constructed within each step of the process.

Adopting a genealogical approach also encourages a third focus - on the means which enable meanings to be assembled at collective levels, for specific issues to be linked to larger questions and for practices to come together in a complex web. Miller and Napier (1993, p. 634) point to a number of examples of such mechanisms which are necessarily historically localized, however, it is the focus on the specific mechanisms of linkages – those people and documents that make concrete the connection of different ideas and attach them to the quality discourse, which is of central relevance to this study. In unpacking the changing meanings of audit quality, attention needs to be placed on those mechanisms which allow for ideas to be disseminated and reformulated at a collective level – through mediums such as textbooks, practitioner manuals, professional publications and journals, governmental inquiries, symposiums, academic discourse itself, and much else which bridge conventionally quite separate domains of activity such as academia and practice. It is within mediums such as these, in addition to key actors, where the transmission and linkage of underlying ideas occur, become stabilised and from which in turn emerges a collective assembled meaning. Within this research, the focus will specifically be on the people and documents linkages which carry and connect disparate ideas to audit quality, and the precise nature of the linking work which is required in order for those collective assembled meanings to emerge. This provides an added level of analysis to the construction process.

Finally, this research will focus specifically on the conceptions and ideas which have come to intersect with world events, underlying ideologies, changing societal expectations, and much else which together shape both the conceptualisation of the audit quality ‘problem’ and hence also the solution to that problem. The focus on conceptualisations is warranted due to action, at a distance (Miller, 1991) or otherwise, being premised upon how problems are conceived. Conceptualisations, like ideas, do not ‘exist in a vacuum’ and inhabit a social setting (Hacking, 1999, p. 10) thereby presenting itself as a research object which necessarily spans the wider contexts, or the ‘social’. Studying audit quality, as a conceptualisation and as an idea in itself, is also consistent with a constructivist stance. Further, conceptualisations of the problem also directly shape the solutions which emerge, which in turn have differing implications. In short, conceptualisations are enabling and prior to any evaluation of their consequences should be the study of their origins.

The overarching approach for this research can therefore be summarised as follows: a constructivist study utilising a genealogical approach with a central data collection focus of the underlying concerns and influences which have underscored the shifting conceptualisations of audit quality. Further methodological considerations will be discussed in section 2.3. Section 2.1 next presents the theoretical framework adopted within this research. Section 2.2 which follows thereafter will present the theoretical developments being proposed within this thesis.

2.1 Theoretical framing: the constellation

In Burchell et al’s (1985) seminal study of accounting change, they developed a ‘conceptual and historic analytic’ (Robson, 1991, p. 549) in order to facilitate a more systematic analysis of the relationship between accounting and the social. Their research object was the social space within which the value added event in the UK took place. Their model consisted of three arenas, constructed for purposes of illustration and analysis, each marking out a particular field of operations, and defined as ‘complexes of issues, institutions, bodies of knowledge, practices and actions’ (Burchell et al, 1985, p. 390). Within each of these arenas was then traced the shifting patterns of relations between the various actors, their interest in economic calculation and in value added reporting in particular. The tracing of the movements within each arena, largely independently, further enabled the authors to potentially recognise the arenas’ autonomies and interdependencies (p. 391). It also opened up for examination how seemingly disparate issues such as economic performance and calculation, and the status of employees and trade unions came to be connected. This approach is consistent with a constructivist stance and allows for a more systematic analysis

by eliminating any a priori assumptions regarding such connections. It also positions accounting and the environment, or the social, at the same 'level' of analysis by not assuming any directionality of influence.

By looking then at these interrelations and at the 'network of intersecting practices, processes and institutions' which gave rise to the value added event, Burchell et al (1985) further advance their notion of the 'accounting constellation'. Specifically, they defined this as the 'very particular field of operations which existed between certain institutions, economic and administrative processes, bodies of knowledge, systems of norm and measurement, and classification techniques' (ibid, p. 400). It is within this constellation which they argue gave rise to the pre-conditions which enabled the value added event to take place. A key argument is that the constellation is an unintended and contingent phenomenon, resulting from a multitude of different actors acting in purposive ways in an array of different arenas, within different systems, processes and networks. Of key importance is the relational dynamics of the constellation.

Using the constellation as the analytical and theoretical approach is particularly useful for this study for a number of reasons. First, the constellation helps to position audit quality at the intersection of the relations between an array of different concerns, ideologies, wider discourses, institutions, actors and much else besides. This in itself highlights the historically constructed and contingent nature of audit quality which in turn allows for a more systematic analysis of the elements constitutive of it. Second, it aids the identification of the conditions of possibility which have enabled the rise (and change) of particular issues within the discourse, thereby helping to unpack any connections which may have become taken for granted over time. Audit quality has, over the years, become steadfastly linked with a number of different issues and themes including peer review, independence, market structure and competition. Notwithstanding the questions regarding how and why these *particular* connections come to be made and then change over time, the common view asserts that high profile failures are sufficiently evident of market failure to justify increasing regulatory intervention. However, irrespective of how one conceptualises failure, it remains so that the number of outright audit failures have been few and far between (Francis, 2004). Using the constellation helps to unpack some of these connections through its explicit recognition that disparate ideas can intersect with accounting (here, auditing) in many varied ways – *over and beyond* audit failures. A framework which incorporates the study of these connections and intersections allows for the potential to examine those specific intersections in more detail. Third, using the constellation, and the arenas upon which it is constituted, enables an identification and focus on both the autonomies and interdependencies of the separate arenas within the constellation, as noted by Burchell et al (1985). The means by

which ideas and conceptions are ‘objectified’ are made and not natural. And they are not solely in the hands of actors. They rely on mechanisms to connect ideas either within the constellation itself or with wider discourses – the linkages being developed further in this thesis (see section 2.2). Adopting an analytical tool which focuses attention and enables the study of these connections is helpful as it is within these linkages where it is put forward that constitution and re-constitution occurs. Through this, and the identification of those relations which are predominantly within the arenas (autonomies) and those which connect to others (interdependencies), the interrelationships between the arenas may potentially also be unpacked. Finally, to be discussed in more detail in section 2.2, this research seeks to develop further the relationship itself between the arenas and the constellation, and to investigate its role in shifting the constellation through time, as a means of reconceptualising the constellation as being more dynamic. Therefore, adopting the constellation and its attendant arenas as the theoretical and conceptual analytic seems most appropriate for this objective.

A number of other notions which are very similar to the constellation have also been developed more widely and applied specifically within the accounting literature. These include the notions of the ‘assemblage’, the ‘network’ and the ‘accounting complex’¹⁰. The notion of the accounting complex and the assemblage itself were referred to by Miller (1991) in his study of the rise of discounted cash flow accounting. Miller explains how the notion of the ‘accounting complex’ appeals to ‘the temporary and often fragile stability established between an *assemblage* of diverse activities, professional associations, institutions and conceptual schema’ (p. 736, emphasis added), highlighting the significance of the relations and intersections between the array of heterogeneous elements which are required in order to achieve a temporary stability of meaning. This focus is also adopted within the constellation, although the integration of the concept of the arena within the constellation is an important element for this current study.

The concept of the network, most famously employed by actor-network theory (Callon et al, 1986; Latour, 1986) is referred to as being constituted by ‘an interrelated set of heterogeneous entities which have been enrolled, juxtaposed and linked to each other by an

¹⁰ Many of these concepts had their roots in or have been adapted from Foucault’s notion of the ‘dispositif’. In his 1977 “The Confession of the Flesh” interview, Foucault answers the question, “What is the meaning or methodological function for you of this term, *apparatus (dispositif)*?” as follows: “What I’m trying to pick out with this term is, firstly, a thoroughly heterogeneous ensemble consisting of discourses, institutions, architectural forms, regulatory decisions, laws, administrative measures, scientific statements, philosophical, moral and philanthropic propositions—in short, the said as much as the unsaid. Such are the elements of the apparatus. The apparatus itself is the system of relations that can be established between these elements” (Foucault, 1977, p. 194).

actor or a group of actors' (Callon, 1986, p. xvi, also cited by Mennicken, 2005). A key distinguishing element with the network is that these entities may be human or non-human. As Justesen and Mouritsen (2011) have also commented, the constellation and the actor-network bear a close resemblance to each other in that both concepts 'allude to the idea of the linkages of heterogeneous effects as a particular outcome of complex, historical processes' (p. 168). With the accounting complex, Miller and Power (2013) also acknowledge its similarity to the network in that they are both relational. The difference lies in the 'atomistic elements' – where these tend to be similar in the network, the complex contains very different components which are 'co-constructed rather than given, or taken as pre-existing in the organizational environment (p. 589)'. Miller and Power (2013) further draw on the image of the 'mutually contingent position of accounting in organizations and capital markets, understood as a space of actors and ideas' (ibid) to further clarify the notion of the accounting complex. In sum, all of these concepts are similar to the extent that 'outcomes', or temporarily stabilised sets of relations, are premised upon a complex web of historical relations which are formed between heterogeneous elements of that web. Central to this complex interplay, however, are the actual linkages - between relations, ideas, actors, institutions, technologies which become formed and stabilised. It is to these linkages, not always empirically explored, which this thesis seeks to examine further.

A problematic common to all of these concepts is an issue of boundaries. As Miller and Power (2013) also highlight: 'The boundaries of a complex are also necessarily contentious...which relations are important in a complex; what is central and what is marginal?' (p. 589). However, despite this difficulty, the authors remain convinced that the conceptualisation of the complex can still be fruitful for it opens up for examination the 'how and why accounting practices change...and how they in turn shape institutional outcomes' (p. 588). In this way, the complex is particularly similar to the notion of the constellation. To the question of boundaries, it is put forward here that a further problematic common to these notions exists with regard to the degree of 'boundedness'¹¹ between actors, institutions, ideas and the relations in between, *within* the assemblage, network or complex. Put another way, it is not only *which* relations that should be 'counted' which poses methodological questions. The *nature* of the relations between these key elements

¹¹ This point bears resemblance to Abbott's (2005) concept of ligation which he defines as the relational process between actors, locations and the relation associating the one with the other (p. 248). (Abbott uses this term to distinguish between his use of the concept of linkages, which refers exclusively to connections between ecologies, as opposed to within). Whilst ligation also refers to the relations *within* an ecology, the point on boundedness made above differs in that it is drawing attention to the formation process of relations within an arena. Relations within a constellation are not always uniform and some will become more tightly held, upon which the arena is dependent, than others.

themselves is also not necessarily uniform, and these differences are also important to acknowledge. To the extent that a group of sub-relations, the networks within the constellation network, within each of these notions become more tightly connected through the nature or quantum of relations, or become more formally bounded together by institutional structures such that they can be seen and defined as a distinct field of operations, constellation analysis becomes additionally helpful as it incorporates and is dependent on the concept of the arena (seen here as a network within the constellation network). This allows one to make inroads into the significance of these differing relations and arenas, the interrelationship and linkages between and within the arenas, their effect on the constellation and hence, our understanding of the nature of change and the underlying research object of study.

Accordingly, and notwithstanding the similarities, the constellation has been utilised within this research as the conceptual underpinning as the notion best aligns with and enables a focus on those aspects which are most closely being examined in this research. These include the conditions leading to emergent or differentiating arenas, the inter-arena relationships, the role of linkages which connect and stabilise ideas, and the relationship itself between the arena and the constellation. On this final point, this research will show that it is the mutually constitutive aspect of this relationship, underpinned by linkages, which gives the constellation the dynamism that contributes to accounting change. This argument will be developed further in section 2.2. For now, the concept of the arena itself needs further consideration and this is reflected upon next.

2.1.1 The arenas

Burchell et al's (1985) model consisted of three arenas, constructed for purposes of illustration and analysis, each marking out a particular 'field of operations'. The arena was defined as 'complexes of issues, institutions, bodies of knowledge, practices and actions' (Burchell et al, 1985, p. 390). Robson (1991), as one of the earlier researchers to draw upon the sociology of translation (Callon, 1986; Latour, 1987) within accounting studies (see also Miller 1991), extended the notion of the arena by arguing that the concept of the arena is dependent upon a process of translation. Translation, a central concept in the examination of change, is referred to by Latour (1987) as 'the interpretation given by the fact-builders of their interests and that of the people they enrol' (p. 109). In general terms, it refers to how ideas are discursively transformed into facts through a series of interpretations by human actors who interpret those ideas according to their own interests. This notion of translation and its positioning within this research will be discussed further in section 2.2.

The three arenas of interest identified for this study are broadly the key sub-fields of the audit field which engages most actively and produces the most discourse on the issue of audit quality. These are the regulatory arena which include all actors, organizations and activities concerned with the rules of governance of the audit profession (self-regulatory or otherwise), the practice arena being those actors and firms and professional institutes concerned primarily with the delivery of services to clients and finally, the academia arena concerned with producing academic research on audit or audit quality research specifically. Whilst these arenas do not constitute the entire audit quality field – it is suggested that the public interest may at least in part be subsumed within regulatory discourse, and clients' interests would be part catered for by the audit firms (practice), the working assumption is that a meaningful extent of key debates and underlying concerns will either be directly or indirectly captured within, and by the development of, the separate arenas of regulation, practice and academia.

This categorization is far from being unproblematic and this is acknowledged. The boundaries of these arenas are by no means clearly delineated, particularly for a profession which has spent the majority of its history under self-regulation. This causes difficulties with determining what constitutes either practice or regulatory activity and concern. The actors themselves within each of these arenas may very well engage in activities which cross over arenas and this in itself may also change over time. Practitioners who engage in 'academic' activities such as teaching are not uncommon within the audit field. Publications, seen as one means in this research of observing the underlying ideas and concerns of key stakeholder groups, may be directed to audiences in more than one arena. As Miller (1991) has also noted, albeit in a more general setting, it has become increasingly difficult since the Second World War to apply a binary categorization of practitioners versus academics and to see them as mutually exclusive categories (p. 735). To further compound these issues, this research attempts to ambitiously add a third arena of regulation as one which engages with and produces much of the discourse on audit quality.

Notwithstanding these difficulties with boundaries, this research suggests that retaining this very broad categorization rooted within a common understanding of these terms and the types of *activities* (as opposed to just the actors) they undertake can still be fruitful for analysis. It allows one to start making inroads into the interrelationships between the arenas and also the investigation of the conditions leading to arena formation or differentiation, which in turn opens up the possibility of examining the internal dynamics of the constellation. Indeed, how the boundaries of the arenas themselves become formed, or shift from time to time, is also an empirical and theoretical matter for consideration.

To essentially sidestep the issue of defining the boundaries of these arenas, the working definition for purposes of this research, and for data collection purposes, will gravitate towards those activities, and the documentary manifestations of those activities, which are most ‘commonly’ understood to be included within the arenas. In addition, the focus will be, as far as possible, retained on the central areas of concern for each arena throughout this history. For academia, this will include academic research publications in research journals. For regulation, this will include regulatory commissions, investigations, policy documentation carried out by those, or on behalf of those, actors or institutions with the legislative authority to govern audit practice. This will include professional institute policies and professional standards released for self-regulatory purposes. For practice, this will include trade publications, practice manuals and in-house publications released by audit firms. In analysing this data, to be discussed further in section 2.3, the working delineation applied was the arena to which the context mostly aligned¹², at least as the initial organising principle.

However, beyond just a research opportunity generated by the availability of discourse, it is suggested here that the arenas of regulation, practice and academia and specifically their interrelationships are in themselves intrinsically of interest – and all the more so as it applies to the debates surrounding audit quality. As Humphrey et al (2011) have noted, despite escalating efforts to regulate audit quality, the relationship between regulation and audit quality (i.e., practice), has never actually been established. Whilst academics participate from time to time in regulatory debates, little is understood about the role academic research plays in influencing these debates or indeed how academic research is ‘consumed’, if at all. Whilst audit research within its wider social and institutional contexts is flourishing, there remains a paucity of research on actual practice thereby suggesting still little engagement between practitioners and academics. Indeed, one concern is perhaps the perceived gap in relevance of academic research to practice. Empirical archival research in the area of audit quality in particular has proliferated, but little of this research utilises actual insights from practice. This observation is consistent with Lee’s (1990) study of the academic accounting research profession and its gradual decoupling from its education-practice roots. Whilst one view may be that academia enjoys a privileged, ‘outside’ position of objectivity and independence, including academia as one of the three arenas collapses this assumption and answers calls from Çalışkan and Callon to include within research designs the impact of academic research itself on the research object of study (Çalışkan and Callon, 2009a, p. 370 - 371). This opens up the potential to also examine the role academia plays in constructing

¹² The subjectivity in this assessment is acknowledged although in actually performing the data collection and analyses, this delineation was in the main readily apparent.

the discourse of its own research objects as one step towards increasing our understanding therein. This ‘equalises’ their position within the discourse and allows us to start examining their influence and the process by which this influence is achieved. The general relationship between academia *and* regulation *with* practice also bears consideration not least because practice is so often the target of research and regulatory efforts. Tracing the constellation through time may provide further elucidations on their interrelationships.

Rather than re-formulating the constellation with unique arenas each time, this thesis will adapt Burchell et al’s (1985) mode of analysis by holding constant the *categorisation* of these three arenas, which will be examined through time in order to capture the interactions which formulate different constellations. The pre-determined nature of these categorisations is not inconsistent with Burchell et al’s (1985) model, for their arenas were also so specified in advance. The authors acknowledged that ‘no doubt arenas other than the ones that we have outlined could be constructed’ (p. 390) pointing towards a rather stylized account of their case study. The arenas put forward for analysis in this chapter have similarly been pre-determined, in the sense of their broad categorisation. However, a question may arise as to whether the holding of these categorisations of arenas constant throughout the examination of multiple constellations compromises the specificity of any one particular constellation in any way.

Burchell et al’s (1985) model was developed to shed ‘descriptive and analytical light on the processes of accounting change’ (p. 390). Their problematic was the accounting and its relationship with the social which decades of research have since investigated. The extension being developed in this thesis is to further show how the constellation mobilises through time, and to further elaborate on the emergence and differentiation of the arenas along with some of the key mechanisms which link and stabilise ideas. Studying how the same broad categorisation of arenas interrelate at different points in time can help in this extension through not least the identification of differences over time and building the bases for comparative analysis. In any event, it is put forward that holding the categorisation of the arenas constant does not hinder the specificity of the constellation as the arenas so specified are also the key producers of the discourse being studied, aligning with the research object of interest.

A final question for consideration is whether or not the concept of the arena is a purely analytical construct or if it is ontological. The position adopted within this research is that they are both, or are at the very least variable ontological objects (Kurunmäki and Miller, 2013; Latour, 1991). The arena has been construed here as specific domains of operations characterised by their particularly close ties and institutional structures which render it

visible as a distinct sphere of activity. These arenas are analytical in the sense that they are defined by the interrelations of heterogeneous elements without clear and defined boundaries. However, they are also decisively real in that audit practice, regulation and academia are all resolutely active fields of real operations which conduct audits, write standards, carry out inspections and publish academic articles. The titles of the arenas of practice, regulation and academia are fully intended to denote these realms of activity to which these names infer. In one sense, it is the stabilisation process of the arena and the transition (variability) to a real field of operations, through the close interrelations and institutional structures which become formed, which is also being examined in this thesis.

The same question might also be asked of the constellation itself, and whether or not this is purely metaphorical or ontological. Again, despite the less obvious ontological activities upon which to refer, the position of this research is that they are both. They are metaphorical in the sense of providing a theoretical framework through which to analyse and make visible the pre-conditions leading to particular conceptions of audit quality, but to the extent that these constructions gain ‘strength’ such that connections become stabilised, the more real the constellation becomes. The network of interrelations which then represent and constitute the final constellation are very real relations indeed.

In sum, drawing upon the concepts of the arena and constellation theoretically, this thesis will seek to better understand the means by which the uses, meanings and nature of audit quality shifts over time. As our *conceptual starting point only*, audit quality is being positioned as an object which is shaped and constituted by the interrelations of the arenas and of the constellation, initially premised on, and to be built upon, Burchell et al’s (1985) model as follows:

Figure 2.1: Initial conceptual framework of the audit quality constellation adopted in this study



In so doing, it aspires to unravel some of the complexities surrounding the longstanding, escalating and resilient discourse on audit quality. It seeks also to contribute to the notion of the constellation, as a means of understanding accounting change, by identifying the key mechanisms of linkages by which the constellation becomes continuously constituted, and re-constituted, over time. Put another way, to be investigated are some of the dynamics which will enable the above diagram to move through time. And hence, also how it will move through time. It is to these developments which we now turn.

2.2 Theoretical developments

Burchell et al's (1985) model was particularly helpful in making inroads into how one might be able to conceptualise the relationship between the social (i.e., the environment) and accounting. In devising a model which drew attention to how the value added event arose out of a 'complex interplay of institutions, issues and processes', it provided one means by which to study accounting within the contexts in which it operates (Hopwood, 1983). Their stated aim of the paper, in rejecting extant theories of change, was to ultimately shed 'descriptive and analytical light on the processes of accounting change' (p. 390).

The proposition being put forward within this thesis is that whilst the constellation may not be a static concept, the current model of the constellation as being constitutive of the three arenas does not adequately model *how* it is dynamic. Moreover, whilst the intersections between different domains of relations of the constellation are implied, the means by which these are made concrete are not actually identified nor made explicit. As mentioned earlier, central to these notions of the complex, assemblage, network and indeed the constellation is the idea of the *linkage* of heterogeneous elements. However, these are not often explored and taken as implicit within these notions. The mechanisms by which these different elements and ideas, in Burchell et al's (1985) case of the social to accounting, are established and become stabilised, are not made apparent within the current constellation model. Whilst Burchell et al (1985) highlight the role of accounting in 'providing the conditions of existence of certain social relations' (p. 402) and how accounting 'is intimately implicated in the construction and facilitation of the contexts in which it operates' (ibid), we know little about the actual intersections of ideas or elements, or the precise moments whereby accounting intersected with the social which enabled the value added event to arise in the form in which it did. Moreover, as the constellation was applied to unpack the pre-conditions leading to a uniquely singular event in time, little is known about how the

constellation then becomes continuously re-made through time. And what this could then inform us about accounting change.¹³

This thesis argues that the notion of the constellation should be reconceptualised more dynamically whereby the arenas and the constellation are mutually constitutive. Not only do the interrelations within and between the arenas give rise to the constellation, the emergence of the constellation concurrently reconstitutes the arenas upon which the constellation is based. This thesis further argues that there are two ways in which a constellation can be conceptualised as being dynamic. The dynamism can take the form of either '*emergent*' or '*reformation*' constellations. Emergent constellations occur when an altogether new field of operations becomes formulated through the emergence of a new event or object, triggering a new arena of activity. The emergence of a new academic arena engaged in auditing research through the advent of statistical sampling in the 1960s is one example, to be examined in chapter three. The second type of dynamic constellation is labelled a '*reformation*' constellation whereby an existing field of operations becomes further delineated or differentiated as a separate arena of operations. The separation of regulatory activities from that of professional practice through the advent of peer review is the example to be investigated in chapter four.

Furthermore, it is also put forward that the constellation, and hence dynamism, is dependent upon key linkages becoming established which harden the connections between disparate ideas and connect them to quality. These connections of ideas need to be crystallised through a carrier – the notion of *linkages* within this thesis, which tend to take on either the form of people or documents. Ideas in themselves can also have a connecting capacity but these would then in turn still need to be carried by one of either people or documents in order to become established and stabilised. World events, most notably crises, also have a connecting capacity through the temporary alignment of interests of the arenas. However, once interests have been aligned, again, any connection of ideas would then need to be embodied through one of either people or documents. Whilst these two media are not purported to be comprehensive, it attempts to capture the key forms of linkages of most relevance to this current study.

Additionally, this thesis posits that merely the existence or formation of such linkages is not sufficient for successful action. A sequence of linkages, connected by the commonality of

¹³ Burchell et al (1985) explicitly state that they have not in their analysis 'suggested or discovered any general theory of accounting change' (p. 402). This, it is put forward, is due to their mode of analysis being focused primarily on the preconditions which enabled or constrained specific innovations to take place and not, as this current thesis aspires, on the more detailed and precise intersections upon which change is grounded (see section 2.2.1).

the underlying ideas of each linkage, is also required in order to successfully evolve technique or regulation. In other words, a chain of linkages is required. An example of this is how ideas of concentration and competition within the audit market were first raised in 1976 by the Metcalfe Commission in the US but it was not until some 40 years later, in the EU, where it became legislated as a regulatory measure. The ideas did not generate sufficient support, or interest, at the time and no further linkages were formed to take the ideas forward. In addition to the historically contingent circumstances several decades later which were required to enable further linkages to form, the linkages themselves needed to be connected in some way in order to form the chain required for successful action. This will be developed empirically in chapter five.

This notion of linkages and the precise nature of the linking work which is entailed, both of which are being empirically investigated in the next three chapters, are of central importance to this study and are considered further below.

2.2.1 Conceptualisation of linkages and their role in accounting change

As alluded to earlier, central to the concepts of the network, complex, assemblage and indeed the constellation is the idea of a temporary stability achieved through intersecting relations. These intersections, however, are not often examined in empirical detail and are implied within these notions. In Burchell et al (1985), the precise nature of the intersections between the network of relations or of the specific ideas which became attached to value added reporting are not explicitly investigated – they are taken as implicit through a sweeping inclusion of any such intersections within the totality of the domain of relations which constituted the constellation. Robson (1991) also noted this gap in commenting that ‘the processes through which accounting and the social are interrelated remain relatively underdeveloped’ (p. 550).

It is precisely some of these intersections, and in particular those which bring together underlying ideas, which this thesis seeks to examine further. As mentioned earlier, the linkages being deployed within this thesis work to bring together disparate ideas and connect them to the quality discourse. And whilst ideas may be co-constitutive or co-constituting in and amongst themselves, of interest here is that precise moment whereby two ideas become linked, and locked, together. As opposed to just a general meaning of ‘connecting together’, linkages within this thesis have a precise meaning. Linkages within this thesis refer to those actual people or documents which embody the connections of particular ideas to quality, and in so doing, harden the connections between those ideas. The argument being put forward is that it is within these mechanisms, over and above just the identification of linkages which are in themselves co-constituted, whereby the micro-processes of linking become

established, paving the way for reform and from which change is ultimately grounded. Hence, studying these mechanisms and the precise nature of the linking work entailed can therefore help inform our understanding of accounting change.

The concept of linking more generally, and in particular the linking capacity of accounting, has also been considered elsewhere albeit in different contexts. In Miller's work on the interrelationship between accounting and the state (1990) and the rise of discounted cash flows (1991), the underlying focus was on the constitutive role, and hence also a linking capacity, of accounting technologies themselves. Robson (1991) developed further the interrelationship between accounting and the social by drawing upon the notion of translation (Latour, 1987) and its role in contributing to accounting change. Here, Robson developed the notion of translation as the process by which pre-existing accounting techniques come to be discursively articulated in ways that construct an individual or a group's interests in those techniques, thereby providing the motivation for accounting change. (p. 550).

The concept of translation (Latour, 1987) is related to the linkages being examined in this study in that they both tend to the question of how ideas become stabilised or objectified as 'facts'. They are also both being used to support the examination of accounting change. In general terms, translation refers to how ideas are discursively transformed into facts through a series of interpretations by human actors who interpret those ideas according to their own interests. It also focuses attention on the work which is required to happen in order for ideas to become operationalised as facts¹⁴. The concept is helpful in examinations of change as it helps to make visible the transformations which occur along the way. The linkages being examined in this study, however, differ in that they focus in particular on how different ideas become connected together and attached to the notion of quality. It does not centrally emphasize the role of interests within this process and is not being conceptualised as an internal transformation based on re-interpretation. Instead, the linkages being studied focuses on the connection of at least two, disparate ideas. Whilst interests play a role in providing the environment for change, it is put forward that this may not be the only pre-condition or means by which ideas become connected and stabilised. The linkages in this

¹⁴ Gendron and Baker (2005) developed this approach further in their study of the development of interdisciplinary networks within accounting research by incorporating a related concept of how ideas travel across disciplines (Czarniawska and Joerges, 1996) and how the focus should be on processes of attention – 'where an objectified idea catches the attention of some people at a given place/moment' (p. 534). This is an added embellishment, still premised upon the idea of translation. In addition, Czarniawska and Joerges highlight the role the mass media plays in constructing problems in society that demand attention. This concept is also of particular relevance in this research given the nature of the high profile failures which have plagued the accounting profession, although neither of these two areas is being centrally focused on within this thesis.

study also tend to be actual things, or media which carry and connect ideas, whilst translation is normally thought of as a ‘process’. Napier (2006) provides clarification of the notion of translation and its linking capacity:

“Translation” provides a way of conceptualizing the “movement” between different persons and places, whereby ideas and practices emerging in one context may be reinterpreted in an apparently different context, until the linkage can appear self-evident rather than merely contingent (p. 461).

The linking *capacity* of translation should not, however, be confused with the use of linkages in this study, the mechanism of which is being empirically unpacked in further detail.

In addition to this, this thesis argues that a sequence of linkages is needed in order for successful action to occur. Successful action is defined as the evolution of a new technique or regulation which constitutes the final embodiment of the ideas being connected together and strengthened through the sequence of linkages. Czarniawska and Joerges (1996) conceptualisation of the ‘travels of ideas’ also argue that there needs to be a sequence for change to occur, although theirs is one premised upon a sequence of, once again, translations. Their focus is on the overall *process* of how ideas transform into action whereas the key emphasis here is on the detailed, micro-level type of linking work which is involved at each link of the chain. Put another way, even translations can take on many different forms (discussed further below). The focus and level of analysis here is therefore at the more granular level of how individual ideas are connected, the premise being yet again that these are the earliest moments where change starts to become mobilised.

The chain currently being conceptualised is formed through the individual linkages themselves being connected to at least another previous linkage through a commonality of underlying ideas. At least one of the underlying ideas being connected in the linkages needs to be in common with one of the underlying ideas being attached in an earlier linkage of the chain. In this way, the mechanism is conceptualised as at least two or more disparate ideas, being carried through people or documents (the linkages) which are connected to the next linkage in the sequence through a shared commonality of at least one underlying idea. And so on, until the linkages become so stabilised and ‘natural’ that successful action obtains. Change in this way is being envisaged as a chain of linkages, whereby the connection of ideas becomes progressively stronger further down the chain until they achieve a ‘reality’.

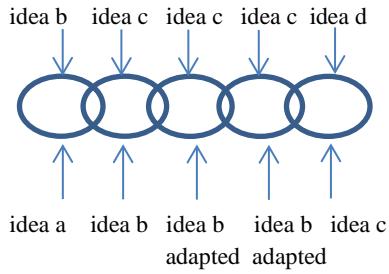
Therefore, instead of this conception of change (oversimplified):

Figure 2.2 Existing conceptions of accounting change

Idea(s) → translation → translation → translation → action

Being proposed is, for example, a sequence such as this:

Figure 2.3 Proposed conceptualisation of a chain of linkages



This conceptualisation is different (not least as it represents a different focus) to a general process of re-interpretation and translation, shaped by actors' interests (Callon, 1986; Latour, 1987). This is not to say that interests don't play a role, but more that they are not the *only* means by which linkages can be shaped and it nonetheless does not help to explain the type of linking which occurs. Indeed, it is put forward here that the *precise ways* ideas within each linkage are connected, even if motivated by self-interests, can differ. It is to these developments which we now turn.

2.2.2 Typology of linkages

Within this thesis, the work of linkages (the hardening of the connection between different ideas) can potentially occur in seven different ways. Whilst this typology does not purport to be a complete list of all means of linking, it attempts to capture some of the key forms of linking work which have been empirically identified within this research. These seven ways are set out in the table below which will serve as an opening heuristic, to be empirically developed in the following three chapters, to help make visible the precise nature of linking work entailed within the constellations. Importantly, we note it is not only a process of translation which occurs.

Table 2.1: Typology of linkages

Linking work involved	Meaning
Collaboration	Where two or more actors form an alliance to exchange ideas.
Rationalisation	Where connections between ideas already made are further justified in a seemingly logical manner.
Repetition	Where connections previously made are reinforced by being repeated.
Brokering	Where new ideas enter a field, usually through an actor who brings with them ideas which have been initiated from outside of that field.
Adaptation	Where ideas or techniques used elsewhere are transported into a different domain of operations and are actively modified in order to make them workable in the new context.
Re-interpretation	Callon's (1986) and Latour's (1987) predominant conception as a process of re-interpretation shaped by actors' own interests; this can also result in new ideas altogether.
Mediation	Moderates concerns and interests of more than one arena to bring about a linkage of arenas; the linkage works in two arenas at once (similar to Abbott's (2005) hinges).

These forms of linking work are not mutually exclusive and some linkages can do more than one. For example, collaboration between two key actors can involve an exchange of ideas which then results in adaptation or rationalisation.

As presented above, the concept of linkages encompasses the concept of translation in that the act of re-interpretation is but one way that linkages can occur/be made. In an alternate view, the reverse can also hold. Translation can encompass linkages if a wider view of translation is taken. As Latour (1993) has clarified, translation refers to “displacement, drift, invention, mediation, creation of a new link that did not exist before and modifies in part the two agents” (Latour, 1993, p. 6 as cited in Czarniawska and Joerges, 1996) and accordingly, with this view, translation encompasses the creation of new links, invention, mediation – overlapping with the typology presented above. Even if this view is taken, the typology of

linkages above still brings to light a more detailed level of analysis. It focuses on the precise mechanism of linking and analyses this further. The argument being put forward is that the examination of this linking mechanism in close detail can help to pin point the precise details of one of the core mechanisms of change, rather than having this all fall under the auspices of ‘linkage’, ‘translation’ or ‘intersections’.

2.2.3 Hinges, avatars and linked ecologies

In Abbott (2005), the concept of linked ecologies is developed to reconceptualise the social world as a number of ecologies, ‘each of which acts as a (flexible) surround for others’ (p. 246). A linked ecologies approach in particular emphasizes the multiplicity of interactions between elements ‘that are neither fully constrained nor fully independent’ (p. 248), thereby bringing a more reflexive approach which especially highlights the relational processes between different elements¹⁵. Concepts central to the linked ecology are that of hinges and avatars. Hinges refer to ‘issues and strategies that “work” in both ecologies at once’ whilst avatars refer to ‘attempts to institutionalize in one ecology a copy or colony of an actor in another’ (p. 245). In drawing on empirical examples from the political, professional and university ecologies, Abbott constructs a more general argument about the structure of social processes.

The concepts of hinges and avatars specifically attend to the interrelationships between different ecologies¹⁶ and an overlap exists with the concept of linkages being deployed here. Hinges and avatars are used to draw attention to the importance of the contingent nature of interecology linkage, that successful action is dependent upon some combination of actors across ecologies, and to also highlight some of the forces which can keep ecologies separate. They attend directly to the interecology relationship. The linkages being studied here are not necessarily at the same level of analysis. They work at a much more detailed unit of analysis in terms of how very initial ideas become connected and stabilised, and what this consequently may reveals about the interrelationship of the arenas or about change. They do not necessarily work only at the level of interecologies, or interarenas presently.

¹⁵ In her study of the relationship between the post-Soviet Russia audit and markets, Mennicken (2010) adopted such an approach in order to similarly bring a more dynamic element to her study. Adopting a linked ecologies approach helped to ‘emphasise change, internal dynamics and the *overlapping and interpenetrating* of previously distinct worlds’ (p. 335, emphasis in original). Here, the emphasis, whilst still on change and dynamics, was on the changing relations between old and new, Soviet and post-Soviet, global and local audit definitions and marketisation attempts, and in drawing out the complexities of such changing relations whereas the current study looks to identify the precise mechanisms of how ideas become connected and are stabilised with respect to its role in contributing to accounting change.

¹⁶ Abbott (2005) also uses the term ‘linkage’, although to refer ‘exclusively to connections between actors in different ecologies’ (p. 249), which should not be confused with the notion of linkage being used in this study.

Conceptually, however, the linkages being put forward here overlaps particularly with hinges as both can attend, at least in part, to how different ecologies (or arenas) become connected and how successful action is dependent upon the issues, strategies, or ideas being workable in two arenas at the same time. Even so, hinges, still need to ‘work’ (i.e. the action) in some way, and the suggestion here and in the typology presented above is that they might work through the mediating of concerns and interests of more than one arena. Avatars, as ‘attempts to institutionalize in one ecology a copy or colony of an actor in another’ (p. 245) are not necessarily a form of linking in itself. However, if successful, they still need to have been made successful and it is put forward that this is at least in part dependent on the linkage mechanisms set out above. If avatars address mostly the making of one copy of an actor from one ecology to another, then perhaps brokering or adaptation are the most closely related mechanisms. Additionally, Abbott’s (2005) concept of ligation refers to the relational process between an actor and a location within an ecology. If this relational process is seen as a linkage, then again, that linkage needs to be made in some way and it is put forward that perhaps some of the detail can be found in the typology set out above. And whilst Abbott (2005) believes that attending to questions such as ‘how hinges are made’ or what are the ‘conditions which make certain things work as hinges and others not’ are merely questions of working out the details (p. 271), this research suggests that some of those details - the linkages in this thesis which carry those critical, connecting ideas and the pre-conditions which enable certain hinges to work, are nonetheless important to be worked out if a more concrete model of change can be furthered.

More generally, the notion of linked ecologies itself bears some resemblance to the constellation and its three arenas which begs the question of whether this attempt to reconceptualise a more dynamic constellation means the notion of the linked ecology is a more suitable conceptual underpinning for this thesis. In particular, the notions of the ecology and the arena are particularly similar in that they are both constituted by actors bound together by relations which in the case of the ecology are ‘neither fully constrained nor fully independent’ (Abbott, 2005, p. 248). The choice lies in the question of focus. Whereas linked ecologies focuses on the simultaneous existence of numerous adjacent ecologies, and their contingent interplay, the constellation enables a focus on the totality of elements and their relations which come to form the preconditions that give rise to particular events in specific ways. Accordingly, a linked ecologies approach starts from the position of more or less already formed ecologies thereby enabling a focus on this contingent interplay, whereas the capacity of mutually constituting, emergent or differentiating arenas is opened up for study within constellation analysis. In this sense, the research objects of study which are enabled by these approaches are very different.

Further discussion and developments on this preliminary theoretical framework will be examined in chapter six. Methodological considerations are discussed next.

2.3 Data sources and analysis

2.3.1 Geographical considerations

The arguments of this thesis regarding the nature and constitution of audit quality are sufficiently high level so as to not be centrally dependent upon geographical considerations. Constellations are not necessarily spacial. Notwithstanding this, the empirical support for this thesis is nonetheless grounded within certain settings which are geographical in nature. The data for this research has been empirically grounded predominantly within the US and the UK. Whilst an explicit comparison between the two jurisdictions is not undertaken, this choice stems from a number of considerations set out below.

The US was selected as the primary empirical location due to its leading role in audit quality developments, both from regulatory and institutional perspectives. These developments have been particularly influential internationally, such as the instigation of peer review in the 1970s and the move to external oversight post-Enron. Much of the quality discourse, intricately tied to the high profile failures within auditing (many of which have stemmed from the US), can be traced to the very early days of the US accounting profession. Key debates on audit quality explicitly manifested within regulatory commissions, policy debates, and standards have also emanated from the US. New institutional structures in the US have also been instigated in the name of audit quality, including for example, the Centre of Audit Quality and the PCAOB – both of which place issues of audit quality centre stage. In addition to this, much of the academic research on audit quality adopts a ‘quantitative’ approach which draws heavily upon the seminal work of American academic DeAngelo (1981). Many of these papers have also been generated from US empirical settings and researchers.

The UK setting, as a ‘secondary’ empirical setting has also been included on the basis of their own developments which in themselves have been influential. For example, the FRC took on a leading role in the mid 2000’s to develop a framework approach to quality which became adopted within the international setting and recent debates regarding the lack of competition within the audit market were particularly pronounced in the UK with a formal referral to the UK Competition and Market Authority for investigation. Including the UK also allows for a more dynamic consideration of how quality debates have travelled from

one jurisdiction to another¹⁷, possibly their interrelationship and also the opportunity to generate a comparative basis by which to consider the generalisability of arguments of this thesis.

Of course, other developments internationally have also been important with the quality discourse more generally. For example, the total quality management philosophies of Juran and Deming had their roots within the quality programmes of Japan. More recent developments within the EU single market initiatives would come to have a profound impact on how audit quality within the UK was understood. Where relevant, these international developments have been accordingly considered and referenced to the extent that they impacted on the movements of audit quality within the US and UK.

The three empirical chapters of this thesis very loosely follow this balance of the discourse and accordingly two chapters are rooted within the US with the final chapter based within the UK. Over time, as the discourse on audit quality became increasingly entwined globally, geographical considerations become even less relevant to the constellation, and hence the arguments of this thesis. Furthermore, the arguments of this thesis are sufficiently general such that they do not rely upon the constellations being continuous – they are presented as relatively discrete moments within an extended history where the audit quality debate was particularly amplified. The selection of these key episodes will be discussed further in section 2.3.3.

2.3.2 Data sources and collection

In pursuing a longitudinal study of the changing notions of audit quality, consideration was given to the nature, types and availability of the discourse, over an extended timeframe, which would capture both the changing notions and the key influences which have shaped those notions. This entailed taking a broad enough approach such that wider social influences and discourses could be captured, yet also specific enough such that detailed movements within the discourse could be identified beyond that of general intersections with social movements for further investigation. Further, in adopting a constructivist stance, it was also important to adopt an approach whereby the meaning of quality was not already encumbered by pre-conceptions of what this may or may not have been. Together, this entailed a shift in focus from ‘audit quality’ as the primary object of the data collection to

¹⁷ This research originally started as a UK premised study, based on the author’s location of residence, place of study, and access to empirical materials. However, it soon became apparent that many of the debates on audit quality occurring within the UK regulatory and practice arenas were heavily influenced by those of the US. Accordingly, the move to focus on and include the US as part of this research was incorporated in order to study these developments from their points of origination.

the underlying concerns and influences which have together shaped conceptualisations of quality at key junctures.

The timeframe investigated for this study spans the period just prior to audit quality emerging as an object of concern to the present decade. As Figure 1.1 of chapter 1 suggests, this emergence occurred in the 1960s. Extending this period further back, to the post-war period in the mid-1940s enabled the examination of some of the origins of quality ideas within the audit field. With nearly 75 years of discourse to examine, the data collection focused on those documents which provided the most representative window into the underlying concerns and influences to the audit quality conceptualisation at the time, and also very initially and broadly, by arena.

The data sources drawn upon for this research were primarily documentary based. The sources selected for examination were directed upon those where the audit quality discourse was most pronounced, such as in the many and varied documents produced by regulators, the accounting professions and practitioners, and academics (essentially the arenas of the constellation). The working basis was that these documents would allow for and provide the opportunity to observe how ideas, rationales and aspirations were manifested, the influences to those ideas, and to start the investigation into how critical connections of ideas to the audit quality discourse were made.

Irrespective of any potential concerns as to a discrepancy between discourse and ‘actual’ practice, it is put forward that paying careful attention to how discourse is articulated is nonetheless warranted - ‘for language is not merely contemplative or justificatory, it is performative’ (Rose & Miller, 1992). Vocabularies enable technologies to be depicted as solutions, to be disseminated through textbooks and to be embodied in the syllabuses of professional bodies. Attending to the discursive enables a focus on the nature of the ‘actuality of which daily practice forms a part’ (*ibid*). As Power (1992) has further argued, it is ‘only when such vocabularies are established can concrete procedures change to fit them’ (p. 59).

This research has drawn upon a wealth of resources wherein the discourse on audit quality has been manifested. A detailed list of these sources has been included in Appendix A. These sources were selected on the basis of having the potential to provide insights into the underlying concerns of key stakeholders and the main debates being held at the time. Where a constant source was available throughout the timeframe in question (ie *Journal of Accountancy* and *Accountancy*), each successive volume of the publication was examined and these sources in particular became a central reference point within the data collection, from where additional sources (such as key regulatory commissions and professional

statements) were further examined. The Journal of Accountancy, as the primary professional journal of the AICPA with an extensive readership, proved to be a key source containing important debates in both the regulatory and professional practice arenas¹⁸; Accountancy provided the counterpart for the UK. Practice manuals with sequential editions were also prioritised in the selection process in order for developments in the discourse over time to be tracked more readily. Professional standards with respect to quality matters were examined, as were further publications from the professional institutes (ICAEW and AICPA).

With these sources identified, the selection criteria for gathering the data was a broad ‘issues and concerns’ underlying the key debates, as opposed to strictly confining the search to that which contained the word ‘audit quality’. Taking this approach enabled the capturing of the emergence of quality as a rising concern, as well as any adjacent concerns which may have sat alongside and/or become subsumed within the quality conception over time. Given the volume of material identified, those issues which constituted sufficient ‘importance’ to be included within the data was difficult to define and necessarily contained some element of subjectivity. However, the operational objective was retained of gaining a sense of those matters which were particularly concerning at the time – certain indicators would help with this assessment, such as the placement of items within the text of the journal or manual (i.e., within Journal of Accountancy as a key article, editorial, or within the president’s address), repetition of the issue within and across multiple volumes, or the nature of the headings. Any explicit debates on audit quality directly would always be collected as part of the corpus of data.

During this data collection phase, either detailed notes were made on these underlying concerns and debates or else copies of any key articles or documents which dealt explicitly on the issue of audit quality were taken. This generated several hundred pages of notes and documents.

Finally, undertaken as part literature review on audit quality but more so with the emphasis as research data enquiry, the question of how audit quality has been conceptualised within academia itself was also examined. To perform this investigation, a list of the top-ranking accounting and auditing journals was compiled from which to source the data. The journals

¹⁸ Key speeches, interviews with regulators, practitioner articles and contemporaneous debates were published in this journal. In addition, the Official Release section of the journal contained all of the key official regulatory releases over the timeframe examined such as professional standards, policy developments and commissions.

included within this review have been listed in Appendix A¹⁹. These journals were then individually interrogated within google scholar, by decade from about 1960²⁰ onwards, for articles which contained the phrase ‘audit quality’ anywhere²¹ within the body of the text. This data enquiry was restricted to a search on the term in order to trace more directly the discourse associated with the term. Therefore, whilst a more literal approach was used here, extending the search criteria for audit quality within anywhere in the body (as opposed to only in the title or abstract) still enabled a broad reach. Arguably, and otherwise, almost all auditing research could be viewed as relating in one way or another to audit quality. This initial search generated 1,894 articles in total spanning 1980 - 2014. From there, these articles were scaled down for examination using a citation threshold of approximately 75²². The total number of articles which met this threshold was 515. These articles were then uploaded into NVivo for further organisation and analysis.

2.3.3 Data analysis

Jørgensen and Phillips (2002) have proposed one definition of discourse as ‘a particular way of talking about and understanding the world (or an aspect of the world)’ (p. 1) and discourse analysis as a methodological approach whereby the starting point is that ‘our ways of talking do not neutrally reflect our world, identities and social relations but, rather, play an active role in creating and changing them’ (p. 1). This is consistent with the premise of this study whereby vocabularies and language are taken to have a performative role (see section 2.3.2). Jørgensen and Phillips (2002) further argue that discourse analysis, theory and method are all intertwined (p. 4) and that the basic philosophical premises must be accepted before drawing upon discourse analysis as an empirical method. These premises, being a critical approach to taken-for-granted knowledge, historical and cultural specificity, knowledge being created through social interaction and the link between knowledge and social action (whereby different social understandings lead to different social actions and

¹⁹ This list of journals selected is not meant to be exhaustive but was compiled as a means of scaling down the data to be investigated. The academic literature produced on audit quality has been extensive.

²⁰ Whilst 1945 was used as the starting point to parallel the data collection in the other two arenas, research publications on audit quality did not start to arise until the early 1980’s.

²¹ This broad search criteria was applied in order to capture any adjacent research concerns which may have influenced (or was influenced by) the audit quality discourse although some remote matches would invariably also be captured.

²² This threshold is admittedly entirely arbitrary but was taken as one means of ‘proxying’ for the paper’s influence on ongoing research and academic debates. This also scaled down the papers published to a manageable number. This threshold was calibrated down to approximately 25 citations for the current decade of 2010 onwards. Further, the analysis which was subsequently performed on these papers indicates that data saturation, especially in terms of how academic research has conceived of the audit quality problem was well reached within a few hundred papers. Analysing any further articles would not have been additive.

therefore the construction of knowledge has consequences) (Jorgensen and Phillips, 2002, p. 5 – 6) are again, consistent with the premise of this study.

Notwithstanding the above, and as Silverman (2015) has observed, discourse analysis is ‘quite heterogeneous’ rendering it difficult to arrive at a clear definition (p. 319) or a single method. Coupled with this is that the volume of data collected for this study proved an additional challenge for analysis and synthesis. Consistent with a constructivist approach, the data analysis was focused on identifying core themes from the discourse collected. With practitioner and regulatory related debates, articles and notes in hard copy, academia was left entirely separate at first. Taking inspiration from Langley’s (1999) strategies for theorizing from process data (where ‘research is concerned with understanding how things evolve over time and why they evolve in this way’ (Langley, 1999, p. 692)), and with a clear analytical commitment for an inductive approach, the starting point was to map out the key developments, influences to those developments, world events and over the passage of time.

The data collected which comprised both regulatory and practice sources were firstly organized chronologically, as the data was not easily and readily separable into distinct arenas. For example, the Journal of Accountancy often contained debates and articles featuring both perspectives. Two descriptive and parallel documents were written to summarise some of the key events and developments for each arena, with the objective of gaining a sense of the sequence of events, and the general development of the debates from both the regulatory and practice perspectives. From here, critical junctures wherein the discourse on quality became particularly heightened and where this intensity converged between regulation and practice, were identified. Initially, five such junctures were identified.²³

Thereafter, with these five junctures identified upon which to organise the data, the data was re-examined in greater detail and an initial attempt was made at coding the underlying themes. This coding included the underlying concerns, key arguments, emergent themes, key influences to the debates and centrally, how audit quality was being conceptualised. This coding went through several iterations and was performed over several weeks of examining the data during which time ‘visual process maps’ (Langley, 1999) were drawn. These maps were revised after each iteration. The analysis, with more detailed notes, was also summarised within excel spreadsheets by juncture and broadly by regulatory and practice arenas. With each map, the coding and underlying data were revisited to check for

²³ These were: the emergence of statistical sampling, the emergence of quality as quality control, the advent of peer review, the rise of independence and finally, the advent of mandatory rotation. As data analysis progressed, it became clear that quality control and peer review should be merged, as should independence and mandatory rotation.

coherence of argument and to apply the data collected onto the visual process maps, thereby ensuring a ‘continual movement between data...and theory’ (Silverman, 2015, p. 123) which is consistent with a grounded theory or inductive approach.

Separately, the corpus of academic articles uploaded into NVivo was examined. Each of these articles (abstract and introductions) were reviewed and coded on the basis of how audit quality was being conceptualised, how they were being ‘handled’ within the research papers, whether they were the independent or dependent variables in the research design, and how they were being proxied. Articles which were very highly cited were reviewed in more detail. These categories, along with a reorganization of the articles chronologically suggested a high level trajectory of academic research on audit quality which was triggered by DeAngelo (1981). A separate document was written to capture the key developments and shifts of this trajectory, including for example, when audit quality became subsumed within financial reporting quality within academic research. This document was placed alongside the two other arenas.

Thereafter, the initial descriptive documents written for the practice and regulatory arenas were re-worked in their entirety, in a more integrated way and framed within a constellation framework, drawing in at this stage the academia arena. Initial attempts were also made to map each constellation, again moving continually from data to these emergent constellation maps. Key developments and junctures within the academia arena were then overlaid on top of the emergent constellation maps. During this process, overlap of the critical junctures initially identified became apparent (for example, quality control and peer review were at first separate episodes), and three key episodes where not only was the discourse was particularly heightened but where the notion of quality underwent a clear shift in its conceptualisation emerged. With the outline of three constellations now emergent and in hand, the data was re-examined again, at a very detailed level, to start tracing the connections within some of the ideas and debates which enabled them to become attached to audit quality at those junctures. Further data was examined at this point, digging deeper into referenced or related documents where available and applicable.

From here, with the periodisation and three key episodes identified, an attempt was made to merge the three arenas and to re-think the data in an integrated way. This led to another attempt to re-map the constellations, with a focus on those factors which led to the conceptualisation of the audit quality problem in their specific ways. This analysis allowed the author to investigate in further detail the linkages which enabled the three problematisations to arise, and which attached the critical ideas to audit quality. At this point also, it became apparent that the three arenas were not at all ‘constant’, or fixed

within this history. This led to further investigations into the conditions of arena emergence or differentiation, which were then incorporated into the constellations being analysed.

As Langley (1999) has cautioned, the use of multiple strategies is often advisable and ‘no analysis strategy will produce theory without an uncodifiable creative leap, however small’ (p. 691). Whilst the volume of data collected proved to be a challenge in robustly synthesising the data, the core shifts in the conceptualisation of audit quality were by and large very clear. Once identified, this aided the process of identifying key influences which shaped those conceptualisations which in turn helped to identify the underlying linkage of ideas.

2.4 Summary comments

Together, the research design set out in this chapter underpins the remaining chapters of this thesis. Chapters three, four and five will investigate three distinct, yet slightly overlapping, episodes within the evolution of the audit quality discourse which empirically draws out the theoretical developments proposed in this chapter. The following chapters will, taken together, present a story of change. It will show how audit quality became repeatedly implicated in a number of wider debates, ideals and ideas, entangled in the contemporaneous concerns of key stakeholders, all of which was only made possible through an almost extraordinary set of circumstances and connections which were each made to be so. In doing so, and in being so constituted, quality reconfigured the very arenas upon which its constellation was based. The following chapters will seek to develop a more dynamic reconceptualisation of the constellation, hinged on a mechanism of linkages, and in so doing, contribute to theories of accounting change. However, it does this in order to ultimately contribute more specifically to our understanding of the nature of audit quality, and to unpack some of the wider meaning and implications of this trajectory since the post-war period.

Chapter three

The pre-quality constellation of statistical sampling (mid-1940s – mid-1970s)

3.0 Introduction

In November 1956, the AICPA formed a special Committee on Statistical Sampling to investigate the possible usefulness of statistical sampling techniques within the field of accounting and auditing. The Committee was tasked with assessing the feasibility of statistical sampling to improve auditing practice and would report to the Committee on Auditing Procedure (the then audit standard setting body in the US). The Committee was led by Robert Trueblood, a leading practitioner at the time who in time became highly involved in regulatory as well as academic pursuits. The formation of this committee represented one of the early efforts of the AICPA to formally engage with the potential use of statistical sampling procedures (Tucker and Lordi, 1997), its interest and widespread use outside of auditing already by then apparent, and went on to play a key role in the formalisation of statistical sampling procedures within auditing. The committee also represented one manifestation of the close connections between academic, regulatory and practice activities at that time, the ongoing dynamics of which will be centrally examined within this thesis with respect to its role in contributing to accounting change.

This chapter traces some of the origins of the quality discourse which would later emerge within the discourse of regulators, practitioners and academics by investigating the historically specific and contingent conditions which enabled the emergence of statistical sampling as a technique within auditing in the 1970s. Notwithstanding the societal rise in statistical thinking dating from the 19th century (Porter, 1986), statistical sampling techniques did not gain prominence in mainstream industry until its high profile use in the area of munitions quality control during the World War II (Trueblood and Cyert, 1957). The roots of statistical sampling within auditing can be traced to this rising interest with statistical quality control procedures and it is these conceptual roots along with the conditions which enabled these ideas to travel into the audit field that forms the starting point for this chapter. This chapter will show that the emergence of statistical sampling within auditing was more than just a technical innovation to improve the efficiency and effectiveness of the audit, conditioned by the rising influence of statistics. Instead, challenging such a view, this chapter will unpack the many diverse and varied elements which were required to converge in order to enable its rise. In so doing, we will see how quality – the idea, even if not yet the term, had already entered the audit field by the 1950s.

By drawing upon Burchell et al's (1985) notions of the arena and the constellation (see chapter two), this chapter seeks to examine both the conditions which led to the emergence of statistical sampling in auditing *as well as* that which was enabled through this emergence. Burchell et al's (1985) analysis was particularly useful in helping to highlighting a connection between accounting and its social context and how seemingly disparate fields of operations together formed the pre-conditions for the value added event to arise. The analysis, whilst historical in nature, was nonetheless focused on a relatively discrete period of time and whilst the potential for unravelling the interdependencies between the arenas was identified (p. 391), this was not in the end a central focus of their analysis. This chapter will attempt to build on this analysis and reconceptualise the constellation by paying particular attention to the relationship between the arena and the constellation. In doing so, this chapter will show that the arena and the constellation are mutually constitutive, hinged on a mechanism of linkages, which brings forth an element of dynamism within the analysis. Specifically, this chapter will develop the notion of the *emergent constellation* by paying particular attention to those conditions which led to the formation of a new arena of operations within the constellation. Emergent constellations refer to those constellations wherein the dynamism can be traced to a mutually constitutive emergence of an altogether new arena of operations. This will enable us to investigate further the relationship between the arena and the constellation, the nature of the linking work entailed and the means by which the constellation can start to be reconceptualised more dynamically. In doing so, this chapter seeks also to start examining more concretely the dynamics of accounting change, as it pertains to the shifting nature of the audit quality discourse.

Whilst the use of test-checking or sampling procedures was not necessarily new within auditing practice²⁴, the integration of statistical methods for both the selection of test samples and evaluation of audit testing result, which started to generate interest during the 1950s and 1960s, was a marked development within auditing. Early articles which appeared on the topic, such as one by statistician Neter (1949) written on request by the Journal of Accountancy, were exploratory in their attempts to ascertain 'whether the application of statistical methods to test-checking can make auditing more useful, more certain, faster and less costly' (p. 390). A number of further articles quickly started to appear in the 1950s appealing to the potential benefits such as the increased 'reliability of sample estimates' (Trueblood and Cyert, 1954, p. 293), cases of how the 'scientific sampling by formula saved

²⁴ Power (1992) argues that a distinction should be made between testing procedures and sampling as early evidence of testing did not incorporate the concept of representativeness. Matthews (2006) disagrees with this assessment and provides evidence suggesting that the difference between 'testing' and 'sampling' is only one of semantics. Notwithstanding this debate, the present chapter focuses not on this distinction but instead on the explicit emergence of the use of statistical techniques within auditing practice.

time in test-checking' (Smith, 1952, p. 62), how 'the judgement of the auditor may be guided, or confirmed, by the use of scientific sampling' (Shartle, 1952, p. 167) and how 'in time alone, the saving has been dramatic...The [sampling] plan has provided a practical method for getting reliable estimates...and the means for measuring their accuracy' (Obrock, 1958, p. 53). By 1968, a practitioner even went so far as to comment that 'The use of statistical sampling in auditing has been the subject of so many articles and reports that there can no longer be any doubt that it is accepted as an effective audit technique' (Kraft, 1968, p. 49).

The advent of statistical sampling within auditing was therefore generally espoused to be a technical innovation, promising both an increase in the effectiveness of the audit through greater 'objectivity' and the potential for cost savings. This view, however, has since been challenged. Power (1992) argued that statistically based sampling developed to rationalise practices which were already in situ and to invest auditing with a 'scientific' authority. Further, any promise of 'objectivity' inherent in statistical sampling could also be seen as a simultaneous promise of 'defendability' (Power, 1992, p. 57). Along a comparable line of thinking, Carpenter and Dirsmith (1993) used an institutional theory perspective to argue that whilst technical innovation was one part of the development, statistical sampling should also be understood as a social phenomenon 'complicit in modifying and controlling the auditing profession's abstract system of knowledge' (p. 41), again reflecting an element of self-interest of the auditing profession. Notwithstanding these views, the historical analysis to be put forth in this chapter focuses more specifically on the conditions of the emergence of statistical sampling to the extent it relates to the origins of the audit quality discourse to come, as well as the role this rise played in the constitution of a new arena of operations. Within this analysis, a key focus will additionally be given to the role of linkages and the specific types of linking work which are required in order for connections of ideas to stabilise - through which the rise of statistical sampling was dependent. The intention also is to lay some of the foundations for the changing notions of audit quality by drawing attention to some of the existing themes, concerns, ideas and conceptualisations which would become embroiled within those later quality debates to come. Even so, it is nonetheless also acknowledged, that even histories have conceptual pre-histories (Power, 1992).

This chapter will examine how the confluence of the increasing significance of the decision sciences and its intersection with audit, the problematization of the lack of uniformity of audit practice, emergent practice concerns of efficiency, and a highly collaborative atmosphere together constructed an environment of receptivity for 'scientific' developments. However, this was not sufficient in itself to enable the rise of statistical sampling, not least as the overlay of a strictly manufacturing based concept could not be easily and directly

transferred to the auditing context. Its direct implementation in the auditing context was highly problematic. A number of key connections between actors, ideas and disciplines were actively forged in order to overcome these difficulties. These connections were made concrete via key people and documents, the linkages, which together brought in ideas from outside of the audit field and connected them to those from within. It was through these connections in this way forged, along with the contemporaneous rise of computer technology, which only then enabled statistical sampling to at last emerge and become established as an audit technique. In doing so, it carried with it those very early ideas of quality into the audit field. Within this process also, however, the constellation itself became re-made through the emergence of a new and more distinct arena of academic auditing research operations, providing the empirical basis for what has been labelled here an emergent constellation.

The theoretical framework and methodological approach for this investigation follows that as set out in chapter two. Together, this chapter not only adds weight to the challenge that technical innovation along with efficiency concerns drove the development of statistical sampling techniques (Power, 1992; Carpenter and Dirsmith, 1993; Tucker and Lordi, 1997) but also to the common understanding that increasing quality concerns within audit have emerged as a natural and directly linear consequence of high profile failures. Notwithstanding the failures which were to come in the early 1970s, this analysis starts to show that whilst failures may have acted as a catalyst for the quality discourse over time, they alone should not be taken as the root cause of the rise of audit quality as an object of concern. Quality ideas had permeated the field even before the failures.

This chapter will proceed as follows. Section 3.1 will trace some of the origins of statistical sampling and how its ideas initially started to permeate the audit field. Section 3.2 will present a high level overview of the audit field, termed the *pre-sampling* constellation, just prior to the emergence of the pre-conditions which contributed to the advent of statistical sampling. Section 3.3 examines closely these pre-conditions which together created the environment of receptivity for scientific developments. Section 3.4 examines the means by which connections between ideas, actors, and disciplines were forged in order to overcome the significant practical difficulties with applying sampling techniques to auditing. These constituted the critical linkages, manifested in this episode through documents and people, which served as some of the key mechanisms for change. Section 3.5 shows, critically, the role the emergence of statistical sampling had in simultaneously reconfiguring the arenas upon which the constellation was constituted. Finally, section 3.6 will present the pre-quality constellation which emerges from this episode and discuss some implications for our understanding of the audit quality discourse.

3.1 The origins of statistical sampling techniques

Whilst the societal rise in statistical thinking has been traced back to the early 19th century (Porter, 1986), the popularity of statistical sampling techniques within mainstream industry did not gain ground until its use in the manufacture of defence materials in World War II (Bowbrick, 1992; Trueblood and Cyert, 1957). During the war, statistical sampling was developed as part of a wider program of statistical quality control techniques to help expedite the process of inspecting every unit of defence materials manufactured. A key actor highly influential in these developments was Walter Shewhart, frequently regarded as the ‘father of statistical quality control’ (Best and Neuhauser, 2006). A physicist and engineer by training, Shewhart was instrumental in bringing together the disciplines of statistics, engineering and economics through the origination of the control chart²⁵ which he called ‘the formulation of a scientific basis for securing economic control.²⁶’ Shewhart’s influential text ‘Economic Control of Quality of Manufactured Product’ published in 1931 was one of the original texts on quality control and testament to this underlying philosophy of embedding economics within quality control. This would come to be an enduring basis from which the Total Quality Management (‘TQM’) movement later spawned and one of the foundations by which it would come to be understood.

During the war, Shewhart served as a consultant on ammunition specifications for the War Department and whilst there, amongst a team of others, spearheaded the development of the Z War Standards²⁷ relating to statistical quality control by the American Standards Association. These standards set out sampling techniques for inspection and were used to expedite the process of inspecting virtually every unit of product. The standards also formed the basis of a number of statistical quality control training courses which were delivered nationwide as part of an Engineering, Science, and Management War Training program. These nationwide courses trained 7,553 people during 409,000 student hours (Wareham and Stratton, 1991), however, uptake in statistical quality control ideas in disciplines outside of manufacturing was slow. Interest in developing statistical quality control procedures increased post-war when American industry struggled to keep up with demand. One turning point also came when Fortune Magazine published an article in 1950 titled ‘Statistical Quality Control is Among the Sharpest Management Tools Developed in Half a Century’

²⁵ The control chart distinguished between common and special causes of variation and was a tool used to determine if a process was in a state of statistical control.

²⁶ From Shewhart’s biographical details, see American Society for Quality biography at http://asq.org/about-asq/who-we-are/bio_shewhart.html

²⁷ See American War Standards Z1.1-1941, Z1.2-1941, and Z1.3-1942.

which raised its profile, particularly within the management sciences substantially (Wareham and Stratton, 1991).

Shewhart's work inspired others, including W. Edwards Deming, a professor of statistics and private business consultant, and Joseph Juran, an engineer turned academic – both of whom worked together with Shewhart and later became key figures in developing quality ideas within management, most notably that of the TQM²⁸ philosophy. Deming was particularly interested in moving the application of statistical methods more widely and it was on the basis of some of Shewhart's ideas from which Deming developed his Theory of Management (Anderson et al, 1994). Deming championed much of Shewhart's work²⁹ and believed that many of his ideas could be applied not only to manufacturing processes, but also to the processes by which enterprises are led and managed. Juran in time came to be known as the 'father of quality' and his Quality Control Handbook, focusing less on statistics and more on management, first published in 1951, became the 'bible' for quality management (Whaley, 2003).

By the mid-century mark, interest in statistical quality control ideas had garnered sufficient attention such that articles³⁰ exploring its use started to appear more frequently within accountancy journals, indicating that ideas of statistical quality control had now reached the audit field. An article in the Journal of Accountancy by then prominent practitioner Peloubet³¹ (1949) entitled 'An inquiry into the need for, and development of, auditing standards' contained a small section querying the applicability of statistical sampling within auditing. This was brought to the attention of Deming and in 1950, Deming traded letters of correspondence with Peloubet entitled 'Can statistical sampling techniques serve the auditor?'. These letters of correspondence were published in the Journal of Accountancy (March, 1950, p. A-16). Within that article, Deming addressed head on one of the core concerns being raised by practitioners regarding the adoption of statistical techniques - that its use would suppress the role of professional judgement. Here, Deming argued: 'The statistical method does not supplant judgments: it supplements judgment, and makes the best possible use of expert knowledge and judgment' (p. A-16, A-18). (This relationship

²⁸ For history and evolution of TQM, see Garvin (1988).

²⁹ Deming and Shewhart also collaborated on many occasions. For example, Deming edited the textbook Shewhart published in 1939 entitled 'Statistical method from the viewpoint of quality control'.

³⁰ For example, see Neter (1949) and Vance (1952)

³¹ Peloubet, having served as a consultant to the War Production Board in 1941 - 42, would likely have been exposed to the statistical quality control standards being utilised for production purposes during the war.

between the emergence of statistical sampling and the contemporaneous discourse on professional judgement will be explored further in section 3.4.) These concerns with the role of professional judgement sat alongside other rising concerns at the time – being the efficiency and, in the face of increased litigation, the defendability of audit practice. The number of articles on the topic appearing within the Journal of Accountancy gained ground throughout the rest of the 1950s and 1960s, a special Committee on Statistical Sampling was convened by the AICPA in 1956 and the first Statement of Auditing Procedures addressing statistical sampling procedures was issued by the AICPA in 1972.

The preceding section has briefly outlined some of the origins of quality ideas and the early roots of when they started to permeate the audit field. At the outset, it could appear that the establishment of statistical sampling procedures within auditing was a natural and inevitable occurrence stemming from a functionalist view to ‘improve’ auditing practices through a more ‘scientific’ means to select and evaluate audit test samples, more ‘structured’ procedures (to ‘improve’ upon subjective judgement) which could be more easily defended and indeed the potential for increased efficiency savings. Notwithstanding these arguments, ideas of statistical quality control techniques entering the audit field, would in themselves not have been sufficient to enable their rise not least as the application of a concept conceived out of the manufacturing domain was highly problematic to apply within an auditing context. Significant differences existed regarding both the nature of the audit ‘errors’ encountered and the population of the sample itself. It took the confluence of a number of different elements to form the pre-conditions which enabled its emergence and it is to this pre-quality constellation, and its conditions of formation, which this chapter focuses. Before this, section 3.2 will first present a high level view of the field just *prior* to the initial emergence of some of these conditions. In this way, the formation process of the pre-quality constellation which, it is argued, was constituted through this statistical sampling episode can be more readily seen.

3.2 The ‘pre-sampling’ constellation: an overview of the audit field in the 1930s and 1940s

This section presents an overview of the audit field in the 1930s and 1940s with respect to its professional, regulatory, research and educational activities, set out here to help emphasise later arguments in this chapter. It has been labelled here, very loosely, a *pre-sampling* constellation in order to help highlight the constellation’s transformative process being examined in this chapter.

In Zeff's (2003) historical account of the US accounting profession, he comments on how from the 1940s to mid-1960s, accounting, auditing and the accounting profession in the US was 'at its peak' (p. 193). The passing of the Securities Act of 1933 and the Securities Exchange Act of 1934, which created the SEC, required all registrants to have their financial statements audited which served to bolster both the demand for and the stature of auditing. The merger between the American Institute of Accountants and the American Society of Certified Public Accountants in 1936 restricted its new members to CPAs only, adding prestige and stature to the Institute. The storm of the McKesson & Robbins³² failure in 1938 was weathered, with the profession emerging relatively unscathed. Zeff recounts how CPAs from the late 1930s onwards served in important governmental positions, gave testimony before Congressional committees and served as expert witnesses in court cases (*ibid*). During this period, the SEC relied heavily on committees of the Institute for 'generally accepted accounting principles' - the Institute was the primary source of authoritative pronouncements in accounting and auditing that the SEC would require for listed companies. The Institute also played a key role in setting its own terms of governance through the setting of 'generally accepted auditing standards', which dealt not just with procedures but the professional qualities and judgement required to execute an audit engagement. Self-regulation efforts were hinged on the profession's Code of Professional Conduct, the earliest version of which was published in 1917. According to Zeff (2003), 'nowhere else in the world did the organized accounting profession possess such a large degree of influence in setting the norms of professional practice' (p. 193).

Alongside the AICPA during this period was the American Accounting Association ('AAA'), formed initially in 1916 as 'The American Association of University Instructors in Accounting'. The Association had initially formed out of a need for accounting instructors to share experiences and ideas on purely instructional matters (Zeff, 1966, p. 5) due to the lack of availability of good textbooks amidst the increase in number of business schools at the turn of the century. Prior to this, accounting teachers had typically come from practice or from the study of economics.³³ Within universities and colleges, accounting (often confused with bookkeeping) instructors did not have any great stature and were 'disdained by academicians in the arts and sciences' (*ibid*). The top priority of the AAA when formed was 'to advance the cause of instruction in accounting' (p. 7) with immediate efforts focused on

³² McKesson & Robbins Inc. (1938) had grossly inflated the value of its receivables and inventory balances, neither having been verified nor confirmed by its then auditors Price Waterhouse & Co. As a result, auditing procedures were amended to include formal confirmation of inventory and receivables balances. For a detailed review of the circumstances of this failure, see Baxter (1999).

³³ The American Economic Association had occasionally allotted a session of its annual meeting to the relation of accounting to economics and the evolution of the accounting profession (Zeff, 1966, p. 5).

standardising curricula across the growing number of business schools. Research was not included in the initial priorities or indeed constitution – the instructional focus was the sole underpinning of the Association when formed and was reflected in its name.

Efforts to broaden the remit of the Association to include research activities in the 1920s and 1930s included amendments in the constitution to encourage ‘practical research in accounting, especially theory and methods’ (Zeff, 1966, p. 30), and the establishment of *The Accounting Review* journal in 1926 although such efforts were stalled due in part to the arrival of the depression but more so to the then lack of researchers in accounting. Attempts to change the Association’s name to the American Accounting Association in the 1920s, to broaden its membership and terms of reference were also met with significant resistance – by instructors and practitioners alike who questioned the role an ‘instructors’ organisation’ should have in accounting research, including the development of accounting principles (p. 37). These views remained even after a 1936 vote to change the name was successful, with the key question persisting of whether the now AAA should begin ‘to engage in the kind of research that had been assumed to come exclusively within the province of the practitioners’ organisation [the AICPA]’ (*ibid*). These views were very much reflective of the then state of affairs: with origins in accounting instruction only, the then Association had little engagement with academic research and key conceptual projects were being led instead by the AICPA. Nonetheless, the bylaws of the new Association created in 1936 included the creation of a new director of research, an explicit manifesto on research activities and for the Association to develop accounting principles and standards. These efforts manifested itself in a highly influential monograph by Paton (a key proponent for change) and Littleton titled ‘An Introduction to Corporate Accounting Standards’ which was published in 1940. A gap then ensued post war and onwards. No other monographs in the series attained such influence until the 1960s with the Association’s publishing of Mautz and Sharaf’s *The Philosophy of Auditing* (1961) and *A Statement of Basic Accounting Theory* (1966). In the intervening decades of the 1940s and into the 1950s (and even beyond), research activities on fundamental questions regarding accounting principles and theory were led by the AICPA. During this period also, both *The Journal of Accountancy*, the key journal of the Institute and *The Accounting Review*, published articles of interest to the profession and indeed, many practitioners themselves published in these journals during this time (i.e., Senn, 1955; Carlson, 1955; Tilly, 1958) yet again indicating the level of authority professional practice was accorded at that time.

This situation did not go unobserved and then prominent academic Mautz, in an article for *The Accounting Review* published in 1963, lamented as follows:

An outsider looking at accounting today would find a situation quite contrary to that suggested...He would find the organization of educators, the expected social scientists, engaged in no great research projects, either as an organization or its members as individuals. On the contrary, he would find the professional organization heavily committed to an extensive research program encompassing not only the solution of the everyday problems of practice but the development of a theoretical structure for all accountancy and a proposed study of the scope of a common body of accounting knowledge...Instead of two arms, research and practice, co-operating but independent...we find one far outweighing the other...(p. 320)

Further on, and more specifically with respect to the lack of accounting research being conducted at that time, Mautz continues with:

So far as I know, we do not have a single research professor of accounting in this country...In the last twenty years or more, very little has been accomplished by the academic side of accounting to increase our understanding of accounting as a field of knowledge (p. 321)

With professional, self-regulatory, and research activities then firmly under the stronghold of professional practice, it is perhaps an overstatement to label this situation a pre-sampling 'constellation'. The network of intersecting practices and institutions did not span very wide and were very closely held within the institution structures of professional practice. In this way and in effect, the circumstances have been conceptualised here as a *singular* arena of operations. The next section will examine the key moments surrounding how, through the advent of statistical sampling, the pre-quality constellation with an emergent academia arena especially around the field of auditing research, would become constituted.

3.3 The rise of statistical sampling (1950s and 1960s)

Thus far, this chapter has outlined how ideas of quality, via statistical quality control techniques, came to be of increasing importance outside of auditing, and provided a high level overview of the accounting and auditing field of operations in the 1930s and 1940s. As a self-regulatory profession with a significant research focus, the then constellation could in this way be seen as comprised of one very closely linked and overlapping field of operations. This section traces the development of these fields of operations within audit, upon which the constellation is constituted, through the emergence of statistical sampling. This analysis seeks to present a further view on the rise of sampling techniques, and to

develop the notion of the arena by attending to its conditions of formation. In so doing, it brings to light the means by which the constellation can be understood as dynamic and continuously in motion.

Specifically, this section examines how the confluence of the rising decision sciences, a problematization of the uniformity of accounting (and auditing) practice, a highly collaborative atmosphere and increasing concerns of audit practice efficiency came together to create an environment which was particularly receptive to statistical developments within the audit field. However, a receptive environment on its own would not have been sufficient in to enable the rise of statistical sampling as a technique, the difficulties in overlaying a manufacturing concept directly to auditing highly problematic. Key linkages were needed in order to forge the connections - amongst actors, ideas, fields of operations, and disciplines in order to overcome these difficulties and only then could statistical sampling emerge as a practice within auditing. In so doing, however, the very arenas upon which the constellation is constituted became reconfigured. It is to this transformative process which we now turn.

3.3.1 An environment of receptivity

The rising decision sciences and its intersection with audit

As set out in section 3.1, the use of statistical quality control procedures during World War II increased the profile of the technique although this in itself should be understood as being nested within a wider movement of the rising influence of the decision sciences. During the war, this was manifested as the use of mathematicians, economists, statisticians and industrial engineers with logistical, planning and managerial issues (Gore, 1956 as cited in Young, 2006). Young (2006) provides an effective account of how this increasing influence permeated many industries of commerce, including education, managerial decision making and eventually accounting and auditing practice (p. 585), which is discussed further here.

The earliest intersection of the interest in statistics with auditing has frequently been traced to a paper by Carman, in 1933, entitled 'The Efficacy of Tests'. The paper was published in the American Accountant and attempted to quantify audit sample risk in not discovering a fraud. His appeal was very much ahead of his time (Power, 1992) as the wider rise in decision sciences had not yet 'taken off' until post-war. Carman's ideas were not taken up until 1942 when a further paper appeared, by another practitioner Prytherch, which explored the laws of probability as it related to the extent of test checking required in auditing. Already in 1942, Prytherch explains his motivation as being influenced by this rising interest in mathematics and probabilities:

Whilst much has been written on the laws of probability in connection with pure mathematics, as well as their application to the various physical and social sciences, I have found very little on the subject in so far as it relates to auditing' (Prytherch, 1942, p. 526).

Notwithstanding these early pieces, McRae (1982) suggests that the 'birth of statistical auditing' (p. 143) came in a paper presented by Lawrence Vance, a practitioner turned academic, in 1947 to the Pacific Coast Economic Association, the ideas of which were printed in his article in the *Journal of Accountancy* in 1949. In that article, Vance refers again the increasing use of statistics outside of auditing and developments with statistical sampling during the war as influences to this motivation (Vance, 1949).

From the late 1940s onwards, academic articles on the subject began appearing with more frequency, including papers which called for the integration of statistical sampling into the accounting curriculum (Backer and Fertig, 1958). Working groups investigating the applicability of statistics to auditing were formed including a highly influential group convened at the Carnegie Institute of Technology in Pittsburgh. Academic interest in statistics, both within auditing and more widely, was being both provoked by this rise of the decision science as well as playing a part in propelling it forward. As McRae (1982) observed, 'Much of the early theoretical discussion of SS appears to have been carried on between academics' (p. 146), to which he also continues with 'If the methods described were being applied in practice it is odd that so little was written about the many practical problems of implementing SS' (ibid). In part, this was due to the connections having not yet been forged to have made this possible.

The rise of the decision sciences not only provoked academic interest but it also intersected with practice. In Wootton and Wolk's (1992) review of the historical development of the accounting firms, they highlight the key driver for change during this time being developments within the decision sciences seen during the war. Citing Carey (1970), they observe:

"Perhaps the most important impact of the war on the practice of public accounting was the application of mathematical and systems approaches to the logistics problems of the military." These mathematical solutions to military problems would develop into what is now called "operations research" or "scientific management" (p. 13).³⁴

³⁴ These developments would come to have a profound effect on practice: '...more important to many firms was the fact that these services could be offered to clients' (Wootton and Wolk, 1992, p. 13). This led to the emergence of management services being offered within the firms which was

The intersection of this growing significance of the decision sciences and statistics with auditing was crystallised within the profession by the formation of the AICPA's Committee on Statistical Sampling in 1956. The Committee was headed by Robert Trueblood, an influential and leading practitioner who would later head the AICPA study group on the objectives of financial statements from 1971 – 1973. Tucker and Lordi's (1997) investigation into the issues and conditions leading to the formation of this Special Committee concluded that efforts to investigate the use of statistical sampling within auditing appear to have been catalysed by the 'widespread recognition of the benefits of statistical sampling which were being realized in other professions and in industry' (p. 93) – symptomatic yet again of how the wider rising significance of the decision sciences intersected with that of auditing, thereby contributing to an environment which was more receptive to scientific developments.

Lack of uniformity with accounting and auditing practices

The regulatory arena within the US was also in significant environments of change in the 1950s and 1960s³⁵. A perceived deficiency in uniformity of accounting standards and therefore demand for standardisation had also already emerged in the US and was very apparent during this time period. The SEC explicitly voiced its concerns regarding the 'uniformity of accounting practices' (News report, March, 1963) and whilst the SEC had in the most part relied upon and supported the profession in defining generally accepted accounting principles and auditing standards, an 'immediate and pressing objective' (News report, January, 1965) was raised to eliminate alternative accounting principles underlying financial statements. The SEC itself was under pressure from the House of Representatives and asked to provide testimony on the 'uniformity in accounting' (Statements in quotes, June, 1964). This perceived deficiency and consequential demand for standardisation is supported by Young's (2006) analysis who argues also that this problematization contributed to an environment of change within regulatory standard setting.

coupled with the concurrent rise of large scale mergers during the period. As clients became more national, mergers were effected within the firms themselves in order to more readily service local offices of clients. Concerns of independence were raised from both inside and outside the profession regarding the auditor's ability to maintain objectivity whilst providing such services to clients, with the increasing scale of clients (and therefore fees) exacerbating the perception. This rising concern of independence would later come to be entangled in the quality discourse (see chapter five).

³⁵ See chapter two for a discussion regarding the empirical setting for this research and how much of the UK discourse followed closely that of the US. Whilst an explicit comparison between the two jurisdictions is not being conducted, both have served as international leaders of the audit quality 'movement'.

It is put forward here that the problematization of the lack of uniformity with accounting practices, which coincided with the increasing status of ‘scientific’ developments, also influenced the outlook on statistical sampling developments within auditing. The idea of standardisation became increasingly desirable and augmented the perceived deficiency of existing audit procedures, which up until then had been common practice to select audit samples and evaluate test results judgementally (and hence, with a lack of standardisation). This intersection could be observed within the statistical sampling discourse: statistical became used interchangeably in the discourse as ‘scientific’ (i.e, see Trueblood, 1957; Davis and Rounsville, 1959) and ‘judgemental’ was soon taken as and used interchangeable with ‘non-statistical’ (Tucker and Lorder, 1997, p. 99). Furthermore, it became understood that judgemental test checking could be ‘improved’ upon through the use of statistical sampling (Trueblood and Cyert, 1957, p. iv). This relationship between statistical sampling and judgement will be discussed further below.

Practice concerns of efficiency

Post-war, efforts within the firms had been to codify procedures to assist returning soldiers to re-engage with practice although an emergent concern for efficiency³⁶ was further exacerbated in the 1960s with the corporate merger movement, the start of litigation against the firms and ongoing difficulties surrounding the role and objectives of the audit³⁷. These put added pressures on the firms for improved efficiency of operations and calls for prioritising efficiency could be seen widely: early in the Cooper manual of 1966, the manual states that “detailed checking undertaken by an auditor should be kept to a minimum” (p. 1), instead exhorting a reliance on the whole system of controls which could then justify the reduction of testing; under Audit Procedures, the manual warns that “It is impossible to carry out an *efficient* audit without a complete list of [client records]” (p. 10, emphasis added); on discussing the audit work undertaken with partners, it suggests various procedures in order that “to avoid time being wasted” (p. 35). Articles appearing in the 1960s in the Journal of Accountancy also highlighted efficiency as a key and rising concern (i.e., Weiss, 1966; Sharlip, 1966; Dale, 1960; Stone and Witte, 1962) within the audit firms during this time of the 1950s and 1960s. Advertisements within the non-indexed pages of the Journal of Accountancy were often geared towards improving the efficiency of audit practice (see for examples, Oct 1960, Dec 1963 and April 1966).

³⁶ See Spicer and Pegler (1951, p. 31) specifying the qualities required of the auditor to ‘carry out his duties efficiently’ (p. 31) and repeated throughout the manuals of the 1960s

³⁷ Most notable of these were those concerning auditor’s responsibilities for fraud detection (e.g., SAP 30, AICPA, 1960).

Practitioner concerns with efficiency inevitably led to suggestions for improvement and these ranged from the development of new audit tools, and techniques such as ‘cycle flowing’ audit work by focusing on key areas once every two or three years (May 1967, p. 307). A practitioner article on ‘The Future Role of the Accountant’ in the April 1965 edition of Accountancy summarised some of these concurrent tensions. There, Burney (1965) noted that along with the core concern of efficiency and the concurrent pressure being brought upon the profession to ‘widen its area of responsibility, particularly in costing and management services’, the solution put forward was to ‘increase its efficiency of operations by improved techniques and methods... that is particularly applicable to auditing’ (Burney, 1965). By then, an increasing number of articles in both the Journal of Accountancy and Accountancy in the mid-1960’s indicated the growing influence of the rise in computer technology (e.g., Rappoport, 1967; Taylor, 1965; Scott, 1966; Bernstein, 1960; Boyce, 1960) and the increasing interest in mathematical models and statistics (e.g., Brown, 1962). Elementary statistics papers and its applicability to auditing had started appearing in the journals (e.g., Brown, 1961; Steele, 1962). Calls for statistics to be integrated into the accountant’s training curriculum started to be made (e.g., Williams, 1968; Kesselman & Phipps, 1962). It is suggested here that the contemporaneous discourse of these concurrent elements helped make plausible, and even thinkable, that such a solution could be found within sampling techniques.

That the establishment of statistical sampling did not arise solely from efficiency concerns of practice has been established (Carpenter and Dirsmith, 1993; Power, 1992; Tucker and Lordi, 1997). However, the significance of the totality of underlying concerns of practice at that time should equally not be understated as it created at the very least an environment within practice which was more receptive to change. Initial investigations into the use of statistical sampling were not rejected outright due to its potential and perhaps even promise to resolve issues within the audit.

A collaborative atmosphere

Finally, this period was also characterised by a particularly high collaborative spirit – amongst practitioners and academics, firms, associations and disciplines. In Zeff’s historical accounts of the US accounting profession, he has commented that the 1960’s especially was a period marked by ‘vibrant dialogue on accounting principles, with accounting participation both by partners in the big firms and by accounting academics’ (Zeff, 1986 as cited in Zeff, 2003, p. 195). He also notes how the period from the 1930’s to the 1970s, The Journal of Accountancy regularly contained articles dealing with accounting and auditing issues of interest to professional practice, as did The Accounting Review up until the 1960s. Leading

partners of the Big Eight firms spoke at public forums and wrote articles and books on the major accounting issues of the time (Zeff, 2003). Academic statisticians published within the *Journal of Accountancy* (Arkin 1958, Arkin et al, 1966) and accountants published widely in management journals (Cyert and Trueblood, 1957). Indeed, the AICPA Committee on Statistical Sampling itself brought together practitioner and academics as a formal forum for collaboration. Of the 11 initial members, nine were practitioners coupled with two academics. The two academics were Vance and Howard Stettler from the University of Kansas who went on to initiate in 1972 the highly successful, biennial Deloitte and Touche/University of Kansas Auditing Symposiums. Stettler recalls his motivation for this initiative as: 'having this as a way to bring together educators and practitioners'³⁸, its emergence again indicative of the collaborative spirit of the times. The two-day symposium provided a forum for academics and practitioners to discuss current and emerging issues in auditing and continues today.

In addition to this, collaboration could also be seen at the association level with the AICPA and the American Statistical Association working together to investigate the use of sampling within auditing. The AICPA actively sought to form greater inter-disciplinary relations with the ASA and this interest was reciprocated with the ASA forming a Committee on Cooperation with Accountants in the early 1960s (Stringer, 1963). One of the most influential papers delivered during this was by practitioner Stringer to the Annual Conference of the ASA in 1963 time (Kinney, 1986). Indeed, collaboration carried on into the firm level as well. In McRae's (1982) investigation of the use of statistical sampling, he notes how firms were not especially proprietary about their in-house developments and were open to sharing both documentation and training courses with each other (p. 309). The institutional perspective of Carpenter and Dirsmith (1993) may help explain why most of the large firms became particularly involved in advancing their own research efforts but even then, information on in-house experimentation particularly with respect to sampling was shared openly between the firms (Tucker and Lordi, 1997) providing further evidence of the very unique environment at the time.

This era of vibrant dialogue between practitioners and academics, firms, associations and disciplines was an important pre-condition for the rise of statistical sampling as it fostered an environment of collaboration which was particularly conducive to the inter-disciplinary efforts required between practicing accountants and academic statisticians within this episode – to be discussed in section 3.4.

³⁸ see University of Kansas, Oral History Project (1990, p. 21) available at: <http://www.kuonlinedirectory.org/endacott/data/OralHistoryTranscripts/StettlerHoward.pdf>

Together, it is put forward that the confluence of all these key elements discussed above not only generated an environment which was particularly receptive to scientific developments, it also created an environment where the forging of connections, via key linkages, to establish sampling procedures was *made to be possible*, especially as significant difficulties had to be surmounted to enable its rise.

3.3.2 Difficulties to overcome

In and amongst themselves, these influences and concerns would not have been sufficient to enable the establishment of statistical sampling as an auditing technique, the difficulties in overlaying a manufacturing concept directly to auditing problematic. Practitioners expressed their concerns and reservations very early on (e.g., Peloubet, 1949). One practitioner summarised some of these concerns as follows:

...the attempt to apply statistical techniques to auditing situations produces several mechanical problems which have not been foreseen. There are the problems of determining the frame and the sampling unit, the fact that present statistical tables are not appropriate for auditing use and the difficulties of sampling extremely skewed populations (Hill, 1958, p. 65).

Whilst the author went on to acknowledge that 'the logical precepts underlying statistical sampling make sense', he remained unconvinced of its applicability to auditing: 'the statisticians have not yet proven to the accountants that they apply to the examination of financial statements' (ibid). Another practitioner, commenting along the same lines, recommended 'serious research into the method before general application' (Johnson, 1953, p. 336).

Even academics, from where very early interest in statistical sampling stemmed, expressed similar concerns. In Vance and Neter's classic text 'Statistical Sampling for Auditors and Accountants' (1956) they note that 'The application of statistical sampling techniques to auditing procedures is not an easy one' (p. vii) and that their textbook would endeavour to point out 'the nature of the auditing or accounting problems that must be solved before statistical sampling techniques can be meaningfully applied...' (ibid, p. viii), again acknowledging the inherent difficulties which would be encountered in applying statistics within the audit context.

Given these difficulties, the eventual emergence of statistical sampling within auditing should not therefore be seen as a logical and inevitable development stemming from efficiency concerns within practice. From the very start, practitioners required much 'convincing' for it to be taken up. The argument being put forward is that key linkages

needed to be forged in order to concretely connect different ideas and overcome these difficulties. It is to these linkages which we now turn.

3.4 Linkages

As set out above, the applicability of statistical sampling was not a naturally occurring event despite an environment of receptivity to scientific developments. Key technical and practical difficulties needed to be overcome and it is put forward that this was achieved by the formation of key linkages which carried and solidified the connections between critical ideas. Specifically, ideas from outside of the auditing field – namely those from the discipline of statistics needed to at first be actively connected to auditing and thereafter also made to be relevant for auditing. This connection to auditing was then further reinforced by appealing to the programmatic aspirations of both improving defendability and the affirmation of the role of professional judgement within statistical sampling. Within this constellation, these linkages took on the form of people and documents. These connections will be discussed in turn in order to empirically develop the notion of linkages and to draw attention to the specific linking work which was entailed. A summary of these linkages, and the specific nature of the linking work undertaken is provided in the table below:

Table 3.1: Summary of paradigmatic linkages which enabled the rise of statistical sampling

Linkage	Connection of ideas made	Form	Types of linking
Stringer/Stephan	Auditing and statistics	People	Collaboration, adaptation
Trueblood/Cyert	Auditing and statistics	People	Collaboration, adaptation
Textbooks	Auditing and statistics Defendability and statistical sampling Judgement and statistical sampling	Document	Rationalisation
Articles	Defendability and statistical sampling Judgement and statistical sampling	Document	Rationalisation, repetition
SAP 54	Judgement and statistical sampling	Document	Rationalisation, repetition

3.4.1 Stringer and Stephan alliance

In McRae's (1982) study of the application of statistical sampling to auditing, he suggests that there were five distinct waves of development in statistical sampling between 1948 and 1980, each initiated by the co-operation between an academic statistician and a practising

accountant. Carpenter and Dirsmith (1993) also comment on these collaborations remarking on the 'active complicity of the accounting profession and its allied academic disciplines' (p. 54) within this episode. Whilst the pivotal roles played by certain key actors such as Kenneth Stringer and Robert Trueblood in moving forward statistical sampling have been documented (see Tucker 1994; Tucker, 1989 and Bryson, 1976), of focus here is not only their heroic accounts of change, but the totality of the elements which were required to come together to enable the rise of sampling, how these elements made the roles they played central and even possible, and their roles in forging the necessary connections to have overcome the obstacles. Within this constellation, key alliances formed by Stringer and Trueblood with statisticians Stephan and Cyert, respectively, constituted some of the key linkages which connected ideas of statistics with auditing.

Tucker (1989 and 1994) has documented the initial efforts of Kenneth Stringer in formulating a statistical sampling plan which could be more readily applied to the auditing context. Stringer, a practitioner with Haskins & Sells (predecessor of Deloitte) initially became interested with statistical sampling during his term at Haskins & Sells' Executive Office where he was given a broad remit to 'explore any ideas for possible improvement in the firm's auditing policies and procedures' (Tucker, 1994, p. 237). He worked under the mentorship of Oscar Gellein³⁹ who had been hired in 1953 to direct the firm's research efforts. Through Gellein's encouragement, and inspired by an article by Howard F. Stettler (1954) which appeared in the *Journal of Accountancy*, Stringer pursued his dissatisfaction with the firm's then process of determining the extent of testing required after an auditor's initial evaluation of internal controls (*ibid*) which was deemed to be subjective, judgemental and inconsistent between audits.

Stringer firstly identified the key statistical areas of acceptance sampling and estimation sampling which were being focused on in contemporaneous writings (Tucker, 1994). Acceptance sampling⁴⁰, an evaluation procedure, had emerged in close relation with the development of statistical quality control techniques of Walter Shewhart and others during the war. Acceptance sampling used statistical sampling to determine whether to accept or reject a production lot of goods. It had an inherently dichotomous nature whereby the decision alternatives were either absolute rejection or absolute acceptance. Stringer deemed this aspect of the technique, along with its inability to be applied to dollar items, to be inappropriate for use in the audit context (*ibid*). In his influential 1963 address to the American Statistical Association, Stringer commented that existing sampling plans shared

³⁹ Gellein also served on the initial AICPA Committee on Statistical Sampling along with Trueblood.

⁴⁰ The development of acceptance sampling has generally been credited to Harold F. Dodge, who had worked closely with Shewhart.

‘the common deficiency of not being related directly to the area of his principal concern – namely, monetary amounts. In addition...the automatic decision rules of acceptance sampling are too rigid and extreme’ (Stringer, 1963, p 158). Stringer also objected to the core statistical premise of a normal distribution used within estimation sampling as errors within an audit population were likely to be rare. Of key concern here was its defendability, in the event that critics would call expert statisticians to testify that existing sampling techniques were unreliable due to the violation of this base assumption (*ibid*).

Faced with these challenges and without a background in statistics, Stringer sought the assistance of a professor of statistics at Princeton University and former President of the American Statistical Association, Frederick F. Stephan. Together, Stringer and Stephan formed a key collaboration bringing together the disciplines of statistics and auditing, as well as the academic and practice fields in a key collaboration where ideas could be exchanged. The outcome of this collaboration was the precursor to monetary unit sampling, which was implemented in as early as 1962-63 within the firm and according to McRae (1982) already in ‘widespread use in the firm by 1966’ (p. 152). In rolling out his plan to the firm, Stringer also conducted what would be known today as behavioural research by asking auditors within his firm to perform a case study on selecting sample sizes. He recounts that the partners ‘were shocked and dismayed at the disparity that the survey showed’ (Tucker, 1994, p. 248) which ‘had a significant influence on the firm’s views ... and the need to improve the situation’ (*ibid*).

Whilst the significant role of Stringer in the development of statistical sampling practices has been documented, this episode highlights several aspects which are relevant to the current chapter. Without undervaluing the highly influential efforts of Stringer, it remains so that this episode is more than just one heroic account of change. This episode highlights some of the many and varied elements, including this alliance which underscored the intersection of audit practice with statistics, that were required to come together in order to facilitate this rapid development of statistical sampling within auditing. Here, the influence of those elements and concerns discussed above - that of the concerns of defendability and the growing problematization of the lack of uniformity of practice played a role in both shaping Stringer’s motivations as well as creating an environment within his firm which was clearly more receptive to change. The dissatisfaction with the large variation in sample sizes became significant enough to mobilise a questionable technique, initially met with much resistance, in a relatively short span of time.

The alliance formed between Stringer and Stephan and the outputs of their collaboration directly linked the knowledge base of auditing with statistics. Very specifically, the

difference in the nature of a manufacturing population of products with an audit population of monetary items was *overcome* by stratifying the audit population such that any individual dollar amount had an equal chance of being selected for testing. With this modification, the foundations of statistical sampling were made to be operationalisable within auditing practice and became a key moment whereby the knowledge base of auditing became infused with sampling practices. The collaborative efforts of Stringer and Stephan resulted in the active adaptation of statistical quality control techniques from the manufacturing sector such that they could be available for use in the audit setting. In so doing, Stringer and Stephan crystallised a key linkage of statistical quality control ideas and auditing, through these collaborative and adaptation efforts. The collaboration, instigated by Stringer, was due to his deep conviction that the applications of statistical theory to auditing had to be the product of synthesis emanating from both disciplines (Stringer, 1963), a conviction which was symptomatic of the wider inter-disciplinary environment at the time, and as discussed earlier. Through this conviction, the alliance was formed which connected not only the actors, but also the discipline of statistics and auditing.

Stringer continued his research efforts after this episode, and in time both served and chaired the AICPA Committee on Statistical Sampling. He also served on the Committee on Auditing Procedures and the Commission on Auditor's Responsibilities (Cohen Commission). As Chairman of the Committee on Statistical Sampling, he introduced an audit risk model that related materiality and reliance on internal control to substantive audit tests of details and analytical review procedures and played a lead role in drafting a related pronouncement issued by the committee in 1972. After retiring in 1981, he worked as a professor of accounting at the New York University Stern School of Business. He was the first recipient of the AAA's Distinguished Service in Auditing Award⁴¹.

3.4.2 Trueblood and Cyert Alliance

Another key actor and alliance which had a highly influential role in the development of statistical sampling was prominent practitioner Robert Trueblood, who had taken on a very early interest with the topic. Trueblood had been a partner at Touche Ross & Co since 1947 and also became highly involved in advancing statistical sampling in the profession. Trueblood formed an early alliance with Richard Cyert⁴², an academic statistician, economist and organizational theorist, and the two disseminated articles on the subject matter early and quite widely (e.g., Trueblood and Cyert, (1954) in the Journal of Accountancy, and Trueblood and Cyert (1957) in Management Science). Both were

⁴¹ Biographical details provided in Stringer and Stewart (1986)

⁴² Cyert later co-authored with James March the influential text 'A Behavioural Theory of the Firm' (1963).

members of Monongahela Project, a research group initiated by Trueblood (Bryson, 1989, p. 116) to investigate the helpfulness of statistics to solve auditing problems. The 'Pittsburgh group', as the group was known on account of being based at the Carnegie Institute of Technology, was comprised of a mix of practicing accountants (Monteverde and Trueblood – both of Touche, Niven Bailey and Smart) and a number of academic statisticians including Cyert. As a culmination of the work of this group, Trueblood and Cyert went on to co-author one of the early and influential textbooks on the subject entitled 'Sampling Techniques in Accounting' (1957), which provided numerous case studies of the application of statistical techniques within accounting and auditing based on real data.

The Trueblood and Cyert collaboration was a fruitful one whereby ideas of each other's discipline could be exchanged. On their collaboration, Cyert reflects upon the nature of their working relationship and upon his role of asking questions:

...I would raise questions like: What kinds of decisions are going to be made on the basis of the data? How much will it matter if you are off by this much or that much?...The question would be phrased in such a way that his judgments [about precision and reliability] could be made (Bryson, 1976, p. 119).

Based in part on the work conducted by the Pittsburgh group, Trueblood concluded that acceptance sampling could not be readily applied to the auditing context as it did not allow for the auditor 'to estimate the dollar magnitude of error as well as the error rate' (Bryson, 1976, p. 126) and instead suggested that survey sampling would be of greater and perhaps of immediate use. The Trueblood and Cyert text strongly advocated such an approach (McRae, 1982, p. 145; Trueblood and Cyert, 1957, chapter four) and their arguments were supported with actual worked examples applying statistical techniques to accounting and auditing data. In this way, statistical sampling was directly adapted and applied to auditing which further solidified the connection between auditing and statistics.

Nonetheless, over the long run, the authors noted that several problems still needed to be resolved before the integration of statistical sampling and auditing practice, including the need to develop an explicit definition of what constitutes an error. Another was the need for homogeneity of procedures selected in particular auditing situations and of the comparability of the evaluation given to the results by practitioners (Bryson, 1976, p. 128). Based largely on the work undertaken through these collaborations, Trueblood went on to serve as the initial chair of the AICPA Committee on Statistical Sampling, along with Oscar Gellein who succeeded him (mentor to Stringer), which sought to examine more formally the use of sampling within auditing and to establish the first auditing standards in the area. One of the final statements released from the committee under Trueblood's leadership equated

statistical concepts with traditional auditing terms: precision was equated with materiality, and confidence level was equated with the auditor's judgement about the internal control system (Bryson, 1976, p. 130), again actively adapting statistical concepts for use in auditing through this commensuration. In these ways, the Trueblood/Cyert collaboration can be seen as another linkage which actively brought together the two disciplines.

Notwithstanding its role as another key, inter-disciplinary alliance, representing both collaborative and adaptation efforts, the historical significance of this collaboration to the evolution of statistical sampling also warrants the consideration of some of the conditions which led to its emergence. In this respect, some of the background thinking and related research programme, along with the motivations, influences and principles which guided the collaboration can be observed within the Trueblood and Cyert (1957) text itself.

In addition to the Pittsburgh collaboration which very much guided the textbook and collaboration, the text reveals some of the key influences on the authors' thinking, over and above that of increasing the utility of auditing techniques (despite this being cited as one of the overriding principles of the text). Here, we can see how ideas outside of auditing came to influence their thinking:

Perhaps the greatest impetus for a considered evaluation of the possible application of statistical sampling to auditing problems comes indirectly from the success of scientific sampling techniques in other professional fields...Testing and inspection procedures involve scientific sampling, as do many problems of engineering design and military logistic' (Trueblood and Cyert, 1957, p. 61).

With respect to statistical sampling specifically, we can also observe that statistical quality control developments explicitly came to bear on thinking of the time: 'In the manufacturing field, statistical quality control came of age during World War II' (p. v). The author's thinking was therefore influenced and only made possible by the concurrent rising of the decision sciences during that time, again highlighting the co-constituting effects of wider ideas outside of the audit field.

In addition, this textbook (along with others of the time) also reveals the means by which statistical sampling was *made* to be relevant to the auditing context, a further connection which was required to enable the rise of statistical sampling. These are considered next.

3.4.3 Textbooks

In addition to alliances as discussed above, the textbooks which were often the outcome of such collaborations were also important elements which helped to connect the discipline of

statistics with audit. This was predominantly achieved through rationalisation efforts which further reified the connection. As above, they can also be seen as linkages in themselves, taking the form of documents.

As Gwilliam (1987) and Matthews (2006) have investigated, the eventual take up of statistical sampling in practice was variable and concentrated in the larger firms. In addition, the adoption did not actually gain ground until the 1980s. As Power (1992) has argued, some of the early textbooks published were therefore well *in advance* of auditing practice, pointing towards their use as ‘some form of rationale for the possibility of a scientifically enriched auditing’ (p. 57). To this, we add that the textbooks served yet another role – that of further reifying the connections between the disciplines of statistics and auditing through these justificatory efforts. Whilst in themselves often an output of collaborative efforts, the additional work of rationalising the connection between auditing and statistics within the textbooks helped to pave further the way for statistical sampling to emerge within auditing. The applicability of statistics to auditing started to appear as more ‘logical’. And in this way, the textbooks served as another linkage.

Both the Vance and Neter (1956) and Trueblood and Cyert (1957) texts argued that the linking up of auditing and statistics was an explicit objective of their collaborations. Trueblood and Cyert (1957) state in their preface: ‘The purpose of this book is to *attempt an explanation of the philosophy involved in the merger of the disciplines of accounting and statistics*’ (p. viii, emphasis added) and that the primary objective of the group was ‘*to further fundamental knowledge bearing on the marriage of statistics and accounting*’ (Trueblood and Cyert, 1957, p. vi, emphasis added). This would be achieved through the examination of literature and the testing of the applicability of methods on live data. The group was formed three years prior to the publication of the textbook, and was based on, amongst other principles, the underlying belief that ‘collaboration between disciplines is thought to be critically important’ (Trueblood and Cyert, 1957, p. vii) with the ‘modus operandi of the Pittsburgh group ...to base its research upon a collaborative effort’ (*ibid*). Whilst this could also be seen as symptomatic of the inter-disciplinary collaborative spirit of the time, these critical textbooks reified the connection between statistics and auditing through not only the advancement of ideas which were well ahead of practice but through providing detailed *justifications* for the ‘marriage’ between auditing and statistics in seemingly logical ways. As Trueblood and Cyert explained:

The accountant must be willing to work closely with the statistician in stating and defining his accounting problems and objectives. The statistician carries the responsibility of understanding the account’s point of view, as a necessary preliminary to join

development of techniques. Both the accountant and the statistician must proceed far enough into the fundamentals of the other's discipline to develop a common language which is a necessary basis for mutual understanding (*ibid*).

The text also illuminates the means by which ideas outside of auditing were *made to be relevant* and applicable within the auditing context despite the incomparable bases from which the technique was derived. Monteverde, a colleague of Trueblood and part of the Pittsburgh group himself explicitly highlighted this incomparability during this time as follows: 'The audit area...is more judgemental and a good bit less objective...than production line operations.' (Monteverde, 1955, p. 590). However, despite this reservation, statistical sampling would come to rise within the audit field. This text reveals one means by which this problematic was overcome, and specifically how it came to be rationalised in a seemingly logical manner.

The authors firstly make the connection between the rise of decision sciences and areas closer to audit – that of financial control systems: 'the scientific method has...found its way into the factory, and is now making significant contributions in the area of financial control systems' (p. iii). From there, a connection between this rise of the decision sciences and statistics was made, appealing to the attractiveness of science: 'In a very general sense, statistics lies at the foundation of scientific inference' (*ibid*). This was then followed by an appeal for the use of statistics within accounting on the basis of its shared use of quantitative data:

Accordingly, since statistics is essentially a methodology for dealing with quantitative data and since accountants are typically concerned with various characteristics of large aggregates of quantitative data, it seems reasonable that accounting should be able to employ to good use the techniques of statistics (p. iv).

Finally, the impetus for the use of statistical sampling was generated through the promise to solve the then concurrent concern within regulation, and by then increasingly in practice, of uniformity:

A field of exploration lies ahead for those accountants who have as yet made little use of statistical techniques in solving their problems. Of particular importance is the possible application of statistical sampling theory to improve....or to serve as a substitute for, the judgmental test-check procedures used so widely in both accounting and auditing' (*ibid*).

Due to the concurrent problematization of the lack of uniformity, existing test-check procedures being performed on a judgemental basis were deemed to be 'inferior', with the

potential solution to the auditor's newly constructed 'problem' offered within the technique of statistical sampling. These passages therefore underscore the point that not only did purely technical and practical issues of application need to be overcome, statistics needed to firstly be made relevant to auditing in order that the 'solution' potentially to be found in statistical sampling could be made even thinkable. And this was achieved through the above linking work of rationalising the potential usefulness of the technique to auditing. The textbook itself, in the form of a document and in this way, acted as a further linkage which solidified the connections between statistical ideas and some of the underlying concerns within audit at the time. This will be developed further in 3.4.4.

3.4.3 The programmatic promise of defendability and the affirmation of judgement

In Tucker and Lordi's (1997) investigation into the AICPA's special Committee on Statistical Sampling's efforts to engage with the issue of statistical sampling, they note how an initial concern of the Committee on Auditing Procedure was the 'the tenability of traditional sampling if challenged in court by a statistician' (p. 93). The Committee's initial research efforts included the seeking of the opinions of both the Institute's legal counsel as well as an external professional as to the legal implications of using statistical sampling. In particular, the concern was whether a new legal hazard would arise should auditor make use of only some, but not all of the statistician's methods. It was only on the basis of these opinions that a statement on sampling procedures was eventually submitted to the Committee on Auditing Procedure (p. 108).

An increasingly concerning environment of litigation against the profession was already present during the 1950s and early 1960s. Whilst the more high profile court decisions (ie Yale Express (1967); Escott vs BarChris (1968)) were not witnessed until the mid-late 1960s, significant rulings against audit firms had already started to occur by 1950s. Price Waterhouse's liability insurance had increased significantly in the 1950s after a \$1.4 million settlement had been obtained by plaintiffs from another accounting firm (Allen and McDermott, 1993, as cited in Tucker and Lordi, 1997). The litigation environment was therefore becoming increasingly relevant for the audit profession, which further exacerbated the growing dissatisfaction with existing sampling practices: It augmented the perceived deficiency of such practices.

It is put forward here that it was the presence of this key concern which further helped the rise of statistical sampling. The initial reluctance of practice was, in a sense, *overcome* by appealing to the promise of a new innovation to provide a more defensible technique. The nature of these appeals was through yet again, rationalisation, and continued repetition. These points were promoted, and repeated, widely at the time, through predominantly

journal articles. Even the very early academic texts appealed to this potential advantage in advocating its deployment:

As long as the standards for selection and interpretation of auditing samples are general and vague, the individual auditor must experience anxiety and doubt in planning, executing, and *defending* his work (Vance and Neter, p. 7, emphasis added).

In Trueblood and Cyert (1957), they similarly state:

Should auditors' present methods of test-checking prove inadequate in a particular case, would it not be difficult for the profession to justify its failure to use a technique found to be of such material help in other professional fields?...What would happen if in a court proceeding involving accountants' liability, a competent statistician were to demonstrate mathematically that the auditor's sampling procedures or conclusions were not statistically justifiable? (p. 61)

In Arkin's (1958) response in the Journal of Accountancy for accountants to make use of statistics, he also puts forward that such an 'objective' approach 'would make the method completely defensible' and then later, how the statistical view 'will provide a sampling technique which is not only objective but defensible even from a legal viewpoint' (p. 67). Whilst Power (1992) has similarly concluded that the rise of statistical sampling was in important part to develop a more defensible technique, to be added here is that the appeal to this aspirational potential was one of the means by which statistical sampling became constituted. Specifically, it connected a key concern of the profession at that time with sampling and overcame initial reluctance through this promise to be more defensible in court. In the event, whilst McRae (1982) has noted that the less litigious climate of the UK during that time could help explain why statistical sampling did not 'take off' as it did in the US, the defensibility of the technique did not actually hold weight in court. This therefore points towards the appeal to the aspirations of defensibility as opposed to any substantive benefits which were actually realised.

A closely related issue to that of defendability was the concurrent emphasis on the role of the practitioner's professional judgement and its relationship with statistical sampling. The threat to practitioners, posed by the advancement of statistical sampling, of the loss of professional judgement was another key issue which needed to be overcome. This was achieved by the clear affirmation of the continuing role of professional judgement, such that the rise in statistical sampling occurred almost in parallel with that of the discourse on judgement (Power, 1992). In so doing, this provided the space by which regulatory standards, a key element in the eventual emergence and adoption of the technique, could be

promulgated and developments in the academic arena could be advanced - both of which also required the implicit co-operation and agreement of practice.

This affirmation of the role of judgment was rife: From Trueblood and Cyert (1957): 'It is not suggested that accountants should summarily substitute decisions based on mathematical formulations for decisions based on subjective judgment. They can, however, develop and use whatever objective rules and devices are available as aids in the decision making process, and they can reduce the area in which purely subjective judgements are required' (p. v). From the AICPA SAP 54 eventually issued in 1972: 'Specification of the precision and reliability necessary in a given test is an auditing function and must be based upon judgement in the same way as is the decision as to audit satisfaction when statistical sampling is not used' (p. 258). From Stringer (1961):

These techniques would not supplant the auditor's judgment, but would only serve as a useful tool in applying it. In fact there are indications that the use of these techniques would bring certain aspects of judgment into sharper focus (p. 63).

The connection of the role of professional judgement with sampling techniques was therefore another necessary linkage in order to overcome the resistance from practice, contributing to the parallel rise of such a discourse. And these predominantly took the documentary forms of journal articles, textbooks and SAP 54 itself. However, in addition, it also directly challenged the role of judgement within auditing, pushing to the foreground questions of its own efficacy and seeking ways to codify it more explicitly. Indeed, with the parallel rise of judgement and its reaffirmations as being encompassed by the remit of the auditor, there was paradoxically also the *concurrent and implicit* challenge to the fallibility of such judgement. Judgement was needed, but that judgment was subject to parameters which could be negotiated from time to time. Trueblood (1957) reconciled this as: "It can be said that scientific sampling *results in* a formalization of human judgements and a minimization of human errors (p. 48, emphasis added). Not only did the connections to professional judgement enable the establishment of sampling techniques, the emergence of statistical sampling itself encountered the issue of the questioning of the role of judgement within auditing.

The significance of these two elements, the shared concern of defendability and the parallel discourse in judgement, is that they both through the making of the connections to sampling – achieved via the rationalisation and repetition work of linkages in these key documents – enabled a temporary alignment of interests which was needed to overcome the initial resistance to its introduction. Indeed, it could be further argued that these two issues in

combination even served to reinforce one another. The discourse on judgement could be viewed also as augmenting the perceived subjectivity of existing sampling procedures, which in turn heightened the issue of defendability.

In summary, the key argument being made is that all of these critical connections, forged, man-made and carried via the people and document linkages as identified, were needed to concretely link up the different ideas, actors, and disciplines together. Different forms of linking work could also be seen, including collaboration, adaptation, rationalisation and repetition. And only in so doing, did statistical sampling become established. In this way, we are able to see the critical role these linkages played within this constellation in enabling the emergence of statistical sampling as a practice.

In addition to this, however, the advent of statistical sampling was not in itself a ‘neutral’ activity and it would come to play a role in re-shaping the constellation. It is to this role of statistical sampling in forming the pre-quality constellation to which we now turn.

3.5 The emergence of the pre-quality constellation (early – mid 1970s)

The analysis thus far has been presented in a predominantly linear fashion to highlight the argument that the advent of statistical sampling was not a naturally occurring innovation stemming from a functionalist view to ‘improve’ audit practice and was instead constituted through the confluence of historically specific pre-conditions and man-made connections. Whilst the focus thus far has been on the pre-conditions which have led to its rise, this section examines the pre-conditions and effects which also *arose through* this emergence of statistical sampling. Indeed the advent of statistical sampling was not a neutral innovation and involved both the re-shaping of practice and the triggering of the formation of an arena around the field of audit research.

An early practitioner article calling for further research in the use of statistical sampling suggested the steps which were recommended in order to explore and apply statistical sampling to audit practice as follows:

...the first step, it would seem, is to state audit problems in such terms that statistical tools can be designed to cope with them effectively and economically. This approach would require that the data presently available on past audits be organized for analytical and comparative purposes, and that in the future whatever additional information may seem fruitful or necessary is obtained. Although the work performed under current practice would not presently be reduced, information would be developed

which could be used to prepare the way for the application of statistical methods. (Johnson, 1953, p. 339, all emphases added).

Whilst the detail of how actual practice coped with the arrival of this new technique is beyond the scope of this current chapter, the discourse at that time provides a window into those adjustments which would have been required in order to apply the technique. Audit evidence, as suggested above, needed to be (re)stated, reorganised, and new information altogether potentially obtained. The influential text by Vance and Neter (1956) sets out early in its preface how the use of statistical sampling would require that

...the auditor *re-examine the purposes of an audit* and of each audit step so that he can *state these purposes in such specific ways* that relevant quantitative measures of the test results can be formulated' (p. vii, emphasis added).

This passage also highlights the potential effects of adopting of statistical sampling, the reformulations which would be required and on areas as fundamental as the audit objective.

The Spice & Pegler manual in 1969 contained a reasonable section on the incremental informational requirements in order to adopt the technique (p. 68-69). Even the more recent guidance from the AICPA, adopted largely unchanged from the original Statement of Auditing Standards No 54 on Auditing Sampling acknowledges that adjustments in audit testing design are required:

Statistical sampling helps the auditor (a) to design an efficient sample, (b) to measure the sufficiency of the audit evidence obtained, and (c) to evaluate the sample results. By using statistical theory, the auditor can quantify sampling risk to assist himself in limiting it to a level he considers acceptable. However, statistical sampling involves additional costs of training auditors, *designing individual samples to meet the statistical requirements*, and selecting the items to be examined. (AICPA, AU350, para 46, emphasis added)

Together, these passages suggest that the advent of sampling was not simply a neutral innovation to be overlaid at will on top of existing audit procedures – its emergence concurrently re-shaped and adjusted audit practice and procedures, even in the developmental phase of the technique, such that sampling techniques could be at first investigated and then later established and applied. In this way, the 'result' was reflective of a technique and practice which emerged hand in hand.

Section 3.2 earlier outlined what was loosely termed a pre-sampling constellation. In that constellation, it was argued that the network of intersecting practices within the field of audit

activities was closely held within the profession and could in this way be viewed as a singular arena of operations. In particular, audit research was in its infancy with the most high profile of accounting theory and principles research activities being undertaken by the AICPA itself. Efforts to encourage research activities in the 1930s and 1940s by the AAA were met with resistance.

The environment of receptivity, particularly with respect to scientific developments, also permeated audit research thinking in the 1950s, despite audit research as a separate field of operation being in its infancy at that time. The clearest manifestation of this came in Mautz and Sharaf's (1961) monograph *The Philosophy of Auditing*, published by the AAA as part of their efforts to increase the association's research output, which has been widely regarded as one of the first attempts to develop a 'theory of auditing'. In that text, the influence of the decision sciences and scientific authority can be readily observed. References to 'science', the 'scientific attitude', the 'scientific thinker' and the 'scientific method' abound Chapter 2 *The Methodology of Auditing*⁴³, its use as a central reference point justified 'because of its advanced development, success and prestige' (p. 19). An explicit call to investigate and encourage the use of statistical techniques in auditing can also be found:

...it must be admitted that as yet auditing has not found ways of improving its use of probability theory through statistical applications to the same extent that other fields have. Thus this remains one of the areas in auditing in which additional experiment is *necessary* (p. 33, emphasis added).

The significance of this plea, and especially within the context with which it was made, is that it connected the rise of sampling techniques with the then increasing call for more audit theory and research. This link was not just related to research into statistical sampling itself but also calls for more scientifically based audit research more generally, echoing a concurrent criticism in the 1950s and 1960s of the lack of such research in US business schools (Zeff, 1989). In the event, the rise of statistical sampling took place alongside that of the rise of audit research, both being propelled forward, and with each other, in tandem.

In Kinney's edited collection of articles for the evolution of statistical sampling, he opined that two practitioner articles in particular - Stringer (1963) post collaboration and already with a sampling plan developed and Elliott and Rogers (1972) which attempted to link statistical sampling with audit objectives, alongside the first regulatory pronouncement of SAP No. 54 (AICPA, 1972), 'provided the primary stimuli for most professors' current interest in auditing as an academic or scholarly area' (Kinney, 1986, p. v), and according to

⁴³ See Mautz and Sharaf (1961) for example: pages 19, 20, 22-24, 26, 27, 29-33

Carpenter and Dirsmith (1993), statistical sampling helped ‘elevate the stature of auditing as an academic pursuit’ (p. 56). Indeed, the number of articles published on auditing related matters in *The Accounting Review* nearly doubled in the decade of the 1970s compared to that of the 1940s and of that increase, those articles on statistics or statistical sampling in particular comprised more than half. A wider search in the journal for instances of ‘audit’ or ‘auditing’ indicate an increase of 47% in two decades of the 1960s and 1970s compared to that of 1930s and 1940s. And again, of those audit or auditing instances which also included ‘statistics’ or ‘statistical sampling’, the proportion was nearly half. Smith and Krogstad’s (1984) citation analysis of *Auditing: A Journal of Practice and Theory* indicates that of the top eight most cited papers in the first three years of that journal, four related explicitly to sampling. A similar analysis and proportion was put forward for the highest cited monographs and books (the remaining entries made up of very high profile regulatory documents such as the Metcalfe Commission (1976) and the Commission on Auditors’ Responsibilities (1978). This is significant as it suggests that statistical sampling had a meaningful influence on the trajectory of academic research itself, especially that of auditing, and on what is otherwise normally thought of as an independent and objective domain of activity. Auditing research, in this sense, flourished *in and through* the advent of statistical sampling.

Power (1992) has argued that the rise of statistical sampling invested auditing (the practice) with a new scientific authority. This argument could also be extended to include that of audit research. With the rise of audit research tied closely to the rise of statistical sampling research and interest, it was possibly the [programmatic] promise of a scientific authority within audit research itself, at a time when the rise of the decision sciences had gained prestige and stature, which was perhaps most attractive in turn leading to the proliferation of audit research specifically. The argument being made is not just that research in statistical sampling tracked the rise of the technique in practice. Whilst this may be part of the story, the argument being considered runs wider into what the advent of statistical sampling meant and enabled for auditing research.

Lee (1993) recounts in his analysis of the social construction of the US academic accounting research profession, how the influence of the decision sciences and the concurrent rise of computing facilities and data bases in economics played a key role in the upsurge of empirical accounting research in the US. The decade between 1963 and 1972 saw a complete transformation between the ratio of normative versus empirical research published in the *Journal of Accounting Research* whereby the ratio reversed from 39% and 5% in 1963 to 0% and 60% in 1972 (Dyckman & Zeff, 1984 as cited in Lee, 1993), propelled significantly by the publishing of Ball and Brown (1968) which provided the critical link

between accounting information and the capital markets. Audit research, however, had not yet been set on this trajectory in the early 1960s. It too, needed a critical link to enable it to travel upon this wider trajectory of empirical accounting research.

In Elliott and Rogers' (1972) influential paper relating sampling to audit objectives, they summarised some of the benefits of statistical sampling as follows:

This sampling plan (or any other) does not replace or reduce the need for audit judgment....All the statistical plan does is to organize the available information into a *quantifiable* form for decision making (p. 55, emphasis added).

But of course, echoes of this argument have already been seen within this chapter. From the earliest academic attempts by Carman to *quantify* audit risk (section 3.4.1) to Trueblood and Cyert's (1957) making of statistics relevant for auditing through the appeal to *quantification* as a common denominator (section 3.4.3.2), these passages together reveal the moments whereby the audit knowledge base – in judgement, decisions, and risk assessments were made to be *quantifiable*. In providing a means for quantifying audit information, statistical sampling was more than just a neutral improvement on audit techniques. It offered the means by which auditing was made amenable to statistical evaluation and in so doing, also being suggested here, provided the earliest foundations for empirical research designs. The advent of statistical sampling forged a critical intersection between the then audit knowledge base, quantification and the discipline of statistics, opening up the pathway for not just research into the use of statistics in auditing but for such research to travel upon the trajectory of statistically based research in auditing. Statistical sampling offered more than just a new research area of interest. Its emergence as a practice provided the means which enabled audit research to start travelling upon this wider trajectory of empirical accounting research.

When statistical sampling at last emerged in the 1970s, officially within SAP 54 (1972), as a more established versus experimental technique, it did so, intertwined with the very beginnings of the constitution of an audit research arena which was co-made to fit with its emergence. Whilst the first edition of the 'special interest', breakaway auditing journal of the AAA, *Auditing: A Journal of Practice and Theory* was not released until 1981, the origins and launch of the journal had already started in 1976 (Flesher, 1991). This was preceded by the AAA publishing its first Statements on Basic Auditing Concepts in 1973. In a sense, these represented the crystallisation of the formation of a new field of operations around audit research signifying sufficient 'demand' for and interest in audit research and the pooling together of a distinct body of knowledge within a separate institutional outlet.

The beginnings of a new arena had thus become formulated. However, it was only through the advent of statistical sampling that the audit research arena was made so. With the emergence of such an arena as a more distinct field of operations, the pre-quality emergent constellation became in this way formed.

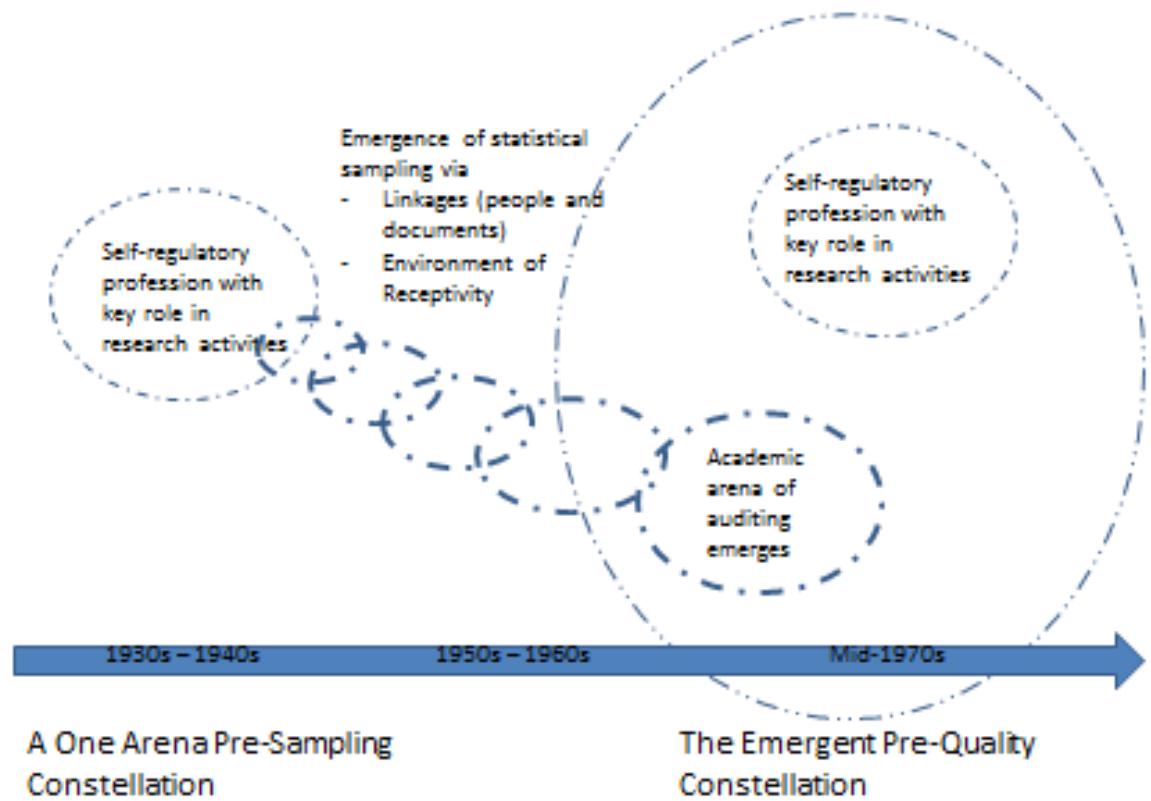
The implications for the audit quality discourse will be considered next in section 3.6.

3.6 Discussion

This chapter has examined the many historically contingent and diverse elements which were required to come together to enable the rise of statistical sampling techniques within auditing. Drawing upon Burchell et al's (1985) notions of the arenas and constellations has helped make visible some of the pre-conditions for this emergence, such as an environment of receptivity constituted by the rising decision sciences, a problematization of the lack of uniformity with audit practice, a collaborative environment and an emergent concern of practice efficiency. However, even then, an environment receptive to scientific developments would not have been sufficient to enable the rise of statistical sampling – its practical implementation highly problematic. Many connections were required to be forged between ideas, actors and disciplines, alongside a re-affirmation of the role of professional judgement and a programmatic promise of its defendability to at last enable its rise. Critical linkages were carried in the form of people and documents which only through them were the connections crystallised. In so doing, however, the arena(s) upon which the constellation is constituted became re-formulated within a concurrent and transformative process.

This relationship between the pre-sampling and pre-quality constellation, transformed via the rise of statistical sampling can be depicted in the following diagram. Figure 3.1 attempts to show how over time, the one-arena pre-sampling constellation evolves, through the advent of statistical sampling in the 1950s and 1960s, into the beginnings of a two arena constellation comprised of a self-regulatory profession and a new academia arena of operations. As this chapter has examined, it was through statistical sampling that this new academic arena of operations emerged. This form of constellation has been thus labelled an emergent constellation to highlight this dynamism involved. Further, it is the argument of this thesis that this dynamism is dependent upon the mechanism of linkages to connect the disparate ideas in order for successful action – here, the evolvement of a new practice, to obtain.

Figure 3.1 Formation of pre-quality constellation via statistical sampling



Burchell et al's (1985) original conception of the 'constellation' was defined as the 'very particular field of operations which existed between certain institutions, economic and administrative processes, bodies of knowledge, systems of norm and measurement, and classification techniques' (p. 400). Their model consisted of three 'arenas', constructed for purposes of illustration and analysis, each marking out a particular 'field of operations', and defined as 'complexes of issues, institutions, bodies of knowledge, practices and actions' (p. 390). Together, the totality of relations which existed between the arenas formed the constellation of pre-conditions which enabled the value-added event in the UK to arise – a one-off event made possible by the historically contingent and specific conditions of one particular moment in time. Once the conditions started to unravel, the value added event which was held together through the relations of the constellation similarly came to pass.

This chapter has drawn upon these notions of the arena and the constellation in helping to make visible those pre-conditions which enabled the rise of statistical sampling within auditing. But in doing so, it has also sought to develop further the notions of the arena and the constellation. Specifically, this chapter has attempted to show (as this thesis will continue to do), that the constellation, with respect to audit quality, is not only constitutive of the arenas but also dependent upon a transformative process whereby the arenas themselves come to be constituted and/or reformulated. In this chapter, an entirely new arena of operations was formed (hence, an ‘emergent’ constellation). The arena and the constellation are mutually constitutive. But furthermore, this particular facet is dependent upon key linkages to make concrete the connection of different ideas and its attachment to the quality discourse. Within this constellation, these linkages which connected ideas from statistics and brought them into auditing, took the forms of people and documents. Together, it is in this way that we can come to think of the audit quality constellation as having a dynamic element and being constantly in motion. The arenas upon which the constellation is constituted are not stable and fixed, ready to be identified and observed. They are co-made along with the formation of the constellation and therefore any stability achieved will likely be temporary. The mutually constitutive aspect of both the arena and constellation, being also dependent upon linkages to ‘capture’ particular ideas, almost with an inadvertent element, ensures a constantly shifting dimension.

This finding allows us to start unpacking more concretely the dynamics of accounting change, opening up the possibility of explaining the means and mechanisms of how and why the notion of quality changes through time. In this constellation, we can see already how the constellation was dependent upon both the constitution of an arena *and* many forged connections – hardened by the linkages which solidified them and were required in order to overcome significant obstacles. The linkages in this episode played a critical role by crystallising the connections of disparate ideas, through a variety of work such as adaptation, collaboration, rationalisation and repetition. This identifies some of the precise mechanisms by which some connections come to fruition, and whereas others do not.

The examination of the Trueblood and Cyert collaboration allowed us to observe how ideas outside of auditing influenced the thinking of the authors and how ideas from afar were then made to be relevant for auditing, thereby allowing the transfer of ideas into a field. In so doing, it showed that connections, of ideas, actors and disciplines are made and are not natural. Clearly, the interests of the key actors played a role – Trueblood spent a year as Visiting Ford Distinguished Research Professor at by then named Carnegie-Mellon

University in 1960, a time he recounts as one of the most enjoyable of his career⁴⁴, indicative of an academic ‘pre-disposition’ within him. Indeed, his appointment was touted as ‘another major step towards strengthening the ties between academic research and the practical application of that research in business’ (from Bryson, 1996, p. 145). The institutional perspective of Carpenter and Dirsmith (1993) may also help explain why most of the large firms became particularly involved in advancing their own research efforts. And Power (1992) has argued through an analysis of the pre-history of sampling that sampling ‘develops to rationalise practices that had been in place for some years and to invest auditing with a new scientific authority’ (p. 37).

For current purposes, however, it is not only the interests based argument of the firms, or even specific actors, and their role in enabling sampling which is of interest. The analysis goes beyond this and the focus is on the totality of heterogeneous elements which were required in order for the constellation to form which is being highlighted, along with a wider argument regarding the very important role of linkages and in particular, the precise nature of their work in enabling accounting change. The totality of heterogeneous elements of course includes the roles of key alliances but of equal significance are those pre-conditions which enabled these alliances to be made central, such as the environment of receptivity to ‘scientific’ developments and an environment of collaboration which made the alliances even possible. It is within this consideration that we can start to see how even the earliest notions of quality can be particularly fragile – being both made by the coming together of these elements but also dependent upon the nature of how the elements become connected (linkages) and in this case, also the constitution of a new arena of operations. Here, a technique which emerged from an inter-disciplinary alliance between auditing and statistics provided a clear impetus for academic research, altering the trajectory for what is normally understood to be an independent field of operations.

This suggests that the identification of the arenas and their intersections with the social are not enough. Restricting the analysis to just the totality of relations in the constellation would not be sufficient to unpack mechanisms of change beyond general intersections with broad social movements. By tracking and examining these relationships – between and within the arenas, and between the arenas and the constellation, throughout the changing notions of quality, we can identify the different forms these connections can take, including any mutually constitutive or recursive properties. Therefore, beyond the mechanics of

⁴⁴ Biographical details within the introduction of Trueblood as new AICPA president (Sept, 1965), from the Deloitte archives available at:
<http://clio.lib.olemiss.edu/cdm/ref/collection/deloitte/id/35800>

accounting change, the relationship between regulation, practice and academia can also start to be unlocked as well.

Finally, this analysis has showed how the emergence of statistical sampling within audit carried with it the roots of quality ideas and how the means by which these ideas were carried into the field were entirely made as opposed to naturally occurring. Indeed this analysis shows that the high profile failures of the early 1970s which were to follow were *preceded* by the most significant developments in statistical sampling, challenging the commonly understood perception that quality concerns within audit have been a direct consequence of such failures - the failures evidence of some efficacy issue within the audit. Any impending litigation in 1960s may have heightened concerns of defendability, however, defendability alone does not 'make' quality – its make-up which already can be seen being comprised of a number of different and shifting elements, including a number of ongoing tensions (see chapter one) of which defendability is but one. This analysis starts to make visible how even the very beginnings of quality was constituted and in doing so, provides the basis for seeing how it is continuously re-made. In using the constellation as the analytic and confining ourselves strictly to this analysis, it allows us to put aside any a priori assumptions or understanding of what quality may or may not be which can so often become further entangled with the more colloquial meaning of the term. Even with this episode, we can start to see how there was nothing natural or inevitable from either quality's conversion from the manufacturing domain to auditing, or its constitution from a variety of heterogeneous elements including actors, alliances, social movements, parallel discourses and much else. As Pflueger (2013) also observed in his examination of making health care quality calculable:

This highlights the essential fallibility and fragility of changing concepts of quality. As based not in some ever more precise uncovering of quality's true essence, but in the chaotic and even sometimes happenchance interaction of diverse elements...(p. 106).

Chapter six will give greater consideration to the meaning and importance of such a constitution. For now, it is put forward that this conceptual heritage is also important as it would come to shape later conceptualisations of the problem of quality which, as we will see, has further implications through the privileging of certain 'solutions'. We will now turn to the examination of the explicit emergence of quality within the auditing discourse which, perhaps of no surprise given this conceptual lineage, appears under the guise of quality control.

Chapter four

Constellation two: The emergence of quality and the rise of peer review (1970s – 1988)

4.0 Introduction

Men invent responses to Quality, and among these responses is an understanding of what they themselves are. You know something and then the Quality stimulus hits and then you try to define the Quality stimulus, but to define it all you've got to work with is what you know. So your definition is *made up* of what you know.

- Pirsig (1974, p. 334, emphasis added).

The early 1970s were a period of intense regulatory institutional change in the US, which saw the establishment of the Financial Accounting Foundation and the Financial Accounting Standards Board in 1972. A number of high profile failures had outwardly triggered a series of congressional hearings, institutional changes and a new focus on the 'quality control' of audit firms in the 1970s. In 1977, the AICPA established the Public Oversight Board to oversee its two newly created practice sections and to oversee the newly established peer reviews of firms. Whilst membership to either practice sections was voluntary, this reorganization would prove to be critical in the road towards mandatory peer review (Fogarty, 1996) which was, despite initial resistance from the profession, overwhelmingly approved in 1988. During this period also, in 1981, DeAngelo published her seminal article on Auditor Size and Auditor Quality which argued analytically that audit quality was positively associated with audit firm size. This paper unlocked an entire research agenda utilising firm size, and other singular variables, as a proxy for audit quality. It was significant also in that quality, as an object of concern, had now emerged and been made visible within each of the three arenas of regulation, practice and academia. This was a critical step in enabling the discourse to intensify.

Following on from chapter three which examined how initial ideas of technical quality permeated the audit field through the rise of statistical sampling, and in so doing concurrently re-shaped the constellation, this chapter examines the explicit emergence and rise of the notion of quality itself within the audit field and how this, through the advent of peer review, also re-shaped the constellation. This chapter takes place in the US from the early 1970s onwards and focuses on the key developments which led to the introduction of mandatory peer review in 1988. Peer review, a compliance based measure by which 'peer' (external) audit firms would review audit firm working paper files, was promulgated as both a key solution to regulating quality as well as the core tenet of the profession's self-regulatory

efforts. At the time, this was a significant intervention from the in-house reviews which had then been taking place and its implementation was a highly controversial development.

Whilst quality emerged as an object of concern during this period, this emergence and its manifestation within each of the arenas took place in very different ways. Through the focal point of the rise of peer review, this chapter seeks to investigate the notion of audit quality by analysing the conditions of this emergence. Specifically, this chapter will investigate how quality became implicated within the relays and intersections of a number of competing tensions, logics and discourses surrounding the audit and in becoming so fashioned, facilitated the emergence of peer review as the ‘logical’ solution to overcoming very historically contingent issues of both practice and regulatory concern. In so doing, this chapter aims to cast some analytical light on the nature of quality’s constitution.

In adopting the theoretical framework and methodological approach set out in chapter two, this chapter draws upon Burchell et al’s (1985) notions of the arena and the constellation to not only investigate those pre-conditions which led to the emergence of peer review but also that which was then enabled by this emergence. As in the rise of statistical sampling examined in chapter three, peer review was not in itself a neutral technology and its emergence concurrently re-configured the arenas upon which the constellation is constituted. In this respect, this chapter seeks to develop the notion of the *reformation* constellation. Reformation constellations refer to those constellations whereby the dynamism can be traced to an existing field of operations becoming differentiated into more distinct and separate arenas. Specifically, this chapter will show how, *through* peer review, the practice arena became reshaped as a self-regulatory model of peer review and the separation of regulatory activities from that of professional practice as a more distinct arena of operations became further reified. Further, we will also see how the rise of audit quality within the academia arena, also emergent from this episode, concurrently set off a new arena of research operations specifically on audit quality – another example of an emergent constellation (see chapter three) nested within this wider constellation. Together, these developments highlight yet again the different ways in which we are able to start to reconceptualise the audit quality constellation as being dynamic.

Moreover, it is put forward that this present constellation, and therefore attendant dynamism, are once again dependent upon a number of linkages to connect disparate ideas. Through the mediums of people or documents, these linkages connect ideas together and attach them to the quality discourse, thereby crystallising these connections. These linkages can shape not only the conceptualisation of the quality ‘problem’ but also the solution which emerges, in this case into that of peer review. These linkages therefore have a central role in the audit

quality discourse, not only in carrying specific ideas into the discourse and making them more concrete but also in shaping the constellation into the specific form in which it emerges.

More specifically, this chapter seeks to show how quality emerged during this period at the intersections of very particular beliefs and ideologies regarding regulatory ‘styles’, a continuing predilection with the issuance of standards, rising public expectations, an emergent distinction of firms based on size and further large scale failures which placed pressures for visible regulatory and practice action. It was at the crossroads of very specific tensions in which quality became implicated and from which it emerged. These tensions included the pressure to demonstrate a regulatory response against a rising ideology of deregulation, a related predilection of issuing standards for performance against a continuing discourse of the need for judgement, and the pressures of making an indeterminate, subjective object such as quality ‘workable’ within the rising trajectory of quantitative research (see chapter three). For the regulatory arena, the emergence of quality derived from a systems-based conception and essentially that of a problematization of quality control of the firm. For the practice arena, quality emerged out of a very specific working papers and educationally focused review programme from within the profession. Within academia, the emergence of quality derived from an economics based conception, proxy-able by single variables such as firm size and others.

Consistent with chapter three, this chapter attempts to show that the developments in the audit quality discourse during this period were not simply logical and inevitable events which followed on naturally from the high profile failures of the time. A host of heterogeneous and historically contingent elements came together, at times in an almost inadvertent way, in order to form some of the pre-conditions which enabled the rise of peer review. And through which the discourse on quality was implicated. Indeed, this progression towards peer review coincided almost entirely with concurrent developments within a wider quality movement more generally. Garvin (1988) has organised the evolution of a wider ‘managerial’ quality movement into four different phases of which the transition between (statistical) quality control and quality assurance regimes overlapped significantly (timewise) with the current developments within audit being examined. This brings into further view the impact of wider discourses and developments on the audit quality debates. However, beyond the influence of such wider social movements, alignments between actors, ideas and arenas still needed to be forged in some way, to shape the rise of audit quality in the form in which it emerged. This, it is put forward, only became possible through the linkages also being currently investigated.

The remainder of this chapter is set out as follows. Section 4.1 will examine the nature of the competing discourses, tensions and logics surrounding the audit in the early 1970s, from which quality control emerged as an object of concern. Section 4.2 will develop the notion of the *reformation* constellation by examining how the advent of peer review concurrently reshaped the constellation through the re-defining and differentiation of the regulatory and practice arenas. Section 4.3 empirically examines the linkages which connected the ideas to the notion of audit quality and in doing so, overcame some of the significant, initial reservations within practice to the adoption of peer review. The focus in this section will be on the precise nature of the linking work which is entailed in crystallising connections. Section 4.4 will include a discussion of the newly reconstituted constellation, how we can start to reconceptualise the constellation as being dynamic, an initial consideration of some of the implications of the means by which quality was made visible during this period, and what this analysis has started to inform us about audit quality. Section 4.5 contains a short epilogue.

4.1 The emergence of audit quality

In the late 1960s and early 1970s, a number of celebrated failures⁴⁵ provoked a crisis of confidence within the profession which have been well documented (e.g., see Zeff, 2003a). The very public nature of the failures sparked congressional scrutiny and a number of sub-committees were formed to investigate the profession and its institutional structures (see Appendix A for timeline of events and developments relevant to this chapter). In addition to the formation of the FAF and FASB, the highly controversial staff study of the Metcalf Commission (1976) entitled *The Accounting Establishment* was severely critical of the profession and in particular the dominance of the then Big 8 firms, calling for amongst others, an independent oversight board which directly threatened the profession's self-regulatory status. A separate subcommittee led by John Moss was convened to investigate the structure and responsibility of federal regulatory agencies who challenged the only newly formed FASB on its independence. In part response, the AICPA launched the Commission on Auditor's Responsibilities (1978) led by Manuel Cohen to re-examine the role and responsibilities of auditors.

The 1970s thus marked the start of a particularly difficult period for the accounting profession. In addition to the very public nature of these failures, litigation against audit firms started to increase which in turn led to elevated professional liability, insurance and

⁴⁵ For examples, see failures of Penn Central Transportation Company (1970), BarChris Construction Corporation (1968), Continental Vending (1970) and Equity Funding Corporation of America (1973).

incorporation concerns (Burton, 1971, p. 48). Litigation also heightened yet again the issue of the defendability of audit work which increased an emphasis on the working papers of audit files (Olson, 1970). Further, the courts had already started to take on a role in determining ‘appropriate’ audit procedures (i.e., establishing procedures for the confirmation of receivables and inventory following the McKesson & Robbins failure of 1938), effectively imposing and defining new audit responsibilities through legal rulings in the aftermath of litigation. The courts also started to provide their own interpretations of auditor responsibilities in the absence of specific professional standards to the contrary (see United States v. Simon, et al (Continental Vending), 1970), which heightened an already increasing predilection for the setting of standards (see chapter three).

The difficulties discussed above added pressure on the profession to act and two very influential study groups were convened. The Trueblood and Wheat Committees were convened in 1971 by the AICPA to report on the objectives of financial statements and on the structure of the standard setting process respectively which very quickly led to the FASB being established. Neither one of these reports dealt explicitly with issues of ‘quality’⁴⁶, however, some of the underlying ideologies of the time can be observed from their reports.

The Wheat Committee had initially been tasked with evaluating how accounting *principles* should be established although this was deemed problematic early on by the Committee. The Committee found the term accounting principles to be elusive and recognised that ‘before a judgment can be arrived at as to how accounting principles should be established, it is necessary to inquire about the scope and nature of the task. What does ‘the establishment of accounting principles’ mean?’ (Wheat, 1972, p. 13). An interview with David Solomons, a professor of accounting and member of the Wheat Commission published in the Journal of Accountancy clarified as follows:

I have thought for a long time that the word ‘principles’ was a slightly pretentious term in accounting. I think we know what principles are in the natural sciences. But accounting arrangements are clearly man-made. There is no one ‘right’ way of proceeding. My own view is that ‘principles’ is too strong a term to describe what a body like the Accounting Principles Board is doing when it issues pronouncements on accounting procedures or methods. ‘Standards’, though, is a totally unpretentious sort of term (Nolan, 1972, p. 18).

By further contrasting the elusiveness of the term principles with the work of the then Accounting Principles Board (APB), the Committee determined that the work of the APB

⁴⁶ A search for the explicit term ‘quality’ within these reports returned nil results.

was more closely aligned with the establishment of accounting *standards* (ibid, p. 19) thereby releasing them of the predicament of defining principles. This predilection for setting standards, over establishing principles, was also observed within the Trueblood Committee which prioritized within its study the ‘creation of a functional framework on which accounting *standards* can be based’ (Trueblood, 1973, p. 9, emphasis added). Three members of the Trueblood Committee, Trueblood, Cyert and Gellein were also active within the developments in statistical sampling (see chapter three) and perhaps this prioritising of standards, due not least to its allure of being more defendable, was not altogether surprising.

Further evidence suggesting this predilection for the use of standards was summarised in a speech made by then SEC Chairman Garrett, Jr. in 1973 to the AICPA. There, he referred to the then heightened issue of professional liability and opted also for the issuance of standards as a potential response:

While the whole problem of professional liability, in my opinion needs re-examination and imaginative thinking, *the establishment of clearer standards* should provide protection as well as guidance (Garrett, Jr., 1973, p. 14 emphasis added).

Indeed, this preference for the use of standards to set performance guidelines of some sort was not just confined to the SEC or to AICPA study groups – practitioners themselves were also calling out for standards to help settle uncertainty regarding performance criteria, particularly in the face of rising expectations. A Price Waterhouse partner surmised at the time: ‘We are living through a period of unusual uncertainty, dissatisfaction and unrest...one of the by-products of this is a tendency to dissect and question the effectiveness of virtually every institution’ (Tietjen, 1971, p 69). He further called for the existing conceptual model of financial reporting to be replaced with up to date ‘[accounting] standards’ (p. ibid). As a further manifestation of this predilection at the time, the 1970-71 Committee on Auditing Procedures issued more Statements on Auditing Procedures than any other committee had before it (Fitzemeyer and Carmichael, 1972, p. 77).

Alongside this preference for the issuing of standards in the early 1970s was an emergent concern with rising societal ‘expectations’ at the time. Ongoing struggles regarding the purpose and role of the audit had given way somewhat to talk of the ‘expectations’ of an audit. A practitioner observed in early 1970, in an article titled ‘What’s expected of an audit?’ (Rea et al, 1970), that ‘there seems to be a feeling on the part of some people that an auditor is primarily a bloodhound engaged in tracking down embezzlers’ (p. 76). The author continued with an attempt to clarify yet again the purpose of the audit (ibid) echoing long-

standing debates on the role and responsibilities of the, being now framed against a question of ‘expectations’.

Later on that same year, Trueblood (1970) published an article in the *Journal of Accountancy* on ‘Rising Expectations’ calling for the profession to scrutinize its whole structure ‘in the framework of rising expectations’ (p. 38) such that the profession’s responsibilities could be met under these new demands. Trueblood argued such rising expectations were caused by ‘technology in general and communications in particular’ (Trueblood, 1970, p. 35) which together ‘intensified moral and ethical problems’ (*ibid*). Within his plea, Trueblood spoke also of the performance gap between these rising expectations and the accounting profession with particular respect to professional responsibility codes and disciplinary procedures (p. 37). This was followed by increasing articles in the *Journal of Accountancy* discussing ‘expectations’. In an excerpt of a report made to the AICPA council by Horton, a practitioner and Chairman of the Committee on Auditing Procedure, also titled ‘Rising Expectations’, Holton demarcated three categories of rising expectations: that arising from the public, the profession, and the committee itself (Fritzemeyer and Carmichael, 1972, p. 77) which together was contributing to the ‘credibility crisis’ in auditing in particular (*ibid*, p. 78).

In 1974, Carl Liggio, then General Counsel for Arthur Young & Company published an article in the *Journal of Contemporary Business*, entitled: ‘The Expectation Gap: The Accountant’s Waterloo’, which was then reprinted in July 1975 in *The CPA*. In that article, Liggio, who has since been credited with coining the term ‘expectations gap’ (Porter, 1993), argued as follows:

The expectation gap is at the heart of the criticism of the profession. Only when this gap is narrowed and reasonable levels of expectation are established as guidelines for professional conduct will the litigious environment in which we exist be sharply narrowed... (p. 23-24).

Also in 1974, in the face of the criticism and litigation, the AICPA established the Commission on Auditor’s responsibilities (the ‘Cohen Commission’) and included in the terms of reference the explicit mandate to consider ‘whether a gap exists between what the public expects or needs and what the auditors can and should reasonably expect to accomplish’ (p. xi). This played a key role in reifying the notion of the ‘expectations gap’ in the discourse.⁴⁷

⁴⁷ After the Cohen Commission, findings of several studies from the US and internationally featured the expectations gap (see Humphrey, 1997, p. 10 – 13). In addition to this, academic interest also

Irrespective of whether or not the expectations gap is imaginary, its existence in the discourse has prevailed since this emergence in the early 1970s. Kinney (2005) in his summary of audit regulation developments over the previous 25 years argues also that the expectations gap is a ‘constant’ within the history of audit regulation which has served as an essential signal to regulators in difficult times. Whether or not the expectations gap is actually ‘constant’ empirically can be debated, however, the consistency in at very least its prevalence served as an ongoing source of tension for the profession especially at that time.⁴⁸

Clearly, these concurrent pressures were interrelated. The failures had brought into regulatory question the roles and responsibilities of auditors, increased litigation had exacerbated practice concerns of defendability and professional liability, and increasing uncertainty regarding the expectations of the audit intensified the extant predilection for standard setting despite this being at odds with the recurring discourse on the importance of professional judgment (e.g., Rosenfield & Loresen, 1974; Frisbee, 1950). Even the debates surrounding the expectations gap became interconnected with these issues with Liggio himself attributing the gap to the ‘different expectation levels as to the both the *quality* and *standard* of the accounting profession’s performance and what it is expected to accomplish’ (1975, p. 24, emphases added). It was in and amongst the convergence of these pressures and within this difficult environment that a new issue of an accounting firms’ ‘quality control’ emerged.

This marked the explicit emergence of quality as an object of concern within audit and materialized as a quality control problem of the firms. An early article by John Burton (1971), a professor of accounting and finance at the Columbia Business School who later went on to become Chief Accountant of the SEC, based on a speech given to the 1970 Annual Partners Meeting of Arthur Young & Company commented as follows:

In a number of *large firms*, there has been recognition of the need for formalized control systems and a willingness to put up with the associated personal inconveniences. But as I look at the profession as a whole, I am not convinced that such recognition is widespread...It is my judgement that, for the profession as a whole,

appears to have been sparked by this emergence and audit research articles with ‘expectations gap’ in its title or abstract featured much more prominently starting from the early 1990’s (for example, see Porter, 1993; Humphrey et al, 1992; Monroe and Woodliff, 1994; Koh and Woo, 1998). This supports a general argument to be made later in this thesis that the academia arena, within this area of audit quality, tends to ‘follow’ that of regulation and practice.

⁴⁸ To this point, Power (1997, p. 9-10) has suggested that the expectations gap, in serving to support an ambiguity about the audit process and its objectives, supports practitioner discretion and in this way can be seen as ‘a resource for the auditing field and not merely a problem’ (p. 10).

the *quality control problem* remains a serious one (Burton, 1971, p.48, emphases added).

This speech was significant in two respects. First, it marked one of the earliest calls for firm quality control, interest of which quickly accelerated from therein. Articles and speeches quickly started to appear in the Journal of Accountancy, honing in on ‘quality control’ as a central issue, particularly from the SEC who were facing public pressures to act. In SEC Chairman Casey’s 1972 speech, he also called for the profession to establish ‘an improved professional *quality control system*’ (News Report, 1972, p. 12, emphasis added) and just a short time later, in 1973, a speech by the next SEC Chairman Ray Garrett, Jr. to the AICPA concurred with this assessment and summarised the convergence of some of the ongoing pressures as the manifestation of a ‘demonstrated need’ for quality control (Garrett, Jr., 1973, p. 14). In a separate speech given by Commission Sommer, Jr.’s to an AICPA conference in 1974, he reiterated the need for an ‘improved systematization of audits, better quality control over them’ (News Report, Feb 1974. p. 9). By as quickly as 1974, now Chief Accountant of the SEC, Burton, had elevated the issue of quality control to ‘high priority’ for both the SEC and AICPA (Statement in quotes, July 1974, p. 59).

Second, and more subtly, Burton’s speech alluded to an adjacent and interrelated issue which had also started to emerge at this time regarding the hierarchical distinction of firms on the basis of *size*. Burton credits the *large firms*’ recognition of the ‘need for formalized control systems’ and attributed these developments to the corporate merger movement (audit firms included), with the size and growth of firms contributing to difficulties in personal communication and *depersonalization* (Burton, 1971, p. 48, emphasis added). He further implied that outside of these large firms where depersonalization had led to a creation of formalized control systems, a ‘deficiency’ existed amongst the rest of the profession – likely the small and medium sized firms without the expertise, resources or perhaps even need to adopt such an approach. Irrespective of the validity of these perspectives, the suggestion that the *size* of firm had a bearing on *quality control* matters was raised and would become interlinked with a sensitive and rising debate within the profession itself regarding the competitiveness of small and medium sized firms (discussed further below). Indeed, in time and by as soon as the late 1990’s, Ramirez (2010) observes how a correlation between size and hierarchical rank, as primarily a matter of organizations as opposed to individuals, would be developed within the audit firm professional landscape across many industrialized countries.

The calls for quality control, were not independent of suggestions of the means by which improved quality control could be achieved. They came, perhaps unsurprisingly given the tensions outlined above, concurrently with calls for more standards in the area. From Casey

were suggestions to include ‘a more active articulation of *standards* of supervision and control to assure responsibility at all levels’ (News Report, Nov 1972, p. 12, emphasis added). From Garrett, Jr.’s (1973) speech:

Whilst I am convinced that the quality of most auditing work is quite high, we recently have seen an increasing number of cases of substandard work....*guidelines* in this area seem possible, and we have attempted to foster that kind of an approach. (Garrett, Jr., 1973, p. 14-15)

In addition to the suggestion of standards in the area, the emergence of quality control as an issue also came with further calls for systems of surveillance to review the work of auditors. In Burton’s early speech given in 1971 mentioned earlier, he followed up his calls for quality control with:

The responsibility of the profession as a whole for maintaining an adequate system of surveillance over the professional practice of accountancy has also been largely ignored...There is no *continuing review of the work* or the competence of members of the American Institute of Certified Public Accountants (Burton, 1971, p. 50, emphasis added)

It is significant here to note the timing of this comment, given in the same speech which problematized early the issue of quality control. This marked some of the very early intersections between the emergence of quality within audit, as a systems-based firm problem of quality control shaped by the predilection for the promulgation of standards, *and* the call for systems of surveillance for the auditor’s work.

Indeed, this concurrent call for standards and or surveillance regimes to tackle the issue of quality control continued to appear in the discourse. In Casey’s (1972) speech, he also added ‘that there should be more ‘formal mandatory self-policing’ so that ‘every professional practice is reviewed periodically by other professionals’ (News report, Nov 1972, p. 13). Burton’s 1974 speech as Chief Accountant added to the high priority of improved quality control, ‘the problem of professional discipline’ (Statements in quotes, July 1974, p. 59). As quickly as the end of 1974, the AICPA released Statement on Auditing Standards No. 4 - Quality control considerations for a firm of independent auditors, which specifically included requirements for firms to develop provisions for inspection.

Notwithstanding the predilection for the issuance of standards as set out above, this concurrent call for quality control, more standards and ideas of the review of the auditor’s work by another party or otherwise, signifies some of the very earliest moments whereby the emergence of quality came hand in hand with a re-defining of (self-)regulatory activities.

For not only were concerns of quality connected to calls for new standards, they were also being aligned with self-regulatory disciplinary or review measures as well. Indeed, this was one of the espoused ‘benefits’ of having standards – the ability to evaluate performance after the audit had been conducted. Ernest Hicks, a prominent practitioner who was also chairman of the AICPA Auditing Standards Executive Committee, instrumental in the drafting of the initial quality controls standards summarised this as follows:

What is the mission of auditing standards? Let me suggest they have two uses: (1) to communicate, before the fact, the requirements of auditing to people of various sorts...and (2) *to evaluate, after the fact*, the professional performance of auditors in particular circumstances (Hicks, 1974, p. 39-40, emphasis added)

And then, included as one of the nine key elements included within the quality control standard as issued by the AICPA in 1974 was the element of inspection, further clarified as follows:

Policies and procedures for inspection should be established to provide reasonable assurance that the other procedures designed to maintain the quality of the firm’s auditing practice are being effectively applied...In pursuing its quality control objectives with respect to inspection, a firm may use policies and procedures such as *designating persons to make inspections at the office in which they regularly practice or at other offices...*(AICPA, 1974, p. 6, emphases added).

With standards in place and procedures for inspection developed, the leap to external review or inspection of the auditor’s work would have been made far more amenable and possible. Therefore, in conceptualising quality as an issue of quality control, in itself an output of the confluence of different elements and pressures as outlined above, its emergence and conceptualisation came hand in hand with the beginnings of a re-definition of self-regulatory activities. Quality was now defined, not least through SAS 4, very precisely as the output of a systems-based conception of quality control, a clear property of the firm. And quality would be through this conceptualisation also be made amenable to inspection through the establishment of policies and procedures – be that internal inspections from the firm itself, or in time, external. However, despite the very initial seeds of peer review being planted in this way, and coming intertwined with the emergence of quality as a problem of quality control, it would be over another decade⁴⁹ before such a controversial intervention would be implemented as a mandatory measure. Section 4.2 will examine this rise to mandatory peer review in 1988, including the role this emergence would take in concurrently re-shaping the constellation.

⁴⁹ This was symptomatic of how ‘controversial’ peer review was at the time although a further, alternative argument will be developed in chapters five and six in that a chain of linkages was required before successful action could obtain.

4.2 The rise of peer review and the reformation constellation

4.2.1 The origins of peer review

Whilst one view from the outset is that the emergence of peer review was a consequence of the failures of the profession, also under threat of external oversight, to provide ‘sufficient’ audit quality, the discussion in section 4.1 suggests that a number of additional factors converged to also play a role in the form of that intervention which was to come. Again, these influences are important to keep in mind as they helped to shape both the conception of the ‘problem’, and within this constellation in particular, the ‘solution’ deployed to address it. In turn, this predisposed a very particular meaning and understanding of quality.

The concept of peer review was not altogether a new invention within auditing when it started appearing in the discourse with more regularity from the mid-1970s onwards. The initial seeds of the idea have been traced back to as early as 1962 with the AICPA’s practice review committee establishing a program designed to monitor standard practice and reporting (Sperry et al, 1987). In 1971, and quite very separate from the then emergent regulatory discourse on quality control, was a tentative initiative with what was termed ‘firm quality reviews’. With its roots in a working paper improvement project initiated by the Kentucky Society of CPAs to ascertain the extent to which its members were following the guidelines for audit working papers, the Accounting Research Committee upon consideration of the program determined that only the state CPA societies or the AICPA could implement and administer the types of programs being recommended. At that time, the three possible courses of action were determined to be: appointing a separate working paper review committee; drawing a committee from practice review boards on consultation or else, developing a professional development course or program (Rea, 1975). A quality review program, to include a comprehensive review of working papers, was subsequently developed.

Conceived of independently from peer review, the objective of the programme was to review, on a post-audit basis, the financial reports, opinions and supporting workpapers of the auditor in an effort to encourage compliance with generally accepted accounting principles and standards (Grimsley, 1973). A system was set up by the AICPA to co-ordinate the supply of teams to perform reviews of firms practicing before the SEC. Participation in the program was entirely voluntary, and had a fundamentally educational focus. One participant noted the advantage of having the exposure, in times of intense change, of the means to upgrade technical competence and technical quality (*ibid*). Another noted that the opportunity to see what another firm was doing enabled them ‘to learn as much as we were ‘teaching’ if not more’ (Rea, 1975, p. 108). Established in 1971 as the

pilot year, the programme did not garner much support as only a small number of firms had participated in the entire program through to 1974 due apparently to cost concerns. However, feedback in terms of the value of the program from those participants appeared to be very positive (*ibid*), particularly with the constructive and educational approach taken.

Further evidence as to the growing ‘profile’ of peer review could also be seen in wider developments where legislation originally attached to President Ford’s energy bill, had specified that the General Accounting Office could exercise *review* rights over the audits of energy companies and their independent auditors (*Journal of Accountancy*, May 1976, p. 91, emphasis added). During this period, the SEC also started to sanction peer reviews, largely spearheaded by then SEC Chief Accountant Burton, as a remedy for perceived audit deficiencies and to settle disciplinary proceedings against firms. In one such example, in a settlement with Touche Ross, the SEC sanctioned the ‘formulation and implementation of qualitative office review procedures requiring periodic review at least once every two years of all Touche offices … to evaluate and ensure the quality of the audit engagement of such offices’ (*News Report*, April 1974, p. 12). This very significant role Burton played in carrying ideas of peer review into the audit field will be discussed further in section 4.3.

The convergence of these pressures and developments led one practitioner to summarise the well-documented sentiments and heightened situation at the time as ‘Peer review is coming, one way or another. Let’s do it our way and not force the government to do it for us.’ (*Journal of Accountancy*, May 1976, p. 91). The establishment of a profession wide program, the voluntary quality control review program, approved at the end of 1976, was helped in its expediency of emergence by the fact that the profession, coincidentally, already had a ‘quasi peer review programme’ in place – that of the working papers based quality review programme discussed above, which could be quickly and practically leveraged to broaden its scope and reach. Indeed, the Cohen Commission subcommittee report specifically referred to this strategy and in so doing, intertwined the two developments:

“Peer reviews of large, complex firms are probably better performed by another CPA firm that has the experience and ability to conduct a large and complex audit. However, the AICPA’s local firm quality review program, which consists of reviews of working papers and reports by a team assembled from different firms, is a workable alternative” (Cohen Commission, 1978, p xxxiii)

In time, it was suggested that the AICPA quality review program and peer review program became so similar that they were difficult to tell apart (McCabe, 1993). These origins of peer review ideas, however, would soon collide with further discourses which only together enabled the rise of mandatory peer review. We turn to these now.

4.2.2 The problematization of self-regulation

Concurrent with these difficulties of regulating quality, results of the Metcalf and Moss subcommittees as well as the AICPA's Commission on Auditors' Responsibilities (CAR) were released. In those highly influential reports, a consistent concern which explicitly emerged was the profession's ability to self-regulate. In the Metcalf Commission (1976), the report highly criticised the accounting profession and proposed periodic federal inspection of auditors of public companies. In particular, the staff study honed in on the dominance of the large firms in both client work and policy setting activities thereby almost inadvertently reifying yet again the hierarchical distinction of the firms based on size. The report also concluded that the SEC had failed in exercising sufficient oversight to the accounting profession. Senator Moss, a supporter of Metcalf's proposals, went on to introduce legislation to establish a National Organization of SEC Accountancy in 1978 whereby firms in SEC practice would undergo periodic peer review. The legislation also called for an expanded SEC role in the standard-setting process, both of which would have effectively removed self-regulation from the profession. Whilst the legislation was not enacted into law, the centrality of the issue of self-regulation within the debates became deeply heightened.

Whilst, perhaps unsurprisingly, the CAR concluded that the existing structure of a private profession regulated by a combination of private and governmental efforts, including the courts and the SEC was adequate, it went on to concede that 'self-regulatory efforts by the profession can be substantially improved' (News report, April 1977, p. 9). These pressures had already prompted the AICPA in 1976 to formulate a dedicated committee on self-regulation, led by practitioner Samuel Derieux. The committee's efforts on enhancing self-regulation, possibly in anticipation of the commissions' results, were already focused on the establishment of the voluntary quality control review program mentioned above, for CPA firms with SEC practices or those which desired to prepare for SEC practices.

These threats to self-regulation, however, were tempered by not only the significant resistance by the profession⁵⁰, but perhaps even more so by the underlying preference for particular regulatory approaches at that time. This preference of the SEC at the time in the 1970s to exercise an oversight role but to leave areas of standard setting to the profession was alluded to by Trueblood's (1970):

⁵⁰ Members of the profession testifying before the Metcalf subcommittee in general 'voiced opposition to any new legislation affecting the profession and to any proposals granting the SEC greater control over the profession' (News report, July, 1977).

The SEC...has *encouraged* the profession to enjoy a largely self-regulating existence. The SEC has looked to the profession for the formulation of principles in both auditing and accounting (p. 38, emphasis added).

This preference was made explicit by SEC Chairman Casey in 1972, addressing a plenary session at the AICPA:

I'd like to make clear at the outset that it is my personal *preference* to keep the formulation of accounting principles and standards and their implementation in the hands of the profession, subject to the oversight of the Commission' (News Report, Nov, 1972, p. 9, emphasis added).

Even more definitively, Commissioner Sommer, Jr. referred again to this ideal in a speech given in 1974, 'Unquestionably the Commission has preferred to have accounting principles established by the accounting profession's duly constituted authorities' (Sommer, Jr., 1974, p. 4). And then further on, he refers to the ideologies underlying the Wheat Commission proposals and summarises that at the base level was:

a belief that in general it is better to leave such matters primarily to the private sector with governmental oversight only. The Commission has accepted this judgment and endorsed the creation of this new framework' (Sommer, Jr., 1974, p. 6).

Notwithstanding the contemporaneous pressures of congressional scrutiny, together these passages underscore an underlying preference of regulatory approach which was not inconsistent with the fundamental ideologies of the concurrent rise of neoliberalism at that time (Harvey, 2005, p. 3). Whilst President Reagan was not elected until 1980, he galvanized a social movement which had already commenced in the 1970s. The ideology that political and economic ideals could be achieved through free markets saw much deregulation throughout industry during this time which was inconsistent with the external oversight of the accounting profession being at that time threatened. A concurrent investigation by the Federal Trade Commission into the competitiveness of the profession in 1977 also signalled this rising influence of a free markets ideology. Therefore, whilst the threat to self-regulation was a significant concern, the idea of external oversight conflicted with the regulatory ideology of de-regulation. This conflict served as one of the key tensions which would come to have a role in shaping the form of intervention into that of peer review.

4.2.3 Emergent traces of calls for transparency and accountability

Closely connected to rising societal expectations were traces of the emergent demand for transparency and accountability, exacerbated first by the Watergate political scandal of the

early 1970s and then followed by a number of cases of illegal campaign contributions and bribes paid to government officials by corporate management. This heightened an issue of corporate accountability⁵¹ and the role of the auditors in detecting and reporting such illegal activity. Even before this, however, calls for the accountancy profession to lift its veil of secrecy (Carmichael, 1977) were starting to emerge and measures were being suggested within new institutional proposals to make more *public* the activities of standard setting and committee work. One of the key recommendations of the Wheat Commission was that the new standards board, when so created, should ‘to the fullest extent practicable, carry out its functions in *public*’ (Wheat, 1972, p. 9, emphasis added). This was elaborated on as also making publicly available transcripts of hearings, minutes of meetings, copies of briefs and position papers (*ibid*). Similarly, the charter given by the AICPA to the Trueblood Committee on financial statement objectives included the requirement that public hearings be held, public records be kept of significant proceedings available to all and that conclusions reached should be explained in the light of the entire public record (Trueblood, 1973, p. 68).

In time, these suggestions would permeate the quality discourse as well. The 1975 SEC Chairman, Ray Garrett, Jr. announced at a conference on SEC developments the SEC’s plans ‘consider the desirability of requiring accounting firms to make public their quality control procedures and to provide a means for their doing so’ (News Report, Feb 1975, p. 10). Commentators wrote that ‘In a free society, no institution vital to the public interest can maintain a claim to legitimacy if its affairs are shrouded in secrecy’ (Carmichael, 1977).

It is put forward that these shifts in societal expectations and demands put further pressure on the shape and nature of the solution to come. It helped create an environment whereby the opening up for view of very private firm policies, procedures and audit working papers could be made thinkable and hence, in time, possible. When quality reviews came, it came attached with calls for the making public of the reports which in itself, also paved the way for peer review. Quality reviews and the reporting therein would need to be conducted by suitably qualified individuals (or firms). The initial voluntary quality review program approved by the AICPA governing council in 1976 stated: ‘An integral part of the quality review program is making available to the public first the names of participating firms and then reports on the audit review’ (News report, June, 1976 p. 10).

⁵¹ See for example: ‘Corporate accountability and illegal acts’ (Carmichael, 1977, p. 77) and Chapter 2 of the Moss Committee report which includes as one of its three major sections ‘the SEC and corporate accountability’ (US House of Representatives, 1976). The title of the Metcalf Commission was: Improving the accountability of publicly owned corporations and their auditors (US Senate, 1977). This ‘accountability turn’ was also seen elsewhere outside of the US, such as in the UK (see Ramirez, 2013).

4.2.4 The re-constitution of the constellation: a reformation constellation

In chapter three, we examined how the emergence of statistical sampling, which carried with it those very early ideas of technical quality into the audit field, concurrently re-shaped the constellation. That chapter focused on the conditions leading to the formation of a new academic arena of operations. Regulatory and practice operations throughout that episode were still closely held under the stronghold of the profession. Within this episode, we will examine how the extant beginnings of the separation of regulatory and practice activities into more distinct and differentiated fields of operations were further reinforced through the advent of peer review. In so doing, we can gain a greater understanding of the means by which the arenas and the constellation are mutually constitutive, contributing to the dynamism of the constellation and hence the changing nature and meaning of quality. At a more detailed level of analysis, this chapter will also show how the advent of peer review, promulgated as an answer to quality control and self-regulation concerns, in turn re-defined the concept of self-regulation altogether, a form of mutual co-constitution of its own.

The seeds of arena separation

As mentioned in the introduction to this chapter, the early 1970s were a period of intense regulatory institutional change in the US, which saw the establishment of the FAF and the FASB in 1973 with respect to accounting standard setting as bodies independent from the Institute. These developments were a marked change from then extant Accounting Principles Board, a committee of the Institute which had gradually been losing the confidence of industry, the large accounting firms and the SEC (see Zeff, 2003a). The Wheat Study Group recommended in 1972 the ceding of authority to an independent body outside of the accounting profession, with full time appointments and a large research staff, the funding of which was to be provided by FAF. Notwithstanding this new structure of independent bodies, the SEC continued to exert its oversight powers by issuing 70 Accounting Series Releases, compared with 126 from the period of 1937 – 1972 (Zeff, 2003a, p. 199), being active within the area of financial disclosures especially and rejecting FASB's statement of accounting for oil and gas exploration.

The loss of the profession's standard setter had other important implications, as observed by Zeff (2003a). The Big Eight firms began to withdraw from an active dialogue over accounting principles and standards due possibly to the increasing 'proliferation, complexity, and technical detail' (p. 200) in FASB's pronouncements and/or else in their belief that their involvement became one of persuading FASB of their views. In addition, accounting academics also started to abandon their interest in policy issues (*ibid*). Without this key dialogue, interaction and actors working across both practice and regulatory issues,

and with new institutional structures in place, the separation of regulatory activities from that of practice, notwithstanding the governance of the profession still falling under that of self-regulation, had already in these ways commenced by the early 1970s. Very quickly thereafter, this separation into two more distinct arenas would be given further momentum once these initial seeds converged with the rise of peer review. In so doing, the constellation became re-shaped once more.

Arena separation becomes further differentiated

Earlier in section 4.1, we saw how the initial emergence of the quality discourse within auditing became intertwined with the development of standards of quality control and the possibilities for inspection of audit work. The idea of peer review was met with significant resistance from the profession when it was first touted as a regulatory measure. However, in the face of severe pressures from Congress, the SEC, and the public, the pressures to act resulted in a voluntary quality control review program, put forward by the AICPA committee on self-regulation in 1976 whereby a detailed review of the audit practices of accounting firms whose clients filed statements with the SEC would be undertaken. This was in effect an extension of the extant local firm quality review program, and had been approved in what then AICPA Chairman Bull hailed as a 'landmark decision' (News report, June, 1976, p. 10). Shortly thereafter, also in 1976, this program was extended to further include voluntary quality reviews of local firms *not* engaged with SEC practice. Speaking about this expanded program, Chairman Derieux stated:

We have concluded also that it is important for the program to include the means for providing assistance to those firms which request it in *organizing* their quality control procedures and in *preparing for participation* in the quality control review program (News report, Sept, 1976, p. 24, emphases added).

Through the problematization of quality control, a concurrent response emerged which was the creation of new structures to assist firms in meeting these quality control requirements. These included options for a quality control system document review, visits to firm offices to review adequacy of documented quality control procedures, and a more technically focused review option which would be the extension element of the extant local firm quality review program. The committee on self-regulation also recommended that additional courses be created by the AICPA to help firms cope with quality control procedures. Finally, in order to assure that participation in the program was being supervised by peers, two subcommittees would be formed to monitor reviews – one for reviews of firms with SEC practices and the other for firms without (ibid).

These recommendations and developments were significant in a number of respects. First, they were the initial mechanisms set up to enable the controlling of the activities of *firms*. Prior to this, the AICPA could only control or discipline the activities of *individuals* (McCabe, 1993, p. 2), primarily through its code of professional conduct. This was a marked change to existing measures which shifted the responsibility of quality, amongst other attributes which had previously been a property of the individual auditor, such as independence, to that of the firm.⁵² Transferring the accountability for quality from the individual to the firm also enabled quality to be made more amenable for checking and inspection. Documentation for firm quality control procedures could be produced, procedures could be checked to ensure they were being adhered to and finally working papers could be checked against quality control standards. All of these were only made to be possible through the conceiving of quality as a quality control issue of the firm. Therefore, the suggestion being made here is that the emergence of quality as an issue of quality control came *together* with these contours of an inspections based regime ‘ready-made’.

In addition, these structures and mechanisms encouraged firms to develop the appropriate documentation in order to comply with standards and procedures, a focus on which would be placed during the actual quality reviews. In *organizing* their quality control procedures and *preparing* for the reviews as noted in the quote above, this suggests that the firms themselves could start to be re-shaped into representations which were more amenable for the quality review process. That documentation could be sent in and approved, and courses could be taken to assist with the preparation of this documentation suggests that compliance could be met in a somewhat templated, model-like fashion. Fogarty (1996) has already challenged the extent to which these documents could represent the underlying reality of quality. However, being also considered here is that these documents had a further role and implication – they additionally aided the means by which the separation between regulatory and practice activities could be further hardened. At the very least, those same documents facilitated the division of labour between those who produced the documents and those who would review them.

Indeed, these new institutional structures of quality reviews being performed by peers, the promulgation of standards and the new subcommittees overseeing the reviews had perhaps the strongest implications in terms of the separation of activities between practice and

⁵² Early editions of the Spicer & Pegler Practical Auditing manuals also spoke of the ‘qualities required of the auditor’ (e.g., 10th edition (1951) and repeated in a further five editions up to 1978 when these words were taken out). During this episode, ‘quality’ shifted from being a trait of the individual to a quality control property and requirement of a firm.

regulation. Together with the above, they were the beginnings of the re-definition of the once tightly held regulatory and practice arenas of activities. Already kick-started with the establishment of the FAF and FASB in the accounting standards space, this separation of regulatory and practice activities for the audit space started to become further reified through these new structures. Through this discourse on quality control and the accompanying developments towards peer review, and despite still falling under the auspices of ‘self-regulation’, a parting of regulatory activities from that of professional practice as a separate arena of operations had intensified.

These initial steps were then accelerated through the convergence of congressional pressure both to improve quality *and* self-regulatory efforts, elevated not least by the publishing of the Metcalf Commission in 1976. The solution to this would be found within peer review. In 1977, the profession formally created the Public Oversight Board (POB) to oversee two newly established Practice Sections – one for firms with SEC registered clients and the other without. The POB was formally responsible for the setting and enforcing of quality control standards and overseeing a newly established ‘peer review process’, which was separate to the voluntary quality control review program approved in 1976. With peer review made mandatory for only those firms which elected to join the Practice Sections, the existing Voluntary Quality Review Program only just approved, was at risk of becoming redundant. The AICPA elected to keep the program running for those firms who elected not to join either of the two new practice sections. Henceforth, this program became known as ‘quality reviews’ and the program administered by the newly established POB as ‘peer reviews’.

Ironically, and as an adjacent and interrelated concern to the rise of peer review, these structural developments exacerbated the ongoing concern from small and medium sized firms regarding their competitiveness. In attempting to respond to some of the pressures of the Metcalf Commission through these changes, of which the dominance of the large firms was heavily criticised, the creation of the two practice divisions, possibly inadvertently, accentuated this hierarchy of firms based yet again on size. One requirement for registration with the SEC practice division was the internal rotation of audit partners and as one sole practitioner noted at the time, ‘How does a small firm rotate audit partners when you have but one audit partner?’ (Linden, 1978, p. 36). In the event, this hierarchical distinction would become even further established during the remainder of the 1970s. A ‘small and medium sized panel’ was formed to contribute to the Moss committee hearings and asked for separate representation on the practice sections’ executive committee – formed initially to dispel large firm domination (*ibid*) but as result *furthered* this distinction. By 1979, concern had reached such a level that the AICPA appointed a special committee on small and medium-sized firms, to be again chaired by Dericuex. In it, Dericuex sought the views of

practitioners to identify those factors that placed the smaller CPA firms at a competitive disadvantage. A separate study was also conducted by Arnett and Danos (1979) entitled *CPA Firm Viability*. Based on a survey methodology, the responses were analysed using, amongst others, firm size as one categorisation. These reports essentially concluded that firm size had no bearing on an audit firm's ability to deliver an audit, or on its quality. However, in practice and whilst examined in a different context, Ramirez (2013) highlights how the small and medium sized firms had great difficulties in coping with the quality inspections to come, complaining that they were built on applying templates which were designed by and for the bigger firms (p. 856). In this sense, quality reviews further reified the hierarchical distinction of the firms based on size already growing during this period. The concerns from the small and medium sized firms unresolved within the profession, and this hierarchy became further solidified by the early 1980s⁵³.

As part of the new institutional structure of practice divisions, several additional committees were established including a quality control standards committee to establish quality controls standards, a peer review committee to administer the program of peer reviews and an executive committee to oversee the activities of the new practice sections, with the authority to administer sanctions against firms as well. The quality control policies and procedures to be followed by both programs would be centralised with the new committee on quality control standards, thereby linking the two programs almost inextricably⁵⁴. The overall objectives of the new SEC practice section was to 'improve the quality of practice by CPA firms' and to 'establish and maintain an effective system of self-regulation...by means of mandatory peer reviews [for member firms only]' (AICPA, 1977, Section III) which reflected the interconnectedness and by then convergence of the discourse on regulating quality with that of maintaining self-regulation (the key tenet of which was to promote peer review). Another objective, even more explicitly, was cited to 'enhance the effectiveness of the section's regulatory system through the monitoring and evaluation activities of an independent oversight board [the POB]' (*ibid*).

The establishment of the POB and the practice divisions were deemed critical by Fogarty (1996) on the road leading towards mandatory peer review for the profession. The creation of these structures helped pave the way for mandatory peer review for the profession – by then only what would be an extension of what was already in place but nonetheless still requiring the overcoming of significant resistance from the profession. For now, however,

⁵³ See AICPA (1980), Dericu Committee, page 9 for summary of AICPA efforts to investigate issues related to firm size

⁵⁴ Indeed, as McCabe (1993) observed, the two programs were so similar it was nearly impossible to tell them apart.

these structures further formalized the emergent separation of regulatory activities from that of professional practice as a more distinct arena of operations. With newly established independent oversight boards composed of public members and all the rest as described above, regulatory activities broke further away from the stronghold of professional practice.

Despite these measures, critics remain unconvinced. SEC Chairman Harold Williams was quoted in an interview as follows:

I don't believe peer review by accounting firms alone is credible in the public's eye. It may well be true in substance, but accountants can't inspect each other indefinitely without some erosion of credibility.
(News feature, Sept, 1977, p. 44).

Congressman Moss also expressed his doubts as to the viability of the new program: '...we will be reviewing the progress of the profession's efforts and commenting on whether those efforts show sufficient promise to continue or whether formal legislative or commission action is needed' (News report, April 1978, p. 7). Outspoken critic Burton continued to lobby that 'a reasonable solution is a cooperative approach of self-regulation under the oversight of a public body such as the SEC' (Burton, 1978, p. 67).

Pressures on the profession and concerns from the SEC did not abate in the late 1970s and into the 1980s. Issues encountered with the peer review process included the legalities of performing peer reviews on audit work being performed outside of the US for US companies, the possible effect on auditor independence in the provision of management advisory services (tasked to the POB to examine), and SEC access to working papers amongst others. The profession's response to all of these was to further promote the peer review program which did not enjoy a large uptake in the early years. The discourse on peer review also moved on to concerns of the profession's ability to develop the appropriate means to sanction firms in addition to the disciplining of individuals (Olson, 1979), imposing a further level of regulatory enforcement within the regime and segregating further regulatory activities from that of practice. A special investigations committee and separate procedures were in time established to deal with cases of alleged audit failures. In short, discipline became an issue of growing focus and with this focus would quite reasonably be followed with new actors, sanctions, and structures to enforce such disciplinary measures, resulting in further separation of regulatory and practice operations.

The reviews soon had a profound effect on shaping the activities within the firms. In addition to the production of new and additional quality control documents of policies and procedures, interviews needed to be held with 'those responsible for quality control functions' (Loscalzo, 1979) inferring that new job titles and responsibilities were being

created out of this process. Indeed, the revised quality control standards which were released in 1980 referred explicitly to ‘the assignment of responsibilities to personnel to the extent required to effectively implement its quality control policies and procedures’ (Quality Control Standards Committee, 1980, item 8). Engagement workpapers were now being reviewed including planning memos, and those which discussed the audit approach and problem areas. Exit conferences were held to discuss findings and deficiencies to be noted in the review reports were made public at the Institute for members of the SEC practice division. However, the extent to which these changes made by the firms could represent some underlying notion of quality remained to be understood, with even a member of the peer review committee commenting on this risk: ‘While the documentation process can be effective as a means of identifying areas in need of attention as well as a communication vehicle, it should be acknowledged that the creation of a quality control document is not an end in itself’ (Frey, 1980, p. 105). This potential gap was also acknowledged by the quality control standards committee within an exposure draft. In attempting to clarify that documentation ‘should be sufficient to enable those conducting an inspection to ascertain the extent of a firm’s compliance with its system’ (News report, March, 1982, p. 14), it did not, however, provide further clarification on what that might entail. What perhaps was more clear, however, was the cumulative effect of these changes in re-shaping practice activities as a representation of a self-regulatory model of peer review. This, in itself, contributed further to the reifying of the separation between regulation and practice.

By the early 1980’s, self-regulation and peer review would come to be understood almost synonymously with quality. Quotes such as the following, by SEC Chairman Williams: ‘membership in the section – with its attendant peer review requirements – provides a basic level of assurance of quality audits’ (News report, February, 1980, p. 7) were common within the discourse. The profession’s self-regulatory efforts were further legitimized through the neo-liberal ideologies intensified under Reagan’s reign of the 1980s. SEC Chairman Shad noted at the time: ‘A strong self-regulatory structure is in the profession’s interest. It facilitates governmental deregulation.’ (SEC Feature, April, 1982, p. 20). Meanwhile, the POB during this period continued to laud the efforts of the profession noting in its 1981-82 report that ‘the self-regulatory structure is sound and is functioning properly’ (News report, Sept, 1982, p. 9). Mautz weighed in with his support of self-regulation and peer review, combining the two in his article entitled ‘How *peer regulation* works – and works well’ (Mautz, 1984, p. 56, emphasis added). The annual report of the POB in 1984 contained a booklet titled: ‘Audit Quality: The Profession’s Program’ which was in ‘in-depth explanation of how the peer-regulatory program combines with other regulatory

efforts to provide maximum protection to the financial and investing public' (News report, Nov, 1984, p. 13) further interlocking its meanings.

However, all was not well, and another spate of alleged audit failures⁵⁵, precipitated by the economic downturn of the 1980's led to yet again a set of congressional hearings in the mid-1980s⁵⁶. During these hearings, the profession was criticised for the very few enforcement actions actually taken and that 'despite continual press reports of audit and accounting problems, the peer review system has not found much to criticize in the way its members perform their responsibilities' (News report, April, 1985, p. 12). SEC Commissioner Treadway, appointed to lead the commission on management fraud, predicted that 'We will...see the emergence of an accounting self-regulatory mechanism with an enforcement focus and capacity' (Collins, 1985, p.55).

Faced with another crisis of confidence and credibility, the AICPA established a special committee on standards of professional conduct for CPAs, to be led by practitioner and former AICPA chairman George Anderson. His report, released in 1986 reflected an underlying philosophy that 'the public's legitimate expectations must be reckoned with; [and that] the profession's response must be *visible* and, to be credible, meaningful' (Anderson and Ellyson, 1986, p. 92, emphasis added). The recommendations of his report included amongst others, a fundamental restructuring of the AICPA Code of Professional Ethics to include a new section on the standards of professional conduct which would now be *enforceable*. In addition, the report called for mandatory peer review, now synonymous with quality reviews, with new powers to require remedial action and to recommend punitive sanctions for non-cooperation or egregious acts. These changes were promoted under the banner of increased 'efforts to ensure quality' (Miller, 1986, p. 152). With additional sanctions and a disciplinary focus, not least to increase visibility of the programme, it is put forward here that these measures would have also further strengthened the separation of the regulatory and practice arenas.

Further, a focus on making the profession's response visible led to calls for a professional organization which would stand for a '*demonstrable quality* of practice' (Collins, 1987, p. 75, emphasis added) – apparently achievable by mandatory peer review which as a solution was legitimized and supported by the SEC at the time, reconciling both their own pressures to regulate quality but to still keep this under the auspices of self-regulation. The then Chief

⁵⁵ See Penn Square Bank and relatedly Continental Illinois National Bank & Trust Co (1982).

⁵⁶ House Subcommittee on Oversight and Investigations of the Committee on Energy and Commerce (Dingell Committee) and a separate National Commission on Management Fraud was formed (which included the AICPA) to be led by Treadway (Treadway Commission).

Accountant affirmed that ‘adopting this requirement will seriously improve overall audit quality’ (Collins, 1987, p. 76).

Whilst peer review was not formally, by majority vote of the profession, made mandatory until 1988, the institutional changes leading up to this point which made it possible had already been put in place. Critically, they did not occur independently of the advent of mandatory peer review – they emerged hand in hand and were entwined with the quality discourse throughout. This suggests that the separation of the regulatory and practice activities arenas, as more distinct fields of operations, was defined *through* the advent of peer review and *that the rise of peer review concurrently re-defined the arenas*. With standards and institutional structures in place, the advent of peer review became all the more conceivable. This once again highlights the very means by which the constellation should be reconceptualised as being dynamic. Whilst self-regulatory activities were already in existence, they were at the start of this episode held closely within the professional practice arena. However, the differentiation of these activities between regulatory and practice was made more concrete through the rise of peer review. This dynamism within the constellation, wherein an existing field of operations comes to be redefined and differentiated into a more separate and distinct field of operations, has been labelled within this thesis a ‘reformation’ constellation.

This chapter does not dispute the argument that the profession implemented these changes in response to external pressures to the potential loss of self-regulation. Indeed, this motivation was made widely and clearly from within the profession at the time.⁵⁷ To this, however, it adds the examination of the influences which converged to shape the central tenet of self-regulatory efforts into peer review, its interlocking relationship with the quality discourse, and how through the advent of peer review, the constellation yet again became re-constituted. Emerging out of this episode of attempts to preserve self-regulation was paradoxically a more defined regulatory arena of operations, self-regulatory or otherwise, but nevertheless split apart from that of professional practice.

Notwithstanding the above analysis, it remains so that the detailed mechanisms by which the many and varied ideas intersected with the quality discourse has yet to be identified. Whilst the existence of an interrelationship between accounting and the social may be well established, the precise means by which these ideas become connected and attached, in this case to the quality discourse, have not always been closely examined. Before we turn to

⁵⁷ See for example, from the AICPA Centennial Issue: ‘Thus, despite misgivings, peer review ... remains the only self-regulatory effort that may effectively deter regulation of the public accounting profession by the federal government’ (Sperry et al, 1987, p. 381).

these linkages, we will first examine how the academia arena of research also came to be implicated within these debates, setting off another emergent constellation, nested within this wider one being examined.

4.2.5 An emergent constellation of audit quality research

Prior to 1980, the academic literature on 'audit quality' was limited. Very few articles were published in the 1970s which focused on either quality control or audit quality per se. An observer noted in Accountancy that 'auditing has probably suffered more neglect by the academics than any other accounting subject...' (April, 1972, p. 18). A lone article containing the term 'audit quality' within its abstract was a paper by Warren (1975) which conceptualised quality control as a problem of reporting uniformity, echoing the problematization of the regulators within the previous constellation. Audit quality had yet to be placed onto the research agenda, despite concerns about quality having already by the 1970s emerged as an object of concern by regulators and accordingly also for the profession. In 1981, DeAngelo published her seminal paper 'Auditor Size and Audit Quality' which argued analytically that there is a positive association between firm size and audit quality due to the reputational consequences otherwise. Audit quality was defined by DeAngelo as 'the market-assessed joint probability that a given auditor will both (a) discover a breach in the client's accounting system, and (b) report the breach.' (p. 186). She further argued that 'The conditional probability of reporting a discovered breach is a measure of an auditor's independence from a given client.' (ibid). In short, quality was defined as a combination of competence and independence.

This paper, along with a contemporaneous paper published by Simunic⁵⁸ (1980) who argued that the amount of excess audit fees earned by an audit firm can be interpreted as the extent of its financial statement verification, provided the roots of a new research agenda largely hinged on these pieces of work. DeAngelo's paper, in particular, 'set the benchmark' (Francis, 2004) and became hugely influential in unlocking an entire research agenda based on using firm size as a proxy for audit quality and remains one of the most highly cited papers on the subject. Given this influence, it is particularly worth considering here some of the conditions which led to its emergence.

58 Here, Simunic (1980) argued that 'differentiated products are not observed directly but rather are revealed by differences in prices which are associated with differences in observed product characteristics' (p. 170). Whilst his study did not, at the time, reveal a fee premium for the Big N firms (apart from one of the then eight firms), which he put down to scale economics, the use of audit fees as an observable construct would in time be used prolifically in the audit quality literature.

DeAngelo's study was firstly informed by the contemporaneous debate mentioned above, emanating from the practice arena regarding the ability of smaller audit firms' ability to compete. Complaints were raised from a group of firms who argued that the then recently devised SEC practice unit at the AICPA was discriminatory against small and medium sized firms. The two studies by the Dericuix Committee (1980) and Arnett and Danos (1979) mentioned earlier were specifically cited within DeAngelo's paper. Thus, the *idea* of investigating firm size came initially from concerns within the practice and then regulatory arenas, a trend which continues to characterize much of audit research today. For example, much audit research in the past decade is motivated by the implementation of the Sarbanes-Oxley Act and PCAOB inspections (e.g., Knechel and Sharma 2012; Gunny and Zhang 2013; Lobo and Zhou 2006).

More importantly, however, DeAngelo's theoretical arguments were greatly influenced by the economic and decision sciences. In her study, DeAngelo drew upon the work of prominent economist Barzel, who in 1977 argued that when quality is costly to evaluate, self-interested individuals will devise alternative arrangements to enable quality-differentiated products to be exchanged. Market forces will dictate that the arrangement chosen will be that which minimises total costs of exchange. Accordingly, these self-interested individuals will develop surrogates to overcome the issue that quality is difficult to observe. Economic theory would also form the crux of DeAngelo's main argument which was rooted in the incentives-based motivation for audit firms to deliver quality audits, due to the reputational effects otherwise.

This influence of the economics sciences on audit quality research specifically, firstly positioned by DeAngelo (1981) and Simunic (1980) was symptomatic of the wider societal rise in the economic and decision sciences, part of which was already seen within the first constellation on statistical sampling. In accounting research more generally, this intersection had already been seen with the highly influential study by Ball and Brown (1968) which unleashed an agenda of capital markets based research still present to today. It had yet, until DeAngelo and Simunic, to filter through into audit research. Lee (2004) has summarised the impact of the rise of economics on accounting research more generally, including how the emergence of computerized economic and financial databases changed the face of accounting research, particularly in the US. An increasing focus by major research journals became issues concerning capital markets and economic agency. Lee argues the quantitative nature of these studies and 'their dependence on accepted economic theories gave them a quasi-scientific appearance' (p. 65) whereas other, normative studies which appeared in the late 1960s were refuted for their lack of scientific credibility (Watts & Zimmerman, 1986, as cited in Lee, 2004). This rise took off at a significant pace, and already by the 1970s and

1980s, the complexity of the empirical accounting research design began to use sophisticated manipulation of databases and the use of advanced statistical techniques to test data relationships.

The significance of this wider societal and research phenomenon on the academic conception of audit quality should not be under estimated. It is put forward here that it helped to shape a conception of audit quality which was entirely rooted within the economic sciences, and in doing so, created a platform for like-minded audit research to follow suit. The rise of the economic sciences also provided the environmental pre-conditions for its rapid take-up by the research community. In the event, this speed of take-up is exactly what followed.

In 1985, a mere four years later, articles such as that by Eichenseher and Shields would state “First, a high-quality audit, such as is provided by Big-Eight firms, obviously implies that there is a small risk of including incorrect or misleading information in the published financial statements” (p. 16). This statement would reflect the implicit assumption that the proxy was *already* widely accepted without need for question. In 1991, articles would already start to reflect a certain taken-for-granted nature of the size proxy. For example, statements such as these were to be seen:

All firms who hire one of the largest eight auditors ...are grouped into the *high quality* subsample, and all firms who hire auditors that are not among the largest fourteen auditors are grouped into the *low quality* subsample” (Feltham et al, 1991, p. 381, emphasis in original).

This assumption that Big N firms are of high quality, and non-Big N firms were of low quality, was often implicitly embedded within the hypotheses of the underlying research design. By 1993, articles such as Aharony et al (1993) would refer to measuring audit quality ‘by the widely used two-tier classification scheme of Big Eight versus non-Big Eight auditors’ (p. 72). Just a little over a decade after the publication of DeAngelo’s paper, the proxy of firm size for audit quality would already be widely established, firmly accepted and securely entrenched in the literature.

What followed from the early work of DeAngelo (1981) and Simunic (1980) was over three decades of academic literature on audit quality. For now, with a newly conceptualised, workable definition in hand, the number of studies which either explored this argument empirically or directly (and indirectly) utilised the Big N firm as a proxy for audit quality for related research questions would start to take off. A handful of other proxies would in time also be developed (restatements, going concern reporting %, accruals quality), but these would be few in comparison to the literature generated. The premise of this academic

conception of audit quality, however, would remain to this day a proxy-based one rooted within economics-based methods of inquiry and analysis (DeFond and Zhang, 2014). This was despite DeAngelo's own acknowledgement that any such surrogate (proxy) used would be 'imperfect' correlated (DeAngelos, 1981, p. 186) and early comments from distinguished researchers that some of the surrogates being used by researchers within this area and specifically that of independence were not recognised by the AICPA (DeFond, 1992, p. 17).

Nonetheless, this has become the primary foundation by which academia has conceived of the issue. And in being so constituted, it set off an emergent constellation of research specifically on audit quality which was also nested within this episode. It is important to remind ourselves from time to time that alternate conceptualisations with different foundations were and are also possible. For example, a closely related body of literature, that of auditor judgement, relies very much on the behavioural sciences even though, arguably, it is a component of auditor competency and hence quality. However, this stream of research has taken on an entirely different underpinning. Alternate definitions of audit quality would arise from time to time, such as that by Willingham and Jacobson (1985), as cited in Knapp (1991), which linked quality with risk: 'a quality audit is one in which an auditor reduces detection risk to a point where ultimate audit risk is at an 'appropriately low level' (p. 37) which arguably has conceptual merit. However, these failed to gain traction within the research community – due, as suggested here, to its lack of translatability into a proxy and therefore alignment with the rising trend of empirical research.

We will return to the concept of the proxy itself in the discussion section of this chapter. For now, we at last turn to those critical linkages which stabilised connections between ideas, shaping the constellation into the form in which it arose – a reformation constellation wherein the regulatory and practice arenas became further differentiated with an emergent audit quality arena arising from within.

4.3 Linkages

This section examines some of the linkages which again connected ideas and attached them to the quality discourse. One of the core arguments of this thesis is that the changing constellations of audit quality are dependent upon these linkages in connecting ideas firstly to each other and then to the quality discourse. And in so doing shifts the discourse to different problematisations of the quality problem. A close examination of these linkages, many of which have been mentioned already in this chapter, aims to help develop a more concrete understanding of how the notion of quality is continually changing over time. The

focus below will be on the precise nature of the linking work involved in crystallising connections.

The linkages for this constellation, as we shall see, yet again tended to take on the different forms of people or documents. These have been summarised in the following table and are discussed thereafter⁵⁹. Due to many of the overlapping ideas, in itself symptomatic of the co-constitutive nature of the discourse, the discussion will be presented by the connection of ideas made as opposed to by linkage.

Table 4.1: Summary of paradigmatic linkages within constellation two

Linkage	Connection of ideas made	Form	Type of linking
John C. Burton	Quality control and the audit firm Peer review and the audit firm Firm size and quality control	Person	Adaptation Brokering Rationalisation
Quality control standards (SAS 4)	Quality control and the audit firm	Document	Rationalisation, repetition
AICPA Practice Divisions	Peer review, self-regulation, quality	Document	Rationalisation, mediation
Working papers	Quality/peer review and self-regulation	Document	Mediation
Derieux Committee	Firm size and quality	Document	Rationalisation
DeAngelo (1981)	Firm size and quality Economic sciences and quality	Person and document	Rationalisation, repetition Re-interpretation

4.3.1 Connecting quality control to the audit firm

As mentioned earlier in section 4.2.4, prior to the emergence of quality control as a key concern during this period, references to ‘quality’ within the discourse tended to be restricted to the ‘qualities’ required of that of the individual auditor. The ten generally accepted auditing standards issued by the AICPA in 1949 were directed primarily at the behaviour of the *individual* auditor or to the supervisory *members* of an audit team (Hicks, 1974, emphasis added). Until the early 1970s, little had been attached to the responsibility

⁵⁹ This table does not purport to contain *all* linkages which were made during this period, but instead represents some of the influential ones which led to the instigation of peer review and to this constellation. The linkages selected here were traced from the discourse analysed and are paradigmatic.

of the audit firm and again, the AICPA could only control or discipline the activities of individuals (McCabe, 1993, p. 2).

Whilst ideas of the technical quality had entered the audit field through the advent of statistical sampling examined in chapter three, the wider concept of quality control had not been applied in the audit setting. We saw in chapter three how statistical quality control ideas could not be easily and readily applied to auditing and it was only on the more limited scale of statistical sampling techniques, specifically adapted for use within a historically specific setting, that some of the ideas were able to permeate auditing. However, as we have already seen within this chapter, the wider concept of quality control soon emerged from within this episode as a key concern for auditing. We will examine below how critical connections to the audit firm, as opposed to individual audit judgements were forged in order for quality control to emerge and to be made operationalisable within auditing. A key actor who actively promoted the advent of quality control, and relatedly, that of the concept of peer review, was John C. Burton.

John C. Burton

John C. (Sandy) Burton (1932-2010), a CPA with also a PhD in economics, was an outspoken commentator on professional issues within the audit field, whose influence on the debates during this period have already been seen above. He had a varied and distinguished career which started as a staff accountant at Arthur Young, a faculty position at Columbia Business School, time as chief accountant at the SEC, followed by deputy mayor for finance of New York City, before returning to academia as Dean of the Graduate School of Business at Columbia⁶⁰.

During his time at the SEC from 1972 - 1976, Burton was a supporter of the private sector's standard-setting efforts. During this tenure, Burton opted to issue Accounting Series Releases which pushed for additional disclosures as opposed to developing new standards (Sack, 2012), which were by then under the auspices of the newly formed FASB. Burton also pushed accounting firms to take greater responsibility. Burton believed that an accountant's task should not be confined to auditing corporate books, but should also include forecasts, judgements on the corporation's financial controls and evaluations of management. Possibly ahead of his time, Burton argued that 'Accountants are not primarily record keepers and checkers,' in the essay titled 'Where Are the Angry Young C.P.A.'s?', 'but measurers of economic and social phenomena whose measurements can significantly influence the allocation decisions of our society' (Weber, 2010). Burton continued to be

⁶⁰ See Weber (2010) and a memorial written by Sack (2012) for biographical details of Burton.

vocal even after his SEC tenure about transparency in financial reporting and argued for this greater role for accountants in public life (ibid). He published widely in the *Journal of Accountancy* and the *Financial Analysts Journal* (Sack, 2012).

As already highlighted earlier in section 4.1, Burton was one of the earliest proponents for a quality control system at the accounting firms, concurrently interrelating also the issue of firm size (discussed further in section 4.3.4.). With the roots of quality control within statistics, of which Burton himself had a keen interest in⁶¹ (Sack, 2012), Burton was one of the earliest proponents calling for quality control within auditing. However, as we similarly saw in chapter three where ideas of statistics could not be readily and easily overlaid onto the auditing context, quality control could only be made to be relevant to auditing if it was somehow adapted for use. Statistical quality control ideas conceived from manufacturing were not commensurate with individual auditor judgements which contained a good deal more complexity, variability and subjectivity in assessment. The *adaptation* required, it is put forward was achieved by essentially *bypassing the individual* and connecting quality control with the audit firm and in so doing, transferring ‘ownership’ of the quality problem from the individual to that of the firm. In this way, and through this modification, ‘outside’ statistical quality control ideas from the manufacturing setting could be more easily made operationalisable within auditing. We will see in more detail further on how this adaptation was achieved at the time through a further rationalisation exercise regarding firm size. However, for now, such was the success of this linkage that the take up of the idea of firm quality control thereafter was rapid. This was buoyed further by support of influential figures such as the then SEC Chairman, Casey and SEC Commissioner A. A. Sommer, Jr. both of whom had also served during the war and were likely to have been exposed to quality control procedures⁶².

We will return to Burton shortly and examine his linking role in introducing peer review to the audit field and in interrelating quality issues with firm size. For now, we will examine how ideas of firm quality control quickly became operationalised, making concrete this connection.

Quality control standards

Whilst firm quality control had now explicitly emerged as a concern, and the attendant possibilities created, the idea still needed to be operationalised in auditing. A key

⁶¹ Burton had served as an assistant statistician for the Brooklyn Dodgers during his college years (Sack, 2012).

⁶² Casey served as chief of secret intelligence in Europe for the Office of Strategic Services in World War II. He was the manager of Mr. Reagan's Presidential campaign in 1980 and became Director of Central Intelligence in 1981. Biographical details from Case (1987).

development which enabled this was the issuance of quality control standards. Ernest Hicks, a partner with Arthur Young & Company and chairman of the AICPA auditing standards executive committee proposed early in 1973 a set of quality control procedures for an accounting firm which covered areas including 'the administration of a *firm* as well as with the *quality* of its audit work' (Hicks, 1974), thereby interlocking together the connection between quality control procedures and the audit firm. These draft procedures, which as even acknowledged by Hicks, were controversial in containing provisions for client acceptance, hiring and promotion practices, independence, supervision and inspection. These procedures were issued by the AICPA very quickly thereafter, in 1974 and without amendment, as Statement of Auditing Standards No. 4 – Quality control considerations for a firm of independent auditors. Within this standard itself, we are able to observe how the linkage between firm and quality control was established, and rationalised throughout in a seemingly logical manner. Indeed, the very introduction of this statement left no room for ambiguity and read as follows:

Rule 202 of the Rules of Conduct of the Code of Professional Ethics of the American Institute of Certified Public Accountants requires members, when they are associated with financial statements to comply with the applicable generally accepted auditing standards. Those standards have to do primarily with the characteristics and conduct of *individual* auditors. *A need has arisen* to identify policies and procedures of a *firm* of independent auditors... that may affect the quality of work in its audit engagements (AICPA, 1974, emphasis added)

From there, the standard explicitly transfers, or at the very least expands, historic responsibilities of the individual auditor to that of the firm, such as:

Complying with generally accepted auditing standards is a basic objective of every *firm* conducting an audit practice (ibid, para 2).

And also, with respect to areas which had been historically governed by the Code of Ethics such as independence:

Policies and procedures should be established to provide reasonable assurance that persons at all organizational levels maintain independence in fact and in appearance (ibid, para 5, emphasis added).

Indeed, all of the nine elements promulgated in the standard as being elements of quality control called for the establishing of policies and procedures, implying that such a measure – essentially the creation of documents, by the firm would enhance quality. This assumption will be examined further in the discussion section of this chapter. For now, the connection of the firm with the responsibility of quality control was made concrete through part

repetition of previous arguments seen within the discourse at the time, and through the rationalisation efforts within the standard itself, which argued in a logical manner the need for firm quality control procedures along with tangible suggestions for how this would be achieved. The statement was approved unanimously by all 21 members of the Auditing Standards Executive Committee. In these ways, SAS 4 served as a further linkage within this constellation, crystallising the connection of quality control, and hence quality, with that of the firm.

4.3.2 Connecting peer review with auditing

With the concrete establishment of quality control as an object of *firm* concern, not least through its regulatory powers of governance, further connections however were still needed in order to enable the rise and operationalisation of peer review. These linkages came once again in the form of John C. Burton, who directly carried with him and transferred ideas of peer review into the audit field, the AICPA Practice Division documents which carried the requirements for voluntary peer review with the attendant capacity to satisfy both regulatory and practice interests, and finally the firm audit working papers themselves which provided the means by which peer review could be made operable. These will be discussed in turn.

John C. Burton

As we saw earlier in section 4.1, the emergence of quality control also came intertwined with the seeds of possibility for peer review or least internal inspections. Notwithstanding this, peer review had not yet been formally introduced into the audit field. This would follow on very quickly through the influential efforts of Burton and some of his underlying beliefs.

During his time at the SEC, Burton was very active in the area of enforcements against some of the major CPA firms at that time⁶³. In an article published in the Vanderbilt Law Review in 1975, Burton described the philosophy behind the SEC's enforcement program and outlined the nature of the sanctions available to the Commission. In this article, we are able to observe the underlying beliefs of Burton at that time. Critically, of the core objectives of the enforcement program, in addition to giving effect and improving auditing standards, and improving public confidence, was to 'encourage the implementation of profession-wide quality controls within firms' (Burton, 1975, p. 21). Further, Burton adds 'The Commission believes...that it will have the effect of promoting improved professional performance' (p. 26). This underlying belief that firm quality control procedures could result in enhanced

⁶³ Laventhal, Krekstein, Horwath & Horwath (ASR 144), Touche Ross & Co (ASR 153), Westheimer, Fine, Berger & Co (ASR 167) and Peat, Marwick, Mitchell & Co. (ASR 173).

audit performance was then carried through to the nature of the sanctions available to the SEC. In addition to having the powers to bar or suspend an individual or firm from practice, and bolstered by his fundamental belief in the efficacy of quality control measures, Burton describes another option:

In the past two years, new sanctions have been developed in consent situations that the Commission believes hold some promise. Where cases raise questions concerning the adequacy of an accounting firm's quality control procedures, the Commission may require the firm to submit its procedures to the Commission's staff *or to a group of outside professionals for review* (Burton, 1975, p. 25, emphasis added)

Such was the sanction put forth to Peat, Marwick, Mitchell & Co for questionable audit practices at Stirling Homex, National Student Marketing and Talley Industries (ASR 173). What started as 'creative sanctioning' (Statements in quotes, 1978, p. 90) and as an idea of a remedial provision in a series of enforcement cases against some of the major CPA firms left a lasting legacy in making tangible the audit field, the very concept of external firm peer review. By directly brokering ideas of peer review from outside of the audit field and operationalising them within, Burton, already a key linkage within this constellation, further brought together the concept of peer review and auditing. With the contours of peer review already made possible, intertwined with the emergence of quality control, and with Burton's 'precedent-setting sanctions' (*ibid*), the notion of an outside inspection 'became the norm for the profession when the AICPA developed the Peer Review Program' (Sack, 2012, p. 153). And as quickly as by 1977.

In 1978, after Burton had moved on from the SEC, he published an article in the *Journal of Accountancy* arguing for the importance of surveillance of auditing practice and proposing a new self-regulatory body under the oversight of the SEC (Burton, 1978). Burton drew an analogy with the National Association of Securities Dealers (NASD), again, brokering ideas from outside the audit field, and suggested that this new organisation might be called the National Association of Registered Accounting Firms.⁶⁴ This new organisation would be responsible for standard setting, firm registration, disciplinary proceedings and regular surveillance of practice. Burton argued that such an institutional structure would provide stability for the self-regulatory approach.

In response to these ideas, former SEC commissioner Sommer, Jr. reflected upon Burton's proposals as representing an accumulation of his past experiences as accountant, regulator

⁶⁴ Burton firmly believed that real breakthroughs came about because people were able to think laterally. In June 1991, Sack and Burton co-authored an editorial in *Accounting Horizons* entitled 'Time for some lateral thinking' (Sack, 2012).

and academic (Nov, 1978). To this, we add his background and personal interest in statistics from where quality control derived. Sommer, Jr.'s observation is particularly relevant in the current study given the linkages which can be, and are, constructed through the biographical journeys of key actors (Padgett and Powell, 2012). In this sense, Burton himself, a leading figure involved in all three arena operations of academia, practice and regulation (much like we saw in Robert Trueblood in chapter three) was himself a product of his environment and of a time where far closer links were held within arenas activities and with each other. For example, one of his early assignments as an associate professor was to chair what became known as the Seaview Symposia from 1968 -1971. These sessions brought together people from the four institutions involved in the financial reporting process: AICPA, the Financial Executives Institute, the Financial Analysts Foundation (today, the CFA) and Robert Morris Associates and was perhaps the first time that leaders from each of the then Big 8 firms and major actors from the prepare and user groups met to share thoughts and opinions of others in the financial reporting process (Sack, 2012). Sack (2012) has concluded that many of Burton's subsequent speeches and writings addressed the issues discussed at the Seaview Symposia. Burton also continued his conversations with inter-arena actors at forums including the University of Kansas Accounting Colloquiums in July, 1973.

In this way, it is put forward that Burton can be seen as a key person linkage within this rise of peer review, first in carrying ideas of quality control and attaching these to the audit firm, and then quickly thereafter in directly carrying ideas of peer review from outside of the audit field to that within. Through Burton and the historical contingent preconditions of the time, the idea of peer review was able to very quickly become established as a regulatory norm.

4.3.3 Connecting arena concerns of quality control and self-regulation

With peer review now carried into the audit field, it remained that the concept's uptake as a mandatory measure needed to generate sufficient support in both the regulatory and practice arenas in order to 'succeed' in this way. This, it is argued, was made possible due to further linkages which were able to satisfy both the contemporaneous concerns of practice (the threat of the loss of self-regulation) and by now the heightened regulatory concerns of firm quality control. In a sense, these two concerns needed to be brought together before mandatory peer review could obtain. This was partially achieved through the AICPA reorganisation into two voluntary Practice Sections in 1977, membership of the SEC Section of which required peer review and the requirements of which were carried through the attendant documentation. Secondly, the audit working papers themselves provided the

means by which this connection could be made tangible, and hence, peer review operationalised.

AICPA Practice Sections and voluntary peer review

Faced with congressional pressures on the SEC to act, and the threats of external regulation to the profession, the idea of peer review, as a potential solution, became quickly normalised. It is argued that this speed of normalisation was due, in part, to the linking capacities of the very idea of peer review itself which could satisfy both practice and regulatory concern. Faced with the pressure to demonstrate oversight, the complete external oversight of which was in conflict with the ideology of deregulation at the time, the SEC were keen to support a measure which would be visible, demonstrable and which would enable them to satisfy these conflicting tensions. Separately, the practice arena was faced with significant threats to also demonstrate the efficacy of self-regulation such that external oversight could also be avoided. The idea of peer review offered a solution to both arenas – it thus became ‘successful’ as it had the capability of satisfying both problems of regulation and practice concurrently. By mediating concerns of both arenas, peer review can be conceptualised as very similar to Abbott’s (2005) notions of hinges, as being issues or strategies which work in two ecologies at once.

Whilst ideas may have linking capacities, however, the position of this thesis is that it still needs to be ‘carried’ through some medium in order to make concrete the connections. Peer review, as an idea, had a linking potential, but this connection of demonstrating self-regulatory efforts *and* improving performance through quality control still needed to be made concrete. Through the making of peer review as a professional firm requirement, first in 1977 and carried through the related professional publications and documents, this linkage became solidified. When a further round of failures and congressional hearings took place in the 1980s, this only strengthened the interests on both sides and support for peer review intensified even further, despite the doubts of the efficacy of peer review as a regulatory measure which were being expressed at that time (see section 4.2). In this way, we have conceptualised the regulatory documents instigating peer review, albeit at this stage on a voluntary basis, as a linkage mediating the interests of both the regulatory and practice arenas concurrently. A further linkage was thus forged.

Working papers

The audit working papers being reviewed within this episode also bear consideration as they became the key mechanism by which the peer review process could be operationalised, and in themselves underwent a transformation. Peer review could not be carried out without

access and the availability of the working papers upon which the compliance reviews were dependent. Despite the reservations regarding whether these papers could adequately reflect some underlying notion of quality, the compliance reviews were nonetheless premised on being able to check performance against the quality control standards issued. These would include documented policies, procedures, and centrally the audit working paper files themselves.

In this way, we can conceptualise the audit working papers as serving as the critical linkage to further concretize the peer review connections between the regulatory and practice arenas being promulgated. Peer review was *realised* through the linking capacity of working papers – from the working papers being ‘of use’, or rather, once again able to serve the concerns of both arenas. However, in serving as a linkage in this way, the working papers themselves underwent a transformation during this period - from highly proprietary documents to being very public items open to external review. This transition, notably, did not occur overnight solely through peer review – the beginnings of this transformation had already started earlier.

More directly, however, the CPA Quality Review Program (henceforth ‘quality reviews’) for local firms which started within the profession itself, had its roots within a project by some state institutes to improve the quality working papers. The original objective of this program was to review, on a post-audit basis, the financial reports, opinions, and supporting working papers of the auditor in order to encourage compliance. A practitioner forum in September 1974 which reflected upon the first two years of the program noted that: ‘The greatest single problem noted was the failure to fully document the procedures performed during the engagement’ (Minkus, 1974, p. 105). This concern was further emphasised by Burton, speaking at a conference on SEC enforcement actions, where a key trouble area was situations where ‘it appears that the audit documentation did not leave an adequate trail of the decisions being made’ (News report, 1975, p. 9). Converging with this was the increasing focus on working papers being raised through the heightened environment of litigation whereby inadequate documentation led to questions of auditor performance. Rising concerns of defendability already seen led some practitioners to note as follows:

...the auditor is in a more defensible position when he has spotted a problem, resolved it and *documented the resolution in his working papers*...A common problem that surfaces in litigation is the insufficient use of memoranda or *documentary evidence* of research, telephone conversations, client or attorney instruction, instructions or approval by higher authorities within the practitioner’s accounting firm or other proof of proper auditing techniques...There is no

substitute for written documentation....(Chazen and Solomon, 1975, p.68-69, emphases added).

This new focus on working papers was therefore already in motion when that very same working papers review program became leveraged by the AICPA to formulate the 1977 peer review program. This was explicitly set out in the objectives of peer review in the AICPA official release: ‘Reviews for this [peer review] purpose shall include a review of *working papers* rather than specific ‘cases’ (AICPA, 1977, item VIII, emphasis added). Challenges with this initial peer review program included whether the SEC themselves could also be given access to workpapers, bringing them even more into public view, heightening their emphasis and focus. With quality being firmly implicated within these programs and developments, the working papers became in this way one of the mechanisms upon which peer reviews could be carried out, and hence, peer review could obtain. Working papers ‘worked’ as a linkage through its capacity to be ‘of use’ and leveraged by two concurrent arenas thereby yet again mediating the interests of both. Again, the implicit assumption was that inspection the quality of audit working papers could be used to observe some other notion of underlying quality. In time, these working papers would become of even greater importance, on account of being open for inspection and graded by external reviewers.

4.3.4 Connecting firm size with quality

A concurrent and interrelated discourse mentioned earlier in this chapter was that on the issue of firm size. Earlier, we saw how Burton was one of the early actors who problematized the issue of size, and its relationship with the quality discourse. We will now examine more closely below how this connection was achieved and in time how this distinction became further reified within the discourse.

In an earlier aforementioned article published in the Journal of Accountancy entitled: ‘An educator views the public accounting profession’ (Burton, 1971), based on a related speech, we are able to observe further how Burton *rationalised* a connection between quality control with firm size. Burton firstly attributes some of the root causes of the then problems facing the profession to issues of professional attitude, lack of innovation, and ‘the very fact of size and growth had created difficulties’ (p. 48). In a very logical manner, he attributed depersonalization as a function of growth, and argued that ‘*depersonalization in turn leads inevitably to the need for control systems*’ (ibid, emphasis added). And it was from here that Burton then identified the ‘quality control problem’ as a serious one for the profession inferring that whilst the ‘large’ firms had installed systems of quality control, the profession as a whole had not. In so doing, Burton interconnected the issue of firm size with quality

control, as an intervening step of transferring the concept of quality from the individual to that of the firm examined earlier.

Adjacent to this, however, it remained that this hierarchical distinction of the firms became further reified in the discourse throughout the decade of the 1970s. Further connections between quality control and firm size were repeated, in themselves also linkages. For example, the author of SAS 4, Ernest Hicks included in his draft of the proposed standard that the need for formal inspection procedures being proposed 'tended to be proportional to the *size* of the accounting firm' (Hicks, 1974, p. 43, emphasis added) thereby justifying the connection between the two. The Metcalf Commission (1976) was exceedingly critical about the dominance of the large firms and whilst 'quality' was not mentioned in much detail, linked with the issue of dominance was the impact this would purport to have on the independence and competence of auditors (in time, audit quality became widely understood as a combination of independence and competence, in part due to this forming the crux of DeAngelo's (1981) definition). A small and medium sized panel of representatives was formed to voice their concerns regarding the anti-competitiveness of the AICPA reorganisation into practice divisions. Specifically, the division of firms based on those with SEC practices and those without implied, in practice, to mean large versus small and medium sized firms. Indeed, the practice of peer review itself was said to be of disproportionate cost to small firms (Derieux, 1980, p. 20).

Such was the concern raised from inside the profession, that the AICPA undertook a number of initiatives to investigate, each of which only furthered this hierarchical distinction. Included in these initiatives were a Committee on Specialization, a Committee on Displacement of CPA Firms, a precursor to the Division for Firms being the Special Committee to Study Proposals to Restructure the Profession and a Committee on Generally Accepted Accounting Principles for Small and Closely Held Firms. A summary of these can be found within the Derieux Special Committee on Small and Medium Sized Firms (1980) report, which in itself was another embodiment of the hierarchical distinction being increasingly made visible. The objective of such a committee was defined as:

To study the future viability and prospects of smaller and medium sized accounting firms which constitute the majority of practice units of the Institute and to develop programs to assure their ability to retain clients of significant size and standing in the financial community in competition with large national and international firms (Derieux Committee, 1980, p. 2)

In addition to investigating the future viability and prospects, the report also interrelated quality to the issue of firm size in a number of instances. For example, in the introduction of the report:

There is concern that smaller firms may be replaced simply because they are less well known, even though the *smaller* firms may well be providing as high or higher *quality* services (Derieux Committee, 1980, p. 5).

Connections such as these were made throughout the report which ultimate rationalised and concluded that a firm's size should have no bearing on its ability to provide a quality audit. This report was then picked up by DeAngelo which we have already seen and served as the motivation for her seminal paper in 1981. In this way, DeAngelo finalised the embodiment of the connection between firm size and quality. Here, she *repeated* the debates regarding the relationship between firm size and quality (p. 183) and *rationalised* analytically that there was a positive association, setting in motion the emergent constellation of audit quality research seen earlier. For example, her very opening paragraphs repeated some of the debates on firm size:

Large audit firms are increasingly criticized on the basis of size alone both by regulators and by smaller firms within the accounting profession...For example, employing the assumption that audit quality is relatively homogeneous across audit firms, Arnett and Danos (1979) argue that size alone 'should not be a prime determinant of future success' (p. 8, emphasis added). Furthermore, they argue that 'as long as professional standards and qualifications were maintained, it is unfair to arbitrarily distinguish between the largest eight and all other CPA firms' (p. 56, emphasis added) (DeAngelo, 1981, p. 183).

And further on:

The Derieux Committee Report stresses the 'concern that smaller firms may be replaced simply because they are less well known, even though the smaller firms may well be providing as high or higher quality services' (DeAngelo, 1981, p. 184).

DeAngelo's core argument that larger firms have higher quality on the basis of the reputational risk otherwise was then set out analytically and rationalised in a highly logical manner:

...the current paper argues that *size alone alters auditors' incentives* such that, *ceteris paribus*, *larger audit firms supply a higher level of audit quality*. When audit technology is characterized by significant start-up costs, incumbent auditors earn client-specific quasi-rents.

These quasi-rents, when subject to loss from discovery of a lower quality audit than promised, serve as collateral against such opportunistic behavior. *This implies that, ceteris paribus, the larger the auditor as measured by number of clients, the less incentive the auditor has to behave opportunistically and the higher the perceived quality of the audit (ibid).*

For present purposes, the argument is that DeAngelo (1981), the person and the document, served as a key linkage which finalised the connection between firm size and quality which had been steadily rising within the discourse and in the decade leading up to the publication of her paper. Rather than just an objective and independent ‘outsider’, as is often the view of academia, DeAngelo (1981) was in these ways very much a part and product of this constellation.

4.3.5 Connecting audit quality with the economic sciences

DeAngelo (1981)

In some respects, DeAngelo (1981) was in itself a ‘perfect storm’ of wider influences outside and within the other arenas which cultivated the conditions of possibility for an almost immediate uptake of her thesis. To date, it remains one of the highest cited papers on audit quality. Some of the key influences to her paper included the wider rise of the economic and decision sciences and issues which arose from within the practice arena itself, most notably that of the concern of small firms and their ability to compete as discussed above. Both of these key influences came from outside of the academia arena. However, these influences would likely not have been sufficient in and amongst themselves to generate her argument – the unobservable nature of audit quality still needed to be overcome. DeAngelo’s solution – to align the concept of a surrogate with a proxy and to analytically justify the use of firm size as that proxy, transformed audit quality into something which was now also observable and in so doing, made audit quality researchable. An ‘operationalisable’ definition of audit quality which critically connected ideas of the economic sciences, the use of a surrogate or proxy, had yet to have been conceived of and therefore, audit quality in its unobservable, subjective and indeterminate state was not until then researchable by empirical means – the importance of this aspect to the research community contemporaneously rising. In this sense, audit quality *had yet to be made so*. By anchoring her use of the surrogate from the economic sciences and neatly linking the concept of a surrogate with quality, DeAngelo captured the essence of the economic sciences within her conceptualisation of audit quality. Thus, it is put forward that DeAngelo’s finding of audit quality’s correlation to firm size was not an entirely ‘natural’ phenomenon which was simply yet to have been discovered. It too was made possible through the confluence of

wider concerns or influences, already seen in earlier constellations, which then emerged following a time lag for ideas to filter through into research and for the academic publications process. The rise of the economic sciences in particular had now found its way within the academia audit arena, which also, critically, provided the conditions to facilitate the rapid take up of her proxy idea within the research community.

In this way, DeAngelo (1981) was additionally important as it served as the key linkage which forged a critical connection within the audit quality discourse. DeAngelo, the person and her research paper, as a document, served as a key linkage in bringing in ideas of the economic sciences from outside of the field and attaching them to audit quality, constructing a conceptualisation of audit quality which was a *re-interpretation* infused with ideas from the economic sciences – through primarily the introduction and the underlying idea of the use of a surrogate. Specifically, DeAngelo (1981) argued as follows:

When audit quality is costly to evaluate, self-interested individuals have incentives to devise alternative arrangements which enable quality differentiated audits to be exchanged. Furthermore, competitive forces dictate that the arrangement chosen will be the one which minimizes the total costs of exchange (including the costs of differentiating quality). This cogent observation was first made in a more general setting by Barzel (1977). *One potential response is for consumers to develop surrogates for audit quality, i.e., to rely on some other (less costly to observe) variable which is (imperfectly) correlated with quality. The argument of the current paper is that auditor size serves as a surrogate for audit quality* (DeAngelo, 1981, p. 186, emphasis added).

This paper, in itself, and as seen earlier, proceeded to set off an emergent constellation of audit quality research specifically which was nested within the wider academia arena of audit research. That this research agenda, with quality now observable and made alignable to the rising trajectory of accounting and auditing research, also consequentially separated the academic arena further away from practice and regulation activities was perhaps, not altogether surprising.

4.4 Discussion

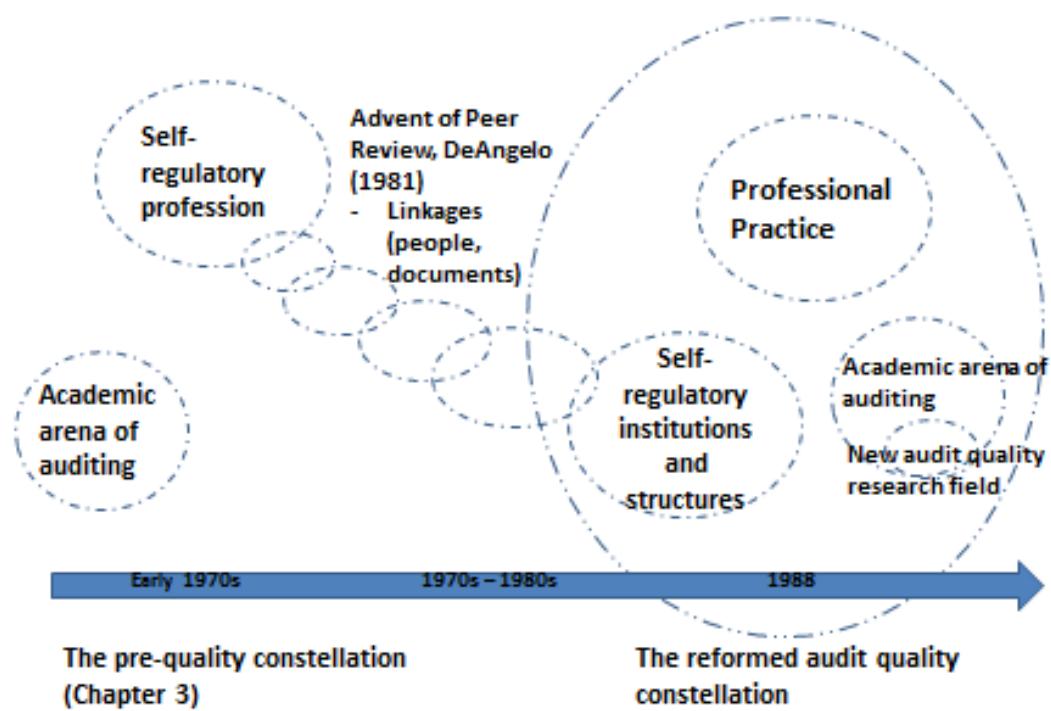
This chapter has drawn upon Burchell et al (1985) to investigate the constellation of tensions and concerns which led firstly to the emergence of quality control as an object of concern and thereafter, closely intertwined, to the rise of peer review. The advent of peer review, however, was not a neutral technology and its emergence concurrently reshaped the

constellation by furthering the separation of regulatory activities, even if still falling under the auspices of *self*-regulation, from that of professional practice. As we also saw in chapter three, the arena and the constellation are mutually constitutive. This element of dynamism within this constellation, whereby existing arenas of operations are further differentiated into separate fields of operations, has been labelled a reformation constellation.

In addition, this chapter also examined the nature of the linkages upon which the constellation, and hence dynamism, is dependent. By again tracing some of the connections which were actually made to give rise to the quality discourse in the form in which it emerged, we are able to see more clearly the precise means by which differing ideas, discourses and logics became attached to the quality debates. It adds analytically to how the quality discourse in audit became implicated in different ideas. Through this episode, quality became firmly understood as a systems-based output of firm practices as well as an issue of firm size within academia. Its emergence in turn sparked an emergent constellation nested within the wider academia arena of research operations, the beginnings of which were examined in chapter three. Through these conceptions within this period, quality became concretely transformed into an issue, problem, and property of the firm.

Following on from Figure 3.1 of chapter three, this transition into the new constellation can be depicted as below. This figure attempts to show the how the audit quality constellation became reconstituted during this period, from a two arena constellation of statistical sampling (carried over from chapter three) to the beginnings of a three arena constellation - where regulatory activities became differentiated into its own arena, and a new academia arena of operations on audit quality specifically emerged. Again, it was through the pre-conditions and linkages of this constellation, and the interrelations therein which enabled peer review and DeAngelos' conception of audit quality to arise. And in so doing, the constellation became re-constituted.

Figure 4.1 Transition to the peer review reformation and audit quality emergent constellation.



It is through the lens of this more dynamic conceptualisation of the constellations in which we are able to start to gain a better understanding of the changing nature of audit quality. In attempting to pursue quality, solutions which are predicated on specific meanings and understandings are adopted, which in themselves re-shape the constellation. The linkages, and the linking work which is entailed, which come to solidify the connections between ideas are central to this re-shaping of the constellation. The ‘solutions’ which have been adopted are therefore critical to this story and are considered further here.

4.4.1 Proxying audit quality

As examined above, DeAngelo (1981) brought into the academic audit quality research field the concept of a proxy, as a surrogate for audit quality. In so doing, an entire research field became unlocked on account of quality having been in this way been made observable and hence researchable. However, this idea of a proxy or surrogate to represent audit quality, as we have seen throughout this chapter, was not only confined to the academia arena. From the early developments from within the profession on reviewing working papers to assist in quality matters, to the instigation of peer review with its attendant standards and documentation within regulatory developments, all three arenas have grappled with the problem of ‘dealing’ with quality in some way. And all of these devices which grew out of this constellation of pre-conditions, and forged linkages, can also be understood as proxies for audit quality. Whether these be the quality of working papers, the quality standards themselves (ICAEW, 2002 as cited in Ramirez, 2013), the process and outcomes from peer review inspections, or firm size, *all* have come to serve as proxies for quality. However, as Fogarty (1996) has already queried with respect to peer review in particular, the extent to which peer review and attendant documentation actually produces quality is problematic.

The conceptualization of quality as an issue of quality control to be remedied through peer review was only made possible by taking a conceptual leap. Quality needed to be made amenable to being regulated. Its lack of regulateability, auditability and even researchability needed to be surmounted, especially when its prominence in the discourse and pressure for action started to rise. In addition, pressures for any actions taken to be demonstrable, and consequently defendable were also prevalent within the practice arena. The solution to overcome this was to adopt that which could be observed – being the documentation of a systems-based process or measurable proxies such as firm size. With this, the gap between this and some other underlying quality was effectively side-stepped.

With this leap, the transformation of audit quality, from a subjective, indeterminate and unobservable notion, into that which could now be observed was essentially complete within the three arenas. It allowed all three arenas to work with quality in their own way, but the

differences between them also serve to highlight the fact that quality can be ‘made visible’ in different ways, premised upon differing conceptions. It is malleable in nature and in this way, audit quality can be conceived of as a boundary object (Starr and Griesemer, 1989 – see chapter six for further discussion). More critically, however, the argument being made is that ‘proxies’ in this sense are being used across *all* arenas, some perhaps more complex than others, but nonetheless all rooted within some form of ‘empirical reductionism’ (Fogarty, 1996, p. 252). This challenges further the extent to which *any* of these bases can achieve a representation of some underlying notion of quality any more ‘accurately’ than others. Whilst they enable each of the arenas to work with quality, it remains questionable the extent to which working with quality *in these ways* relates to working about some other notion of underlying quality. In a series of case studies of large scale state engineered failures, Scott (1998) presents a compelling argument that ‘rationalizing and standardizing...into a legible and administratively more convenient format’(p. 3) enables the reality they are depicting to be remade, once again pointing towards this problematic relationship. This will be examined more closely in chapter six. For now, several other transformations with quality occurred within this process of making quality observable and it is to these, and their implications for how we can come to think of quality, which we now turn.

4.4.2 Key transformations

As discussed in section 4.3.1, one of the key transformations with quality during this period was its construction as a firm property. In problematizing quality as a quality control issue, in itself a conceptual legacy from the statistical sampling episode examined in chapter, quality control could be made more easily operationalisable if it was taken as a firm problem. Indeed, the academic conception of quality as a matter of firm size also furthered this transformation by reifying this connection. Systemising individual judgements was not workable. This transformation was also in line with the contemporaneous trend seen within the audit firms of ‘de-individualisation’, due to the significant growth of the firms occurring at that time. Quality so too became swept into the management operations of the firm once it was conceived of as a firm problem.

Second, quality during this period subsumed the adjacent concern of independence. Through both the quality control standards issued and through DeAngelo’s academic conception, quality became increasingly thought of as a combination of competence and independence. Concerns of independence were initially only included within the AICPA’s code of professional ethics as a responsibility for the *individual* auditor well before the quality discourse emerged within audit. During this episode, independence concerns were

formally included within the quality control standards issued by the AICPA thereby transforming, or at least expanding, the concept of independence into being a problem of the firm, as a component of quality, along with it.

Third, the workpapers of audit files underwent a dramatic transformation during this period through both its use and role in operationalising peer review. Not only did the advent of peer review lead to a production of additional documents of policies and procedures, but the nature of those audit working papers themselves was transformed. From once very proprietary documents, workpapers became subject to inspection and in so doing, became a critical focal point from where judgements on quality would be made. A practitioner review of 83 peer reviewers' comments found that within the 11 categories of quality control system design and compliance findings, a problem with *the inadequacy or the lack of documentation* was the most consistent finding across all 11 categories (Bremser, 1983). Raised as a core issue, this would only increase the focus on workpapers even more. As the key mechanism of the audit which was observable, this conceivably would have led to the inordinate focus on that documentation, which in turn reifies quality as so described (Fogarty, 1996). In time, these working papers would become a key basis on which audit quality gradings of the firms was based.

And finally, the concept itself of self-regulation underwent a transformation in meaning and definition. Self –regulation came to be understood during this period synonymously with peer review and 'peer-regulation' through which the discourse on audit quality became increasingly implicated. Despite emerging as a more separate arena of operations within this chapter, the activities still fell under the auspices of 'self-regulation'. However, what comprised self-regulation which emerged with mandatory peer review, disciplinary bodies, and new institutional structures in place was radically different than the private and internal partner reviews before the rise of quality concerns. Moreover, with these new structures came the creation of roles and responsibilities to manage the program, thereby shifting the administration of certain activities external to the firm. This speaks to the operationalisation of a new management style: regulating quality became regulation via quality control.

Closely linked to these transformations was quality itself becoming transformed within this episode from indeterminate and undefinable to observable and precisely defined. In the intersection with wider discourses and influences, the underlying meanings of quality within each arena were 'subject to new interpretations in accordance with such ideals, discourses' (Robson, 1991, p. 566) and thereby transformed. Importantly, quality had now been made visible across all three arenas, albeit in different ways. Thus, whilst the discourse may have been unified through the joint use of the word quality, and notwithstanding the dominance of

the regulator conception given its powers of governance, the development, themes and underlying conceptions of the three arenas were on quite separate trajectories, heading if anything in the direction of increasingly defined boundaries of separation.⁶⁵

4.4.3 Making audit quality

In *Making Things Auditable*, Power (1996) argues that auditing is constitutive of an active process of constructing auditability. In that paper, Power draws upon the case of making quality auditable whereby auditing quality is an active process of constructing its auditability. There, Power (1996) also argues that 'quality is an empty concept without accreditability and hence auditability. In this way, *audit processes have the potential to become constitutive of quality*' (p. 300, emphasis added). This will be examined further here. However, a distinction should be made with the present argument which is that in making quality visible, quality itself (as opposed to the audit of it) becomes constructed.

The previous section outlined how the initial ideas of peer review originated within a working paper review based program of firstly a state institute which was then picked up by the AICPA as an internal, educationally based measure. The rise of peer review became intertwined with this program and in time, the focus shifted away from that of an instructive and educational optionality to an emphasis as a disciplinary mechanism to be conducted on a mandatory basis. The underlying approach of both of these systems, conceptual roots aside, was premised on a systems-based conception of quality whereby some underlying quality could somehow be revealed and improved upon through process based measures. In other words, quality was an output based conception and the means to tackle it would be to control the process by which it is generated. This is akin to a manufacturing process which, given the conceptual roots of quality as examined in chapter three, is not altogether surprising.

Seen this way, one means to understanding quality lies in this transformative process of making quality observable, such that it may be made auditable, regulateable, and even researchable. Once observable, quality starts to become understood in those very specified ways, gathering pace, such as we saw within the academic conception. In time, these bases become so normalised to the quality discourse that they start to appear as if they were natural attributes all along. In addition, quality can become further reified, through the

⁶⁵ As an indication of the growing separation between these different arenas, in 1985, the *Journal of Accountancy* released a call for more 'practical articles' (*Journal of Accountancy*, June, 1985, p. 10). Articles should 'help solve practice problems, help apply new standards or advance new ideas in management accounting...Authors should emphasize examples from experience. Writers from academe or consultants may wish to pair with or consult CPAs in practice or in industry to obtain more "nuts and bolts" data.' (*ibid*, emphasis in original).

intensification of activity and discourse around those same bases on which it was made observable (c.f. Espeland and Sauder, 2007).

Taken together, therefore, it is put forward that making quality observable was thereby critical for the discourse to gain momentum. Similar to measures, which cease being measures once they become a target (Strathern, 1997), the audit quality proxies used also have limits by restricting the thinking and focus to only that which is ‘counted’. The making observable of audit quality risks displacing the focus of the original concerns to that which can be observed, endowing it concomitantly with a capability to rise to dominance within the discourse. Whilst failures and sub-standard performance may have played a role in exacerbating debates, the argument here is that they were *not the only* elements which have shaped this outcome. Taken together, this section (and thesis) questions the assumption that quality is a pre-existing reality ‘out there’ ready to be revealed (and acted upon) and was instead, shaped by a process of constructing both the problem and the form of the solution to that problem, a number of historically contingent pre-conditions and forged linkages. It is within this process also where the transformation of quality into that which observable played a key role in constructing quality itself. In being understood as that which has been made observable, quality in this sense, became made.

4.5 Epilogue

In October 1994, the AICPA Council approved the combination of the Peer Review Program with the Quality Review Program, effective April 1995, which for purposes of this thesis marked, in a sense, a culmination of this episode. The new combined program, called the AICPA Peer Review Program, was intended to eliminate confusion among members and the general public caused by having two similar but separate programs in operation. The merging of the two programs effectively formalised the shift in nuance and meaning of quality between the regulatory and practice arenas, an alignment of which for all intents and purposes had already by then occurred. Quality was now ‘institutionalised’ in the very precisely defined systems based approach of peer review (Fogarty, 1996) for the regulatory and practice arenas, whereas the academic conception of quality remained a proxy based one rooted within the economic sciences. Overlapping with this episode, however, was the beginnings of the transference towards a new constellation: the shift in the audit quality discourse to that of the re-intensification of independence and the problematization of market structure and competition, particularly so in the UK and the EU. Concerns of independence had already been raised as potential issues within the Metcalf and Moss reports in the 1970s and indeed this tension with auditor independence underscored much of

the discourse at the time. Whilst independence was during this period explicitly subsumed within the quality discourse via quality control standards and peer review, independence remained an area issue of concern to the regulators *throughout* this period which became exacerbated in time by collapse of Enron. This primacy of belief underscoring regulatory concerns was summarised by SEC Chairman Williams at the time:

I believe the crux of the whole problem is independence... A major problem of the accounting profession is that it lacks the appearance of independence in an area where appearances are as important as realities...Intimately tied to the independence problem are concerns relating to self-discipline and quality control (News feature, 1977, p. 42).

It is to this third and final constellation, empirically located this time in the UK, which this thesis now turns.

Chapter five

Constellation three: The rise of independence and the turn to mandatory rotation (1990s -2014)

5.0 Introduction

Mandatory firm rotation removes the incumbent who's potentially the strongest candidate. I don't think mandatory rotation deals with the core issue, which is audit quality.

- James Chalmers (2014)⁶⁶, PwC Head of Assurance

In June 2014, the European Commission finalised its investigation into the reform of the audit market and legislated, amongst other initiatives, mandatory audit firm rotation for countries within the European Union. Shortly thereafter, the UK Competition and Market Authority⁶⁷ published the results of their exhaustive investigation into the UK audit market and in light of these EU reforms recommended mandatory audit firm re-tendering which could then converge with the EU rules on rotation. Whilst tempered from initial proposals, this was nonetheless a significant regulatory intervention within the audit market in the EU and extended recommendations enacted in 2002 to internally rotate audit engagement partners after a period of seven years. Moreover, the reforms prescribed a highly controversial regulatory measure which had had a complex history of debates as to its 'effectiveness'. Central to the discourse on these developments was, once again, that of audit quality.

Following on from the discourse of quality control and peer review as examined in chapter four, this chapter continues the examination of the rising discourse of quality within auditing and locates this in the most recent turn involving a problematization of independence and a lack of competition within the audit market. As Khalifa et al (2007) have observed, a shifting discourse to one of 'audit quality' itself within the professional practice audit field occurred post-1990s which was, in part, sustained by a number of world events that followed. The collapse of Enron in 2001 sparked a crisis of confidence and led to a chain of significant regulatory events in the US, most notably that of the Sarbanes-Oxley Act and the creation of the PCAOB. Following those events of the early 2000s and triggered from this US lead, regulatory developments internationally became dominated by the turn to external oversight of audit firms and its attendant focus on audit quality. In 2006, the independent

⁶⁶ From 'FTSE 350 audit tenders to almost double in 2014' available at:

<http://www.ft.com/cms/s/0/51d56c68-23c8-11e4-be13-00144feabdc0.html#axzz3zfRKdViC>

⁶⁷ Formed in April 2014 following the merger of the Office of Fair Trading and the Competition Commission.

oversight bodies from then just 17 jurisdictions established the International Forum of Independent Audit Regulators (IFIAR) to facilitate dialogue and coordination of oversight activities. Just ten years later in 2016, its membership had grown to include independent oversight bodies from some 50 jurisdictions, reflecting the growth of such oversight regimes internationally and consistent with the global rise of regulatory capitalism (Levy-Faur, 2005). Amongst the sharing of knowledge and the promotion of collaboration and consistency in regulatory activity, a key objective of IFIAR is on providing a platform to share dialogue for organizations with a specific interest in 'audit quality'⁶⁸.

The global financial crisis of 2007 did little to abate the heightened concern with auditing (Sikka, 2009) and further intensified the calls to reinforce, amongst others, independence, transparency and once again audit quality. In the EU and the UK, a number of investigations were held, almost concurrently, to investigate these and re-emerging issues such as the concentration of the audit market and the role of auditors in the crises. These included an inquiry by the UK House of Commons Treasury Committee into the banking crisis in 2008, an EU consultation into the reform of audit policy in 2010, and an investigation by the UK Competition Commission on audit market concentration in 2011. Emerging out of these investigations in 2014 was EU wide legislation for mandatory audit firm rotation. Tendering will be required for Public Interest Entities ('PIEs')⁶⁹ every ten years, with mandatory firm rotation after twenty years. Proponents of mandatory rotation argued it would 'solve' both issues of independence, by breaking apart any relationship between auditor and corporate which may have become too 'familiar' over time, and also issues of competition by forcing a churn in the supply side of audits through enforced tendering. Linked to the tendering process were recommendations for full transparency on the proposing firm's audit quality, including the disclosure of the most recent results of any firm inspections undertaken (EC, 2010; FRC, 2013).

One view from the outset of these developments may be that Enron, and the highly publicised level of non-audit services provided by the Houston office of Arthur Andersen, was the final 'straw' and a clear indictment of the lack of independence of auditors. However, concerns regarding auditor independence have had a longer history than just that which comes to the forefront at times of crises. And the reasons which lead to 'gatekeeper failure' are a good deal more subtle, involving a complex interplay between economic,

⁶⁸ See www.ifiar.org/About-Us.aspx

⁶⁹ EU PIEs are defined as entities - including EU PIE subsidiaries of non-EU parents - incorporated in an EU member state with equity and/or debt listed on an EU "regulated market". Private banks, insurance undertakings and certain listed funds are also included. In the UK this includes entities with listings on the London Main Market, and excludes entities quoted on the London Alternative Investment Market.

institutional, cultural, legal factors and more (see Coffee, 2006). Whilst crises serve to punctuate the discourse and trigger the resurfacing of particular concerns, issues which surround the audit, as mentioned in chapter one, are perennially present. They include, for instance, the existence of the expectations gap, the role and responsibilities of the audit especially with respect to the detection of fraud, the concentration of the Big N firms and the alleged, consequent lack of competition, as well as the independence of auditors. Indeed, in 2006, several decades on from when some of these tensions were first debated, the remaining Big 6⁷⁰ firms themselves jointly released a report which raised all of these exact issues yet again, framed within a call to address the issue of auditor liability.⁷¹ Specifically, the firms argued that without restrictions on auditor liability, resolutions to all of the above issues could not be achieved and should another audit Big N firm be allowed to collapse in the wake of the demise of Andersen, the stability of the capital markets would be placed at risk. However, echoes of some of these arguments and more can be traced back to the Metcalf Commission, some 30 years prior and even beyond. Similar issues and arguments were yet again taken up within more recent contemporary regulatory discourse (e.g., EC, 2008a and 2008b). This suggests that despite multiple episodes of regulatory intervention, these perennial issues of the audit – many of which have at varying times been implicated within the debates on audit quality, remain profoundly resilient.

Following the same approach as in previous chapters, this chapter seeks to examine those pre-conditions leading to this latest turn within the discourse which locates the lack of competition and independence as particularly central issues with audit quality. This chapter will investigate how the convergence of a number of events, discourses, ideologies and decisions led to the legislation of mandatory rotation within the UK, which in itself was nested within wider, parallel debates on audit reform taking place within EU at the time. This chapter will show how during this period, concerns of independence, notwithstanding its long and protracted history, came to rise from *within* the discourse on quality starting from the 1990s onwards and how this intensification became interconnected with the problematization of the lack of competition within the audit market. This chapter will show how further failures and crises and the attendant pressure for visible action converged with the ideology of the free markets and the EU single markets project, to problematize the lack of competition within the audit market. And in doing so, implicated audit quality within the interrelations of the discourse. With the increase of competition promising to also address

⁷⁰ Comprised of the now Big 4 firms and the next two largest firms internationally of Grant Thornton International and BDO International.

⁷¹ See *Serving Global Capital Markets and the Global Economy: A View from the CEOs of the International Audit Networks* (November, 2006)

the heightened concerns of independence, the road to mandatory rotation as a ‘logical’ remedy became paved.

This chapter will also continue the examination into the role of linkages in enabling this latest conception of the audit quality problem. In addition to analysing the key document linkages upon which this current constellation was dependent, this chapter will also seek to highlight the relationship *between* the linkages themselves. Within this current constellation in particular, many of the ideas, discourses and debates which occurred post-Enron and post-2007 global financial crisis, and certainly within this past decade, were recurrent arguments seen before. Furthermore, the more contentious of propositions such as the concentration of the Big N firms, attendant market structure issues and even the very idea itself of mandatory rotation as a means to increase competition, had all been made within the Metcalf Staff Study released in 1976 in the US. However, it was only 40 years later that some of these ideas became operationalised in the EU, transcending both time and space. This chapter seeks to not only examine those pre-conditions leading to this latest turn to competition and independence, but to also develop the notion of linkages and its role in formulating the constellation, further. This chapter will in particular highlight that linkages on their own are insufficient. A sequence of linkages to connect ideas is required for successful ‘action’ - the linkages themselves need to be connected in some way, through either the underlying ideas being held together or through an alignment of interests. It was only when this sequence of linkages became connected within this current constellation, amidst the historically contingent circumstances of this past decade, that ideas which were first connected to the audit field some 40 years earlier could obtain. This suggests a different way to conceptualise accounting change, over and above the identification of linkages, and as an alternate view to one hinged on translation (see chapter two). The linkages themselves also need to be connected.

The detailed empirical setting for this chapter starts briefly in the US where debates on independence were rising and influential to the UK discourse. Thereafter, the setting transitions to the UK⁷² where the discourse on issues of competition and market structure

⁷² The episodes being investigated in this thesis are discrete and sometimes overlapping periods within the history of the discourse and therefore, it is put forward here that the strength of the arguments being made in this chapter are not any less significant due to the examination of a UK context. The theoretical developments being examined in this thesis are sufficiently general to be considered across jurisdictions. In addition, the examination of both the Journal of Accountancy (US) and Accountancy (UK) during this 50 – 60 year period indicates that the UK debates are nonetheless highly influenced by that of the US. It is also put forward that within this contemporary constellation in particular, due to the globalisation of capital markets, clients, audit firms, and the international coordination between regulators, institutional differences between the UK and US

became especially pronounced. The UK was included within the EU proposals for audit reform and was also subject to both the House of Commons inquiry into the banking crisis and Competition Commission investigation. During the lead up to the implementation of mandatory audit firm rotation, a great number of documents were produced from various inquiries, consultations, investigations and proposals. It is through these documents where we are able to observe the underlying ideals and influences through which this latest conceptualisation of quality was articulated, constructed and in time understood. As a reminder, however, this contemporary notion of competition and independence as the central audit quality problem, stood in stark contrast to the previous notions of quality examined thus far and again it is to this changing notion of quality which this thesis seeks to unpack.

The remainder of this chapter is structured as follows. Section 5.1 examines the intensification of the debates on independence from the 1980s onwards and how the attention became increasingly focused on that of the ‘appearance’ or visibility of independence. Section 5.2 investigates the confluence of elements which led to the problematization of the lack of competition in the audit market. Section 5.3 examines how this problematization converged with the rise of independence concerns which, together, shaped the regulatory solution into that of mandatory audit firm rotation. Section 5.4 examines the nature, and sequence of linkages, along with the precise nature of their linking work, which were required in order to enable the rise of mandatory rotation. A preliminary discussion of the implications for how we can come to understand the notion of audit quality is included in section 5.5, which will be further developed in the next and concluding chapter of this thesis.

5.1 The rise of independence

5.1.1 Early US developments

Concerns with independence within auditing have had a longer history than that even of quality. The establishment of the Securities Act of 1933 and the Securities Exchange Act of 1934, included the requirement that financial statements included in registration statements filed under those acts be ‘certified...by an *independent* public or certified accountant’ (emphasis added) and whilst not defined outright, included a set of rules which set out what it meant to *not* be independent. Mautz and Sharaf (1961) indicate how the concept of

context may have less of an influence on the arguments of this chapter. The constellations being examined within this thesis are also not necessarily continuous.

independence within auditing had already been well established by the early 1960s within their opening sentence of the independence chapter in their monograph:

The significance of independence in the work of the independent auditor is so well established that little justification is needed to establish this concept as one of the cornerstones in any structure of auditing theory (Mautz and Sharaf, 1961, p. 204).

However, whilst the idea of independence within the audit is universally supported (Flint, 1988), it remains so that the concept is neither simple nor easily defined. Beattie and Fearnley (2002) in their literature review of auditor independence and non-audit services, summarised some of the more ‘representative definitions’ (p. 4) found within the literature⁷³ as reflecting ‘the importance of objectivity (ability to suppress biases) and integrity (willingness to express an opinion that truthfully reflects the evaluation of what has been discovered during the audit) as two key aspects of auditor independence’ (Dunmore and Falk, 2001, p. 8 as cited in Beattie and Fearnley (2002)).

An important dimension of independence is that, similar to quality, the concept is also not readily observable which has historically proved problematic for the profession. A clear distinction has emerged within the literature between independence ‘in fact’ (which cannot be observed) and independence in appearance (by definition observable), the latter of which has, as a result of this observability, received the greater attention. Added to this is the complexity that the concept of independence itself, like quality, has also been shifting through time (Colson, 2004; Baker, 2005; Nouri and Lombardi, 2009). These shifts have subtly moved from the responsibility to serve absentee owners (early 1900s), to one of objectivity and neutrality in the reporting of financial statements in accordance with standards (1970s), and according to Baker (2005), to being that of ‘trusted advisor for clients’ in the 1980s (p. 25).

As an adjacent concept to quality, the connection between independence and quality was formally made through the initial quality control standards issued in 1974 whereby responsibility for ensuring independence was *also* to be included within a *firm’s* quality control policies and procedures. DeAngelo (1981) further reified this connection through her conception of audit quality as being comprised of a combination of independence and

⁷³ These include, for example: ‘the conditional probability of reporting a discovered breach’ (DeAngelo, 1981, p. 186); ‘the ability to resist client pressure’ (Knapp, 1985); ‘an attitude/state of mind’ (AICPA, 1992; Moizer, 1994, p. 19) and a more recent example, ‘freedom from those pressures and other factors that compromise, or can reasonably be expected to compromise, an auditor’s ability to make unbiased audit decisions’ (ISB, 2000). To date, whilst universally supported as a concept within the audit, a universal definition has yet to be established.

competence⁷⁴. In time, however, concerns with independence would start to rise from even within quality and come to dominate the discourse. A number of key elements of the 1980s converged to enable this intensification, which then gained momentum from the 1990s onwards⁷⁵.

In Zeff's (2003b) summation of the development of the US accounting profession, he concludes that the situation the profession found itself at the turn of the millennium, post-Enron, Andersen and the PCAOB, was brought on by a series of defining events and decisions, many of which stemmed from the 1980s. These included actions by the FTC and the Department of Justice to force the profession to repeal its ban against competitive bidding and solicitation, the increasing competitiveness for audit clients by the firms exacerbated by the economic recession at the time, and the accompanying expansion into tax and consulting services which led to a consequent change in mentality of top management. It is put forward that all of these defining moments, which would come to have a profound and lasting effect on the profession, can *also* be understood as being intricately linked together with the discourse and concern of independence. In this sense, the history of the development of the accounting profession could also in this way be told through the lens of the history of the profession's struggles with demonstrating independence – either in fact or in appearance. The Anderson committee appointed in 1985 to take 'a fresh look at standards of professional conduct' (Anderson and Ellyson, 1986a, p. 92) observed even then, with respect to the profession's expansion into non-audit services and its tension with maintaining independence that 'many observers are concerned...that the long-term consequences for the profession of uncontrolled expansion of [non-attest] services will be a *diminished faith* in the auditor's independence' (Anderson and Ellyson, 1986b, p. 43, emphasis added).

These developments in US, along with the moves towards mandatory peer review examined in chapter 4, were being closely watched at the time in the UK. Contemporaneous articles started to appear in Accountancy tracking the US developments with interest and increasing

⁷⁴ Within the academic literature, independence has, much like quality, been predominantly investigated (quantitatively) empirically through the use of observable proxies. In this respect, as some of these proxies have been used to investigate *both* quality and independence (e.g., propensity to issue going concern reports or discretionary accruals), the close connection between independence and quality has become further reinforced. To date, independence is widely understood to be a component of audit quality.

⁷⁵ As an indication of this rising concern in the 1990s, the number of articles printed in the Journal of Accountancy containing the term 'independence' for the decade of the 1990s was nearly fivefold higher than that of the 1980s and continued to rise into the decade of the 2000s. This is also consistent with a Google Books Ngram Viewer chart for auditor independence which shows a sharp rise in the number of matches in the 1990s, continuing into the 2000s. The domination of independence within the audit quality discourse is indicated also in this graph which shows the number of matches for independence *overtaking* that of audit quality from 1996 onwards.

frequency (e.g., Radford (1979), Young (1980), News, Nov 1984). Moves to install quality control standards, by both IFAC and the UK Auditing Practices Board were also following the US lead in the 1980s. Whilst one practitioner made the early comment that 'In the UK, reaction from the majority of leading accounting firms to the controversial issue of extending peer review to international operations of US firms has been hostile.' (Radford, 1979, p. 70), developments in the UK nonetheless quickly followed on from that of the US. By 1984, one commentator observed that 'there are some voices being raised in the UK that a similar system should be established' (News, 1984, p. 5) and in 1987, audit practice inspections by the ICAEW were approved in advance of the EC's Eighth directive, with the responsibility of setting auditing and ethical standards as well as the conducting of independent inspections eventually moved to the FRC.

Further developments in the 1980s US which were being followed closely within the UK included another set of congressional hearings (Dingell Hearings) in the aftermath of a number of business failures within the savings and loan industry. There, the continued concern with independence once again manifested itself as one of the three main areas of focus for the inquiry, in addition to the role of the SEC and accounting standards. In his opening speech, inquiry chairman Dingell stated his belief in the significance of *perceptions* of independence:

It is not enough that financial statements be accurate; the public must also *perceive* them as being accurate. Public faith in the reliability of financial statements depends upon *public perception* of the outside auditor as an *independent* auditor (News, 1985, p. 4, emphasis added).

This underlying belief in the perceptions of independence in sustaining public confidence, along with the inherently unobservable nature of independence in fact, would underscore much of the regulatory debates and developments to come.

5.1.2 UK developments (late 1980s onwards)

In the late 1980s, a number of new acts were legislated within the UK Parliament including the Financial Service Act 1986⁷⁶, which set out the terms of regulation for the financial services industry, and the Insolvency Act 1986, which set out all the legal provisions for personal and corporate insolvency. In addition, the European Commission issued the Eighth Company Law Directive in 1984 which called for a number of harmonisation provisions on

⁷⁶ This Act was repealed on 1 December 2001 and superseded by the Financial Services and Markets Act 2000. Under this new Act, the Securities and Investments Board and Self-Regulating Organizations created under the Financial Services Act 1986 were merged to form the Financial Services Authority (FSA).

the education, training, and qualification of statutory auditors (essentially, those provisions relating to the ‘competence’ of auditors). It also contained some minimum provisions required relating to the professional integrity and independence of auditors and called for national governments to take responsibility for audit regulation, which was in stark contrast to the then existing system of professional self-regulation. Together, these all put the spotlight on the self-regulation of the auditing profession within the UK. Maintaining the independence of the profession through monitoring of compliance with quality control standards, of which the independence of auditors was included, became the strategy adopted (e.g., ICAEW, 1985; APC, 1983; News, 1986).

In 1987, the DTI released a consultation document (DTI, 1986) regarding the implementation of the Eighth Directive which provided a ‘clear lead’ (News, 1987, p. 5) to the profession on several issues, including that ‘active monitoring of professional competence as an important feature of the new regulatory system’ (ibid). On the issue of independence, whilst the DTI agreed that the then extant rules within the UK were sufficient to satisfy the requirements, a concern which appeared to have arisen with the DTI was the perception that the Directive required independence to be dealt with in legislation, and that matters of independence should therefore not be left entirely to the profession’s self-regulatory efforts (see also Evans and Nobes, 1998):

The ethical rules of the various bodies would seem to be sufficient to satisfy the spirit of the Directive. The critical question is whether the Directive can be properly implemented within the terms of Community law if those rules are not written into public law or the Secretary of State at least has the capacity to exercise control over them. It is difficult to see how the UK could be regarded as having ‘prescribed’ that audits should be carried out with professional *integrity if the rules defining professional integrity were a matter of private law over which the Secretary of State had no control* (DTI, 1986, p. 28, emphasis added).

Linked to this belief that the legislation of independence should be made more visible, a number of propositions such as the separation of the audit function from other services, the establishment of a regulatory general council and mandatory rotation were put forward within the consultation document – despite these being outside the remit of the Directive. Cooper et al (1996) argue that these additional points can only be understood in terms of the changing political context in the UK and in particular, the significance of the New Right philosophies which stressed the free markets (p. 603). This will be discussed further in the next section. For now, the severity of these proposals in terms of its threat to self-regulation

and in a bid to ‘improve’ independence alarmed the professional accounting and audit bodies (*ibid*).

With independence in sharp focus, and in particular the rising importance of its visibility - through enactment in law or otherwise, and in response to further points raised within the Directive regarding the incorporation (i.e., outside shareholdings) of audit firms and its compatibility with independence, the three Institutes of Chartered Accountants (of England and Wales, Scotland and Ireland) convened a joint Working Party on Independence and Incorporation in 1988 to examine the issue further. The working party noted that the issue was ‘contentious’ and that ‘the debate on this issue should be encouraged to continue’ (ICAEW, 1988). Its results were then fed into a further consultative document released by the ICAEW to its members which maintained further the intensity of attention on independence issues later on that year.

Within this environment, the economic recession in the early 1990s brought with it yet another spate of high profile and unexpected corporate collapses, including Polly Peck, BCCI and the Maxwell companies. Headlines such as ‘Record number of companies go under’ (News, 1992) were prevalent in the press. The discourse on audit quality was again heightened⁷⁷, with a central focus of the discourse during those troubling days of the early 1990s that of the independence of auditors (and in particular, the tension to maintain independence when audit firms were faced with economic pressures). Articles had already by then started to appear in the more mainstream business press questioning the independence of auditors (e.g., Auditors in firing line, FT.com, 1986). Highly controversial proposals for the EC’s Fifth Directive included drastic reforms such as the prohibition of auditors from becoming directors or employees of clients for three years, mandatory change of auditors after 12 years and extension of auditor liability to shareholders and third parties under any circumstances. Independence concerns underscored all these proposals. The then editor of Accountancy, Singleton-Green commented at the start of the decade on the situation as follows:

The fundamental problem is that, especially in the press, there has been a growing atmosphere of cynicism about auditors’ independence in recent years....regardless of how little justified the thinking behind them may be, something will now have to be one

⁷⁷ For examples: DTI inspector reports heavily criticised auditors during this time with one firm responding with the need for a continue programme of ‘quality’ improvement (Jenkins, 1990); the ICAEW released a publication ‘Profit from Quality’ linking economic and efficiency pressures with quality in 1992 - this ‘trade-off’ between pressures on margins and quality was further taken up as ‘The Auditors’ Dilemma’ (Darnill, 1992).

to restore confidence in auditors' independence (Singleton-Green, 1990, p. 22)

Commenting further, Singleton-Green stated that 'Nobody worried much about independence 10 years ago, when changes of auditor were rarer' and then proposed the handing back of the appointment of auditors to the shareholders: 'Giving real power to the shareholders would restore the *visibility* of auditors' independence from management...The issue of auditors' independence is now coming to a boil. Action needs to be taken to reinforce public confidence.' (ibid, emphasis added). These comments, yet again, underscored the growing *belief* that *perceptions* of independence were at the crux of the issue and improving the 'visibility' of independence would provide suitable redress. This was further made apparent by the Auditing Practices Board releasing a consultation document on 'The Future of Auditing' which rooted the issues as a problem of 'present perceptions' surrounding auditing, of which the 'greatest' of these related to the perception of the lack of independence of auditors (APB, 1992).

These debates on independence and quality of the early 1990s were also nested within wider developments in both the discourse on total quality management⁷⁸ and corporate governance and accountability more widely (see below). Added to this was the then European Commission's position on independence, in a follow-up to the controversial proposals of the Fifth directive, to move forward with developing a framework of principles with the more detailed rules left to the member states. This placed continuing pressures on independence. The Commissions' thinking at that time was set out by Karel van Hulle who stated:

I know many people argue that independence is a state of mind and should stay the subject of self-regulation. We believe that the mind of the auditor could do with help to maintain his independence. It is not enough for the profession to set the rules (News, 1991, p. 9).

In the midst of these debates, the 1990s saw a number of significant regulatory developments introduced within the UK pertaining to audit regulation and corporate governance more generally. These included, on account of the implementation of the Eighth Directive which was given legal status within the Companies Act 1989, the establishment of the FRC and a new system of licensing and monitoring under delegated authority from the DTI. In addition, the Cadbury Committee set up in the aftermath of the failures of the early

⁷⁸ For example, the discourse on audit quality in the early 1990s intersected with wider discourses on Total Quality Management (West, 1991; Kelly, 1991), developments within the British Standards Institute in quality management accreditation (BS5750 and also ISO 9000 internationally, for example see Goodwin, 1991) and concurrent developments by IFAC in developing policy statements regarding quality control (IFAC, 1991).

1990s to review corporate governance, released its Code of Best Practice in 1992. This included the recommendation that all listed companies establish an audit committee, comprised of non-executive directors and with at least three members being independent. In 1991, the Auditing Practices Committee, which had been comprised of only auditors, was replaced by the Auditing Practices Board, which was to be comprised of an equal membership of auditors and non-auditors. Underscoring all of these developments was a ‘stronger framework for independence’ (Beattie et al, 1999, p. 70).

In addition to the above, developments pertaining to the regulation of independence more explicitly were also occurring, further making concrete this central focus of concern. In 1997, the UK Chartered Accountants Joint Ethics Committee’s released a statement on Integrity, Objectivity and Independence – a principles based framework for independence which identified threats both to independence in fact and in appearance and the safeguards to control these threats. The European Commission also continued to focus its attention on the issue and prioritised its agenda during this time on external quality assurance, auditing standards and auditor independence (EC, 2003) following its recommendation on ‘Statutory Auditors Independence in the EU’ in May 2002 (EC, 2002c).

Seen within this context of the rising intensification of independence concerns, argued here to be that which was *over and above other* problems surrounding the audit, the collapse of Enron in 2001 and the widely implicated level of non-audit services being provided by the Houston office of Andersen, was all that was needed to bring the mounting, underlying concerns of independence to a shattering head. Auditor independence was condemned. With the financial crises of 2007 coming so soon thereafter and issues of independence high in public and regulatory consciousness, the Treasury select committee of MPs, as part of their report into the causes of the banking crisis, reported on the audit industry which had otherwise emerged relatively unscathed as follows:

We strongly believe that investor confidence, and trust in audit would be enhanced by a *prohibition on audit firms conducting non-audit work for the same company*, and recommend that the Financial Reporting Council consult on this proposal at the earliest opportunity (House of Commons Treasury Committee, 2009, p. 84, emphasis added)

This prohibition was recommended despite a finding that auditors had not actually failed in their duty⁷⁹, and instead once again reinforced the underlying belief that increasing the visibility of independence was warranted as it would enhance public confidence.

5.1.3 Summary comments

This section has attempted, at a high level, to trace the rise of independence concerns within the quality discourse and how this came to dominate the debates, possibly even ‘crowding out’ other quality concerns such as competence. A long and protracted history has no doubt been oversimplified in order to draw out this trajectory amidst the complexity of many interrelated factors. This rise can perhaps also be most helpfully thought of as a constellation in itself of overlapping and competing elements and discourses. The key argument being made is that during this period, the confluence of a number of different elements including: the prevailing economic climate, the interjection of high profile failures, the EC’s efforts to harmonise regulations across member states, the expansion of the audit firms into non-audit services, the inherent lack of observability of independence and finally, the underlying belief that the problem of independence was one of perceptions contributed to this rise. With this last point especially, efforts therefore became focused on making both independence and regulatory reforms more visible - through the promulgation of detailed rules, explicit standards or radical proposals of reform, all targeted at increasing the visibility and improving perceptions of independence. However, this only fuelled the rise of independence concerns further. Whilst the large scale failures played a role, they were not, it is argued, the only element leading to the rise of independence which, as this discussion has attempted to show, started on its trajectory well before the collapse of Enron. Indeed, research conducted at that time indicated that rarely had independence been found to be implicated in audit failures. Based on an analysis of lawsuits and prosecutions of auditors for securities fraud, Bartlett (1991) found that most lawsuits and prosecutions of auditors have been based on assertions of incompetence or lack of due diligence in the application of auditing standards, rather than lack of independence.

In itself, the ascent of mandatory peer review in the US in the period up to 1988 (see chapter four) signalled a wider and increasing focus on the ‘ideal’ of independence, through the promulgation of peer review as an *independent* inspection regime. Concerns of independence during this time were not just restricted to the independence of auditors.

⁷⁹ The report explicitly states the following: ‘We have received very little evidence that auditors failed to fulfil their duties as currently stipulated...The fact that some banks failed soon after receiving unqualified audits does not necessarily mean that these audits were deficient. But the fact that the audit process failed to highlight developing problems in the banking sector does cause us to question exactly how useful audit current is.’ (House of Commons Treasury Committee, 2009, p. 77).

Whilst auditor independence remained a key area of debate within the regulatory discourse, further articles within Accountancy also indicated a rising trend with independence concerns more widely. Manifestations of this came in different guises from questions regarding the independence of the Accounting Standards Committee and its funding arrangements (Accountancy, 1980), the replacement of the ASC with the more independent Auditing Practices Board, the rise of the independent non-executive director (see recommendations from Cadbury Committee and Cross Report) in parallel with the emergence of the audit and remuneration committees (to be comprised of a minimum number of non-executive directors, a number of whom should be independent), and the establishment of the Financial Reporting Council in the UK, and its auxiliary bodies, as an independent body to regulate auditing. In general terms, the significance of independence as an ideology and precondition of 'good' governance has been steadily rising over the course of the past three decades.

The profound belief that perceptions were at the crux of public confidence in the capital markets came to become of even greater importance once this belief intersected with the ideals of the free markets, which in itself was further intensified with the EC's single market programme and objectives (see section 5.3). This in turn heightened the importance of both the capital markets *and* the role audit had in sustaining the confidence within those markets. The concept of independence, inextricably linked with the ideal of audit, was made in this context even more so fundamental.

As highlighted above, this rise of independence did not occur detached of the contemporaneous political ideals, economic climate or wider concerns and discourses of the time. Of particular relevance during this period was also the level of competition within the audit market – indeed, the level of competition brought about by the economic recession of the early 1990s, deemed then to be excessive, had been implicated in at least the perceived decrease, in audit quality. However, as this chapter will now examine, threats to audit quality would also be implicated within the accusations of too *little* competition. These debates regarding the level of competition within the audit market would soon take on a central role within this shifting discourse on audit quality, made all the more so when it started to be articulated through the lens of prioritising 'well-functioning' capital markets. This next section will investigate the pre-conditions which led to the rise of competition as central to the audit quality discourse and how these then converged, interrelatedly, with the intensification of independence concerns such that the 'logical' solution to these problems became increasingly seen as that of mandatory audit firm rotation – a measure which had not long ago been deemed too blunt and radical an instrument to be implemented.

5.2 The problematization of competition

In the aftermath of Enron and the subsequent demise of Andersen, the European Commission approved the acquisition of Andersen in the UK by Deloitte & Touche (as well as the merger of Andersen with Big 4 firms in a number of separate European countries), which led to the current audit market configuration of being comprised predominantly of the Big 4 firms. At the time, the European Commission had declared the merger to be compatible with the common market.⁸⁰ Shortly after this approval, the UK Office of Fair Trading released a statement on 22 November 2002, having declined to launch an investigation into the audit market, based on conclusions reached as follows:

...we have conducted a preliminary inquiry into whether, given the current market structure, there are competition problems in this sector. We have not found evidence to suggest that firms have acted to prevent, restrict or distort competition. Nor have we had complaints that they may be doing so (p. 4).

However, despite these conclusions reached in 2002, the concern of the lack of competition in the audit market would rise suddenly over the course of the next decade leading to the OFT's formal referral to the Competition Commission for investigation in 2011, less than ten years later. On 21 October 2011, the day this referral was made, John Fingleton, the then Chief Executive of the OFT released a statement, diametrically contrary to the 2002 statement, as follows:

The market for large company audits lacks sufficient competition and does not work well for customers. It is highly concentrated, largely supplied by four big firms, with clients rarely switching between auditors. There are also high barriers to entry for new and smaller competitors. These are not the indicators of a competitive market (OFT, 2011).

The underlying arguments of high concentration and the lack of sufficient competition had been heard before. Similar to independence, concerns about the lack of competition in the audit market, tied to the concentration of the Big N⁸¹ firms, had already been raised previously. Most notably, the Metcalf Commission Staff Study of 1976 was eminently critical of the domination of the then eight largest firms and even specifically recommended within its conclusions that: 'Congress should consider methods of *increasing competition* among accounting firms for selection as independent auditors for major corporations (US Senate, 1976, recommendation 4, emphasis added). The staff study also went on to

⁸⁰ Case No COMP/M2810 – Deloitte & Touche/Andersen (UK), 01/07/2002

⁸¹ N refers to the contemporaneous number of large audit firms at the time, which historically has varied from 8, 6, 5, and now 4 through mergers and the collapse of Arthur Andersen post-Enron.

recommend, as a means of achieving this increased competition, a consideration of mandatory audit firm rotation. Whilst mandatory audit firm rotation was not then recommended in the final report released, a critical link between competition and mandatory rotation had been made which would re-surface time and again within the debates on audit quality. Elements of this interconnectedness were already seen within the discussion in section 5.1 on the rise of independence and how mandatory rotation was put forward within the debates as a potential remedy.

Important to note, however, is that previous arguments had also conversely been that of *too much* competition, allegedly leading to cost pressures which have had a negative impact on quality. The Cohen Commission asserted in 1978 as follows:

It is not the lack of competition but possibly *excessive* competition that appears to present a problem to the public accounting profession today. Time and budget pressures frequently cause substandard auditing (Cohen Commission, 1978, Section 9, emphasis added).

This argument was then seen again in the 1990s in the UK with the economic recession taking hold combined with the removal of advertising prohibitions, which led to allegations of severe price cutting ('lowballing') by the firms. With the 'optimum' level of competition difficult to ascertain and subject to perception, this instance at the very least highlights not only the recurring but the malleable nature of some of those issues connected to the quality discourse. This will be examined further in chapter six.

For now, this section will investigate how the confluence of the ideology of the free markets, the stability of the capital markets, and the EU single markets project increasingly became the lens through which the audit quality problem was articulated, leading to the problematization of the lack of competition as one of the central issues of audit quality in the decade leading up to 2014⁸². In addition, failures and crises during this period continued to exacerbate the discourse on audit quality and arising liability concerns of the audit firms post-Andersen collapse led to the firms themselves further solidifying the connections between the stability of the capital markets and the issue of competition.

⁸² Mandatory audit firm rotation was legislated in both the EU and the UK in 2014, effective for 2017.

5.2.1 Ideology of the free markets and prioritising the stability of the capital markets

In chapter four, we examined how a growing preference for de-regulation in the US as a mode of regulation under the Reagan administration helped in part to construct an environment whereby peer review emerged as the advocated regulatory technology for quality. The close ties between Reagan and Thatcher reinforced this view within the UK which manifested itself as part of a wider movement now commonly referred to as neo-liberalism (Harvey, 2005) or 'Thatcherism' (Hall, 1983) in the UK. Cooper et al (1996) provide an account of how by the late 1970s, liberal economic theory – 'a belief in the effectiveness and disciplinary effect of free markets, and in the value of a retreat from Keynesianism to monetarism from the State was not to intervene in the real economy' (p. 594) and how this ideology was affecting not just economic but also social policy in the UK (*ibid*).

For the current episode and the audit field specifically, this ideology manifested itself within the audit environment in different ways. In 1981, pressure from the Monopolies Commission and the Office of Fair Trading led to the permitting of advertising by audit firms which until then had been prohibited. This was a marked change within the audit market in the UK and the influence of a free markets ideology in enabling this change was commented upon at the time within a lead article in Accountancy:

The two, possibly conflicting, influences of 'consumerism' and free competition now mean that freer advertising for 'closed-shop professions' will be seen as politically desirable (and ideologically sound) whatever the political complexion of those in power (Accountancy, 1981, p. 1)

In addition, these ideals could also be observed within key regulatory documents at the time playing a role thereby in shaping contemporaneous debates. In Cooper et al's (1996) examination of the implementation of the EU's 8th Company Law Directive, they found that questions of the incorporation of audit firms as an alternative ownership structure (several countries in the EU had a requirement that a minimum proportion of its owners were actual auditors) emerged not as responses to the requirements of the Directive, but as a means of promoting audit firms as successful players in the international market for audit services (p. 609) which by then had become a key tenet of the government's drive for improving the competitiveness of industry. This was also significant in that it represented another manifestation of how audit was being called upon to realise these free market principles.

This rising influence on the audit market itself corresponded also with developments internationally whereby, following the Asian crisis of 1997, 'financial stability' began to be

seen as a potential problem in a rapidly globalising world (Humphrey et al, 2009). A new organisation called the Financial Stability Forum was set up by the G7 in 1999, a key mandate of which was to set up a system of standards and codes for good financial practice. Those countries who complied with such standards and codes would gain better access to finance from the IMF and more widely from the financial markets which in theory would further encourage the use of the standards and ultimately, it was reasoned, improve financial stability (Wade, 2007b as cited in Humphrey et al, 2009). These developments formed part of a much wider international financial architecture which has been examined by Wade (2007a) and Humphrey et al (2009). For current purposes, the stability of the financial markets was becoming a rapidly increasing and global priority and implicated auditing in two important ways: the inclusion of ISA's in the FSF's recommended list of standards augmented the role of audit in ensuring financial stability and secondly, the prioritisation of the stability of the markets would come to be increasingly seen as being applicable to the audit market itself. In so doing, a new visibility of audit market structure issues became apparent, having been constructed in these ways. This will be discussed further below.

Concern with the stability of the capital markets became further intensified after the 2007 global financial crisis, and also when considered against a backdrop of the EU's single market project. This will be considered next.

5.2.2 EU single market ambitions

Closely linked to this profound belief in the free markets were developments within the EU during this period, and in particular its goal of achieving a 'single market'. In 1992, the Treaty of Maastrict laid the basis for further cooperation of the member states in foreign and defence policy and critically, in the creation of an economic and monetary union, to include a common currency. This paved the road to the development in 1993 of the 'single market', the idea that the EU is seen as one territory without any internal borders or other regulatory obstacles to the free movement of goods and services. The 1993 agreement was premised upon four 'freedoms' of movement of goods, services, people and money. Further underpinning this ideal was that 'a functioning Single Market stimulates competition and trade, improves efficiency, raises quality, and helps cut prices.'⁸³ In itself, these underpinnings forged the connection between the stimulation of competition and quality. The EU currently proclaims that 'the European Single Market is one of the EU's greatest achievements' (ibid). A new currency, the euro, was launched in the world money markets on 1 January 1999 and became the unit of exchange for all EU member states except Denmark, Sweden, and the UK. Efforts were then moved onto supporting a 'constitution for

⁸³ http://ec.europa.eu/growth/single-market/index_en.htm

Europe' and the Treaty of Lisbon, which invoked the idea of an 'ever closer union', was approved at the EU intergovernmental conference of the 27 member states held in Lisbon in December 2007. The Lisbon Treaty came into force on 1 December 2009 and the European Union officially replaced and succeeded the European Community.

Within the context of these developments and in support of the EU's single market ambitions, the overall objective of creating an efficient EU capital market by the mid-2000's became the European Council's target (EC, 2003). Critically, it was not only towards achieving a single market within the EU which was of importance - these ideals were soon transferred to the audit market *itself* (Humphrey et al, 2011). In a 1996 consultation on 'The Role, the Position and the Liability of the Statutory Auditor within the European Union', Section 8 of the Green Paper referred specifically to this issue and stated:

Despite the public interest considerations involved in the statutory audit, here is no convincing reason why the Treaty provisions on freedom of establishment and freedom to provide services should not fully apply to the trade in audit services (EC, 1996, p. 35 also cited in Humphrey et al, 2011, p. 434).

This extension of the single market principle to the audit market itself was particularly significant for the audit quality discourse to come as that which posed a threat to the achievement of this principle became understood as attendant issues and priorities. Applied to the audit market, the implications included an open concern for market structure issues such as the concentration of the Big 4 firms, the lack of choice within the market for large companies and more explicitly, the consequent impact this would have on competition – here, the presumption of which the extant market was lacking. Indeed, in a communication from the EC to the European Council and Parliament on 'Reinforcing the statutory audit in the EU' published in the aftermath of Enron, the document explicitly concludes with the following under 'Market structure and access of the EU audit market':

The financial reporting scandals in the US have led to the loss of one of the 'big 5' international networks of accounting firms. As a consequence, only four big international networks of audit firms remain. This could potentially raise *competition concerns*...A high degree of concentration could make *market access* for audit firms in the EU increasingly difficult. The *impact on the audit market* of the loss of one of the large networks is being examined by the responsible department on a country by country basis. Questions were also raised in the European Parliament on the concentration of the *audit market* in the EU...The Commission proposes to carry out a study into the present structure of the *audit market(s)* in the EU. (EC, 2003, para 4.3, all emphases added).

In 2007, the EC released the following statement to follow an independent study commissioned to study ownership rules of audit firms, showing how improving competition in the market had now been prioritised and were being carried through:

The European Commission has published an independent study on the ownership rules that apply to audit firms and their consequences on audit market concentration. The study analyses whether changes to the ownership rules of audit firms might help *increase the number of international players in the audit market...* The study will contribute to the Commission's work on how to *improve competition in the audit market* (EC, 2007, emphasis added).

In these passages, we can clearly see how problems of the audit had now become articulated through the lens of promoting an audit market, the consequence of which was the prioritisation of improving market access and competition. However, it was only through this prioritisation under the ideology of the free markets, the EU's single market ambitions and the high profile failures which disrupt the public confidence in those markets, none of which were necessarily, or perhaps even at all, rooted within a systemic failing of the efficacy of the audit, which *made* competition an issue. With such a problematization of competition as a key issue within the audit, the 'natural' remedy would be to look for ways to inject more competition into the market.

With the financial crisis arising soon thereafter, and these problems of the audit still 'unresolved', the debates became further exacerbated. The discourse at the EU level also became closely connected with that of the UK. The UK OFT fed into both the EU Green Paper on audit policy (2010) and the House of Commons Treasury Committee inquiries (2009) into the banking crises. The UK government's response to the results of the inquiry re-affirmed these same priorities as follows:

The Government notes the Committee's findings. The Government's policy towards the audit of the largest businesses aims to meet three distinct policy objectives: audits that are *high quality* and *independent* of the body being audited; *a competitive market* in the supply of audits; *an audit market* that is resilient and could withstand the withdrawal of one of the major firms....(House of Lords, 2011b, para 173, emphases added).

Specifically, independence and competition emerged as the central issues of the audit quality discourse during this period and the articulation of the audit quality problem had in this way become increasingly normalised. In the heightened environment of concern post 2007 financial crisis, these unresolved 'problems' would only become further exacerbated in the

discourse. In November 2011, after a consultation period given impetus by the financial crisis, the Commission adopted proposals for a regulation on the quality of audits of public-interest entities and for a directive to ‘enhance the *single market* for statutory audits’, a clear application of the single market principles to the audit market. The headline read: ‘Restoring confidence in financial statements: the European Commission aims at a higher quality, dynamic and open audit market’ and the accompanying statement read as follows:

The 2008 financial crisis highlighted considerable shortcomings in the European audit system...Under the proposals adopted today by the European Commission, this situation is to change by clarifying the role of the auditors and introducing more stringent rules for the audit sector aimed in particular *at strengthening the independence of auditors* as well as greater diversity into the current *highly-concentrated audit market*. Furthermore, the Commission is also proposing to create a *Single Market* for statutory audit services allowing auditors to exercise their profession freely and easily across Europe, once licensed in one Member State. There are also proposals for a strengthened and more coordinated approach to the supervision of auditors in the EU. Taken together, all the measures should *enhance the quality* of statutory audits in the EU and restore confidence in audited financial statements, in particular those of banks, insurers and large listed companies (EC, 2011, emphases added).

5.2.3 Failures and crises

As seen in chapter 4, crises and failures punctuate the debates on audit quality. Their very nature brings to the foreground the ongoing difficulties surrounding the audit by serving as a reminder, in a very public way, that the audit is fallible and invariably triggers action for remedies. Even before the collapse of Enron, business failures, be they audit failures or that caused by the prevailing economic climate (with the public unable to discern the difference), have historically prompted a new cycle, or wave, of regulation (Kinney, 2005).

For this particular episode spanning commencing from the early 1990s onwards, the recession of the early 1990s, accompanied by another spate of failures such as Polly Peck International (1990), BCCI (1991), and the Maxwell companies (1992), the collapse of Enron in 2001 and the financial crisis of 2007 once again all served to intensify the debates on audit quality. As in previous chapters, the argument being put forward does not refute the significance of the role failures and crises have played in punctuating the discourse - only that failures *alone* have not been the sole cause of either the rising discourse on quality *nor* do they serve as definitive ‘proof’ of the problematization which arises as central to that discourse, notwithstanding the self-evident nature of that discourse which ensues. A key

role of failures and crises is their part in providing the public pressure and regulatory scrutiny which constructs an environment for change. A further implication arising is that they can initiate further, specific concerns.

In the aftermath of the demise of Andersen, liability concerns of the remaining firms emerged as a central issue for the profession practice arena. In a joint statement released in 2006 at the Global Public Policy Symposium in Paris, the then largest Big 6 firms internationally, in an attempt to generate support for their cause of reducing liability exposure, appealed to the stability of the capital markets which, as set out above, had arisen as a key issue:

That the current *audit services market is competitive* does not mean that it can afford to lose another major network, through a liquidation-forcing liability verdict or criminal prosecution. Indeed, there now is widespread recognition throughout the global enforcement community that the loss of another major audit network would *have a major deleterious impact on the capital markets* (DiPiazza et al, 2006, p. 15, emphasis added).

Added to this was an appeal to harmonise differences in liability regimes to enable ‘truly global networks’ which was then linked with the promise of ‘strengthening audit quality’ (see p. 14): ‘But while we believe we are able to deliver *high quality audits* of global companies, our networks cannot become truly global...without further liberalization and harmonization of national [liability] rules’ (p. 14, emphasis added).

Even within this concern of firm liability, we can already see the interconnections with the wider economic discourse prevailing at the time which provided the framing through which auditor liability regimes was being articulated. Within the free market environment as set out above, it was by drawing upon this prioritisation of the stability of the free markets through which the firms attempted to raise their concerns of limiting liability. In so doing, it reified connections between the discourse of liability concerns, that of the capital markets, and of quality. By further raising the threat to competition should another of the big firms suffer a collapse, the potential issue of the lack of competition became further solidified. This was deemed a significant enough concern at the time, as evidenced by the then European Commissioner for Internal Market and Services Charlie McCreevy’s agreeing to undertake an investigate into the specific issue of audit firm liability. This plan was presented as follows:

As a first step, we will carry out a study on the economic impact of the alternative liability regimes, the competition in the market and the availability of the insurance (McCreevy, 2005).

Whilst the focus of that study was on liability regimes and reducing the risk of further concentration in the audit market, this was yet again another manifestation of the increasing problematization of competition within the audit services market.

It is put forward here that the convergence of the above factors enabled a fully articulated issue of competition within the audit services market, which concurrently implicated audit quality. However, this was only made possible through the very specific ideologies and priorities of the free market, the EU single market objectives, failures and crises and the relays in between all of these discourses through which this particular problem of the audit quality materialised. With the audit quality problem so conceptualised, the possibility of mandatory audit firm rotation became a more likely and indeed even ‘logical’ solution to the problem. Despite academic and other research pointing towards, at best, mixed results in terms of its relationship to audit quality (SDA Universita Bocconi, 2002), particularly within the empirical research setting, mandatory rotation was in any event promulgated. This next section will trace the rise of mandatory rotation within this context and see how mandatory rotation became increasingly understood as the solution to audit quality once this active articulation of the problem as one of competition, and also that of independence, was established.

5.3 The rise of mandatory audit firm rotation

5.3.1 UK developments

In the days after Enron, a working group entitled the Co-ordinating Group on Audit and Accounting ('CGAA') issues was formed by the Chancellor of the Exchequer and the Secretary of State for Trade and Industry in order to investigate the UK's arrangements for audit and accountancy regulation. In their final report, the issue of competition was raised although it deferred to the OFT's decision not to commence a formal investigation and concurred with the OFT's conclusion to keep the market under review (CGAA, 2003, p. 15). In arriving at that conclusion, the CGAA also concurred with the OFT's justification on the grounds that 'the market for auditing and accountancy is highly concentrated; has become increasingly global; and that taking action at a national level does not appear to be the best way to proceed,' (*ibid*) alluding to the significance of wider, international debates on the issue. In its investigation into the key issue of independence, the CGAA concluded that internal audit partner rotation after five years should be adopted, but *not* mandatory audit firm rotation. The arguments *for* mandatory firm rotation set out in that report were as follows:

...in a long term audit relationship, the auditors will tend to identify too closely with management, their proper professional scepticism will be diluted and they will be more likely to smooth over areas of difficulty in order to preserve the relationship and in particular the long term income which flows from it. In other words, the longer their tenure, the more likely that the auditors will be less rigorous, more inclined to rely on what they are told by management and less likely to press on difficult issues. *All these factors suggest that rotation would enhance audit effectiveness and quality. In any event, whether or not rotation enhances independence in fact, it improves the perception of independence and thus confidence in audit.* And, by requiring companies to make a change, it *encourages competition.* (CGAA, 2003, p. 25, all emphases added)

Whilst the CGAA did not recommend firm rotation, on grounds of the cost implications and citing the lack of evidence of an actual correlation to an improvement in audit quality from those countries (Italy and Spain) which had adopted such a measure (SDA Universita Bocconi (2002)), the above arguments were telling in several respects. It pointed towards a continued belief that the perceptions were significant in underpinning confidence in the audit and also highlighted the continued prioritisation of the market more generally by drawing upon competition as a potential benefit of rotation. With the concerns of independence and competition by then firmly established, mandatory rotation was, despite the explicit acknowledgement that 'actual' improvements to independence were questionable, made and seen to be a viable option to solve these issues.

The CGAA report also considered the issue of mandatory *tendering* also being considered by the OFT at that time. Citing from a statement from the OFT 'As long as the risks....can be controlled, we believe that compulsory re-tendering could be potentially pro-competitive and may even open up the market to mid-tier firms' (CGAA, 2003, p. 27), the CGAA also discounted this as an option on the basis that it would cut across the enhanced role they saw for audit committees in the appointment of auditors. This statement, did, however, confirm once again that competition was now seen as an almost taken for granted 'good' thing for the market: opening up the audit market to mid-tier firms would be beneficial to address the perceived difficulties of market concentration.

With issues of competition and market structure issues now established, along with concurrent EU developments in the area (particularly with respect to ownership rules, liability regimes and market concentration), the FRC and DTI jointly commissioned a study entitled 'Competition and choice in the UK audit market'. This report concluded in 2006

that they UK audit market was characterized by a high degree of concentration, infrequent competitive tendering, little choice primarily in the FTSE 100 financial services sector (which would be exacerbate by the loss of another Big 4) and finally, that these issues were likely to persist due to significant barriers (FRC/Oxera, 2006, p. i). This then led to the formation of the Market Participants Group by the FRC to address some of these issues who shied away from such blunt regulatory instruments and instead developed 15 recommendations which were primarily grounded in an approach of greater disclosure, promotion of understanding and transparency (FRC, 2007) but were subsequently accused of lacking teeth. By the FRC's own admission: 'By 2010, all but one of the MPG recommendations had been implemented, but there has been no discernible change to levels of market concentration. It is clear to us that audit regulators do not have sufficient tools to effect changes to market structure...' (see www.frc.co.uk) and instead deferred to wider regulatory developments which were by then also taking place.

In the aftermath of the financial crisis, the House of Lords Select Treasury Committee announced in 2008 the terms of reference for an inquiry into the banking crisis, seeking to identify lessons which could be learned. There, the Committee concluded that whilst auditors had not failed within their duty, the fact that the crisis occurred without any warning from auditors once again called into question their usefulness (House of Lords, 2009). A secondary inquiry was launched in 2010 by the House of Lords Select Committee on Economic Affairs specifically on the heightened issue of Auditors: Market concentration and their role. The inquiry stated that 'concern about concentration of large-firm audit in the hands of the Big Four, and the impact on competition, choice, price and quality was our main motive in launching this inquiry' (House of Commons, 2011, p. 9) and that further, 'concerns about market concentration and about the scope, relevance, quality and regulation of traditional audit were exacerbated by the financial crisis of 2007–09' (House of Commons, 2011, p. 8). The inquiry examined a number of measures to reduce concentration and increase competition including mandatory tendering (recommended) and rotation which was still deemed to be 'radical' (p. 16). As one of the main conclusions reached, the inquiry recommended that the OFT conduct a detailed investigation of the large-firm audit market, with a view to an inquiry by the Competition Commission. Whilst recognising that the global reach of the Big Four firms went beyond the scope of a national competition authority (cited previously by the OFT as a reason not to investigate), the inquiry concluded that 'when London is both the incubator of at least some of the Big Four and one of the world's leading financial centres, it seems right for the UK to take a lead' (House of Lords, 2011, abstract).

With this pressure placed on the OFT to act, and having previously decided that no competition issues had been brought to their attention, the OFT announced on 17 May 2011 that it had 'provisionally decided that the competition issues that it had identified in the audit market passed the statutory test for referral to the Competition Commission' (OFT, 2011) and held a series of roundtable and meetings during June to consider potential remedies for the market. In July 2011, the OFT announced that it had reached a provisional decision to refer the audit market to the CC, and opened a public consultation which ran for six weeks. Following this process, the OFT concluded that there 'is a reasonable chance that appropriate remedies will be available to the CC in the event that it finds one or more adverse effects on competition' (OFT, 2011) and accordingly announced its referral to the CC in October 2011. Responding to the OFT's decision to refer the supply of statutory audit services to large companies to the Competition Commission, Lord MacGregor, chairman of the House of Lords Economic Affairs Committee (EAC), reaffirmed the problem of audit as a failure of competition:

I welcome the OFT's decision. One of the main recommendations of the Economic Affairs Committee's Report in March on "Auditors: market concentration and their role" was that the OFT conduct an in-depth investigation into the audit market, with a view to a possible referral to the Competition Commission. The EAC did so because of the continuing dominance of the Big Four in the large-firm audit market and the failure of previous attempts to introduce *greater competition*.⁸⁴ (emphasis added).

The CC inquiry commenced shortly thereafter, and under the powers of the Enterprise Act 2002, proceeded to investigate more narrowly whether they were features of the audit market which prevent, restrict or distort competition with the supply of audit services to large companies in the UK and whether there were adverse effects on competition. Their final report, released in 2013, recommended mandatory *tendering* at least every ten years to increase competition and other measures to strengthen the accountability of the auditor to the audit committees. In reaching these conclusions, the CC also took into account concurrent developments within the EU at this time which converged with the CC inquiry. EU regulation, to which this chapter now turns, by then had mandated an actual *change* of auditor for public interest entities every ten years with an allowance for one extension giving a maximum period of 20 years provided that retendering takes place at least every ten years. With the UK recommendations needing to tie into that of the EU, the effect was to install

⁸⁴ See news announcement available at:
<http://www.parliament.uk/business/committees/committees-a-z/lords-select/economic-affairs-committee/news/audit-inquiry-ofc-announcement/>

mandatory rotation with the UK every 20 years, with mandatory tendering after ten. We will outline the EU developments before providing some summary comments on this section.

5.3.2 EU developments

Debates in the UK were not being held in isolation and were nested within wider deliberations being held at the EU level. A number of consultations and publications were also released by the EU during this time. In each of these, we can observe yet again how problems of audit were being articulated through the lens of prioritising the audit market (with its attendant issues) and that of independence.

In the aftermath of Enron, the EU released its reaction to the collapse (EC, 2002), with the accompanying press release highlighting again the prioritisation of the capital markets:

The paper emphasises that the EU is already working on most Enron-related regulatory issues through the Financial Services Action Plan, which aims to establish an *efficient and competitive capital market* that deserves investors' trust (EC, 2002b, IP/02/584, emphasis added)

This release was closely tied to a related publication 'Statutory auditors' independence in the EU', a result of a two year project wherein efforts to harmonise independence rules across member states were released in a series of principles based recommendations. Whilst these were set as 'recommendations', the Commission also made clear that action by member states was expected. Then Internal Market Commissioner Bolkestein stated as follows:

Although the Recommendation is not legally binding, it will serve as a clear benchmark of good practice that the Commission expects to be immediately applied throughout the EU audit industry. In three years time, the Commission will review how the Recommendation has been applied in practice and will consider whether binding EU legislation may then be required. However, the Commission may act earlier if it is not satisfied with Member States' application of the Recommendation (EC, 2002a, IP/02/723)

It was within this statement on independence where the principle of 'rotation' also came into effect. In a pre-cursor to mandatory firm rotation, *internal* rotation of the key audit partner after 7 years was installed as a measure to improve independence. Whilst mandatory firm rotation was not yet deemed compulsory at that stage, the concept became further rooted as one means by which independence of auditors could be improved.

From the mid-2000s onwards, a number of consultations and commissioned external reports were released on issues relating to the audit but almost all articulated through a prioritisation

of the impact on the capital markets. Following McCreevy's statement in 2005 regarding out a study on the economic impact of the alternative liability regimes and the competition in the market (see section 5.2.3), a consultation on 'auditors' liability and its impact on the European capital markets' was released (Jan, 2007). In Oct of that year, the EC published a commissioned study⁸⁵ on the ownership rules that apply to audit firms and their consequences on audit market concentration. The study analysed whether changes to the ownership rules of audit firms might help increase the number of international players in the audit market, contributing to the Commission's work on how to improve competition in the audit market (EC, 2007). The central focus of all these consultations was that of market concentration and its possible detrimental effects on independence.

In June 2008, the results of the consultation on the limitation of auditors' liability were released. There, the EC stated explicitly that its recommendation was made with the main purpose to 'encourage the growth of alternative audit firms in a competitive market.' Internal Market and Services Commissioner McCreevy said at that time:

After in-depth research and extensive consultation, we have concluded that unlimited liability combined with insufficient insurance cover is no longer tenable. It is a potentially huge problem for our capital markets and for auditors working on an international scale. The current conditions are not only preventing the entry of new players in the international audit market, but are also threatening existing firms. In a context of high concentration and limited choice of audit firms, this situation could lead to damaging consequences for European capital markets (EC, 2008a).

In arriving at its recommendation to limit auditors' liability, the conclusions were reached clearly with the stability of the markets in mind and further that 'good' capital markets would require further choice and reduced concentration of audit firms. It was also within this context that a follow-up consultation was established in November 2008 'on ways to help create more market players' (EC, 2008b). In 2008, the final report on the consultation on control structures was released which took place in the midst of the aftermath of the financial crisis. The emphasis on the capital markets, explicitly linked to audit quality, became even more pronounced with McCreevy stating:

The current financial crisis makes it vital that we have a truly sustainable audit market, and the consultation results published today provide valuable insight into problematic issues. The Commission will now carefully consider what actions can be taken

⁸⁵ Report prepared by Oxera: Ownership rules of audit firms and their consequences for audit market concentration (October, 2007)

at EU level to *encourage new market players*, whilst ensuring that auditors' independence and *audit quality* are not undermined (EC, 2008b, emphasis added).

With the spotlight on corporate governance and audit issues, yet again after crisis, on October 2010 the Commission launched a consultation on the role of the auditor, the governance and the independence of audit firms, the supervision of auditors, the configuration of the audit market, the creation of a single market for the provision of audit services, and others. The Commission were also by their own admission 'keen to assume leadership at the international level on this debate' (EC, 2010, p. 3). The associated Green Paper: Audit Policy: Lessons from the Crisis⁸⁶ opened with three general questions including 'do you believe that the general level of "audit quality" could be further enhanced?' (EC, 2010, p. 5), yet again implicating audit quality within these contemporaneous concerns. The introduction of the document highlighted key concerns of independence (p. 3) and market concentration (p. 4) and within the body of the document, put forward the following as a potential remedy to address these issues,

Mandatory rotation can not only *enhance* the independence of auditors...it could also *act as a catalyst to introduce more dynamism and capacity into the audit market*...Such mandatory rotation should be accompanied by mandatory tendering with full transparency as regards the criteria according to which the auditor will be appointed. Quality and independence should be key selection criteria in any tendering procedure (EC, 2010, p. 16, emphasis added)

In citing both the promise to enhance independence *and* dynamism in the market, both now firmly established as particularly pressing problems, the possibility of mandatory rotation became an increasingly viable option. This was despite a number of complex debates and having previously been seen as too blunt a regulatory instrument (e.g., CGAA, 2003) with a number of potential disadvantages. In defending some of the more radical measures, Internal Market and Services Commissioner Michel Barnier reiterated arguments and problems of the market and independence and further emphasized the need to restore confidence in the audit:

Investor confidence in audit has been shaken by the crisis and I believe changes in this sector are necessary: we need to restore confidence in the financial statements of companies. Today's proposals address the current weaknesses in the EU audit market, by eliminating conflicts of interest, ensuring independence and

⁸⁶ Humphrey et al (2011) provide a detailed analysis on the development of this green paper and its underlying perspectives and assumptions.

robust supervision and by facilitating more diversity in what is an overly concentrated market, especially at the top-end (EC, 2011).

By 2013, concerns with audit were firmly positioned as one of ‘reforming the audit market’ and with the heightened pressure for action, the ongoing focus on independence and competition/concentration issues as the key problem of audit, the desire to be seen to be leading the debate at the EU level, and the prioritisation of the capital markets especially at the EU level, the agreement reached on mandatory audit firm rotation along with other regulatory measures were hailed by EU Commission Michel Barnier as follows:

I welcome the agreement reached this morning between the European Parliament and EU Member States on the reform of the audit sector. This is a *first step towards increasing audit quality* and re-establishing investor confidence in financial information, an essential ingredient for investment and economic growth in Europe.

Although less ambitious than initially proposed by the Commission, landmark measures to *strengthen the independence of auditors* have been endorsed, particularly in the auditing of financial institutions and listed companies. This will ensure that auditors will be *key contributors to economic and financial stability*.

With the agreement, audit firms will be required to rotate every 10 years....The new rules also provide innovative tools to limit the risk of conflict of interest. To avoid the risk of self-review, several non-audit services are prohibited under a strict ‘black list’, including stringent limits on tax advice and on services linked to the financial and investment strategy of the audit client. In addition, a cap on the provision of non-audit services is introduced.

Taken together, the agreed measures will considerably *strengthen audit quality* across the European Union (EC, 2013, emphases added).

Barnier’s belief and explicit link between the benefits of mandatory rotation and audit quality were also separately reinforced: “mandatory audit firm rotation would boost the quality of audit, shattering the perverse pressure on partners not to lose long-standing clients” (Orlik, 2011, p. 1). Following this agreement from the member states, the revised directive was approved on 3 April 2014. Announcing this approval, the EC stated as follows ‘The new rules will strengthen the quality of statutory audit, reinforce the independence of statutory auditors, and improve supervision’⁸⁷, converging with the renamed Competition and Market Authority in the UK releasing its results of its investigation into the audit market.

⁸⁷ See http://ec.europa.eu/finance/auditing/reform/index_en.htm

5.3.3 Summary comments

This section has outlined some of the key developments and comparatively quick timeline leading to the legislation of mandatory audit firm rotation in EU and UK particularly given the history, longevity and complexity of the debates regarding its use as a regulatory intervention. Whilst being mentioned in at least as early as the Metcalf Commission in 1976, mandatory rotation had not, however, ever been seriously considered or adopted in any significant scale within Europe⁸⁸ or the US. Indeed, recent academic research has summarised some of the strongly divergent views on the issue and also the unsettled nature of its relationship to audit quality (Jenkins and Vermeer, 2013). The disadvantages cited were many and were well known to governments and regulators. For example, the House of Lords Select Committee on Economic Affairs cited some of these disadvantages (House of Commons, 2011, p. 16) and another comprehensive list was generated by the CGAA in 2003. These included: the possibility of the negative effects on audit quality and effectiveness in the first years following a change; substantial costs of having to switch regularly; no strong evidence from Italy or Spain which had mandated audit firm rotation; consideration of the issue by Ireland and Australia who concluded against such a requirement and indeed competition implications itself expressed by the OFT characterising it as a form of compulsory re-tendering with one of the potential bidders excluded (CGAA, 2003, p. 26 – 27). Whilst regulators in the US were watching EU developments with interest, such a measure was not adopted in that jurisdiction. The specific and necessary pre-conditions, set out in this chapter, were not present in that context.

Thus, it was under this, at best, grounding of uncertainty from which mandatory rotation prevailed. This, is it argued, was not necessarily or entirely rooted within any proven efficacy issues of the audit, despite the many, unsubstantiated claims to the contrary especially at the EU level. It was within the re-intensification of independence concerns, the problematization of the issue of competition arising within the context of the EU single and capital market imperatives, the pressures to act from large scale failures and to ensure those actions were highly visible, the belief that perceptions could sustain confidence within the capital markets, the liability fears from the remaining Big 4 should another firm be allowed to fail and the political ambitions within the EU to be held at the centre of debates which together provided the necessary conditions of possibility for mandatory rotation to rise. Bound together with and emerging from all of these interconnecting debates and discourses was the promise to deliver audit quality.

⁸⁸ With the exception of Italy and Spain

5.4 Linkages

The analysis presented in sections 5.2 and 5.3 attempted to trace the pre-conditions which enabled a very particular conceptualisation of the audit quality problem to arise. Amidst the interrelations between the discourses, key linkages needed to be forged (forming the actual intersections) between disparate ideas and attached to quality in order for mandatory rotation to have been implemented - all the more so given its unproven and radical nature. This section will examine some of these key linkages and draw attention to how the linkages themselves also needed to be connected, through a sequence of linkages with common ideas, in order for mandatory rotation to have obtained. In itself, mandatory rotation was the final embodiment and solidification of the connection between independence problems and competition ideas with quality.

A summary of these linkages examined below has been set out in the following table:

Table 5.1: Summary of paradigmatic linkages leading to mandatory rotation

Linkage	Connection of ideas made	Form	Type of linking
Metcalf Commission (1977)	Competition and audit market; Competition and mandatory rotation; Mandatory rotation and independence	Document	Rationalisation
EU (1996) Consultation	Quality, single market and audit market	Document	Brokering, rationalisation
EC (2002c) on internal rotation	Quality, rotation and independence	Document	Rationalisation, repetition
EU (2010) Consultation	Quality, rotation, independence, competition	Document	Repetition, mediation
House of Lords (2011) on mandatory tendering	Quality, tendering and competition	Document	Rationalisation

5.4.1 Metcalf Commission

As seen earlier in this chapter, the idea of mandatory rotation was not new to this decade and had been first most visibly raised within the Metcalf Commission Staff Study of 1976. In this highly influential and critical study, the two key accusations were the SEC's failure to exercise appropriate oversight of the accounting profession, and the dominance of the then Big N (8) largest accounting firms - which the study alleged had led to their collective failure to carry out their duties independently (US Senate, 1976, p. v). A number of recommendations were made regarding the framework for standard setting, periodic quality

reviews of work, and also radical suggestions for increasing competition amongst the accounting firms for audits of major companies. Measures recommended for increasing competition included a ‘mandatory change of accountants after a given period of years’ (p. 21) and also ‘amendment of Federal securities laws to require that more than one accounting firm be on the ballot at annual meetings’ (*ibid*). Separately, the study also recommended that the federal government should investigate ways to ‘relieve excessive concentration in the supply of auditing and accounting services to major publicly-owned companies (p. 23).

The Metcalf Staff Study put forward a number of controversial ideas and proposals at the time regarding the governance structure of the profession and responsibilities. However, coming so soon after the formation of the FAF and FASB in 1972, and due to this highly controversial nature, not many of these recommendations were actually enacted into law. The final report issued two years later tempered many of these initial ideas. For purposes of this current episode, however, it is put forward that this staff study served as one of the early linkages of this constellation in connecting together some disparate and controversial ideas. Not only did the staff study serve as one of the earliest and most high profile documents which further problematized independence, it linked those problems of independence with levels of market concentration, through a rationalisation exercise centred on the dominance of the large firms. The very opening pages of the 1760 page staff study contained precisely this rationalisation exercise. From page 4 onwards, under the heading ‘The “Big Eight” Accounting Firms’, statements such as the following highlighting the size and dominance of the firms could be seen throughout:

These eight firms are *so big and influential* in relation to other accounting firms that they *dominate* the practice of accounting in the United States and probably throughout the world (US Senate, 1976, p. 4, emphases added).

This was then followed by repeated claims regarding the size and influence of the Big Eight firms:

The *influence exercised by the “Big Eight” firms far exceeds* that which might be expected from the number of CPAs working for them....Because of their *large size*, the “Big Eight” firms exercise *substantial influence* directly on accounting practices promulgated or approved by the Federal Government. They also exercise *substantial indirect influence* through the American Institute of Certified Public Accountants (AICPA), which they control, and through the accounting practices followed by their corporate clients (US Senate, 1976, p. 4-5, emphases added).

This problematization with the size and influence of the firms was then linked to an issue of concentration: ‘The supply of auditing and accounting services to corporations listed...is

heavily concentrated among the “Big Eight” firms’ (p. 5). And from there, with concentration now constructed and seen as a concern, the related idea of competition almost ‘logically’ became seen as an issue: ‘Excessive market concentration traditionally causes problems concerning the price and availability of goods and services. The concentration of major corporations as clients of the “Big Eight” indicates a need for an investigation of possible *anti-competitive* effects’ (*ibid*, emphasis added).

With the connections between independence, concentration and competition so rationalised, the concept of mandatory rotation could be more readily seen as a potential and even logical solution to problems of competition and independence as so conceived. In addition to this, importantly, was the underlying assumption implicit in these ideas, that competition was ‘good’ for auditing: it would prevent auditors from becoming too comfortable in their relationship with their clients, with newer auditors presumed to more likely act with greater independence. Counter arguments to this were the high costs of switching and the risk of *more* failures due to the lack of familiarity with client work processes and procedures. In any event, the key argument is that this relationship was unproven.

Despite audit quality not yet being identified within the Metcalf staff study, this underlying assumption was a significant conceptual linkage which would be drawn upon in order to implicate quality much later (all the more so once independence became subsumed within quality). The staff study was therefore particularly significant as it constructed a critical connection between competition, mandatory rotation *and* independence, the correlation of which was all largely unproven. Indeed, diametrically opposed accusations of too much competition resulting in low-balling and poor performance were also being made elsewhere. The very notion of competition itself therefore, in coming tied with ideas of independence, can also be understood as a linkage. The linking capacity of ideas, however, still need to be made concrete through one of people or documents and it was through this documentary linkage of the Metcalfe Commission where the idea of competition, intertwined with independence, was made concrete within the audit field. It is in this way also that the Metcalf Staff Study served as a key linkage for this constellation in not only bringing in ideas of competition into the audit field, but by also implicitly linking competition *and* independence as being ‘solvable’ by mandatory rotation, through its detailed, and highly critical, rationalisations.

However, as evident with the very few ideas of the staff study which were actually taken up, without then a sufficient chain of linkages and the necessary pre-conditions to enable these ideas and connections to be taken forward, these initial proposals would not be operationalised until some 40 years later and even then, not in the same jurisdiction. A

chain of linkages was required in order for this action to be ‘successful’, which are examined next below.

5.4.2 EU (1996) Green Paper consultation

As discussed in this chapter thus far, a confluence of priorities and discourses led to the problematization of the lack of competition within the audit field. Arguably, the most significant of these was the EU’s single market ambitions through which audit became increasingly called upon to help fulfil. In the 1996 EU green paper⁸⁹ consultation document entitled ‘The role, the position and the liability of the statutory auditor within the European Union’, these priorities could clearly be seen to have already been firmly established. Within that document, the EU’s single market ambitions and the attendant ‘freedoms’ were the explicit lens through which the issue of audit quality was articulated. Statements such as the following, to justify renewed EU action and the release of the Green Paper itself, could be seen:

There is no common view at EU level on the role, the position and the liability of the statutory auditor. The absence of such a common view has a negative impact on audit quality and on the freedom of establishment and freedom to provide services in the audit field (EC, 1996, p. 4).

And further, even more explicitly and emphatically: ‘The justification for EU interest and action in this area rests in the Single Market’ (EC, 1996, p. 7).

With the Single Market so prioritised, bringing to the fore its underlying free market doctrines, it was only then a small step to take in order to apply those same principles to the audit market services itself, which, as discussed earlier in section 5.2.2, was in the event exactly what happened. The *transfer of the single market principles* of ‘freedom of establishment and freedom to provide services’ (EC, 1996, p. 35) to the *audit services market itself* was a critical moment whereby market principles would become applied to the audit field itself.

In this way, this document also served as a key linkage in directly brokering the underlying ideals of the free and single markets and rationalising its applicability to the audit field in a seemingly logical way. As set out in section 5.2.2 and highlighted again here, the document argued that ‘*there is no convincing reason why* the Treaty provisions ...should not fully apply to the trade in audit services’ (EC, 1996, p. 35, emphasis added) thus making this transfer of ideals seem a perfectly rational and logical sequence of events. This document

⁸⁹ Green papers were seen as one of the ‘privileged instruments for consultation of Member States and interested parties’ (EU, 1996, p. 4)

therefore represented another actual intersection between wider EU discourses and ambitions, and auditing. This connection manifested itself not only through this transference of market ideals onto the audit market itself, but also, through the calling upon audit to help deliver these goals:

...the increased reliability of [the financial information published by companies] together with the increased reliability of that information as a result of the audit by an independent and qualified professional were regarded as an important contribution to the completion of the Single Market (EC, 1996, p. 4).

In so doing, the audit *market* became a new priority, with the attendant focus on related issues such as market structure, efficiency, audit firm concentration and of course, competition. These would align with ideas first put forward in the Metcalf Staff Study and in this way, these two linkages, through their underlying ideas, became so connected.

With audit market structure problems so constructed and pinned to audit quality, it would only be a matter of time before ‘solutions’ emerged. The final solution of mandatory rotation would be ‘achieved’ in three distinct stages of regulatory reform, each serving as a key linkage carried by documents which further reified the idea that the problem of audit quality was rooted within a lack of competition in the audit market, intertwined with a problem of independence. With the connections becoming further solidified at each stage, the advent of mandatory rotation became increasingly less ‘radical’ as the connections became further strengthened. The possibility of mandatory rotation came further into light with the sequential establishment of each of these linkages, which were internal partner rotation, mandatory re-tendering and finally, that of mandatory rotation itself.

5.4.3 EU (2002c) Statutory Auditors' Independence in the EU

The 1996 Green Paper referred to above generated over 100 written responses to the Commission with most commentators expressing the view that action at EU level was necessary (EU, 1998, p. C143/13). On 15 January 1998, the European Parliament approved a resolution broadly supporting the Green Paper and stressed the importance of the role of the auditor as an essential underpinning of the Single Market. Further, the European Parliament called upon the Commission to consider whether further legislation would be required to achieve greater harmonisation of independence rules in support of these priorities, symptomatic of the rise of independence within this episode.

As a result of this, the EU Committee on Auditing was created and immediately established statutory auditors' independence as one of their priorities. In 2002, a set of ‘best practice’ recommendations were released under the publication ‘Statutory Auditors' Independence in

the EU: A Set of Fundamental Principles' which explicitly prioritised the capital market and the focus on independence:

The benefits of safeguarding the statutory auditors' independence include efficiencies and other positive effects that, ultimately, contribute to the overall efficiency of the capital markets (EU, 2002c, p. L 191/23)

And further, to implicate audit quality within the discourse: 'This Recommendation is an important step towards assuring audit quality' (EU, 2002c, p. L 191/24). With the problem of audit quality so firmly conceived as a heightened problem also of independence, structural solutions were more readily forthcoming. Section 10 of this 2002 recommendation, entitled 'Senior personnel acting for a long period of time' *repeated* old arguments as follows:

- (1) Trust or familiarity threats may arise where certain members of the Engagement Team work regularly and for a long period of time on an Audit Client engagement, particularly where Public Interest Entity Audit Clients are concerned (EU, 2002c, p. L 191/33)

This document further *rationalised* that action was now required in order to mitigate these threats, despite these threats having been raised many times before and the efficacy of such regulatory devices remaining unproven:

- (2) To *mitigate these threats*, where the audit of a Public Interest Entity is concerned, the Statutory Auditor is required: (a) *as a minimum to replace the Key Audit Partners* (*) of the Engagement Team (including the Engagement Partner) *within 7 years of appointment to the Engagement Team*. The replaced Key Audit Partners should not be allowed to return to the Audit Client engagement until at least a two years period has elapsed since the date of their replacement...(EU, 2002c, p. L 191/33, emphases added).

It was within this recommendation, and document, where the principle of rotation in the EU became established, albeit at this stage only internally with the key engagement partner. However, this principle could only have been conceived of as actionable after the rise of independence became so firmly entrenched within the discourse. The idea of rotation carried with it the implicit assumption that trust and familiarity were central threats to the maintaining of independence, however unproven. An enforced change of audit partner would, however, perhaps enhance the appearance of independence which had also been deemed a priority in order to support confidence in the capital markets. Nonetheless, by re-introducing the concept of rotation and bringing it into the audit field, it solidified the linkage of independence with that of rotation and moreover, *that quality could in this way be*

improved upon. It is in this way that this regulatory document (promulgated as recommended ‘best practice’ along with threats of further action should recommendations not be complied with) has been conceived of as the next linkage in the sequence. It adjoined onto the previous linkages through the commonality of ideas: the role of audit in supporting the capital markets, the significance of independence in carrying out this role and most critically, that rotation could and would enhance that independence.

5.4.4 EU (2010) Green paper on Audit Policy: Lessons from the Crisis

As set out earlier in section 5.3.2, the European Commission launched a consultation in 2010 on ‘audit policy’ which attempted to re-invigorate debate on issues surrounding the audit (e.g., role of the auditor, governance of firms, market structure). In that document, as seen earlier, audit quality was centrally implicated with these issues by serving as one of the three, very opening, organising questions. The other two questions related to the general approach and purpose of the Green Paper, and the need to better set out the societal role of the auditor.

In the EC’s keenness to ‘assume leadership at the international level on this debate’ (EC, 2010, p. 3), the document *repeated* a number of recurring arguments with respect to the audit, such as the importance of independence, the role of audit in re-establishing trust and market confidence, the expectations gap, and the priority of creating a single market for audit services. Further, it re-emphasized the importance and priority of financial stability, and invoked a ‘too big to fail’ argument, with respect to the audit firms, to support this concern:

The potential collapse of one of these firms could not only disrupt the availability of audited financial information on major companies, it would also be likely to damage investor trust and confidence and could impact the stability of the financial system as a whole...The Commission recognises that continuity in the provision of audit services to large companies is critical to financial stability (EC, 2010, p. 4)

From here, the document outlined a long list of items which were to be included in the consultation. Importantly, the concept of mandatory rotation as a potential remedy for problems of the audit was introduced *twice*. Mandatory rotation was presented as an agenda item and potential solution to the ‘threat of familiarity’ under ‘Governance and Independence of Audit Firms’ (EU, 2010, p. 10) *as well as* under the section headed ‘Concentration and Market Structure’ (EU, 2010, p. 15) where it was called upon again to ‘introduce more dynamism and capacity into the audit market’ (EU, 2010, p. 16). In so doing, mandatory rotation was called upon to answer, and to mediate, concerns of *both*

independence and market concentration and in this way, *strengthened* the critical linkage between the two. It is put forward here that this document therefore served as another key linkage in enabling the rise of mandatory rotation. It repeated earlier ideas of rotation and independence, in itself escalating the rhetoric, and linked these with concerns of market concentration. Critically, rotation was offered as a potential solution to mediate both the concerns of independence and market concentration, and in so doing, strengthened the chain of linkages

5.4.5 House of Lords (2011)

With the principal of rotation having been earlier established and linked to the promise of improving independence, the heightened problematization of the lack of competition was still seeking remedy. As mentioned earlier in section 5.3.1, a number of working groups and inquiries were convened in the UK in the decade following the collapse of Enron to post-financial crisis where encouraging competition was seen as a key priority in order to promote and ‘improve’ audit quality. In all of these, mandatory rotation was considered but still seen as too unproven and radical a measure to be implemented. However, as a middle ground, mandatory *tendering* emerged as a viable option, in particular to address problems of the lack of competition. In the follow up to the the House of Lords banking crises inquiry, *Auditors: Market Concentration and its Role (2011)*, where recommendation for the OFT to consider referral of the audit market to the CC was made, mandatory tendering was formally recommended. The very lengthy document rationalised that:

The very long tenure of auditors at large companies is evidence of the lack of competition and choice in the market for the provision of audit services. A regular tender, with a non Big Four auditor invited to participate, should promote greater competition to the benefit of both cost and quality. We recommend that FTSE 350 companies carry out a mandatory tender of their audit contract every 5 years. (House of Lords, 2011, para 175).

In the UK, the FRC took this on to give effect to this recommendation. In October 2012, the FRC updated the Corporate Governance Code and introduced a new provision, on a comply or explain basis, requiring FTSE 350 companies to put their audit out to tender every ten years. Their justification for this development, *and in rejecting rotation*, in an accompanying ‘Notes on best practice’ was:

As the independent regulator responsible for promoting high quality corporate governance and reporting in the UK, the FRC seeks to promote high standards in audit. If that objective is to be achieved, the FRC believes that a company should be able to retain the firm that it believes is best able to undertake its audit. The FRC

therefore believes that tendering, not mandatory audit firm rotation, is the appropriate way forward. Tendering provides an effective way by which companies can examine whether they have the best auditor available, yet does not preclude the reappointment of the incumbent auditor if that firm is demonstrably the best able to undertake the audit. Tendering also has the potential to stimulate innovation in the way audits are conducted as audit firms seek ways to demonstrate the merits of their audit tender (FRC, 2013, p. 1)

Further, in best practice advice on 'Making the decision', the key recommendation was to 'Put audit quality, not price, at the top of your list', which incorporated the consideration of publishing FRC quality inspections and the quality of each firm's understanding of the audit risk areas and approach (p. 7) to justify the selection process, thereby once again implicating audit quality within this time the device of tendering.

Whilst mandatory rotation was rejected at this stage, it is put forward that this intermediate step of tendering was a significant linkage within this constellation as it further hardened the connection between competition, tendering, and quality. Implicit in the idea of tendering was that it would increase competition within the market, which in itself was 'good' for audit quality. With independence already established as that which could be 'enhanced' by rotation, the final leap to mandatory rotation was in this way made much smaller. And by once again, drawing upon previous connections and linkages and building upon the underlying ideas being made, the chain of linkages became in this way made stronger.

As set out in section 5.3.2, whilst the 'landmark measures' (EC, 2013) enacted by the EU in 2013 to implement mandatory tendering of audit firms after ten years, with the possibility of one extension period (essentially resulting in mandatory rotation after twenty), were considerably less ambitious than that which had been initially proposed, mandatory rotation was nonetheless installed into the EU audit market in 2014. The convergence of this ruling with the UK's CMA's inquiry into the audit market led also to a convergence of its recommendations, which had earlier put forward a provisional remedy of mandatory re-tendering after every five years. These reforms were received with relief from the Big 4 firms. James Chalmers, PwC Head of Assurance stated that the package of measures recommended by the CMA was a 'sensible' outcome and would 'taken together...enhance competition, transparency and quality'⁹⁰.

Mandatory rotation thus served as the final embodiment of the linkage of this episode, solidifying the connections of ideas of both independence (rotational element) and

⁹⁰ See: <http://www.pwc.co.uk/who-we-are/competition-commissions-audit-market-investigation.html>

competition (tendering element). Irrespective of the ‘severity’ of the final remedies put forward, it remains so that this trajectory of mandatory rotation, spanning some 40 years and travelling across jurisdictions, could only have been made possible within the historically contingent pre-conditions and the *sequence* of linkages which carried and made concrete the underlying ideas being connected. These connections of ideas became further reified and stronger through each linkage in the sequence, picking up on previous connections, solidifying or bringing in new connections. Uniting these ideas, discourses, and indeed linkages themselves, was a promise to delivery audit quality. In this way, we can start to see how ultimately it was *through* audit quality, that these connections were being held together and stabilised, and how audit quality within the discourse came to be understood as those underlying conceptualisations themselves. The underlying ideas being attached to quality via the linkages became absorbed into quality itself. This will be examined further in chapter six. A discussion of how this analysis helps us to think about quality follows.

5.5 Discussion

This chapter has examined the next shift in the discourse of audit quality to centrally that of a problem of the lack of competition in the audit market and auditor independence. It examined some of the pre-conditions which led to the intensification of independence concerns from within the quality discourse and how this converged with the problematization of a lack of competition within the audit market. Seen through the lens of the EU’s single market and wider, free market ideals, audit quality became increasingly articulated as a problem, and hence ‘property’, of audit market structure - the attendant alignment of quality with the notion of competition continuing the trend of de-individualising the quality problem (see Table 1.1). With the problem so conceptualised, mandatory audit firm rotation, a highly controversial and debated regulatory measure without any clear correlation to improvements in audit quality, was called upon to solve both problems of competition and independence. Despite academic research being ‘inconclusive’ on the relationship between mandatory rotation and audit quality, the audit firms (both Big 4 and non-Big 4) also opposing such a measure⁹¹ and even clients expressing doubts (see Ewelt-Knauer et al, 2012 for review) mandatory rotation in any event became legislated within the EU. This chapter has argued that this was in part enabled by the linkages which were forged, through rhetoric, association, and more precisely, the linking work within the constellation dynamics, which connected ideas of independence and rotation, and tendering and competition together. With these linkages so forged, the step to mandatory rotation

⁹¹ For examples, see PwC (2013), Ernst & Young (2013)

became increasingly seen as the ‘logical’ remedy to the problem of independence and competition. And in having been in this way made conceivable and hence, possible, the way for reform became paved.

With mandatory rotation yet to come fully into effect, it remains to be seen how this will reshape the constellation of practice, regulatory and academia arena activity. With the formation of the academia arena through statistical sampling (chapter three), and the separation of practice and regulation through peer review (chapter four), the continued separation of the arenas as three distinct fields of activity can at the very least be anticipated to be further reified through the advent of mandatory rotation. Developments in this direction can already be seen with the formalisation of external quality inspections by regulatory bodies thereby increasing the institutional boundaries between practice and regulation. The academia arena has spawned an entire industry in itself of audit quality research, steadfastly using proxies (e.g., Big N, % of going concern opinions, abnormal accruals, and audit failures) to both research and represent quality. DeAngelo (1981) has generated nearly 4,500⁹² citations alone. Further, tendering activity can be anticipated to have a role in re-shaping practice activities, with tendering decisions needing to be outwardly justified by reference to audit quality assessments of the firms. Conceivably this could lead to added resources and attention from the audit firms being diverted to accommodating quality reviews, also in a sense a proxy for quality, and a common consequence of organisations in situations where the means (proxy)-end relationship is obscure (Bromley and Powell, 2012, to be discussed further in chapter six).

In general terms, the considerable rise of neoliberalism and its attendant economic ideals of the effectiveness and discipline of the free market, was also particularly significant for this current episode. Intricately tied to the rise of neoliberalism was the notion of competition itself, and importantly how it became constructed during this period as ‘good’ for auditing and audit quality. As Davies (2014) has observed more widely in his examination of the ‘limits of neoliberalism’, the rhetoric of competitiveness seemed to serve a crucial function in winning moral and political arguments. And this clearly played a role within this episode in nurturing the rise of competition as being unquestionably ‘good’ and even taken-for-granted as one critical element which could, and would, improve audit quality. Davies (2014) goes on to question why economics should be a better basis for government as opposed to other political or scientific forms of authority and that efforts to replace politics with economics , and judgement with measurement, confront a limit beyond which they collapse (p. 8).

⁹² Google scholar citations extracted on 6 June 2016.

Thus, irrespective of arguments regarding the ‘optimal’ level of competition within the audit market, the present argument focuses on how it was through the interrelations (linkages and linking work) of contemporaneous discourses and priorities of financial stability, the free market, the EU’s single market ambitions and competition which served to harden the connections between audit quality, independence and competition. These relations served as the lens through which the quality discourse would come to be articulated, showing acutely one means by which quality is constitutive of these wider discourses and priorities, or if you rather, the social. However, the argument currently being made is not merely an analysis of the latest struggles to regulate quality, conditioned by the rise in this period of neoliberalist tendencies and policies. More importantly, and evaluated as a longitudinal study, the central argument of this thesis rests on what this analysis in turn reveals about quality itself.

The pre-conditions which gave rise to the advent of mandatory rotation suggest that the quality discourse, at any given time, is located within a wider network comprised of an intersecting social, political and economic field and not necessarily, or at least entirely, rooted within any underlying ‘reality’. World events periodically punctuate that field which leads to attendant changes in practice, regulation and academia. It is, however, at the interrelations of these discourses which gives not only the contemporary meaning of quality but also endows quality with the means by which its nature is exceedingly malleable and its reach is spread. This malleable nature gives quality the means by which multiple actors from different domains to act together, and separately through the development of arena specific proxies, all in the name of quality. In this sense, we can conceive of quality as a boundary object (Starr and Griesemer, 1989). Through these actions, which are dependent on the linkages to bring together ideas, those arenas of activity become re-configured in part leading to new conceptualisations of the problem and in this way, a changing discourse and meaning of audit quality.

The gradual acceleration of activities falling under the auspices of quality is evidence, if nothing else, of this intrinsic power central to the concept of quality. Its ambiguity in meaning and susceptibility of being shaped by wider, contemporaneous discourses at the time is what enables quality to perennially re-invent itself and sustain itself within the discourse. In this sense, quality is highly susceptible to continual failure as the constellation will always be in motion and is not necessarily rooted within any intrinsic reality of audit. As previously outlined in this thesis, difficulties and tensions perennially surround the audit which perpetually fails to deliver to expectations. With the dynamic nature of the constellation, from time to time specific issues come to the forefront but are never resolved. And so, when the next failures or crisis occurs, the debates resurface with more intensity,

with the central focus being shaped by the contemporaneous discourses and concerns of that time.

In 2016, some four decades after quality explicitly emerged within the audit field, quality is still not universally defined. An examination of the transparency reports of the Big 4 firms for 2015 indicate the firms do not define quality despite a rise of metrics to help measure various components of it. A Forum of Firm symposium held in 2011, assembled a group of experts to discuss several elements of audit quality. David Maxwell, chair of the Transnational Auditors Committee stated at that time: "This symposium was designed to encourage participants to exchange views on audit quality from the perspectives of different stakeholders, including users, practitioners, and audit committees...The discussion raised questions on how *audit quality should be defined*, as well as ideas for practitioners to consider implementing in their audits." (IFAC, 2011, emphasis added). Quality continues to be elusive. The current shift in the quality discourse, found within the UK Competition Commission inquiry, seeks to break down quality further into components such as objectivity and professional scepticism. These represent continued attempts to probe quality although focussing on such equally subjective and nebulous concepts will only pose similar difficulties. This does, show, however, how quality's elusiveness becomes implicated within its own transformations and its spread of its reach.

In the debates about independence, a clear distinction has been made between independence in fact and independence in appearance. With its close association with quality, this begs the question as to whether the same could be said about quality. Is there a quality in fact, which remains perpetually unobservable and a quality in appearance which can be proxied, measured, and made visible? Or are they one and the same? According to the analysis in this thesis, quality is that which is made visible and also, a historically contingent convergence of very particular pressures which both construct and attempt to solve problems of that time. In this sense, this thesis ultimately seeks to show how audit quality has come to be primarily, and merely, a basis through which very particular sets of historically contingent concerns, pressures and practices within the audit field come to be articulated. Underneath this articulation and all the proxies, understood widely, in making quality visible, it remains questionable whether or not there is such a thing as quality in fact. What is the relationship between the proxy and the underlying reality, if such a reality exists? These issues and more will be explored further in the next and concluding chapter of this thesis.

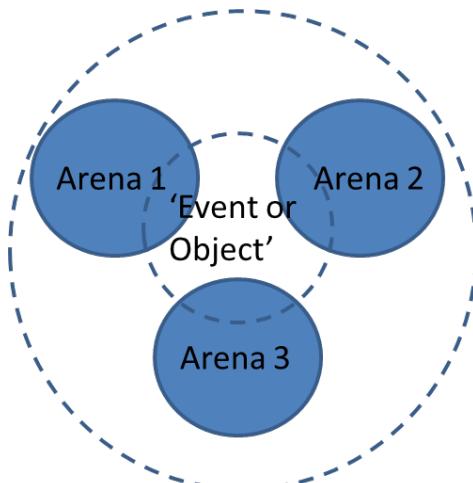
Chapter six

The changing constellations of audit quality

6.0 The changing constellations of audit quality

This thesis has thus far mobilised and attempted to build upon Burchell et al's (1985) notions of the arena and the constellation in the examination of the changing nature of the audit quality 'problem'. Chapter three examined the origins of quality ideas within the audit field in the pre-quality constellation and showed how through the advent of statistical sampling, a new academic arena of audit research emerged, changing with it the shape and constitution of the constellation. The quality-related problem then, even if not so articulated, was with the perceived lack of objectivity and defendability of auditing practice. Chapter four next examined the emergence of quality within the audit field, as a quality control problem, and how through the regulatory and practice pressures to regulate and demonstrate quality, the separation of the professional practice arena between regulatory and practice activities became further delineated. Chapter four also examined how the newly emergent academia arena became further established once an observable, and hence researchable definition of audit quality was developed. Out of this episode emerged a new constellation yet again, with the regulatory arena becoming further defined and a new sub-arena of academic research specifically on audit quality arising. Finally, chapter five examined how audit quality became once more reconceptualised, within the UK and EU especially, as a problem of independence and the lack of market competition. This paved the way for the radical implementation of mandatory audit firm rotation despite its complex history of debates and its relationship with audit quality unsubstantiated. With the three arenas of regulation, practice and academia now established and separate, this constellation essentially brings us to that of Burchell et al's (1985) model of the three arena constellation. In what has been labelled here its 'static' form, characterised by already formed arenas, the constellation can be in very simple terms depicted as follows:

Figure 6.1: Depiction of ‘static’ constellation as conceptualised in Burchell et al (1985):

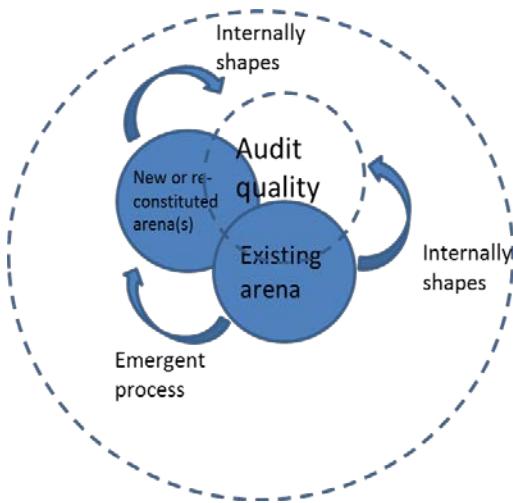


The network of institutions and relations which constitutes the constellation governs how the central event or object, often externally emplaced such as the value added event, is interpreted and evolves. In each of the three arenas constructed by Burchell et al (1985), their shifting relations and interest with the value added event shaped the arenas' adaptation of the value added event. It was through the relations of the constellation that the value added event rose in the form in which it did. Yet, value added was robust enough to still maintain meaning across the arenas. In this way, the central object can perhaps be most helpfully conceptualised as a ‘boundary object’ (Starr and Gresemer, 1989), being objects which are adaptable within different actors and domains but still robust enough to maintain some meaning across them.

The developments examined in the preceding chapters, however, indicate the constellation is not always so ‘static’ in nature and the arenas themselves can also be formulating or changing within and through each constellation. By attending empirically to the mutually constitutive aspect of the arena and the constellation, and to the specific and important role of linkages and the linking work entailed in the formation of each constellation, this thesis has attempted to reconceptualise the constellation as being dynamic in nature. It developed the notions of the emergent and reformation constellations, and drew attention to not just the significance of the linkages, but also the types of linking work involved in attaching different ideas together and to the quality discourse. This dynamism has been very simply depicted as follows, whereby the arenas and constellation are mutually constitutive, and

audit quality can be seen as the emergent central object, being shaped and formulated *through* the network of relations *and* the co-constitution of the constellation.

Figure 6.2: Simplified model of ‘dynamic’ constellation



This diagram does not purport to capture all elements that could potentially shape the constellation but is instead meant to highlight the internal dynamism which has been conceptualised from the core empirical contributions focused on within this thesis. Within this ‘dynamic’ constellation, new (‘emergent’ constellations) or differentiated (‘reformation’ constellations) arenas are concurrently being formed alongside the co-constitution of the central object, thereby re-constituting the constellation through this emergence. Whilst audit quality can also be thought of as a boundary object in this constellation, it is perhaps also helpful to think of dynamic constellations as modelling the formation process of the boundary object, which draws greater attention to the dynamism involved. A further consideration of the notion of boundary objects and its relevance to the current study is included in section 6.1.2.

This longitudinal study has, in a sense, attempted to re-construct the genealogy of the constellations which has led to the present day discourse of audit quality. Tracing the conceptual roots, linkages of ideas and constellation dynamics over time was in attempt to further our understanding of both a profoundly resiliently topic of interest as well as some of the more precise dynamics of change. This research suggests that the audit quality constellation is continuously in motion, forming and reforming, the dynamics of which constitutes the shifting nature of its discourse.

In reaching such a finding, or in adopting such a view, an alternate interpretation may very well be that instead of a story of change, as has been consistently presented thus far in this thesis, this research could otherwise be understood as a story of stability: the constellations examined in the three preceding chapters represent three key moments wherein the constantly shifting constellations achieved a stability in meaning, albeit temporarily before shifting to the next conceptualisation. This understanding would be consistent with Abbott's (2016) processual approach which 'starts from the premise that the social world is one of constant change' and consequently 'stability must therefore be explained' (p. 1). Whilst adopting such a view does not undermine some of the key developments proposed within this thesis, perhaps greater attention would have been given to the conditions enabling the chain of linkages to be connected or that which shapes and constitutes the sufficiency of the strength of the chain in order for stabilisation to be achieved. These avenues for future research and more are discussed in section 6.3.

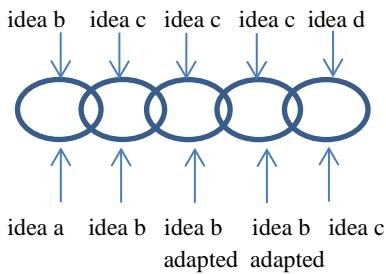
Beyond the developments put forward on the notion of the constellation, however, is what this present analysis has ultimately helped to reveal about accounting change, audit quality itself and the interrelationship between the arenas. It is to these findings which we now turn.

6.1 Key findings

6.1.1 On accounting change

In pursuit of the dynamism argument as set out above, this research attended to the specific linkages which carried and connected ideas to the audit quality discourse and to the more precise linking work which was being enacted through these connections. The argument of this thesis is that the linkages and their work play a critical role in the dynamism of the constellations as it is within these linkages where some of the very origins of change are crystallized. For the three audit quality constellations examined, people and documents are central elements in constituting these linkages. Furthermore, the different types of linking work which took place within this research could be seen as falling into seven different types. On this basis, an alternate conceptualisation of change was also put forward: a chain of linkages which hold together disparate ideas is required in order for successful action to obtain. Figure 2.3 has been reproduced below as a reminder of this conceptualisation.

Figure 2.3 Proposed conceptualisation of a chain of linkages



These findings were clearly an attempt to theorise across the changing constellations, with aspirations of moving forward our understanding of the dynamics of accounting change. They represent some initial steps in opening up the possibility of developing a more generalizable model of change. In so doing, the question will no doubt arise as to whether or not such an ambition would ever be compatible with a genealogical approach. In Miller's examination of the rise of discounted cash flow in the UK he states that he is not giving a 'formal model that specifies certain invariant entities or theoretical categories' (1991, p. 758, also cited in Napier, 2006, p. 461), and in Napier's (2006) synthesis of accounting change literature published in *Accounting, Organizations and Society*, he further concludes that this 'reluctance to impose a general model on a specific problem or event is characteristic of a genealogical approach.' (p. 461). Further emphasized is that 'accounting constellations are not general formations but are specific to particular problems' (Napier, 2006, p. 460).

This feature of the genealogical approach, which allows for a greater understanding of the 'network of intersecting practices, processes and institutions' (Burchell et al, 1985, p. 400) through which new accountings 'emerge and mutate' (Napier, 2006, p. 461), is therefore seen as both its strength and potential weakness. The specificity inherent in adopting such an approach to understand particular events or objects could also be the delimiting factor in enabling any findings to be more generalizable (Cooper, 1980 as cited in Napier, 2006). This dilemma was aptly summarised by Napier (2006):

...either we attempt to explain change at a general level by reference to a broad theory (whether that is economic rationalist or Marxist), or we view change at a specific level, with local explanations that illuminate a particular story but that cannot easily be transferred to other sites of change...the challenge is to bring each case under the general theory...(p. 467)

With full acknowledgement of such a dilemma, this research has sought to make tentative steps towards a middle ground. This thesis has sought to move forward from the specificity of a singular problem, by providing some initial steps and elaborations towards a more generalizable model. By incorporating a longitudinal approach and holding constant the research object of study, this research has within its approach and design, aspired to attend to this ambition even if the findings are deemed to be confined to the changing nature of the audit quality problem. Notwithstanding this, examining the changing constellations over time has not only given us insight into how this particular problem has been made and critically re-made over time. Coupled with this has been a greater understanding of some of the more specific, yet precisely on account of this specificity, perhaps also more generalizable, mechanisms of change.

Thus, it is this specificity, being put forward as some of the key findings of this research, which is also being put forward as that which contributes to our understanding of accounting change. In one of Hopwood's (1987) earlier calls for research into processes of accounting change, he lamented then as follows:

As of now we have only a limited understanding of the conditions which provide the possibility for particular conceptions of the accounting craft, the forces that put accounting into motion, the processes accompanying accounting elaboration and diffusion, and the varied human, organisational and social consequences that can stem from changing regimes (p. 207).

Since then, nearly three decades of research have addressed various components of this research agenda, in part summarised in Napier (2006). Genealogies of calculation (Miller and Napier, 1993) now form a firmly established research approach, and have encouraged and enabled a focus on those pre-conditions leading to particular conceptions of the accounting craft. And in drawing on the 'constellation' and the like, the wider social, institutional, political and economic forces which put those changes in motion have also been made visible. The interrelationship between accounting and the social (Burchell et al, 1980) has become firmly established. The incorporation of key concepts from the sociology of translation such as the concept itself of translation and action at a distance (Miller, 1991; Robson, 1991; Robson, 1994) has provided further insights into processes of accounting change in particular. Miller (1991) drew on the concept of translation to help articulate the linkage between wider programmes of economic growth and the use of discounted cash flow techniques whereas Robson (1991) elaborated upon the notion of the arena as being dependent upon a process of translation – to show how the social 'passes through'

accounting (p. 550). Notwithstanding these significant contributions, this thesis has sought to provide further insight still into the more precise dynamics of accounting change over and above these higher level arguments of accounting and social interaction – a further level of detailed analysis which includes the carriers of linkages, the nature of the work linking entailed, and the chain of linkages which is required in order for change to obtain. In so doing, the aspiration is to move us forward from a comparatively general argument of the interrelationship of accounting and the social hinged on a mechanism of translation, to some more precise, micro-level dynamics which can perhaps be more readily tested empirically within different settings of change.

On this final point of the accounting and social interrelationship, Napier (2006) noted that ‘traditional’ views of accounting have tended to keep distinct the categories of ‘accounting’ and the ‘environment’ and that the directionality of influence was predominantly that of the environment flowing to accounting (p. 456). These early views of change were also rooted within contingency theory. However, advances since then have challenged this directionality of influence with the recognition that accounting can also influence its environment (Hopwood, 1992). Subsequent research which pursued this agenda nonetheless also retained this separation between the ‘accounting’ and the ‘social’, perhaps by necessity given the research object of interest. And regardless of directionality of influence or the unit and nature of analysis, many of these approaches, especially those which adopted a genealogical method (present study included) were still predominantly premised upon a core of contingency theory, albeit with varying levels of complexity.

Whilst this research has endeavoured to identify some of the more precise dynamics of change, it has not made explicit this distinction between ‘accounting’ and ‘the social’. Maintaining the unit of analysis at the level of ideas, and how they become connected, highlighted the co-constitutive nature of both accounting and the social. No *a priori* directionality of influence was applied in the analysis beyond unpacking those influences which helped to shape the constellations in question. No clear line was drawn between that which formed the social and that which formed the accounting. Indeed, for the changing nature of the audit quality problem, the current research object in question, it is not altogether clear whether such a distinction is helpful or further, even relevant. This research has attempted to show how audit quality has ultimately been constituted through the dynamics of relations within the constellation. No ‘core’ or ‘essence’ of audit quality was identified within this analysis and in this way, this thesis argues that perhaps this dichotomy is neither apparent nor necessary. This logically leads to a question as to whether or not such a distinction even subsists. Perhaps, it is *all* just the social. Borrowing from Abbott

(2016), there may be no accounting and social interrelations. There are only interrelations. And perhaps it is therefore not *accounting* change which this thesis informs, but again more generally, just change. If this view on there only being interrelations is pursued, and we entwine with it the making of audit quality's visibility examined in chapter four, we can start to consider more carefully the implications of audit quality being constituted in this way. In this sense, this constitution of audit quality is both its making and undoing. It enables the making of its visibility in different ways, but nonetheless all through the use of proxies in a broad sense, which leads to the reification of quality (discussed further below in section 6.1.2) in those particular ways. However, quality, once made operationalisable, contributes to re-shaping the discourses, be these for regulatory, practice or academic purposes. Quality becomes implicated in its own continuously changing nature and consequently leads to its undoing – or perennial failure. The question which remains is what we are left with. These findings on audit quality and more will be examined next.

6.1.2 On audit quality

This research has attempted to show, as set out in the ambitions of chapter one and repeated here for reflection, that audit quality is only in part an individual auditor judgement issue. It is also 'a function of what gets accepted, stabilized and institutionalised as a way of doing things' (Power, 2003, p. 389). Power further called for a 'deeper institutional understanding of the *sources of that stability, and ideas of audit quality*' (*ibid*, emphasis added). From one overarching perspective, this research has precisely attempted to attend to these underlying ideas of quality and the sources of their stability (linkages). In doing so, this thesis has started to unpack some of audit quality's wider constitution, over and above that which is related to auditor judgement. Indeed, the argument presented above in section 6.1.1 contended that the 'problem' element of audit quality might even be construed as *all* socially constituted. From the origins of quality ideas within statistical sampling, to the advent of peer review emerging hand in hand with the conceptualisation of a quality control problem, and finally to the shift again to issues of independence and competition, this history has sought to show some of the sources and means by which very disparate ideas come to be attached to and thereby implicate audit quality. Critically, this thesis has also shown that neither the sources of these ideas nor their attachment mechanisms are necessarily rooted within an underlying efficacy issue of the audit. Nor do they arise solely from the very high profile failures which have, and will no doubt continue, to prevail.

The linkages identified in this thesis are significant, and not only in their role and work in carrying and attaching disparate ideas to the quality discourse as discussed above. In chapter

five⁹³, an argument was presented that linkages on their own are insufficient and a sequence of linkages is required in order for successful ‘action’ to obtain. Ideas of mandatory rotation first raised in the 1970s in the US were not successfully implemented until some four decades later in the EU. This, it was argued, was due to the lack of the preconditions for the required chain of linkages to carry the ideas through to ‘completion’ to form. The argument was then made that the linkages themselves needed to be connected through a commonality in their underlying ideas in order for the sequence to be formed. A similar argument can also be seen within chapter four on peer review by considering the period in between ideas of peer review entering the audit field and when it became formally mandated. This argument bears further consideration here.

A closer consideration of the people and document linkages identified in chapters four and five (see tables 4.1 and 5.1) and in particular, the underlying ideas being connected, suggests that within each linkage, at least one of these underlying ideas needed to be common with that of a previous linkage in order for the chain to grow in ‘strength’. The tables presented in those chapters therefore represent not just the more significant, paradigmatic linkages for each episode, but also this sequence of linkages. Upon closer inspection of this chain, it is suggested here that the ‘connector’ between the linkages is, perhaps, quality itself. It is put forward here that it is the notion of quality itself which serves as the commonality which holds together the disparate ideas, and in this way, connects together the individual linkages, completing the sequence. Beyond a general argument about intersecting discourses, it is in this *specific* way that quality became implicated within the discourse and debates. It is *through* quality that the sequence is made, and hence, *through* quality that successful evolution of techniques or regulation such as statistical sampling, peer review or mandatory rotation obtained.

Further to this, in chapter four we examined how quality, building upon this current conceptualisation as the element which connects the linkages, emerged hand in hand with the making of its visibility across the three arenas. In addition to the conceptual heritage of statistical quality control and the pressures which led to a more process-oriented output view of quality, quality emerged from this episode transformed from a subjective, indeterminate

⁹³ A similar argument holds for both chapters three and four although it was not presented until chapter five to avoid complexity within those chapters. For present purposes, we will refer to the empirical data examined in chapters four and five only as the rise of statistical sampling examined in chapter three took place prior to the term quality explicitly emerging in the audit field, and therefore the role of quality as the ‘connector’ within this argument is not as explicitly seen as in chapters four and five. Irrespective of this, the argument would still hold for chapter three, if one were to follow the ideas of quality instead.

and unobservable notion to that which was visible. This transformation is significant as it enabled all three arenas to start working with quality in some way. Indeed, as discussed in chapter four, proxies were not limited to the academia arena and in a sense, working papers, checklists and even inspection of that which could be documented, also served as proxies for quality. However, the question is not simply how ‘representative’ or ‘accurate’ these proxies reflect quality. Instead, the present argument focuses more so on the implication for our understanding of quality when these means to the ‘uncovering’ of quality become the ends.

In Bromley and Powell (2012), the authors develop an additional notion of decoupling, having been most commonly thought of as the gap between policy and practice. The authors argue the more prevalent and consequential form of decoupling is means-end decoupling, whereby the gap which exists is instead between means and ends. Set within an organizational context, means-end decoupling⁹⁴ occurs in settings where:

...formal structures have real organizational consequences, work activities are altered, and policies are implemented and evaluated, but where scant evidence exists to show that these activities are linked to organizational effectiveness or outcomes (p. 496).

Means-end decoupling therefore entails the implementation of policies even if ‘the link between formal policies and the intended outcome is opaque’ (p. 489). Bromley and Powell (2012) also observe that often, ‘extensive rhetoric or cultural beliefs posit a causal link between activities and outcomes’ (p. 496) – precisely that which was examined as part of the current study, which in part explains why organizations would commit substantial resources towards implementing policies and practices which have a ‘tenuous link to core goals’ (*ibid*). The authors summarise some of the wider reasons why this situation might arise, owing predominantly to the rise of external, competing pressures and increasing societal rationalization trends such as accountability, assessment, and transparency. To this impressive list, we add the demands for quality.

⁹⁴ This setting whereby organizations are characterised by severe ambiguity without clear or consistent notions about what they are trying to do, how they are supposed to do it, or who it is that should make the decisions have been elsewhere examined as ‘organized anarchies’ (Cohen and March (1974), Cohen, March and Olsen (1976) as cited in Padgett (1980)). Here, the ‘garbage can model of organizational choice’ attempts to describe how decisions are made under these trying circumstances (Padgett, 1980). Whilst this setting may also be relevant to the current study, means-end decoupling provides a richer understanding of the more precise consequences of using proxies to represent quality.

Applied to the present study, the concept of means-end decoupling, especially from the practice and regulatory arenas' perspectives, can help us to understand not only why decoupling would occur but also, more importantly, the process by which the means become the ends. In other words, how working papers, firm size or inspections may be made to be commensurate with quality. Here, Bromley and Powell (2012), citing from a number of different studies surmise the following reasons: the risk of an inordinate focus on the process rather than the intended outcome, internal and external stakeholders valuing efforts to monitor and evaluate (even in the absence of a clear link between policies and outcomes), the risk of data collection becoming an end in itself, the gap between means and end going unchallenged, and how the 'emphasis on measurement can become a valued activity in itself, a taken-for-granted means of achieving ends' (p. 506). In short, these risks all suggest why and how, for present purposes, the regulator's conception of quality, and consequently also the practice arena's, become reified. The proxy for quality, however conceived, becomes taken for granted as the 'underlying' quality, following the phenomenon which was already seen in the academia arena (see chapter four).

This process of 'reification', where means becomes ends, is further informed by reference to Scott's (1998) concept of 'legibility'⁹⁵. In a series of large scale failures of state-initiated engineering, Scott examines how in each of these cases, the governance philosophy of the state was dependent firstly upon that of legibility – 'rationalizing and standardizing...into a legible and administratively more convenient format' (p. 3) which provided the social simplifications required in order to enhance state capacity. As Scott argues, these simplifications:

...made possible quite discriminating interventions of every kind, such as public-health measures, political surveillance, and relief for the poor.... They did not successfully represent the actual activity of the society they depicted, nor were they intended to; they represented only that slice of it that interested official observer. They were, moreover, not just maps. Rather, they were maps that, when allied with state power, *would enable much of the reality they depicted to be remade* (ibid, emphasis added).

The force of law is also highlighted, especially relevant given the regulatory arena's powers of governance in the current study, and in particular its role in creating as opposed to just describing systems. For the current study, we are able to see how inspection of working

⁹⁵ Whilst Scott's (1998) empirical case studies are on a much grander scale to the current research, he argues also that his conclusions – and in particular the implications of legibility and simplification, can be equally applied to capitalist markets which is much closer to the current research object of interest.

papers or mandatory rotation did not necessarily mirror or represent the actual activity of the audits which these proxies were meant to depict. They only represented those aspects which were of interest to the regulatory arena, such as peer review or competition, interest of which was shaped by contemporaneous discourses at the time. However, as above, these proxies were not only maps of those particular aspects of quality which were of interest. When allied with the regulatory powers of governance, the focus on these means, measures or proxies bore the risk of re-making the quality which it was meant to depict. Within chapter four, practice became re-shaped as a self-regulatory model of peer review, with the attendant focus on working paper documentation. With mandatory rotation, the audit market became re-shaped with increased tendering activity and competition. Competition, of interest to regulators, and a proxy in itself, became re-made as the protector of quality.

Irrespective of whether Scott's argument of intentionality holds for quality – perhaps all three arenas fully intended on seeking the most 'accurate' representation of quality as possible, the current argument is that in making quality visible, closely tied with which its legibility into the systems, procedures and processes of the audit firm could be made possible, the *reality of quality was in this way made concrete*. Indeed, alternatively, the making of the legibility of quality was dependent upon the development of proxies, all of which were visible and measurable. Traces of this have already been seen within the three preceding chapters with the evolution of sampling techniques which reinforced the underlying ideas of quality control and the subsequent creation, administering and checking of quality control documentation which enabled quality to be made legible and possible to be acted upon within the firms. Overlaying an inspection based regime in firstly peer and then external review only further solidified quality in these ways, with the inordinate focus on the quality which could be *seen* (i.e., documented.) With more recent developments with quality gradings⁹⁶ on audits, upon which individual auditors or audit teams become held accountable by their firms as performance measures, Hacking (1999) reminds us how classifications and the matrix within which it is embedded can impact the individual, changing how they feel about themselves, their experiences and their actions and in that indirect way, the individual auditor in this case may well be socially constructed (p. 11). And within this process of legibility and beyond, profound transformations occurred which further enabled this making of quality: proprietary audit firm working papers which became publicly open for inspection, the working papers themselves became a representation of quality, audit firm size becoming firstly the predominant, and latterly the outright substitute

⁹⁶ The Financial Reporting Council Audit Quality Reviews assign 'gradings' on audits as follows: Good (category 1), limited improvements required (category 2A), improvements required (category 2B) and significant improvements required (category 3)

measure of quality for the academia arena, and finally competition, once deemed to hinder quality yet somehow transformed into a ‘protector’ of quality. Each of these, and more, were further steps which gradually solidified the reification of the means of quality for its ends.

Centrally, this thesis therefore challenges the idea that quality is something which is ‘out there’, ready to be revealed, targeted and improved upon so long as unlocking or even building the right window can be achieved. By attending to the means of its constitution, this thesis has opened up for consideration the relationship between *the* quality that is understood through document intensive technologies such as peer review or the reductionist approaches of adopting observable characteristics such as firm size as proxies, and some *other* substantive notion of quality which remains perpetually unobservable. To summarise where we have arrived with the present arguments: the conceptualisation of the ‘problem’ of audit quality is all socially constituted; the means (proxies) adopted to ‘deal with’ quality (the outcome or end) are at risk of becoming the ends in itself; drawing upon the notion of legibility, the means in themselves have consequences in terms of re-making the reality which they seek to depict; this reality of quality which becomes fashioned has the added implication of shifting the constellation, giving rise to new a new constellation of actors, arenas and discourses which together with world events, shape new conceptualisations of the audit quality problem.

This thesis therefore suggests that they are actually just one and the same: there is no *other* substantive notion of quality. With quality acting as the medium through which disparate concerns and ideas are held together, quality can only be understood as that which becomes shaped and constituted and made through its legibility, in the context of the historically contingent and competing discourses, tensions, concerns and logics prevailing at that time. Together, this reinforces yet again that quality, as so constituted, is not rooted within anything naturally ‘intrinsic’ about the audit. Beyond just being susceptible to and shaped by contemporaneous concerns and discourses, quality is the abstract notion with the capacity through which disparate ideas can be connected. Its abstract nature enables it to then also become constituted in a number of very particular ways.

If quality is *not* to be understood as anything intrinsic, then how else can we more positively conceptualise quality? As alluded to earlier in this thesis, Starr and Greisemer’s (1989) notion of a boundary object, as objects which are both adaptable to different viewpoints yet robust enough to maintain identity across them can be of some help. By thinking of audit quality as an object whereby multiple actors across different arenas have interests in

‘improving’, and whereby differences in meaning may need to be reconciled in order for these ‘improvements’ to be sanctioned, drawing upon the notion of the boundary object can help to understand how audit quality, as an abstract notion, provides a ‘means of translation’ (Starr and Greisemer, 1989, p. 393) such that coherence across intersecting social worlds may be achieved. In their field study of activity-based costing implementation, Briers and Chua (2001) extended Starr and Greisemer’s typology of boundary objects by adding a fifth form. ‘Visionary objects’ are defined as follows:

...conceptual objects that have high levels of legitimacy within a particular community. They can evoke similar emotive and an affective responses from a wide spectrum of people; possessing a sacred quality that makes it difficult for a ‘rational’ person to be against them...the precise identity of these objects is not known until it is customized and tailored to specific settings.’ (p. 242).

Within the current study, audit quality can be conceptualised as being most closely aligned with such visionary objects. In itself, the rhetoric of quality is difficult for a rational person to argue against and indeed, no such oppositions were observed within breadth of the empirical data examined. However, the precise identity of quality does not become known until it became customized, and proxied, within specific settings and arenas. In drawing upon the visionary object, it helps us to see how audit quality is only able to achieve a stability in meaning, through which translation (in the current study: linkages) can be made, by way of its vagueness and hence, adaptability in different arenas. It is precisely this vagueness which has implicated quality in its own rise.

In a question of focus, an alternative, or rather additional, argument could also be made that audit quality could likewise be conceptualised as a mediating instrument (Miller and O’Leary, 2007). In a similar argument to that of the visionary object above, where objects possess a sacred quality making it difficult for ‘rational’ person to argue against, this sacred element could also be seen as including an aspirational aspect. In chapter three, we saw how the programmatic promise of scientism and defendability came to provide the preconditions for the emergence of statistical sampling. In chapter four, we examined how peer review was called upon to solve problems of both self-regulation and quality control and how even within the academia arena, quality helped pave the road for a new arena of academia operations. And finally, in chapter five, we saw how quality became implicated and called upon to help realise the EU’s single market project. Each of these examples points toward an enduring, aspirational element within quality. Focusing on this aspirational element, and the interlinked abilities to both ‘envision a future’ and to ‘link a multitude of actors and

domains' (p. 701) to pursue these aspirations, aligns quality more closely to a mediating instrument. Whilst this research has delved deeper into the more precise types of linking work involved, we have also seen how audit quality has been called upon to 'frame and stabilise the interrelations among the multitude of components' (p. 731). And so, in these different ways, the notion of audit quality can perhaps, depending on what the focus of interest is, be aligned to *both* boundary objects and mediating instruments either in terms of what the notion has held together or has enabled,.

Beyond the identification of audit quality as another instance of a boundary object or mediating instrument, however, the transformations of quality itself seen within this trajectory of its changing problematisations are in themselves of importance. The transformation of quality's visibility, its gradual de-individualisation and transition to firstly an audit firm and then audit market property, and the adoption of a predominantly process-oriented output view of quality has been enabling in many ways. It has allowed quality to now be inspected and graded, served as an organising principle through which much regulatory action has been mobilised, evolved practice and regulation, and created new arenas of operations altogether. In so doing, the linkages of underlying ideas have become hardened and been made sufficiently concrete such that those ideas have started to appear in the discourse as if they were natural attributes of quality all along. They have stabilised, are no longer even questioned, and in this way have gradually assumed their taken for granted status as underlying problems of the audit. And so, the effects of quality being constituted in these ways have been powerful but perhaps not necessarily in ways they were intended. The wider, and final, question which remains is the meaning and importance of some of these transformations and it is at last to these which we will now turn, after some brief comments on the interrelationship of the arenas.

6.1.3 On the interrelationship of the arenas

In one sense, this thesis has examined the formation process of the now three distinct arenas of regulation, practice and academia within the audit field. What started initially as a singular arena of operations (see section 3.2) has gradually split apart into three. This development was achieved, in part, through quality, as seen in the three preceding chapters. Statistical sampling, which carried those initial quality ideas, provided the stimulus for a new academic arena of operations to emerge and through the pressures to regulate and demonstrate quality, the regulatory arena then split apart from professional practice with the advent of peer review and even further through mandatory rotation. A sub-arena of more specialised academia operations emerged once DeAngelo (1981) made audit quality

researchable. Mandatory rotation is anticipated to further reify the distinction between regulation and practice.

This formation and differentiation of the changing arenas within the audit quality field can provide some elucidations on the interrelationship between the arenas. Both regulatory and academia arenas have been seen in this thesis to stem initially from a ‘core’ of professional practice. Notwithstanding the regulatory arena’s conferred powers of governance, the core target of both the regulatory and academia arenas is on that same arena from where they both withdrew. Arena formation and differentiation has in this sense possibly fuelled a disconnect with professional practice. With increasing pressures for evidence based regulation and rationalizing trends in society, counting only that which can be seen, quality within the firms have become reified into the regulator’s conception of quality which may not be aligned with different actors in different arenas. Blunt measures such as mandatory rotation satisfy pressures for high visibility devices but may also further fuel the disconnect with practice by being based on rather grand assumptions as opposed to underlying practice issues.

The academia arena also bears further consideration here. Whilst typically thought of as a neutral and independent arena, this research suggests that academia within this sub-field has predominantly taken the lead from practice and regulatory issues in motivating their research studies. Within these changing constellations, they have been more followers than leaders. In itself formed from the confluence of contemporaneous discourses and event, academia has developed an entire sub-field of research activity on audit quality which is premised very little, if at all, on underlying practice. In this way, both the regulatory and academia arenas have developed an entire system of operations which have effectively, and paradoxically, side-stepped practice. Working *with* quality in these ways is not necessarily the same as working *about* quality, and all the more so given how quality is being constituted (see above). Together, all three arenas, however, contribute to the emergence of quality in its very particular forms which contribute to its legibility and ultimately to the changing constellations of audit quality.

The above suggests that the shifting arenas are more than just an elaborated story of emergence and differentiation – the changing arenas have both reflected, and fuelled, the growing disconnect between regulatory and academia operations with that component of quality from where this story started: the individual auditor judgement (see Table 1.1). This will be considered further in the final remarks of this thesis, section 6.4. For now, we have

at last arrived at the consideration of the wider meaning and importance of the emergence and rise of audit quality which has been examined over the course of this thesis.

6.2 The economization of audit quality

In 1990, Hopwood argued that economic discourses have provided a powerful basis for accounting elaboration and change (p. 15). Accounting could and was being changed in the name of discursive developments and Hopwood wished to especially emphasise the role of economic discourses in this process. In attempting to examine the relationship between economic discourses and accounting change, Hopwood explained:

The aim in so doing is to probe into both the ways in which the abstract generality of economic discourse can provide a context for accounting elaboration and change, and how, in turn, accounting can itself provide a specificity to conceptions of economics which enable it to infuse and change organizational and social affairs...Economics, so used, is seen as a means for helping accounting to become what it should be, but what currently it is not...(p. 128)

This relationship was developed further by Miller and Power (2013) who defined 'economizing' as the 'processes and practices through which individuals, activities and organizations are constituted as economic actors and entities' (Miller and Power, 2013, p. 560) and further, that accounting could be seen to be a 'mechanism by which the economization of organizational life becomes elaborated and institutionalized.' (p. 555). This conception of economizing is similar to Çalışkan and Callon's (2009) notion of economization. Here, the construction of action (-ization) into the word is to help imply that the 'economy is an achievement rather than a starting point or a pre-existing reality that can simply be revealed and acted upon' (p. 370). They define economization as 'the assembly and qualification of actions, devices and analytical/practical descriptions as 'economic' by social scientists and market actors' (p. 369). Whilst acknowledging that there may not be a consensus on what might be the content of the qualification of 'economic' (p. 370), in their conception also, it is the *processes* by which actions, devices and descriptions become economic which is being emphasized. And that these processes are important to consider due to the increasingly dominant role of economic knowledges within society.

Whilst Çalışkan and Callon's (2009) focus on 'the processes that constitute the behaviours, organizations, institutions and, more generally, the objects in a particular society which are tentatively and often controversially qualified... as 'economic'' (p. 370), was not a central

nor initial research object of interest within this study, some of the key transformations seen over the course of this history presented indicates that a gradual alignment of quality to that of the ‘economic’ has been slowly occurring. Here, by ‘economic’, we refer specifically to those aspects of economization whereby certain activities and organizations (i.e., both audit firms and arena activities relating to quality) have come to be increasingly conceived of in the terms of market ideals, including where academic research itself on audit quality has become increasingly entangled with the discipline of economics and alignable with capital markets based accounting research. And whilst perhaps these are not the modalities of economization *per se* in Çalışkan and Callon’s (2009 and 2010) terms, viewing these transformative shifts which have occurred with audit quality through the lens of economization can perhaps help us to understand even further the nature and constitution of quality, and the wider meaning and importance of its rise in these ways.

A high level summary of the key transformations, which were initially set out at the start of this thesis in Table 1.1, indicate a gradual procession of quality being transformed from a property of the individual auditor to eventually that of the market, along with the attendant changes to conceptualisations of the underlying quality problem. Whilst not a story of marketization in itself, one of the core modalities of economization as set out by Çalışkan and Callon (2010) and defined as that which leads to the establishment of economic markets, each of the three preceding chapters has nonetheless revealed some very important shifts with quality. And it is within these key shifts which have both enabled, and show the process by which, quality has been transformed into that which is seen through the centrality and prioritisation of market ideals. In so doing, the process by which quality has been in these ways economized has been revealed.

In chapter three, we saw how the discipline of statistics entered the audit field hand in hand with ideas of statistical quality control and in so doing, an alignment between the discipline of statistics and auditing was formed. In itself, the manifestation of statistics in the form of statistical sampling in auditing had its conceptual roots within the economizing concern of *efficiency*. As Kurunmäki et al (forthcoming) have noted, economizing has many components but the concern with the idea of efficiency is a centrally implied one. Linked to the then rapid growth of firms and the impracticality of testing all transactions, statistical sampling, in part spawned from these efficiency concerns and offered a solution to that problem. This alignment was further solidified when statistical sampling provided academia the means by which a new arena of audit research was to emerge, thereby implicating the scholarly discipline within its own rise. Through this constellation, quality ideas shifted from being understood as a property of the individual auditor, to that which could be

achieved through the techniques of statistical sampling. In so doing, the discipline of statistics entered the auditing field, which through the shared use of quantitative information and statistical methods, provided a stepping stone for the discipline of the economic sciences to ‘enter’ the field. However, quality also became *amenable* to being aligned with the economic sciences through this intermediate step of statistics. In the event, all of these conceptual roots were significant, in laying the foundations for the events and developments which were then examined in chapter four.

Here, the emergence of peer review, rooted within a core conceptualisation of the problem as one of quality control, was dependent upon ideas of statistical quality control being, and being able to be, operationalised in some way. This ‘way’ was through the transference of quality control onto the responsibility of the audit firm. This would more easily enable quality control standards to be written, adhered to and checked against. Whilst perhaps seen more widely as rational and logical especially in the context of growing audit firms and client size (again with at least some implied concern for efficiency), for current purposes, this meant that the de-individualisation of quality and transformation into a firm property was solidified. This was a key step in the shift from quality as a property of the individual to that of the market, acting again as a critical stepping stone towards economization. Firms were more amenable to being governable, to being made commensurate with one another, thereby allowing market based notions such as competition and benchmarking to gain traction (*ibid*). Within this chapter also, we saw how audit quality within academia became explicitly re-interpreted through the economic sciences, further enabling audit research more generally to follow the rising trend of quantitative, and market based, research occurring at that time, yet another modality of economization. And finally, with audit quality firmly secured as a property of the audit firm, the shift from firm to market structure ideals seen in chapter five, through being implicated within the discourses of financial stability, the free markets, and the EU’s single market project was made a smaller and more attainable step. With this step so taken, the underlying ideas of competition became quickly prioritised as the key element which would protect quality. By the end of constellation three, audit quality – across all three arenas, could be seen as having been constructed through the lens of the market based ideals of free markets, competition, and even market facing research.

Çalışkan and Callon (2009) have noted that the study of economization can involve, amongst others, ‘investigating the processes through which activities, behaviours and spheres or fields are established as being economic’ (p. 370). And importantly, that such processes should not and cannot be dissociated from the scholarly discipline which also seek to study the subject – in this present study, the academia arena. It is being put forward here

that this research has, almost in an advertent way, revealed the process and means by which quality has been economized over the past half century. The trajectory of quality examined in this thesis *is but another way through which economic forms of life have been enacted*, a further aspect of economization (Çalışkan and Callon, 2010). Seen this way, we have at last arrived at one underlying meaning and suggested interpretation of this historical examination of quality set out within the entirety of this thesis. This research puts forward that the emergence and rise of audit quality, what this has caused and enabled, its means and consequences have, in the end, ultimately been in the name of economization. And not entirely, as perhaps regulation, practice or academia may advocate, acting in their own purposeful ways and as their discourse suggests, in the name of quality.

Quality was seen within this historical trajectory as having undergone a process of being constituted as an economic ‘actor’ and in also being performative within that process. The economizing transformations, as seen above and throughout this thesis, have reshaped constellations. In serving as another modality in which economic forms of life have been enacted, through being subjected to increasing rationalisations and adherence with economics and economic ideals, quality can also in this way be seen as having been transformed into yet another basis upon which economies and economic activity are dependent. Whilst not serving as another example of marketization (Çalışkan and Callon (2010), being suggested here is that quality has been implicated in economic activity through contributing to the judgments which precede price and exchange. Callon and Law’s (2005) discussion of the notion of qualculation, as calculation to *include* judgment, can help to illuminate and support this argument. Here, calculation is taken to be understood not just in arithmetical form, but as a three-stage process which results in ‘a ranking, a sum, a decision. A judgment. A calculation’ (p. 720). The argument being put forward is that *that* judgment on quality is required prior to, or even serves as part of, the economic activity that follows. Further, Callon and Law (2005) argue that both qualitative judgments and quantitative calculations are about ‘arraying and manipulating entities in a space in order to achieve an outcome’ (p. 720). However, importantly, objects such as quality currently, do not pre-exist in that space for qualculation to occur – ‘they are also being made by it, made into a shape that fits’ (*ibid*).

6.3 Key contributions, limitations and future research

This research has sought to contribute to our understanding of the emergence, rise and meaning of audit quality by unpacking the changing nature of the audit quality ‘problem’. It has challenged some commonly held views in terms of the need for concern of audit quality and the relationship between high profile failures and quality demands. This thesis has extended Burchell et al’s (1985) notions of the arena and the constellation through the development of emergent and reformation constellations, and in so doing, contributed to our understanding of the more precise dynamics of accounting change. Through the focus on linkages, the media with which they are carried and the more detailed types of linking work involved in connecting ideas to the audit quality discourse, a new conceptualisation of change was put forward which attempted to weave a middle line between the specificity of this particular research object and more generalizable theories. This thesis has also provided another facet of how economization is being enacted within different forms of life, from the vantage point of quality.

Within the context of these aspirations, several limitations of this study are acknowledged. The potential size and scale of this project necessitated careful scoping decisions to be made during the research design stage in order to manage this scale. The arenas were limited to three key domains as opposed to the entire field. The constellations examined, whilst somewhat overlapping, were nonetheless relatively discrete and not continuous. Linkages which emerged from the analysis phase were paradigmatic as opposed to a complete data set. Data sources were limited to those which were considered to provide the richest window into the discourse being examined. A high level of judgement and subjectivity was involved, coding and identifying themes notwithstanding, in interpreting the data, in addition to more general limits of discourse analysis as providing an appropriate window into the underlying concerns of actors and domains at the time.

These limitations, however, can perhaps also provide a useful starting point for some potential research avenues in the future. Examining the transitions between the constellations may help to shed even more light on the conditions which lead to change. Further research can be conducted to build upon the initial steps made regarding the importance and nature of linkages in crystallising change, and the conditions of the ‘chain’ of linkages put forward in this thesis. For example, how and why do some ideas and connections get picked up versus others, and what are the conditions which lead to the chain gaining in sufficient strength in order for change to obtain? Testing the findings put forward in this thesis in different empirical settings is an obvious area to help move closer to a more

generalizable model of change. In addition to these, the role of technology, perhaps in enabling the legibility of quality within audit firms was not addressed in this thesis. And in arguing that a disconnect has arisen between the three arenas, a fruitful area of extended research would be in examining how the firms have now operationalised quality and how organisational practice has been reshaped by quality demands⁹⁷. The organisational consequences of the current quality regime could be thus investigated more fully which would help also to bridge academia with regulatory policy. This agenda would also be consistent with the call by Miller and Power (2013) for research which ‘reacts to the reductionism...and which focuses on the processes by which accounting *representations* and metrics are simultaneously powerful *interventions* which shape people, practices and organizations’ (p. 556). The consequences and implications of the representations and metrics, the proxies within this research, provide much scope for further research.

Separately, the other themes touched upon within this thesis but not investigated fully, include the study in greater detail of how academia influences, and is influenced by, the subject areas it studies, as well as the consequences therein. Here, tracing the constellations which have given rise to particular research objects, and the elements which have influenced their subsequent trajectory could perhaps provide elucidations for self-reflection as researchers. And finally, with the remarks on the relationship between economization and quality made within this chapter, a further research program might continue to focus on uncovering empirically the different and broader modalities of economization and identifying their specific importance and consequence for society.

6.4 Final remarks

One of the conclusions reached by Scott (2009) regarding the consequences of legibility is that formal schemes of order are ultimately untenable without some elements of the practical knowledge that they tend to dismiss (p. 7). As of writing, towards the end of 2016, the audit quality constellation has possibly started to shift yet again, towards a concern with professional scepticism⁹⁸ as a means to improving audit quality. This indicates that regulatory struggles to tame audit quality have possibly been unsatisfactory – despite nearly

⁹⁷ For example, initial interview and proprietary firm data on an internal quality improvement project from a London based audit firm was obtained as part of the data collection for this research and will be examined through the lens of this thesis as a future project.

⁹⁸ See APB (2012) Professional Scepticism - Establishing a common understanding and reaffirming its central role in delivering audit quality and the IAASB (2015) Invitation to Comment - Enhancing Audit Quality in the Public Interest: A Focus on Professional Scepticism, Quality Control and Group Audits.

half a century of efforts of increasing emphasis to improve quality, failures have persisted and regulators are continuously seeking other avenues to pursue quality. At a very high level, this could be seen as perhaps the start of a shift back towards a conception of audit quality as a property of the individual, where the solution to such a problem would be to look to training and ethics for quality. In other words, a turn back towards the individual professional judgment and practical knowledge, which have possibly been overridden within these increasing trends for rationalization. This conclusion would be similar to that reached by Gill (2009) who investigated the relationship between knowledge and ethics in the individual auditor and brought to attention the unintended consequences of highly technical accounting rules. Bromley and Powell (2012) also speak of further consequences such as the diversion of resources from core goals when the means take priority over the ends.

Yet, we have been here before. In structure versus judgement, the mechanistic versus the organic (Dirsmith and McAllister, 1982), this research has reaffirmed that attempts to codify and measure human judgement (Fogarty, 1996) are fraught with difficulties and inevitably subject to failure, due not least to their very role in changing conceptualisations of the underlying problem. It is aspired that this research has made inroads into a case for creating a greater space where judgement can be expressed⁹⁹, perhaps through language and spirit as opposed to purely proxies which can be counter-productive. Framework approaches to quality proposed by the FRC (2008) and IAASB (2014) which take a broader view imply value in such an approach (also, Francis (2011)). Perhaps even greater and more creative efforts are needed in these directions to counter the rising tide of the ‘audit society’ (Power, 1997) such that greater coherence between regulation, academia and practice may be achieved.

⁹⁹ I would like to thank Professor Chris Humphrey for suggesting this point.

Appendix A: Data sources examined

Source of data	Year(s) examined
Professional journals	
Accountancy (ICAEW)	1960 – 2013
Journal of Accountancy (AICPA)	1945 – 2010
Professional publications	
APB: The Future Development of Auditing	1992
ICAEW Audit Faculty publications on quality matters	2006 onwards
ICAEW: Independence and Incorporation – a Consultative Document	1988
Report on small, medium-sized firms (Derieux committee)	1980
Summary of the conclusions and recommendations of the: Commission of Auditor's Responsibilities (Cohen Commission)	1978
The AICPA Division of CPA Firms	1977
The Institute Responds (response to the Metcalfe Commission)	1977
The Tricker Report: governing the Institute in the 1990s	1983
Trueblood Commission: Objectives of Financial Statements	1971
Wheat Commission: Study on Establishment of Accounting Principles	1971
Professional standards or statements	
APC Draft Auditing Guideline – Quality Control	1983
APB SAS 240: Quality Control for Audit Work	2000
‘Expectations Gap’ standards	1988
IFAC Assuring the Quality of Audit and Related Services	1991
IFAC Control of the quality of audit work (Exposure draft 7)	1980
Interpretations of Statement on Quality Control Standards No. 1	1980
SAS No. 4 – Quality control considerations for a firm of independent auditors	1974
SAS No. 25: The Relationship of Generally Accepted Auditing Standards to Quality Control Standards	1980
Statement on Quality Control Standards ('SQCS') No. 1: System of Quality Control for a CPA Firm	1980
SQCS No. 2/4: System of Quality Control for a CPS Firm's Accounting and Auditing Practice	1996/2000
SQCS No. 3: Monitoring a CPA Firm's Accounting and Auditing Practice	1996
SQCS No. 5: The Personnel Management Element of a Firm's System of Quality Control	2000
UEC Auditing Statement No. 6: Quality Control – ensuring and improving the quality of audits	1979

Commissions, communications, inquiries and investigations

Competition Commission: Statutory audit services for large companies market investigation	2013
Competition Commission: Statutory audit services for large companies market inquiry – provisional findings report	2013
Co-ordinating Group on Audit and Accounting Issues	2003
DTI consultation document on implementation of 8 th directive	1987
EC: Consultation on ways to help create more market players	2008
EC: Consultation on control structures in audit firms and their consequences on the audit market (summary report)	2009
EC: Statutory Auditors Independence in the EU	2002
EC: The way forward	1998
EC: Reinforcing the statutory audit in the EU	2003
EC: Green paper on role, position and liability of auditors	1996
EC: Green paper on reform of audit policy	2010
EU Eighth Company law directive	1984
FRC: Audit Tenders Notes on best practice	2013
FRC: Discussion paper, Promoting Audit Quality	2006
FRC: Final Report of the Market Participants Groups	2007
FRC: The Audit Quality Framework	2008
FRC: Reporting on audit quality monitoring, consultation document	2006
House of Commons inquiry into banking crisis	2009
House of Lords: Auditors: market concentration and role	2011
IAASB: Audit Quality, An IAASB Perspective	2011
IAASB: A Framework for Audit Quality	2014
IAASB: Consultation Paper, A Framework for Audit Quality	2013
Improving the accountability of public owned corporations and their auditors – Report of subcommittee on reports, accounting and management of the Committee on Governmental Affairs (US Senate) – intro only	1978
Metcalfe Staff Study: The Accounting Establishment	1976
National Commission on Fraudulent Financial Reporting Summary of recommendations	1987

Commissioned research publications

Ownership rules of audit firms and their consequences for audit market concentration (Oxera)	2007
Competition and choice in the UK Audit Market (Oxera/FRC)	2006

Practice manuals

Cooper Manual of Auditing	1966, 1969
Coopers & Lybrand, Manual of Auditing	1981, 1984, 1992
Coopers & Lybrand Student's Manual of Auditing	1971, 1979, 1985
Thomson Learning Student's Manual of Auditing	2000
Thornton Baker / Grant Thornton audit manual 1990	1981, 1983, 1986,
Spicer and Pegler Practical Auditing (10 th – 18 th editions)	1951 - 1990
Thomson McLintock audit manual	1983
Practice management manuals (ICAEW)	1993, 1996, 2013
Practice assurance manual (ICAEW)	2005, 2007, 2009
Longman Audit and Accountancy Manual	1982

Academic research articles (see section 2.3.2) 1980 – 2014

from the following journals:

Abacus
Accounting and Business Research
Accounting, Auditing and Accountability Journal
Accounting & Finance
Accounting Horizons
Accounting, Organizations and Society
Auditing – A Journal of Practice & Theory
Critical Perspectives on Accounting
Contemporary Accounting Research
European Accounting Review
International Journal of Auditing
Journal of Accounting and Public Policy
Journal of Accounting, Auditing & Finance
Journal of Accounting Research
Journal of Accounting and Economics
Review of Accounting Studies
The Accounting Review
The British Accounting Review

Appendix B: Timeline of significant developments leading to mandatory peer review

Year	Event/Development
1968	Federal ruling on BarChris Construction Corporation invoked liability provisions of Securities Act 1933. First case which dealt explicitly with accountants' liability setting forth judicial guidelines with respect to materiality and standards of care. AICPA forms two subcommittees to examine the issue.
1969	USA v Carl Simon (Continental Vending) ruling whereby accountants were found guilty of criminal conviction for the first time in some 70 years
1970	Failure of Penn Central Transportation Company, the then largest bankruptcy in US history
1971	Emergence of firm quality control as an object of concern
	Separate implementation of the CPA Quality Review Program launched by AICPA (post-audit reviews or working papers to encourage compliance with auditing standards and principles)
1972	Wheat Commission releases report on establishment of accounting principles; Trueblood Commission releases report on objectives of financial statements
	FAF and FASB formed
1974	AICPA releases SAS 4: Quality control considerations for a firm of independent auditors
	SEC imposes a number of 'quality reviews' against firms as part of sanctioning measures.
1976	Release of Metcalf Commission: The Accounting Establishment
	Extension of CPA Quality Review Program to Voluntary Quality Review Program ('quality reviews') – to include firms with and without SEC practices.
1977	Release of Cohen Commission: Commission on Auditors' Responsibilities
	Formation of the POB and two new practice sections to oversee both the existing quality reviews (for any firms who did not sign up to either of two practice divisions) and a new peer review process. Membership in either section is voluntary.
1978	Release of Full Metcalf Commission: Improving the accountability of publicly owned corporations and their auditors
1982	Collapse of Penn Square Bank and relatedly Continental Illinois National Bank & Trust Co
1985	ESM Government Securities, Inc failure
	Dingell Subcommittee established on the accounting profession and SEC oversight; Treadway Commission established on fraud
	AICPA Special Committee on Standards of Professional Conduct (Anderson Committee) recommends new code of conduct, mandatory peer review and continuing professional education.
1988	Mandatory peer review overwhelmingly approved at AICPA membership vote

Appendix C: Timeline of significant developments leading to UK and EU mandatory rotation

Year	Event/Development
1976 (US)	Release of Metcalf Commission: The Accounting Establishment (the dominance and concentration of the Big N audit firms cited as a key problem and the idea of mandatory audit firm rotation is put forward as a means of increasing competition)
1984	EU releases Eighth Company Law Directive
1987	DTI releases consultation document on implementation of EU Eighth Directive
1990-1992	Failures of Polly Peck International, BCCI and Maxwell Group companies
1996	EU Green Paper into role, position and liability of auditors (applies single market principles to the audit market)
2001	Collapse of Enron
2002	EC releases recommendations on 'Statutory Auditors Independence in the EU' (internal partner rotation after a period of 7 years)
2007	Collapse of Lehman Brothers, triggers global financial crisis
2009	UK House of Commons Treasury Committee holds inquiry into the banking crisis
2010	EU Green Paper and investigation into the reform of audit policy
2011	UK House of Lords Economic Affairs Committee inquiry on market concentration and role (recommends tendering) UK Office of Fair Trading refers the audit market to the Competition Commission for investigation
2012	FRC amends UK Corporate Governance code to mandate 'comply or explain' tendering
2014	EU legislates mandatory rotation (tendering after ten years), effective for 2017 CMA releases recommendations of inquiry – mandatory tendering after ten years

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