

**REINING IN AUDITORS: ON THE DYNAMICS OF POWER SURROUNDING AN  
“INNOVATION” IN THE REGULATORY SPACE**

by

Bertrand Malsch, Ph.D., M.B.A.  
HEC Montréal  
Édifice Côte-Sainte-Catherine  
3000, chemin de la Côte-Sainte-Catherine  
Montréal (Québec)  
Canada H3T 2A7  
E-mail: [bertrand.malsch@hec.ca](mailto:bertrand.malsch@hec.ca)

Yves Gendron, Ph.D., C.A.  
Faculté des sciences de l'administration  
Pavillon Palasis-Prince  
2325, rue de la Terrasse  
Local 6224  
Université Laval  
Québec City (Québec)  
Canada G1V 0A6  
Tel.: (418) 656-2131 ext. 2431  
E-mail: [yves.gendron@fsa.ulaval.ca](mailto:yves.gendron@fsa.ulaval.ca)

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## **Abstract**

In the aftermath of Enron and the collapse of Arthur Andersen, new “independent” institutions were created to oversee financial auditing. Based on a modified version of Lukes’ multidimensional model of power, we first investigate how the creation of the Canadian Public Accountability Board (CPAB) has affected the dynamics of power among the main players enlisted in Canada’s regulation of public accounting. Our findings strengthen the view that a “form of allegiance” was, at the time of data collection, developing between CPAB and the largest Canadian accounting firms. Through a second analytical movement, we extend the boundaries of our argument, showing that patterns of resistance against the logic of arm’s length regulation operate in a variety of audit regulatory sites. Our conclusion points, in particular, to the spatial gap – and incidentally the limitations – of any attempt to control and supervise a globalized industry from a national or regional perspective.

**Keywords:** Accounting regulation; Auditor independence; Dynamics of power; Globalization processes; Independent audit regulators; Resistance.

# **REINING IN AUDITORS: ON THE DYNAMICS OF POWER SURROUNDING AN “INNOVATION” IN THE REGULATORY SPACE**

## **Introduction**

Crisis and regulation intertwine. As observed by Hancher and Moran (1989, p. 284), “regulation almost always happens because some sense of crisis is precipitated”. In the past, auditors largely self-regulated and were subject to peer reviews, although the effectiveness of such mechanisms was questioned sporadically (e.g., Fogarty, 1996; Lennox & Pittman, 2009). However, high-profile bankruptcies, which in 2001-2002 threatened the legitimacy of public accounting (Guénin-Paracini & Gendron, 2010), precipitated the establishment of new disciplinary mechanisms in various countries to control the audits of public companies’ financial statements. In a very powerful demonstration of isomorphism in times of crisis – both mimetic and coercive (DiMaggio & Powell, 1983) – new regulatory structures mushroomed around the globe to monitor financial auditing and secure its legitimacy, for instance the Public Company Accounting Oversight Board (PCAOB) in the USA, the Canadian Public Accountability Board (CPAB), and the Haut Conseil du commissariat aux comptes (H3C) in France.

The subjugation of accounting firms to independent monitoring is typically viewed as one of the most substantive and fundamental changes in the history of contemporary public accounting (e.g., DeFond, 2009; Latshaw, 2003). Audits of public companies are no longer understood as a self-regulated professional activity; instead accounting firms are now accountable to regulatory organizations localized outside the boundaries of the profession’s jurisdictional domain. A range of practices are established to show that the new regulatory organizations are indeed in control of financial auditing – for example through inspection reports and instances of disciplinary actions taken against deviant accounting firms. The increasing degree of attention devoted at the international level to coordinate independent regulation through network structures such as IFIAR (International Forum of Independent Audit Regulators) and EGAOB (European Group of Auditors’ Oversight Bodies) provides another reinforcing signal (Humphrey, Loft, & Woods, 2009). Nonetheless, from a critical perspective, we may wonder about the extent to which the influence of the new regulatory mechanisms is consistent with the claim that audit

quality is being reinvigorated by removing control and discipline from the profession. As argued by Humphrey (2008, p. 185):

A key task for [auditing] research is one of understanding, whether in terms of studying the political nature of audit regulatory processes or what happens when auditors and regulators claim to work in the name of the public interest and how auditing and auditing regulations help to define and/or translate matters of social concern.

The institutionalization of external surveillance, as deployed on public accounting firms, allows us to examine issues of power and resistance in the regulatory space surrounding a professional setting. Our focus in this paper is on the dynamics of power, which the establishment of new independent regulatory organizations engendered, and the extent to which the regulatory innovation translates into substantive change in the profession's regulatory space or arena. That is, how distant is independent surveillance from self-regulation?

Accountancy's regulatory space (MacDonald & Richardson, 2004; Young, 1994) involves a complex and interrelated network of national and international organizations – professional bodies, accounting firms, regulators – in the design, assessment and control of the overall quality of financial audit work (Humphrey et al., 2009). Contemporary regulatory spaces are characterized with relatively fragile and negotiated boundaries, subject to the influence of a range of actors and interests (Djelic & Sahlin, 2009; Gendron & Spira, 2009). Regulatory spaces are, therefore, always contested and their occupants continually involved in quests to mark the field with their own imprimatur: “Regulation is indisputably a political process and it thus exhibits one of the defining features of any such process – it involves the contest for power” (Hancher & Moran, 1989, p. 4).

Based on a modified version of Lukes' (1974, 2005) multidimensional model of power taking into account processes of overt conflicts over preferences, agenda setting and discursive construction, the present paper first investigates, through a case study, the extent to which the creation of CPAB in Canada has affected the dynamics of power among the main players enlisted (e.g., Big Four firms, professional institutes, regulatory agencies, etc.) in the country's regulation of public accounting. Our preliminary reason for undertaking this study was that a sense of uncertainty and instability, being engendered by the formal authority attributed almost overnight to independent audit regulators in rendering financial auditing (historically bounded with a status of professional autonomy) subject to outside oversight, challenged fundamentally the dynamics

of power surrounding accountancy's regulatory spaces. Patterns of influence and resistance are likely to be more salient in turbulent times. We were interested especially in examining which organizations gained, maintained or lost their position of power in the regulatory space under study, and the extent to which the new regulatory practices are consistent with the independent regulator's claim of "outside monitoring".

Our analysis, however, is not constrained to a single national site. Of course, "regulation occurs, it is a truism to observe, in a particular place, and therefore place matters" (Hancher & Moran, 1989, p. 283). Historically, nation state boundaries provided one of the most important delineations of place, but it is clear that national peculiarities are not the whole story anymore. Economies of "advanced" capitalist nations exhibit increasingly similar patterns of extensive regulation being dominated and shaped by a small number of large international networks or organizations (Humphrey et al., 2009; Suddaby, Cooper, & Greenwood, 2007). Accordingly, our analysis is also directed at the exercise of power and influence in the globalized audit regulatory space. As observed by Djelic and Sahlin (2009, p. 198), the current transnational "elaboration and deployment of new types of regulatory frames are in great-part interest-driven and reflect logics of power and control".

Through a second analytical movement, we, therefore, extend the boundaries of our study to developments taking place in some other national jurisdictions and at the transnational level. Although the extension of our analysis is not as profound as in the CPAB case, it provides some insights into the dynamics of power which the creation of independent audit regulators engendered in other spaces, and the collaborative processes taking place across networks of regulators in trying to ensure that their mandates and practices are coherent and consistent. In particular, the broadening of our empirics provides us with a reasonable basis to maintain that the interplay in processes of power and resistance, which we uncovered in the Canadian regulatory space, is not unique and that the impact ensuing from the creation of outside regulators in terms of establishing an arm's length relationship between overseer and overseen is less profound than is often claimed at the rhetorical level. Our study concurs with recent calls for a deeper problematization of the complex and shifting domain of the international audit regulatory arena (Cooper & Robson, 2006; Humphrey et al., 2009; Richardson, 2009).

## **Investigating power**

Complex and elusive, the concept of power constitutes perhaps one of the most fundamental notions that social scientists should investigate (Flyvbjerg, 2001). As observed by Bromwich and Hopwood (1982), the continued expansion of the auditing profession depends in part on its response to some of the very severe challenges it faces. Research has a role to play in clarifying the nature of these challenges and in exploring the possible responses. In particular:

Research has to explore fundamental questions about why and where the auditor's authority and power in society reside and how this location changes over time. (Bromwich & Hopwood, 1982, p. 21)

Power has been investigated in accounting literature through a variety of approaches (Cooper & Robson, 2006). Our investigation is predicated on a modified version of Lukes' (1974, 2005) multidimensional model of power. The thrust of Lukes' work is that studies of power need to pay attention to overt and covert influence. Power always constitutes a convoluted matter of exploitation and control, of sustained dependence and inequality on the one hand and legitimate domination on the other hand (Hardy & Clegg, 2006). As a result:

Studies applying what Lukes (1974) refers to as the first dimension of power ought to be augmented with analyze [*sic*] which attend to other power dimensions: agenda building and the systemic and pervasive forms of structural and ideological power. (Cooper & Robson, 2006, p. 426)

In his model of power, Lukes (1974, 2005) sketches three different modes or dimensions to explain the notion of power. In the one-dimensional view, he conceives power as intentional and active: it should thus be understood through the study of overt influence. Power, then, consists of defeating opponents' preferences surrounding explicit situations of conflict between interests. Preferences are assumed to be exhibited in actions and can be discovered by observing people's behavior.

The one-dimensional view of power was originally criticized on the grounds that power implies two faces. That is, power is also exercised when actors strive to reinforce socio-political values and institutional practices that limit the scope of the political process which is subjected to public consideration:

To the extent that a person or group – consciously or unconsciously – creates or reinforces barriers to the public airing of policy conflicts, that person or group has power. (Bachrach & Baratz, 1962, p. 8)

Lukes points out that Bachrach and Baratz's views strengthen the understanding of power by introducing the notion of covert biases. The second dimension of power is exercised when one party manages to prevent grievances from ever being discussed. This is essentially power by manipulation and the classic example is agenda setting. However, Lukes maintains that the two-dimensional view of power remains limited in that it is focused on observable conflicts, whether overt or covert. Another of his criticisms is that two-dimensional power is over-committed to the study of *concrete* decisions and non-decisions, whereas inaction can also be the outcome of culturally patterned collective behavior.

To overcome these limitations, Lukes argues that a third level of power operates. Ideologically, it shapes people's thoughts and wishes so that differences of interest are prevented from occurring in the first place. For Lukes, ideology impacts people's desires in a way that is contrary to their "real" interests; that is, if they were free to choose, they would choose something other than the ideologically agreed upon desire. The absence of grievances therefore does not necessarily imply genuine consensus because power also operates ideologically, influencing people's thoughts and desires so that they accept their role in the existing order of things. Moreover, Lukes stresses that ideological power operates not through formal indoctrinating techniques but through the preclusion of alternatives, so that people come to see the status quo as natural, inevitable and common sense.

Lukes' third dimension of ideological or latent power has engendered a number of criticisms (Clegg, 1989; Hayward & Lukes, 2008) – in particular that reliance on people's purported "real interests" creates insurmountable difficulties. In her study of power in the household, Vogler (1998) provides a compelling summary of these difficulties:

Lukes' concept of ideology [...] rests on the idea of a single dominant or hegemonic ideology rooted in class interests, which constrains the subordinate classes in ways which are contrary to their "real interests". There are two problems here. First the general reductionism involved in explaining ideology in terms of a society's economic arrangements (class relationships) and secondly, the insuperable problem of identifying people's "real interests", particularly when they themselves do not articulate them. (Vogler, 1998, pp. 699-700)

As a result of this problematization, Vogler (1998, p. 701) proposes a re-conceptualization of Lukes' third dimension of power, namely, as being discursively predicated (Foucault, 1986). A discourse is understood as a group of statements, ideas and practices that provide a language for

making sense and talking about a particular topic at a particular place and moment (Hall, 1992). Vogler's (1998, p. 701) re-conceptualization is predicated on the following argument:

Whereas Lukes sees power as operating through ideology to shape people's beliefs and desires in ways which go against their real interests, Foucault sees power as consisting of disciplinary mechanisms and discourses which not only affect how people live and speak but actually constitute them as subjects [...]. Instead of analysing interests and ideology [Foucault] therefore argues that we need to study the ways in which social reality is constituted by discourses.

For Foucault (1983, pp. 789-790), power is less a contest between opposing actors than a question of government:

This word [i.e., government] must be allowed the very broad meaning which it had in the sixteenth century. "Government" [...] designated the way in which the conduct of individuals or of groups might be directed: the government of children, of souls, of communities, of families, of the sick. [...] To govern, in this sense, is to structure the possible field of action of others.

Discourses play a key role in "government". They operate as mechanisms of power deployed on the individual's subjectivity and, as a logical consequence, on communities:

Just as a discourse "rules in" certain ways of talking about a topic, defining an acceptable and intelligible way to talk, write, or conduct oneself, so also, by definition, it "rules out", limits and restricts other ways of talking, of conducting ourselves in relation to the topic. (Hall, 1997, p. 44)

This excerpt is especially relevant for our purposes, because it depicts power as the subtle influence that discourses, which prevail in one's environment, can have on shaping the self and the organizations in which people work. Individuals can therefore be viewed as being surrounded, in the social web, by a range of more or less contradictory discourses. These discourses play a central role in the construction of their self (Dent & Whitehead, 2002; Foucault, 1981). Under this perspective, discourses and their underlying systems of representation can be viewed as "places" from which individuals can position themselves in constituting their subjectivity (Woodward, 1997). Whether individuals, in constituting their self, take up some surrounding discourses consciously or are covertly influenced by others is a matter of debate in the literature (Haynes, 2006) – although it has been recently shown that individuals' reflectivity plays a role in the process (Alvesson & Willmott, 2002; Gendron & Spira, 2010).

Foucault's concept of discourse is therefore useful, not just because it side-steps the unresolvable dilemma of deciding between true and false consciousness, but because it involves

an alternative view of power. Along this view, “Power is not [only] something that is acquired, seized or shared, something one holds on to or allows to slip away” (Foucault, 1981, p. 94). It is also a strategy, “an impersonal property of social practices and mechanisms, akin to an open ended grid or network, permeating all aspects of society, often enjoyed as well as suffered and affecting the dominating as much as the dominated” (Vogler, 1998, p. 702). From this point of view then, “interests are thought to be constituted in discourse rather than pre-given, and discourses are only thought to be able to generate dissatisfaction and resentment when they coexist with alternative discourses which construct things in different and contradictory ways” (Vogler, 1998, p. 702).

In brief, how people think about and make sense of an object, such as regulation, does not emerge out of the blue, but in a discursive context characterized with certain conditions of possibility. A thorough examination of the dynamics of power in regulatory space, and of the flows of change and inertia it generates, needs to pay attention to the actors involved in overt conflicts (level 1), the issues they mobilize and those they avoid (level 2), and the discursive context (level 3), both within the field and at its periphery. More specifically, our study of power dynamics is centred on the rivalry between two logics which co-exist under tension (Gendron, 2002) within most, and perhaps all contemporary regulatory spaces; that is to say the logic of arm’s length regulation and that of self-regulation.

Finally, it needs to be recognized that, while the dimensions of power can be distinguished at the analytical level, it can be relatively difficult to disentangle their respective patterns of influence when examining empirical data. Hence the case study section below is not structured in accordance with the dimensions of power – but along certain themes which emerged from our analysis of the empirics, which we interpret relying on the multidimensional lens.

### **Constitution of data**

To carry out the empirical component of our research we rely on public statements issued by a number of independent audit regulators and regulatory agencies, internal documents which we obtained from one interviewee, documents retracing the public consultation process initiated in June 2003 on regulatory project 52-108 regarding the creation of CPAB, and minutes of all meetings held between 2005 and 2009 by two agencies set up by the European Commission,

namely, the EGAOB and the Audit Regulatory Committee (AuRC).<sup>1</sup> The minutes include information on meeting discussions, summaries of decisions, supporting documents (e.g., committee reports) as well as records of motions (both carried and lost). We also rely on two rounds of semi-structured interviews.<sup>2</sup> The first round of interviews, carried out from 2003 to 2005, is part of a larger programme of research devoted to the examination of auditor trustworthiness in times of turbulence. More than 60 interviews were carried out, mostly in Canada, with audit committee members, financial analysts, financial auditors, regulators, etc. The interviews explore participants' views on the collapse of Enron and Arthur Andersen, as well as post-Enron regulation. Two of these interviews take on special significance retrospectively in the context of the present study: one with the first chief executive officer (CEO) of CPAB, and the other with a member of CPAB's board of directors.<sup>3</sup> While our commitment to protect the anonymity of participants and of their employing organizations prevented us from quoting directly CPAB's CEO, we were able to compensate through the incorporation of publicly available statements made to the press. From the onset, CPAB required that no other employee be interviewed regarding the topics falling under the umbrella of the programme of research on auditor trustworthiness.

The second round involves seven interviews conducted in 2008-2009 in Europe, aimed at extending the boundaries of our findings beyond the CPAB case. The interviews involve three high-ranking partners of the Big Four, as well as one board member and three executives from independent audit regulatory organizations. The interviews were centred on the nature of the relationship between regulatory organizations and public accounting firms, as well as the nature of the surveillance exerted by the regulator. All of the interviews that we conducted for the paper lasted between 60 and 90 minutes, and all were recorded and transcribed. Our empirical material relates to a specific time frame, from the establishment of CPAB in 2003 until year 2009 when our last interviews were carried out.

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<sup>1</sup> Between 2005 and 2009, the EGAOB met 20 times, while the AuRC met 25 times. Some of the minutes provided by the AuRC and the EGAOB are relatively brief, as if these entities are concerned with the extent of information that they reveal in the public sphere.

<sup>2</sup> Given the sensitive nature of our object of study we are very cautious in protecting interviewees' identity. Information regarding interviewees is therefore purposively kept minimal.

<sup>3</sup> While in this paper we do not rely extensively on the larger set of first-round interviews, they nonetheless informed our understanding of the context in which new regulatory entities were created following the collapse of Arthur Andersen.

## **The dynamics of power in the Canadian regulatory space**

### *Background*

Making sense of economic regulation involves understanding the terms and discourses under which organizations enter regulatory space or defend their position within it. In turn, this is influenced heavily by the prevailing general political attitudes and legal traditions surrounding the space (Hancher & Moran, 1989). To help us identify some of the main implications ensuing from the creation and establishment of CPAB, we portray its official nature and highlight some recent developments regarding accountancy's regulatory space in Canada.

Canadian chartered accountants (CAs) have historically been regulated almost exclusively through their self-regulatory bodies, namely the Canadian Institute of Chartered Accountants (CICA), and provincial institutes. Several committees of the CICA are involved in standard setting. The provincial institutes deal especially with the enforcement of standards, for instance through periodic inspections of public accounting firms. Canadian auditing standards are set by the Auditing and Assurance Standards Board (AASB) of the CICA. The voting members of the AASB are staffed entirely by accountants working in accounting firms and in industry. The AASB is subject to the oversight of the Auditing and Assurance Standards Oversight Council (AASOC) — an “independent” body established in October 2002 (i.e., a few months after the collapse of Arthur Andersen) by the CICA. The Council is made up of eight voting members from high profile organizations (e.g., two law firms; one bank; one accounting firm; two regulatory bodies, etc.). AASOC is responsible for appointing AASB members and for ensuring that the standard-setting process is responsive to the public interest. Certified General Accountants (CGAs) and Certified Management Accountants (CMAs), two other categories of professional accountants in Canada, have also been regulated by their respective self-regulatory bodies. Although for a long time only CAs were permitted to conduct public audits in Ontario and Québec (MacDonald & Richardson, 2004), the two provinces recently passed legislation allowing CGAs and CMAs to engage in public accounting if appropriately qualified.

As a result of the corporate scandals of Enron et al., and the swift passage of the Sarbanes-Oxley Act (SOX) in the USA in the summer of 2002, Canadian regulators felt an urgent need to react; investor confidence in Canadian capital markets was apparently jeopardized. Canadian securities authorities sought to elevate corporate governance by introducing new rules on audit

committees and CEO/CFO certification. New requirements for auditor independence were adopted, reflecting updated global standards. Most important in the context of this paper, the scandals translated into the incorporation (2003) of CPAB, which formally aims to oversee the audit engagements pertaining to the financial statements of public companies.

CPAB is structurally idiosyncratic to the Canadian political and juridical environment. Since accounting oversight comes under provincial authority, there was no single body at the federal level that could pass a law authorizing its creation. CPAB developed as a private-sector initiative, supported especially by Canadian Securities Administrators' National Instrument 52-108, which requires auditors of public reporting issuers to register with CPAB. The agency's official aim is to "contribute to public confidence in the integrity of financial reporting of public companies in Canada by promoting high-quality, independent auditing" (CPAB, 2003). CPAB staff conducts inspections of the participating public accounting firms in accordance with the number of reporting issuers they audit. For instance, accounting firms that audit 100 or more reporting issuers are inspected annually. In 2008, CPAB employed 24 full-time inspectors and earned revenues in excess of CDN \$12.5 million. Our empirical analysis of CPAB covers the events surrounding its establishment in 2003, until year 2008.

#### *The accounting establishment prevailing in the initial confrontation*

Our analysis indicates patterns of resistance to the institutionalization of arm's length regulation in Canada. Essentially, these patterns reflect an overt conflict of preferences surrounding the foundation of CPAB, opposing certain stakeholders to the accounting establishment (i.e., the largest accounting firms and the CICA). Although the relationship between firms and their professional institutes can be quite strained (Gendron & Barrett, 2004), when their interests converge they can be close allies.

Of the 18 commentaries produced through the public consultation process surrounding proposed instrument 52-108, only eight were generally supportive of the creation of CPAB. In particular, we found a pronounced difference of appreciation between accounting firms and the CICA on the one hand, and the CGA and CMA institutes as well as certain key players in Canadian business on the other. While the former praised the architecture of the new regulatory regime, the latter tended to be critical of the proposed agency's governance structure and its favoritism towards the CA branch of the accounting profession. For instance:

[Our] concerns [about CPAB] have three basic components: 1. Our view that CPAB is a flawed model of public policy; 2. Inconsistencies between this model and the comparable model in the United States, which we conclude it is intended to emulate; 3. The aforementioned exclusion of 35,000 professional accountants [i.e., CGAs] from a regulatory model dealing with their profession. (Carpenter – CGA Association of Alberta, 2003)

Other stakeholders expressed concerns on two fronts. The costs generated by the development of an additional regulatory system were criticized, particularly in light of the significant presence of small public companies in the Canadian context. The lack of independence of the new regulatory entity from the accounting profession was also brought to light:

We also have concerns on the impact the proposed auditor oversight rules will have on small reporting issuers, who are an important part of Canadian capital markets. In addition to added costs from an additional layer of regulation, smaller accounting firms with few public issuer clients may choose not to enter participation agreements with CPAB given that it would not add value to the majority of their private issuer clients. (Stymiest – TSX Group, 2003)

Our fear that the board is too closely aligned with the accounting industry is also reflected in the fact that the funds for the continuation of the CPAB will not come from the capital market as in the United States but from the member accounting firms that must register with the CPAB. We are of the opinion that the accounting industry is too closely entwined with the CPAB to make this a truly independent organization. (Hession – Ontario Teachers' Pension Plan, 2003)

While the memoranda issued by the CGA Association and Ontario Teachers' Pension Plan covered several pages, those issued by PricewaterhouseCoopers (PwC) and Deloitte & Touche gave their full support to the regulatory project in just a few lines. The comments made by KPMG and Ernst & Young were somewhat more substantial. Although generally supportive of the creation of CPAB, the two firms formulated some criticisms regarding the proposed notification system, which they viewed as being too unpredictable:

We believe the proposal [...] that a Firm must notify all of its reporting issuer audit clients of all sanctions imposed by CPAB should be reconsidered. It is impossible to assess the reaction of a Firm's clients to such a communication. As a result the impact of the sanction may be much more severe than intended by CPAB. (Thesberg – KPMG, 2003)

Notification of [sanctions] to audit clients, prospective clients and regulators are very serious matters and we are understandably alarmed that such requirements be

introduced into our national securities regulations without a much better understanding of [...] the means the CPAB will use to classify inspection findings, specify remedial actions and otherwise take action against auditors with which the CPAB has quality concerns. (Ernst & Young, 2003)

In January 2004 – i.e. three months after the end of the period of public consultation, the regulatory authorities issued a number of responses. This last phase of the consultation process is particularly important for the purposes of our analysis since it helps to make sense of the power exerted by the different parties operating within the regulatory space: “Identifying who prevails in decision-making [...] seems the best way to determine which individuals and groups have more power in social life, because direct conflict between actors presents a situation most closely approximating an experimental test of their capacities to affect outcomes” (Dahl, 1961, p. 4). Overt conflicts and their resolution can be seen as a kind of trial of strength, that is to say as a test of the power of the different parties involved. From this point of view, the results of the consultation process clearly emphasize the significant role of the accounting establishment in influencing the way in which CPAB was initially structured. The criticisms concerning the lack of independence from the profession – especially the CA profession – were rejected in block:

[The] CPAB is and will remain dominated by members who are independent of the accounting profession. In this respect, we note that four out of the five members of the Council, as well as seven out of eleven members of the Board of Directors, will be independent of the accounting profession. (CSA, 2004)

Yet from a critical perspective, the response of the Canadian Securities Administrators (CSA) is far from being convincing. Although CPAB is overseen by a Council of Governors that is dominated for the most part by individuals external to the profession, as of June 2008, its board of directors included four professional accountants (out of 11 directors). All members of CPAB’s executive team were professional accountants (June 2008). CPAB’s structure of governance is, therefore, not exempt from the influence of the professional accountants that it aims to regulate. Beyond such structural matters of “detail”, the following public statement from the first CEO of CPAB points to a relative proximity between the political agenda of accounting firms and that of the new regulatory organization:

At the time the board was created, it was post-Enron. The Americans had put the PCAOB in place as part of Sarbanes-Oxley, and other countries were starting to respond as well. I agreed with the premise that it was time to have more independent oversight of the accounting profession. [...] And I liked the proposal in Canada because it contemplated an oversight organization that would be not only independent

from the profession but would also operate at arm's lengths from government. I believed, and still do, that if government tried to regulate the accounting profession directly it just wouldn't work. (*The Bottom Line*, 2006, p. 5)

It was also pointed out to us that one of the main reasons for CPAB having been able initially to attract experienced staff from accounting firms relates to generalized disdain, within the CA profession, towards government intervention. Being accountable to outsiders (i.e., politicians and public servants) was apparently not a conceivable option – to the point that it reportedly motivated a number of public accountants to join the private-sector regulatory ship.

The three levels of power were therefore involved in developing a network of resistance against the logic of outside surveillance. Drawing on the first level, it appears that the accounting establishment was largely successful in the representations it made to the CSA, since the latter ultimately favored the establishment's views in the design of the new regulator. The third level of power is also mobilized through the incorporation within CPAB of individuals, at the executive and staff level, having been extensively socialized as professional accountants in large accounting firms, over the course of one or even a few decades. Indeed, we argue that one of the chief ways in which the accounting establishment benefitted from a longer-term ability to influence day-to-day decision-making and agenda building within CPAB occurred when the regulator was designed initially; that is to say through the decision to employ a fair number of individuals who share and identify significantly with the profession's dominant discourses. The distrustful views expressed above regarding government regulation illustrate this point, resonating with one of the dominant discourses within the professional accounting community. As argued by Ellwood and Newberry (2007), anti-government political interests are influential in networks of accounting stakeholders – most notably professional auditors, audit committee members and certain regulatory organizations. The following interview excerpt from a board member of CPAB further illustrates the matter, in arguing that the “legislative pendulum” movement regarding regulatory reforms as sustained through SOX went too far:

The pendulum has swung probably too far on the rules and you do hear that a lot from a lot of people now, you hear board chairmen and CEOs saying: “Well, we've really cleaned up our governance, now we can get back to creating value, which is our real role.” And there's a lot of truth in that. You know, good financial statements is not an end, it's a means to an end. (Board member of CPAB and executive director of a provincial institute)

The quote brings to the fore the un-palatability of additional regulation as a solution to business scandals. As noted by Spira and Page (2003), self-regulation as a solution to governance problems generally suits many parties: accountancy then avoids state regulation (which is seen as inflexible and difficult to influence); agents of the State and politicians avoid taking responsibility for an activity which they know will be inevitably the subject of criticisms as future scandals unfold. As a result of the discourse of self-regulation being widely endorsed within accountancy, it is perhaps no coincidence if the public consultation process surrounding the creation of CPAB was literally taken over by public accountants and a few representatives from the private sector. Of the 18 participants involved in the public consultation process, seven were then working in accounting firms (including the Big Four); four were representatives of accounting institutes, and the seven remaining participants were employees from major actors in the Canadian business community (e.g., Telus, Ontario Teachers' Pension Plan). Remarkably there was no participation from any government agency or representative, as if these parties had internalized an attitude of relative quietness regarding government intervention in business.

The overwhelming presence of professional accountants within CPAB constitutes a strong manifestation of power. The recruitment policy of CPAB targets former partners explicitly. As shown in Table 1, all of CPAB's executives (in 2008) had professional accounting backgrounds; in particular, four of them (out of eight executives) had been partners previously in international accounting firms.

[Insert Table 1 about here]

Interestingly, each of the Big Four as well as defunct firm Arthur Andersen are represented, thereby indicating a close professional and cultural relationship, at least in theory, between the executive team of CPAB and the accounting establishment. Below the executive level, a slide drawn from a CPAB presentation delivered during a workshop held in May 2007 at the annual meeting of IFIAR in Amsterdam (Appendix I) indicates that the organization's inspection staff is made up mostly of professional accountants – many of them having worked previously in large accounting firms. As observed by a business periodical columnist that we interviewed, basically, CPAB employs professional accountants who previously worked, for a relatively long period of time, in accounting firms with high level of responsibilities. He added that these individuals have been socialized extensively as professional accountants, and they have developed psycho-emotional linkages with the profession. As stressed in the last sentence of the following quote,

the columnist is doubtful as to whether it is reasonable to expect CPAB to adopt a critical philosophy in its regulatory activities:

[About CPAB] I think it's a waste of time – because one auditor is checking another auditor. It's like one executive going in and saying to another executive: "You are paid too much." That executive is then going to come back and examine the other's executive pay and say: "You're being paid too much." They are not going to criticize one another. (Columnist, March 2005)

However, nothing definitive is set regarding the dynamics of power within regulatory spaces. Established networks of power are always subject to destabilization. For instance, they can be destabilized through the occurrence of some event that is widely interpreted in ways that threaten the legitimacy of existing regulatory institutions or through the unpredictable behavior of key economic agents. This is precisely the point illustrated in a report issued by the Fraser Institute in 2006, which restated to a significant extent the criticisms already articulated by the CGAs in 2003:

The independence of the CPAB is [...] called into question by the fact that many members of the CPAB board of directors also fill influential roles in public companies that are themselves subject to public audits. A reasonable argument could be made that these are activities that affect or reasonably create the appearance of affecting the board member's independence or objectivity. Combining the predominance of accounting industry representatives on CPAB with public company executives raises doubt about the rigor that the CPAB will bring to accounting regulation.<sup>4</sup> (Pritchard & Puri, 2006, pp. 2-3)

Perhaps even more noteworthy is the source of the criticism. On the Canadian political scene, the Fraser Institute, whose motto "a free and prosperous world founded on choice, markets, and responsibility" is characteristically neoliberal, represents a highly influential voice within the business community.<sup>5</sup> Its common views and positions favor self-regulation over government intervention. The publication of this report three years after the creation of CPAB is intriguing since, at least on paper, the formal ideological position of the Fraser Institute is

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<sup>4</sup> At the time of writing, CPAB was overseen by two bodies of control: the Council of Governors and the Provincial Audit Regulator Members. The latter vote on by-law amendments, appoint CPAB's financial auditor, and receive CPAB's annual financial statements and financial auditor's report. Provincial Audit Regulator Members include a representative of each of the ten provincial institutes of CAs, and the CGA Associations of British Columbia and Alberta.

<sup>5</sup> The Fraser Institute is a fiscally conservative think tank based in Canada that espouses free-market principles. Its stated mandate is to advocate for freedom and competitive markets. It generally opposes public policy solutions based on government spending, taxes, deficits and regulation. The Institute has attracted well-known individuals to its ranks, such as founding member Friedrich Hayek.

relatively similar to the free-market logic that CPAB's board and top executives tend to endorse. As such, the report brought to the fore a significant gap between the ideal of arm's length monitoring and actual architecture of CPAB. Nonetheless, in spite of the Fraser Institute's strong criticisms, CPAB's structural governance largely favored the interests of the accounting establishment at the time of writing our case study (2008).

### *Representing audit regulation and softening findings*

Recall that our re-conceptualization of Lukes brings to the fore three dimensions of power, which can also be construed as places from which influence can be studied: influence on overt decisions; influence on agenda building; and discursive influence on actors' mindsets. In this subsection, our point of departure relates to the third dimension of power – but the overt conflict and agenda-building dimensions are also mobilized.

Regulatory initiatives do not originate from heaven; instead, discourses play a significant role in the process, through “the formulation and the justification of idealized schemata for representing reality, analyzing it, and rectifying it” (Rose & Miller, 1992, p. 178). Therefore, it is relevant to examine the discursive process by which a new regulatory organization is legitimized, not least how the organization is represented as a solution to issues defined as problems in the regulatory environment. In particular, we study the representations used to justify the existence of CPAB, which its promoters sought to impose in the community as being self-evident. Our analysis indicates that CPAB often (but not always) promoted the preservation of a self-regulated regime of audit regulation, in which its role and interventions were represented and acted upon from a technical perspective, in the service of capital markets and their laissez-faire logic.

The documents retracing the public consultation process initiated in June 2003 on regulatory project 52-108 were particularly useful for our purposes. The following excerpt contextualizes the public appeal for consultation:

Following these corporate failures, the US government enacted the Sarbanes Oxley Act of 2002 and introduced numerous reforms. One of these reforms was the creation of the Public Company Accounting Oversight Board (PCAOB) to oversee the auditing of public companies that are subject to US securities laws. [...] Although the corporate scandals that triggered the threat to market confidence took place in the United States, they have revealed the vulnerability of our markets and the need to strengthen existing requirements in our jurisdictions. In response, several initiatives have been introduced to address the issue of investor confidence and to maintain the

reputation of our capital markets internationally, including the creation of the CPAB.  
(Ontario Securities Commission, 2003)

From the viewpoint of its initiators, the creation of CPAB ensued essentially from the foundation of the PCAOB in the USA and the obvious need to align Canadian regulation with the practices of its powerful neighbor. The implementation of CPAB was not represented as an answer to an unambiguous internal problem within Canadian accountancy, and still less as an answer to problems of legitimacy concerning the profession's historical regulatory authorities. Paradoxically, CPAB was construed mostly as a non issue. The intent was certainly not to disrupt the general philosophy of the regulatory system, but "to strengthen existing requirements in our jurisdictions" (Ontario Securities Commission, 2003). CPAB was also associated with the goal of preserving the reputation of the Canadian financial sphere on the international stage. Sending a strong signal abroad was central to CPAB's initiators. Yet strong signals do not necessarily translate into the field's dominant logics being substantively transformed. Instead, what emerged is a conception of CPAB as a monitoring device whose main functionality is to reassure capital markets about the quality of financial audit work. Substantive reform was not considered as a priority; the impetus was to ensure that status quo in current capitalistic institutions is not threatened by events widely construed as destabilizing scandals.

Adhering to a regulatory perspective predicated on a logic of technicality – overlooking the systemic political and social dimensions of audit regulation while conceiving of the latter as a technical means in the service of the market – is not neutral. Indeed, defining the moral and political ideals upon which regulation is predicated constitutes a political act of power which can impact the nature of subsequent deliberations and institutionalizations taking place in the regulatory space (Malsch, 2010). In our case, CPAB's work has often been constrained to the examination of financial auditing within a regulatory framework of instrumental rationality (Schön, 1983), whereby efforts are made continually to adjust technical means to unambiguous, stable and unquestionable ends. Thus, instrumental regulation implies the technical monitoring of audit practice through reliance on prevailing standards of practice, that are assumed to be logical, efficient and effective. In so doing, ends are protected from fundamental doubt; technically-oriented regulation is at the service of the forces and interests which today dominate the status quo, that is to say economic laissez-faire. To make our point clearer: technical regulators view the

problems of audit practice from a narrow perspective, not being able to conceive them as indicative of broader, systemic deficiencies.<sup>6</sup>

Interestingly, in spite of the desire to follow the American example, CPAB's structure is significantly different from that of the PCAOB. The PCAOB is required to make an annual report of its activities to the Securities and Exchange Commission (SEC) and to Congress (Sarbanes-Oxley Act, § 101). Although the PCAOB is not accountable directly to Congress, the SEC is. In contrast, CPAB is monitored internally by a Council of Governors and is not subject to direct legislative oversight. Although four out of the five members of the Council of Governors are top executives from regulatory organizations (e.g., head of the Office of the Superintendent of Financial Institutions of Canada; chairperson of the Ontario Securities Commission), the lines of accountability in relation to legislative oversight are blurrier than those surrounding the PCAOB, thereby suggesting a distinct political inclination.

Regulatory discourses also have what Rose and Miller (1992, p. 179) call an "epistemological character"; they are articulated in relation to some conception regarding the nature of regulation. In our case, it should be emphasized that CPAB's spokespersons sought regularly to promote a market-based regulatory environment. Be it in presentations delivered to members of the accounting profession or the business community, the regulation of the accounting profession has been considered generally as a mechanism in the service of a much wider machinery constituting the country's financial system – which fundamentally does not need to be overhauled, although some tinkering may be warranted from time to time. This epistemological stance is particularly apparent in the following extract drawn from a speech by Gordon Thiessen, the first chairperson of CPAB's board of directors and former governor of the Bank of Canada, before the International Federation of Accountants (IFAC)'s ethical committee:

Good audits are a form of public good, to use the language of economists. Audits are a public good in that they provide benefits to the operation of financial markets in general and not just to the board of directors and the shareholders of the company being audited. [...] The more we all act ethically and demand that others do the same, the better our economies and financial markets will function. (Thiessen, 2005)

Delivered in 2005, Thiessen's speech addressed the regulation of financial auditing in a way that is particularly reminiscent of the basic philosophy that sustained the original proponents of CPAB surrounding its creation in 2003. Financial auditing is defined as a public good, yet its

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<sup>6</sup> We thank one of the reviewers for having made us aware of this point.

ends remain subordinated ultimately to the improvement of market efficiency. The public good is thus construed as an economic good, whose strengthening necessarily benefits everyone in society.

Not only is the discourse of technicality promoted at the front-stage level, for instance in blurring lines of accountability and in presenting financial auditing as a terrain naturally amenable to free market, but its language is also reflected in the practices of the regulatory organization, not least regarding its inspections and how they are represented in the public arena. As detailed below, our analysis indicates that CPAB's reports tend to be characterized by the disclosure of shadowy or vague findings and by interpretations that are significantly reflective of a technically-inclined regulatory logic. Over time, this discourse can shape "the values, beliefs and opinions of less powerful groups, effectively determining not only whether certain demands come to be expressed and needed but also whether such demands will ever cross people's minds" (Gordon, Kornberger and Clegg, 2009, p. 17). In other words, vague and technically-oriented discourse can influence what is considered to be legitimate while preventing crucial issues that may question this legitimacy from emerging for public debate.

To exemplify this, we turn our attention to CPAB's disclosure policy in analyzing the following excerpt, drawn from a speech delivered by Thiessen's successor, in which he justifies the lack of transparency in CPAB's reports, before the members of the Toronto Economic Club:

Many ask me why the results of our individual inspections of audit firms are not public, just aggregate results. [...] You can have full disclosure or you can have effectiveness, but you can't have both. What do I mean? Well our counterpart in the US issues a public report on each firm [...]. I gather that, in part because of negotiating the language of the public part, and a lot of vetting by legal departments, their reports take materially longer to issue than CPAB's. So I will be very loath to change this model fundamentally in the short term. (Le Pan, 2008, p.5)

Unlike its American counterpart, the Canadian regulator does not publish reports that detail the results of the inspections at the firm level. In trying to justify this policy, the chairperson of CPAB claims that total transparency implies the fear of legal implications delaying publication and the implementation of recommendations within accounting firms. Reflecting the logic of a technician who wants to make sure that the technology can deliver on time the expected output, speed in delivering inspection services is privileged over the production of detailed narratives – which are necessarily more informative but more controversial socially or politically.

Several consequences ensue from the discursive influence of the logic of technicality. In particular, through the publication of relatively vague and general reports often centered on technical problems, critical questions about the ends of auditing are prevented from entering the field of visibility. For instance, while serious concerns regarding the impact of partner compensation practices upon auditor professionalism have been regularly expressed in auditing literature in the last two decades (Covaleski, Dirsmith, Heian, & Samuel, 1998; Hanlon, 1994; Humphrey & Moizer, 1990; Sikka & Willmott, 1995, 1997; Wyatt, 2004), CPAB's public reports tend to superficially discuss compensation practices, in reassuring ways that suggest that the issue is now under control in the largest firms<sup>7</sup>:

Generally, the larger firms have articulated strategic priorities that include an emphasis on audit quality. This was reinforced by the focus group findings in 2004, which showed that participants consistently ranked audit quality higher than other priorities as a determinant of their compensation and advancement in the firm. The leaders of the larger firms, in their internal communications to partners and staff, are increasingly emphasizing the need to make an uncompromising effort to do the highest quality work on every engagement. (CPAB, 2005, p. 8)

Methodologically speaking, how does CPAB support its enthusiastic interpretation? Through a reading of the firms' strategic priorities, as well as focus groups conducted in each of the firms. We can assume that each focus group involved a number of participants, either from the same hierarchical level or split hierarchically, being asked to collectively assess the impact of certain attributes (such as audit quality, selling new services) on remuneration and promotion. The decision to rely on the focus group methodology can be questioned in light of people's tendencies to align with socially acceptable norms when surrounded by their peers (Feldman, 2003), and in light of the evidence that people tend not to be very good at disregarding their self-interest (Moore, Tetlock, Tanlu, & Bazerman, 2006). In this respect, it is useful to note that the focus groups probably took place in 2004, a relatively short time (i.e., about two years) after the collapse of Arthur Andersen, when the Big Four were stressing formal discourses of audit quality in order to defend their legitimacy. It would have been surprising to see focus group participants

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<sup>7</sup> However, it needs to be recognized that CPAB points out that the compensation issue is less under control in smaller accounting firms. For instance: "Performance evaluations continue to be an area where CPAB would like the majority of regional and local firms to improve and build more rigour into the process. In particular, CPAB would have expected audit quality to play a larger role in the partner and staff performance assessment process and in decisions regarding compensation and promotion. This criterion was often absent." (CPAB, 2007, p. 21) Nonetheless, our analysis of the same report indicates that the matter is discussed quite superficially therein, as if the linkages between the specific concern and the overall risk of systemic failure had not been thoroughly considered.

expressing publicly discordant viewpoints in a significant way. In brief, this mode of investigation is unlikely to challenge the deeper social, political or psychological foundations of compensation practices.

Contrasting with the relative inattentiveness devoted to social, political or psychological issues, detailed narratives about technical deficiencies are found often in CPAB's reports. For instance, in the following excerpt, we learn that accounting firms operate electronic investment monitoring systems into which partners and professional staff are required to record their personal investments and transactions. Basically, these systems compare individuals' investments against a firm's master list of audit client securities that are ineligible investments. The mechanics underlying investment monitoring constitute a zone of comfort where CPAB can confidently deploy its expertise:

Pursuant to SEC requirements, the four largest firms must undertake internal audits of their investment holdings of partners and managerial employees to ensure that the portfolios entered by individuals into their independence monitoring systems are accurate and complete, and do not include prohibited client securities. [...] The audits to date have identified a number of exceptions, which usually involved the failure of individuals to input some of their investments into the investment monitoring system. However, each firm also found a few cases where the non-reported investments were securities on the firm's prohibited investment list. There is no evidence in any firm of improper motivation in holding or failing to report holdings of client securities and, although numerous, each individual exception was clearly of an insignificant nature. (CPAB, 2007, p. 11)

As indicated in the quote, failures in reporting some investments are considered as relatively minor and insignificant incidents. The rhetorical strategy is de-dramatization. Yet, it can be argued that those several "exceptions" mentioned in the regulator's report are not insignificant in nature; unethical behaviors often begin as minor questionable calls which later escalate into violations of ethical standards (Moore et al., 2006). Nonetheless, the key point that we want to stress is that focusing on mechanics that aim to control relatively superficial aspects of auditor independence is far removed from investigating more substantive issues, such as the extent to which the fear of losing audit fees actually impacts auditors' decision-making.

The illustrations provided above regarding focus groups and breaches in reporting investments are consistent with CPAB constraining (perhaps unconsciously), to some extent, the scope of its investigations to means and technicalities instead of questioning ends and investigating more substantive issues. This suggests that CPAB's executives and staff might be

affected by a sort of discursive myopia vis-à-vis the profession that they are required to monitor and evaluate, blurring what would otherwise be conceived of as controversial and substantial issues.

In addition to discursive influence, our analysis also indicates a deliberate strategy to keep negatives out of the public sphere – or at least to downplay their significance. A significant trend in the public reports consists of interpreting findings in very general terms, as if the objective is to give public opinion and legislators the impression that audit regulators perform effective investigations, while more critical issues are downplayed or left out of the reports. During our investigation, we learned that a number of deficiencies, as revealed through CPAB’s inspections, are not specified in CPAB’s public reports in order to prevent the legitimacy of accounting firms from being questioned in the press and in the eyes of the public. This preventive strategy is explicitly inscribed in CPAB’s formal rules:

A draft or final Inspection report is intended as a private communication from the Board to the participating audit firm. [...] If the participating audit firm has not addressed the weaknesses, deficiencies or recommendations to the satisfaction of the Board, [...] the Board may make public on its website the relevant portion or portions of the final Inspection report that deal with such weaknesses, deficiencies or recommendations and the fact that they have not been addressed to the Board’s satisfaction. (CPAB, 2006, rules 413-416)

CPAB’s public reports will therefore be very general, and explicitly refrain from incorporating information which criticizes specific accounting firms:

In its reports, the Board will use its best efforts not to publish information that would enable the identification of the firm or firms with respect to which such weaknesses were found or recommendations relate. (CPAB, 2006, rule 419)

In so doing, the public reports fall within the umbrella of Barthes’ denunciation of the rhetoric of social immunization: “One immunizes the contents of the collective imagination by means of a small inoculation of acknowledged evil; one thus protects it against the risk of a generalized subversion” (Barthes, 1972, p. 150):

[The audit regulator] finished its work on the reports on the four major firms and there was a highly sterilized version of that report that was published or made public on the website and so on. [...] But the firms are taking it very seriously. There is a lot of onus on them to do so, because if they don’t, [their private] report is made public in six months. So in their business, that’s very critical. I mean, [reputation] is what killed Arthur Andersen. [...] The firms know that they must come out of there with a good report card. (Board member of CPAB)

The rationale underlying sterilization is the belief that the firms will be more inclined to make substantive changes if CPAB is not perceived as an antagonist, but as a constructive agency:

Headed by chairman Gordon Thiessen, the board also found several cases of conflict of interest and lax accounting standards at three of the 46 audits that were checked. [...] Thiessen declined to name the offending auditing firms, saying he can accomplish more by dealing in private. (*The Bottom Line*, 2004a, p. 1)

Yet it was also indicated to us that being specific on negatives would not be fair fundamentally to the firms because, by and large, the quality of their work is quite good:

David Scott, CPAB's chief executive officer, said many of the problems he found were minor, the result of work that was done in haste and without full documentation. He said auditors did not always complete the required paperwork, and sometimes took short cuts. "We felt the auditors did not do enough work to reach the conclusions they did" Scott said. "The auditors should have done more work". But he added: "I don't want to leave the impression that there is negligent or sloppy work. CAs work under significant time pressure. They don't always dot the I's or cross the T's". (*The Bottom Line*, 2004a, p. 2)

Consistent with a dominant theme in political science literature (Baron, 1988), CPAB appears to be more concerned with harms that it can create through offensive public reports, than those it creates through the release of superficial information. Audit regulators, like all forms of organizations, are politically inclined towards the promotion of some interests and the suppression of others (Gordon et al., 2009). Arguably the construction of superficialities in CPAB's public reports benefits primarily public accountants as the reports prevent grievances from being voiced in the public arena. The process is, therefore, consistent with the second level of power as described by Bachrach and Baratz (1962) in that certain actors within the regulatory organization, who nonetheless are somehow attached to the accounting profession, play a role in creating or reinforcing barriers to the public airing of policy conflicts. Interestingly, discursive and agenda-setting forces, although obeying distinct logics of power, operate simultaneously in attempting to preserve the influence of the logic of self-regulation. The former force conceives of audit regulation from a technical angle that aims to legitimize free-market principles and low transparency in disclosure policies. The latter secures the profession's interests in confining deliberately the scope of public scrutiny to relatively safe general issues.

Further, even when CPAB discloses what can be construed as disturbing findings, the ways in which the findings are presented tend to tone down the matter, especially when the disclosures relate to the largest accounting firms. CPAB reports do not highlight safe and technical issues exclusively. The reports need to be somewhat critical, otherwise the work of CPAB would possibly not be taken seriously, thereby preventing the regulator from establishing its legitimacy. In particular, sanctions are applied on a number of deviant firms; for instance, in 2007 seven firms were required not to accept any new clients (reporting issuers), and three firms had to have all their audit reports reviewed by an external firm before issuance (CPAB, 2008a). Yet the identity of these firms, as well as the specific deficiency at the origin of the sanction, are not specified. Also, a public presentation given in 2008 by CPAB's CEO, which summarizes the findings of the annual inspections from 2004 to 2007, shows an increase, over time, in the number of deficiencies within the six largest audit firms (see Table 2). For instance, the percentage of auditing and accounting deficiencies detected in inspected files increases respectively from 5.9% and 1.5% in 2004 to 8.5% and 3.8% in 2007. However, an interpretive slide specifies the following explicitly regarding these results:

- “Is the situation worsening? Probably not, in four years of reviews CPAB:
- Now uses more functional specialists
  - Is selecting higher risk files
  - Is probably becoming more stringent
  - Is spending more time on its file reviews.
- Also GAAP itself is becoming more complex.” (CPAB, 2008b, slide #31)

[Insert Table 2 about here]

Whether or not these reasons are well-founded does not matter for the sake of our argument; what does matter is that they justify a trend which otherwise would probably be embarrassing for the firms. Moreover, just after presenting the findings regarding the six largest firms, the slide show puts on view the findings pertaining to smaller firms. As shown in Table 2, the proportion of deficiencies is significantly higher than in the larger firms, providing a relative sense of comfort regarding the audits carried out in the larger firms. Through representations conveyed in public, an instrument of public action such as CPAB influences the construction of hierarchies among the firms it oversees. In this context, the massive gap between national and non-national audit firms does not provide merely a reassuring sense of comfort regarding the quality of the work achieved in the largest firms. It might also reinforce the concentration of the

audit market in the hands of the biggest players and marginalize further the involvement of medium-sized accounting firms. That being said, the main point ensuing from our analysis of CPAB's slide show is that findings, which could have been construed as problems, are framed instead in a way that does not clearly problematize them. Again, the reporting practices of CPAB tend to avoid the presentation of unpalatable findings, especially when the interests of the largest accounting firms are at stake. Another indication of CPAB reports' quite uncritical stance is the lack of angry reaction from inspected firms. In the words of a journalist commenting on how accounting firms receive the public reports, "there was barely a ripple from this [accounting] industry" (*The Bottom Line*, 2004b, p. 2).

In short, our analysis brings to the fore significant patterns of resistance vis-à-vis the possibility of strengthening, through the establishment of an independent regulatory organization, the profession's accountability to outsiders. Research indicates that, in general, professional accountants are reluctant to the idea of outside regulation, even when being asked on the matter shortly after the collapse of Arthur Andersen (Gendron & Spira, 2009). However, finding that patterns of resistance towards outside regulation are significantly influential within the confines of the new regulatory organization constitutes, at the very least, a controversial result. These patterns are conveyed especially through a discourse that represents CPAB and its role in a particular way, as a monitoring device that seeks to ensure that accounting firms' audit machineries deliver services in a smooth manner and in ways which benefit capital markets, without being overly concerned about the commercial and political ends which underlie the growing deployment of auditing in society (Malsch, 2010; Suddaby et al., 2007).

One caveat is important to stress at this point. CPAB's actions should not be interpreted as having been planned thoroughly to ensure that it becomes a relatively safe harbour for protecting the interests of public accounting firms. The influence of discourses is often subtle, and the individuals working in CPAB may, indeed, have believed that they were acting appropriately and diligently in their day-to-day undertakings. However, when we look at the broader nature of CPAB's formal discourses, structures and practices, we see the organization's work from a more critical angle.

All in all, it appears that the emergence and consolidation of CPAB did not translate into the network of power within accountancy's regulatory space being radically changed. According to our analysis, the logic of self-regulation influences the new regulatory organization

significantly, in spite of the efforts of a number of non-accounting organizations to constrain the influence of the accounting establishment and its key allies (not least the CSA network – Richardson, 2009) in reshaping regulation in accordance with their interests. Of course, the creation of CPAB in the Canadian space modified, to some extent, the structure of power; it would be naïve to maintain that the accounting establishment benefits today from the same room to manoeuvre as before the foundation of CPAB. For instance, the logic of arm’s length regulation is influential when certain concerns are expressed in public reports: “CPAB notes that it is not reporting significant overall improvements in audit quality in respect of the firms that it reviewed in the last quarter of 2006 and calendar 2007” (CPAB, 2008a, p. i). However, a few lines below, in a section of the same report devoted to the analysis of deficiencies found in the largest accounting firms, one can read the following (p. ii): “Each firm has made progress since CPAB commenced its quality inspections and substantially all of the recommendations made to the firms following those inspections have been implemented”. Do these two contradictory statements reflect differences of opinion within the group of people who collaborated to the production of the document? Further, another excerpt is consistent with smaller accounting firms being stigmatized while the tone of criticism is softer regarding the largest firms:

Although these concerns apply to both large and small firms, in the larger firms it is usually the case that the controls in a firm’s system have not been applied as designed whereas in the smaller firms, many of which do only audits of relatively small reporting issuers, there is often an absence of the control systems themselves. (p. ii)

While the logic of arm’s length regulation is present to some extent in CPAB’s reports, it often seems to be subordinated to the logic of self-regulation, especially when the points being discussed relate to the largest firms. Our findings reflect a regulatory organization characterized with an identity under tension: although being formally accountable to the public, the regulator is influenced partially in practice by a private circuit of power. It is probably no exaggeration to posit that today’s discursive environment within CPAB is not in accordance with the power relationship that was supposed to develop from overseer to overseen.

### **Extending boundaries: Constructing transnational resistance**

Globalization raises challenging issues for the regulation of business and professions (Arnold & Sikka, 2001). In the domain of accounting, for instance, transnational accounting firms operate globally and rely increasingly on international standards in carrying out their

activities. However, the mechanisms by which the firms are (legally and ethically) accountable are found mostly at the national level. Nonetheless, Humphrey et al. (2009) as well as Suddaby et al. (2007) point out that, increasingly, embryos of transnational regulatory structures (e.g., IFIAR) are present in the accounting scenery. From a global perspective, then, accountancy's regulatory space involves a complex constellation of actors and relationships mixing accounting firms, governments and regulatory organizations, constituted nationally and trans-nationally. Since uncertainty is one of the hallmarks of the territories of regulation – and “a powerful force that encourages imitation” (DiMaggio & Powell, 1983, p. 151) – typically regulators find it reassuring to compare and discuss their work altogether, in an effort to ensure that their local practices and structures are in accordance with the “norm” or, when regulators deviate from the norm, trying to innovate and develop new knowledge and practices, that their undertakings are reasonable in the eyes of their peers (Frumkin & Galaskiewicz, 2004). The machineries of knowledge (Knorr Cetina, 1999), which underlie regulators' work, do not operate carefully planned experiments producing context-free results, which are then disseminated in a unidirectional way, from global to local. What is called local is to some degree constructed on a transnational basis and what is called global is often, and perhaps always, mediated through local sites of experience (Robertson, 1995). The important point to remember for the sake of our argument is that, in a world perceived increasingly as globalizing, national regulators are likely to engage regularly with one another in extensive discussions on the matter of their local and global experiences. Empirical support can be invoked easily, for instance through the establishment of IFIAR, which formally aims to share knowledge and promote collaboration in regulatory activity. On the one hand, such transnational formal structures constitute mechanisms by which power can operate on a global basis. On the other hand, influence can be exerted from one national or regional regulatory body to the next.

As a member of IFIAR, CPAB is exposed to globalized channels of communication while being able to exert influence through these channels. For instance, it can promote specific representations of regulation (recall the presentation made during a workshop held in May 2007 at the annual meeting of IFIAR in Amsterdam, in which CPAB describes its recruitment policy targeted towards former partners). It can, therefore, be argued that the patterns of influence which we documented above in the CPAB case are likely to be tied, to some extent, to developments in other regulatory organizations and spaces.

In this section we examine the extent to which indications of the patterns of influence that we documented in our analysis of the Canadian case are found in other jurisdictions. In so doing, we seek to extend the boundaries of our thesis, in that resistance against the logic of arm's length regulation is not circumscribed to one particular territory. While the extent of empirical evidence that we mobilize is not as extensive as in the previous section, our analysis nonetheless brings to the fore certain patterns of influence, as well as certain aspects of the ways in which power operates across regulatory organizations.

### *Commonalities at the level of discourse*

Similar discourses permeate audit regulatory sites in presenting financial auditing as a terrain naturally amenable to free market, whose smooth functioning requires only a moderate or minimal level of regulation. Like Canadian securities authorities, the European Commission, which carries the primary responsibility in European Union (EU) for developing new auditing legislation and framing regulatory agendas (Humphrey, Kokkali, & Samsonova, 2010), seems to be genuinely concerned with the threat that scandals, such as Enron et al., pose to the maintenance of its "efficient and competitive" capital markets. Financial auditing regulation is constructed as a monitoring device, ultimately subordinated to the improvement of market efficiency, while egalitarian-based issues such as citizens' rights and public interest are downplayed:

Auditors are our major line of defence against crooks who want to cook the books. Parmalat was a reminder of what happens when that defence fails. Faith in financial reporting and in the markets is destroyed. Unless it is swiftly restored, investment, jobs and growth will be lost. [...] What we are proposing [i.e., common criteria for public oversight systems] would inject more rigour and a stronger dose of ethics into the audit process, bolstering that defence on which all market economies rely. (European Commission, 2004)

Moreover, not only is the logic of technicality influential at the front-stage level in justifying the establishment of new regulatory structures, but its language is also influential within European regulatory networks in presenting inspections and findings as a terrain amenable to low transparency. In the following quote, a top executive from one of the European regulators invokes reasons similar to those mentioned by his Canadian counterpart in justifying a restricted disclosure policy. Speed in detecting problems and implementing solutions is favored over detailed public narratives whose production allegedly engenders serious legal issues:

If I would go to an audit firm and they would know that in all cases there would be a public report on all my activities at that audit firm, I see the big risk that it starts to be a very legal affair, where each element of information, before it's transferred to the auditing oversight body, there is going to be a lawyer involved saying: "Whoa, whoa, should we give that information or shouldn't we give that information?" So I'm very concerned that if we would have a system where each inspection is publicly reported, or would in summarized form end up in a public report of an individual audit firm, is that it will fundamentally change the role between the inspector and the audit firm. (Executive from audit regulator B)

When looking at the substance of public reports a number of similarities between EU jurisdictions and Canada also emerge. For example, until 2007 the Audit Inspection Unit (AIU) in the UK provided, in its public reports, general information about audit deficiencies and quality control weaknesses – without disclosing the identity of the specific accounting firms found not to be compliant with audit and accounting standards. A relevant illustration is provided in the 2007 public report, where the AIU discusses superficially the issue of partner compensation practices. The following excerpt exemplifies the integral section of the report devoted to the firms' human resource policies:

We have invested considerable effort in reviewing the firms' partner and staff appraisal processes and in particular how audit quality indicators have been incorporated into the processes. Last year we made a number of recommendations in this area and it is pleasing to see the significant progress made. Some firms have given priority to revising their partner appraisal processes, with staff processes yet to be reviewed. Others have changed their processes but it is too early to assess the effectiveness of the changes due to the timing of our inspection visit not coinciding with the appraisal cycle. However we observed that the timeliness of the completion and approval of appraisal documentation and other procedures for both partners and staff continued to be a problem at a number of firms. (AIU, 2007, p. 10)

This excerpt is remarkable in the high degree of non-information that it provides on the issue of human resource policies. Does it imply that the firms' compensation practices in the UK are now designed in ways which are unlikely to jeopardize auditor professionalism? The AIU, however, modified significantly its disclosure policy from 2008, when it started reporting publicly on every firm it inspects. As seen in the following excerpt from the 2009 report on PwC, more detail is provided and the tone is more critical:

One element of the staff bonus scheme relates to the relevant business unit's performance against certain Key Performance Indicators (KPIs). We note that the basis of this has changed for 2009 to give a 40% weighting to financial growth as part of the KPI element, double the 20% weighting given to the other KPIs, including

audit quality. This represents a change from an equal weighting of 25% for each KPI last year and emphasises the importance of financial growth to the firm. We consider that the underlying message that this change gives represents a potential risk to audit quality in the future. (AIU, 2009, p. 10)

Interestingly, the AIU had commented the previous year about PwC's compensation policy, and a conversation between the two organizations developed on the matter in the press and beyond:<sup>8</sup>

The firm [PwC] must demonstrate "more clearly" the extent to which remuneration is based on considerations of audit quality, the AIU added. PwC's response said that the AIU's report supported the reliability of its audit opinions, but was concerned that its length and its tone made it difficult for readers to understand the "overall positive conclusion". It disagreed with the AIU's comments on the remuneration of key audit partners. (AccountancyAge, 2008)

Given that the matter of compensation policy is still problematized in the 2009 report, it appears that PwC decided to engage in a trial of strength with the AIU. Overall, these recent developments pertaining to the dynamics of power surrounding the AIU indicate confrontation in the overt decision-making arena between regulator and regulatee. The logic of arm's length regulation seems to be relatively influential within the AIU, at least since it modified its disclosure policy. This does not invalidate our argument, however, since our interest is in studying patterns of power and resistance – not in demonstrating the untenable position that either one of the two logics is totally absent from the regulatory space. Moreover, it is useful to stress that, to our knowledge, the AIU, through its most recent public reports where the logic of arm's length regulation is more palpable, stands in a particular category as regulator. Typically the other European regulators are not as critical in their reports. For instance, H3C in France continues to issue very general reports which do not identify firms (Hazgui, Manita, & Pochet, 2010). Further, H3C reports do not discuss thoroughly the issue of partner compensation. On the contrary, H3C even celebrates the quality of internal control within large accounting firms – a huge contrast from the concerns that qualitative research has brought to the fore on the matter (Gendron & Spira, 2009; McNair, 1991; Sweeney & Pierce, 2004):

From all the inspections which were carried out, positive points emerge regarding the firms' commitment in establishing procedures to strengthen audit quality.

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<sup>8</sup> For instance, references to the PwC/AIU clash over remuneration were made during the Treasury Select Committee's investigations of the banking crisis in January 2009.

Commitment was found through the formalization of procedures and rules, and through the direct involvement of the auditors involved. Highly complex and detailed in the largest firms, and quite comprehensive in mid-tier firms, procedures and rules have even been found within firms where the proportion of auditing services is not preponderant. (H3C, 2008, p. 47 – our translation)

In sum, we found a number of commonalities across the discursive schemes used to make sense of and represent audit regulation and its need in Canada and Europe. From these commonalities emerges a sense that patterns of resistance to the logic of arm's length regulation are influential across a number of jurisdictions. Of course, the degree of influence varies in time and space – as we saw with regard to the AIU.

#### *Commonalities at the level of resistance*

Confrontations which are best appreciated in terms of the first level of power are also present in European jurisdictions. We were provided with an internal report developed by a strategic committee of the national office of one of the Big Four firms, in which a number of actions to reduce the power of independent regulatory organizations are explicitly considered. Overall, the document adopts a very negative tone against audit regulators – “The road to hell is paved with good intentions”, reflecting the firm's intention to promote its own interests in trying to attenuate the range of sanctions that regulators can impose:

The brutality of some sanctions that can be imposed by regulators is a concern to accounting firms. Being suspended from auditing public companies implies the death of the firm. Regulators know this and they are worried at the risk of another large accounting firm collapsing, especially since it is almost impossible for a medium firm to develop as a Big firm – the barriers to entry are insurmountable. [...] In order to reduce the threat of a Big Four firm collapsing, it is highly appropriate that regulators replace the suspension scenario with one which is predicated on financial penalties.

The message is clear. The accounting firm seeks to provide its partners with some knowledge of regulators' basic concerns and fears in the hope that this knowledge will pay off eventually in convincing inspectors to be flexible in their approach to penalize deviations from audit standards. Resistance can therefore occur behind the scene, when the regulator and the inspected parties discuss the results of inspections. Resistance from the overseen is also sustained by derogatory attitudes that a number of public accountants manifest towards the claims for expertise as advanced by regulators and their inspection staff. For instance, in the following

quote, the audit partner expresses a strong sense of disrespect for audit inspectors on the basis that they are former auditors who never made it to partner status:

[The board of regulator B] is mostly made up of public servants who basically do not have any linkages with accounting and finance culture. Listening to them is pitiful. They will say anything! In addition, [regulator B] recently created a body of inspectors made up exclusively of former managers from audit firms. Most of these inspectors are incapable and embittered people who failed in their career path in being promoted to the partner level. Their only obsession is to castigate their previous employers. The regulator gives huge responsibilities to people who never signed any official report when they were in public practice. (Big Four executive partner, July 2008)

Resistance from the profession is also palpable in the following quotes drawn from interviews conducted with executives of two national regulators based in the EU. As such, the quotes are consistent with our claim that the logic of arm's length regulation constitutes a very sensitive issue for a profession bounded historically to the logic of self-regulation:

Difficulties should be expected when someone abruptly says to a self-regulated profession that the self-regulation regime is done. Accountants have had to go through a difficult psychological mourning. A number of accountants still try to fight behind the scene. [...] Accountants tend to be critical of [audit regulator A], but it needs to be stressed that even today, one of the Big Four still has an information system which is unable to identify situations of conflicts of interests when the firm is involved both as consultant and auditor. (Executive from audit regulator A)

As oversight body, we have been very strong pushing towards a system where we would do the work, we would have full time inspectors. [...] In the beginning the audit profession was not willing to accept that position. They said we can do much more, we have the knowledge, we have the expertise so clearly the profession was pushing for a model where they would still do more kind of the monitored peer review and there has been a struggle between the profession and the oversight body on what the roles were. (Executive from audit regulator B)

The first quote above is noteworthy for the feeling of pity (which the interviewee manifests towards public accounting firms) that constitutes another manifestation of power in accordance with the firms' interests. The second quote indicates resistance from the profession towards arm's length inspections; although ultimately, the profession's viewpoint did not prevail. Interestingly, our analysis also indicates that the creation of regulatory organizations in the EU is more the outcome of fear than of a genuine willingness to institute a mechanism aimed at protecting the public interest. Threats that US authorities would not recognize the quality of audits carried out in

Europe reportedly played a key role in the decision to institute independent regulatory offices in EU countries:

I do not accept the imposition of US standards on our firms and that is why the European Union strongly opposes registration of EU audit firms with the United States' Public Company Accounting Oversight Board. The EU will regulate its own businesses. (Bolkenstein<sup>9</sup>, 2003, p. 1)

When we started the oversight in Europe, one of the main objectives was [...] to set up oversight in a way that the US oversight body won't visit Europe. That means you have something at least as heavy and as serious as the PCAOB. So yes that's something that was on the agenda here and I know that of course when they prepared EU directive, they also looked into PCAOB regulation. (Partner of a Big Four)

The rise of independent audit regulators takes place in a field of power and international relations extending well beyond forces and pressures deriving from single regulatory spaces. As suggested by Suddaby et al. (2007, p. 357): "Professional regulation, at the transnational level, is now a negotiated product from an increasingly broad and heterogeneous network of actors". The EU's historical foreign policy to position as an alternative and credible opposition force to US regulatory ambitions was reportedly significant in the introduction and design of European independent regulators. The creation of IFIAR was also perceived as a threat against the development of a unified European regulatory space:

One [Member State] delegation questioned about the value added of the new forum [IFIAR]. [...] The delegation expressed the view that Europe will have less influence, that Member States will become divided working independently at international level. The priority is to work at EU level and perhaps later at the international level. It was underlined that Member States have to give priority to implement the 8th Directive. Another delegation proposed to be cautious but expressed the view that the advantage of a Forum is that it is not binding. (Summary Record, Second Meeting of the AuRC, March 2006, p. 4)<sup>10</sup>

The following excerpt, from the European Commissioner for internal markets and services, provides a sense that US Big Four firms can exploit the setting of US/EU rivalry to play their own partition, claiming deontological issues to obstruct the implementation of transnational inspections:

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<sup>9</sup> Frederik Bolkenstein, European Commissioner in charge of the domestic market from 1999 to 2004.

<sup>10</sup> The AuRC is composed of representatives from Member State governments (no participation of profession is allowed). Its main task is to decide and guide the European Commission on audit policy issues.

I would like US firms to contribute constructively to the issue of access to audit working papers and inspection reports. We cannot continue to merely push the issue back to rules about professional secrecy and legal privilege and leave all this to the lawyers. [...] I call on the CEOs to actively support regulators to find a solution and not just to present legal arguments. (McCreevy, 2008)

Patterns of resistance to arm's length regulation are also found in the minutes of the meetings of the EGAOB between 2005 and 2009.<sup>11</sup> For instance, in June 2007, the EGAOB invited the European Associations of the accounting profession to discuss a proposal to update the 2006 European Directive on Statutory Audits. Although by 2006 some members of the EU already had voluntarily established independent oversight bodies (e.g., Germany and the UK), the 2006 Directive required the establishment in Member States of independent audit regulators to supervise the application of government regulations and professional standards. The update proposal developed in the context in which US, Japanese and Canadian authorities were in the process of examining the recognition of the EU oversight bodies (European Commission, 2008). It seems that concerns had been expressed regarding significant differences that the 2006 Directive allowed to Member States in setting up their own regulatory inspection processes.

The minutes of the meeting expose a major disagreement between the Fédération des Experts Comptables Européens (FEE) – once described by Hopwood (1994, p. 246) as being “possibly the most active and influential audit industry lobby organization in the world” – and the EGAOB. Contrary to the position of the EGAOB, the FEE supported a system of delegated inspections in which inspections can be carried out by professional bodies and practicing auditors – not necessarily by staff employed formally by regulatory oversight bodies. The minutes of the meeting describe the controversy as follows (EGAOB Meeting, Summary Record, June 2007, p. 2):

The most controversial point discussed with EGAOB participants appeared to be the possibilities of involving professional bodies and practicing auditors in the conduct of inspections. It was argued by the Associations that while the consistency in the inspection systems is desirable one should bear in mind that a “one size fits all approach” is not likely to be possible in all Member States. FEE supported a system of delegated inspections as equivalent to a system of inspections.

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<sup>11</sup> EGAOB was established in December 2005 and is composed of high level representatives from the entities in charge of the public oversight of statutory auditors in Member States. The first aim of the Group is to ensure the effective coordination of public oversight systems within EU. It also provides technical input to the Commission on implementing measures (Humphrey & Moizer, 2008).

The position of the FEE reiterates an argument articulated initially in a 2004 press release entitled “Europe’s accountants ask commission, council of ministers and parliament to address weaknesses in proposed EU audit directive” (FEE, 2004), in which the Fédération heavily criticized the decision of the European Commission to set aside the profession from European regulatory bodies. The intensity of the polemic is palpable in the following extract:

The Commission wishes to exclude the audit profession from national oversight systems. FEE believes that a separate oversight for listed companies will introduce a false dichotomy, without any evidence that this could improve oversight results or enhance the credibility of the mechanism.

The updated version, adopted officially in 2008, reflects partially the views expressed by the FEE. Although the European Commission “recommends an active role of the public oversight authorities in inspections” and “invites Member States to clarify that practitioners from audit firms (peers) should no longer have a leading role in inspections system and inspections teams”, “Professional associations can still assist the public oversight authorities, but should be subject to important safeguards, including accountability to the public oversight authority” (European Commission, 2008). In practice, a system of delegated inspection is thus still possible.

Nonetheless, the logic of arm’s length regulation sometimes prevails in official deliberative arenas. In this regard, the following minutes of another EGAOB meeting show clear opposition from the European body to adopting a scheme elaborated on by the European Contact Group (ECG<sup>12</sup>), on the basis of the overly conciliatory position of the latter towards the profession:

**EGAOB members** pointed out that the model suggested by the ECG only entailed limited sanctions and that this is neither viable nor convincing. Systematic non-compliance must be sanctioned. It is also in the interest of the firms. If sanctions are not imposed there would not be a level playing field among firms. [...] The Chairman thanked [participants] for the contributions and he concluded that the EGAOB could **not** support the paper on quality assurance developed by the ECG. (EGAOB Meeting, July 2006, Summary Record, p. 6)

Overall, our transnational examination of the dynamics of power underlying the establishment of independent regulatory bodies indicates that regulatory spaces are permeated with conflicts opposing the logic of self-regulation to that of arm’s length regulation. Through these conflicts the interplay between processes of power and resistance develops in many ways –

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<sup>12</sup> ECG is a lobbying group, European in focus, which represents the interests of the Big Four accounting firms and the two largest mid-tier firms.

sometimes overtly in deliberative arenas, sometimes subtly through common discourse being shared across participants of different organizations. In particular, our analysis substantiates the point that the creation of a network of independent oversight bodies did not translate into the disappearance of self-regulatory forces. Patterns of resistance were found across a variety of contexts – yet to varying degrees. Regulatory spaces, including the nature of the relationship between regulator and regulatee and the social roles that these actors adopt in façade and action, are characterized deeply by the tension between arm’s length regulation and self-regulation.

Drawing on our analysis, it can be argued that regulatory spaces and their underlying dynamics of power do not develop solitarily, in silos, but instead are related to practices, discourses and social forces taking place elsewhere. Formally speaking, “connecting” different worlds (Mennicken, 2008) occurs especially through mechanisms by which actors from different regulatory organizations share information with one another – for instance through IFIAR and EGAOB which explicitly encourage the sharing of knowledge and experiences across regulatory bodies. As observed by DiMaggio and Powell (1983, p. 152): “Organizations tend to model themselves after similar organizations in their field that they perceive to be more legitimate or successful”. Concretizing regulation is a complex endeavor and inter-organizational comparisons play a key role in constructing comfort in regulatory networks regarding the “appropriateness” of structural designs and practices. The production of comfort is subject to all three levels of power in erecting boundaries of inclusion and exclusion surrounding ideas and actors within the regulatory arena.

Finally, globalizing processes do not necessarily involve the co-presence of different actors. For instance, concerns regarding the acceptability of European regulatory practices in the eyes of the US regulator were often expressed in the European material we analyzed. Being involved in absentia constitutes a manifestation of power although, in our case, it was not influential to the point of modifying the European Directive in ways which are unpalatable to the European Associations of auditors. However, the general point we would like to make on globalizing processes is that the “other” (especially other regulatory bodies) is mobilized significantly in power dynamics surrounding regulatory spaces. From this perspective, it is also relevant to recognize those who are excluded from the realm of the influential “others”. In particular, we would like to stress that the public is often a marginal figure in the discourses constructed by the actors we studied. The public and its interests are quite marginalized in the power dynamics

played out at the junction of the global and the local, which oppose the logic of arm's length regulation to that of self-regulation. This is perhaps the most disconcerting feature of our findings.

## **Conclusion**

Claims of independence are at the core of various institutionalized forms of expertise in society – for instance journalism, judgeship, academia and financial auditing. These claims are especially fragile, however. As a result of the collapse of Arthur Andersen, various mechanisms were mobilized to secure auditors' claim of independence. One of these mechanisms was the creation of independent audit regulators, which aim to promote auditor independence through inspections of public company audits carried out by bodies of inspectors that are not formally comprised within the scope of the profession. The presumption is that independence of financial auditors is now under control given the watchdog function of independent audit regulators. The present paper questions the aura of legitimacy surrounding the word "independent" in the term "independent audit regulators". In so doing, our empirical analysis strengthens the view that a "form of allegiance" is developing between the largest accounting firms and the oversight bodies which are supposed to monitor them from a distance (Humphrey et al., 2009, p. 817).

Complexity underlies the diffusion and implementation of regulatory innovations, but complexity is often downplayed, even ignored, when we look at official discourses. Relying on a modified version of Lukes' multidimensional model of power, a contribution of the present study is to examine patterns of resistance taking place in the aftermath of a regulatory innovation, in a relational environment where certain dynamics of power, located both in discourses and individual actions, interact to modify, discredit and maintain regulatory traditions. As observed by Clegg (2006, p. 849): "Historical traditions change, not inexorably, but for reasons of power, imagination and context. The capacity to be able to conceive difference – imagination – has to be allied to the capacity to make a difference – power." In the language of Clegg, our analysis illuminates how the collective and individual imagination of dominant actors engaged in regulatory processes surrounding the institutionalization of CPAB was influenced by certain discourses, and how the deployment of language upon imagination combined with very concrete episodes of agenda setting and overt confrontation in forming a private circuit of power aiming to preserve, under the guise of outside regulation, some of the foundations of the historical self-

regulatory tradition within the Canadian regulatory space. Of course, though, power and resistance inevitably intermingle (Foucault, 1981). Our point is not that the logic of arm's length regulation is extirpated from the Canadian regulatory space under examination. However, as illustrated above, both in relation to developments in Canada and in the international regulatory arena more generally, our analysis indicates the self-regulatory logic being much more influential than anticipated from the rhetoric which underlies official pronouncements.

It is relevant to stress that the targets of regulation, especially the Big Four firms, are far from being powerless in the face of audit regulators. The Big Four firms are diversified organizations that are often larger than their Fortune 500 corporate clients (Suddaby et al., 2007). They possess significant resources to organize in the face of adversity (Sikka & Willmott, 1995; Sikka, Willmott & Puxty, 1995) and are able to exploit the “regulatory gap [that] has developed between traditional regulators historically tied to the territorial nation state and global accounting firms which are increasingly influential in new transnational regulatory institutions” (Suddaby et al., 2007, p. 357). From this perspective, the US / EU rivalry highlighted in our analysis is not indicative merely of audit regulation as a political arena opposing two superpowers. It also points to the spatial gap – and incidentally to the limitations – of any attempt to control and supervise a globalized industry from a regional perspective, be it American or European. It is clear that many of the important decisions relating to the way in which audits are conducted and how audit firms are organized are now increasingly made at a global basis (Loft, Humphrey, & Turley, 2006), not only through the agency of those accounting firms that have the resources to audit multinational corporations, but also through private standard-setting bodies such as IFAC or the International Accounting Standards Board (Humphrey et al., 2009). We are, therefore, confronted with a major regulatory gap where both the international firms and the global standard-setting bodies are not subject to global and strong regulatory oversight.<sup>13</sup> There is no independent audit regulator to deal with the global scope of PwC, Deloitte & Touche, Ernst & Young or KPMG international. As long as regulatory apparatuses remain underdeveloped spatially and fragmented, it is very unlikely that highly efficient forms of regulatory power will develop to oversee, control and question the increasing expansion of professional service firms’ jurisdiction. And the lucid

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<sup>13</sup> It should be noted that private-setting bodies are typically “overseen” by committees that claim genuine public representation. For instance, IFAC is supervised formally by the Public Interest Oversight Board (PIOB). This type of overseeing, by a committee within the organizational structure of the overseen, is named “embedded oversight” by Loft et al. (2006, p. 435). The extent to which such committees do adhere and promote the logic of self-regulation is an empirical question.

observation by Cooper and Robson (2006) that conglomerate accounting firms have become less the subject and more the site of professional regulation will continue to challenge fundamental principles of democratic control.

International accounting firms are powerful, and it is probably easier for them to sway debates and reforms in accordance with their own interests when the regulatory environment is not adapted to the firms' globalizing tentacles. Nonetheless, even if the regulatory gap is to be spatially overcome eventually, the firms will still be able to benefit from discursive influence. The third level of power should not be ignored in regulatory debates. While staffing regulatory organizations with highly experienced auditors may be necessary for operational purposes, these individuals constitute footholds by which the profession's discourses, internalized in their mind through many years of experience in public accounting firms, can act upon and influence everyday decisions within regulatory settings.

In their review of research on accounting regulation, Cooper and Robson (2006) also consider the complex nature of regulation processes. In particular, they emphasize that, inevitably, actors in the field have significant discretion as to how regulation is interpreted and enacted, and they call for researchers to study these processes through detailed and contextualized studies. Our paper extends this literature through the development of a better understanding of the processes by which regulation is mobilized and implemented in a local site. As such, our study is noteworthy since extant research on accounting regulation provides limited insight into the political dynamics surrounding the deployment of audit regulation in contemporary settings (Humphrey, 2008). However, local regulatory sites do not exist in a vacuum. They intertwine with global and complex circuits of power and resistance (Djelic & Sahlin, 2009). Although international audit regulatory structures such as IFIAR and EGAOB are still in their infancy, research needs to be particularly attentive to "globalized" interactions between local and global sites of audit regulatory production. As shown through our paper, deep-level understandings can be gained when one juxtaposes the local and the global perspectives.

To conclude, intellectual vigilance is required especially in times of social and economic turbulence. As observed by Djelic and Sahlin (2009, p. 175): "Our transnationalizing world is a world where institutional rules of the game are in serious transition". In the context of the financial crisis of 2007 to the present, the regulatory transition constitutes a critical opportunity for the research community to focus its analytical gaze on the redistribution of power. Not only

should researchers keep under review the regulatory arrangements and re-arrangements “that the accounting and auditing profession and global financial regulators have struck with society” (Humphrey, 2008, p. 188), but, hopefully, they will be able to intervene (Neu, Cooper, & Everett, 2001) in informing society about some of the key challenges that regulatory regimes face in today’s complex, fragile and globalizing world.

#### **Abbreviations used in the text**

AASB: Auditing and Assurance Standards Board (Canada)  
AASOC: Auditing and Assurance Standards Oversight Council (Canada)  
AIU: Audit Inspection Unit (UK)  
AuRC: Audit Regulatory Committee  
CA: Chartered Accountant  
CEO: Chief Executive Officer  
CFO: Chief Financial Officer  
CGA: Certified General Accountant  
CICA: Canadian Institute of Chartered Accountants  
CMA: Certified Management Accountant  
CPAB: Canadian Public Accountability Board  
CSA: Canadian Securities Administrators  
ECG: European Contact Group  
EGAOB: European Group of Auditors’ Oversight Bodies  
EU: European Union  
FEE: Fédération des experts comptables européens  
GAAP: Generally Accepted Accounting Principles  
GAAS: Generally Accepted Auditing Standards  
H3C: Haut Conseil du commissariat aux comptes (France)  
IFAC: International Federation of Accountants  
IFIAR: International Forum of Independent Audit Regulators  
KPI: Key performance indicator  
PCAOB: Public Company Accounting Oversight Board (USA)  
PIOB: Public Interest Oversight Board  
PwC: PricewaterhouseCoopers  
SEC: Securities and Exchange Commission (USA)  
SOX Act: Sarbanes-Oxley Act of 2002 (USA)

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## Appendix I

### CPAB Staffing Model

#### Source of CPAB inspection staff

- Retired Big 4 partners
- Professional Institutes (Standard setters, inspectors)
- Specialized industry (banks, oil & gas)
- Big 4 executive directors/principals (technically oriented)

#### Influencing Factors

- Second/third careers
- Life style considerations

#### Aim for

- 1/3 Retired Partners
- 1/3 Ex Technical Principals
- 1/3 Other (banks, internal audit, industry experts, functional experts)

Source: IFIAR Audit Inspection Workshop, Amsterdam, 30-31 May 2007, presented by Don Cockburn (CPAB's vice-president).

**Table 1**  
**Background of CPAB executives in accounting**

Position within CPAB	Accounting experience		
	Former employer(s)	Chartered accountant?	Partner in public accounting firm?
Chief executive officer	Institute of Chartered Accountants of Ontario <sup>14</sup>	<b>Yes</b>	No
Senior vice-president	Arthur Andersen	<b>Yes</b>	<b>Yes</b>
Vice-president and chief information officer	Deloitte & Touche	<b>Yes</b>	<b>Yes</b>
Vice-president	Ernst & Young	<b>Yes</b>	<b>Yes</b>
Vice-president	PwC	<b>Yes</b>	No
Vice-president	CICA <sup>15</sup> , KPMG	<b>Yes</b>	<b>Yes</b>
Vice-president and chief financial officer	PwC	<b>Yes</b>	No
Vice-president and general counsel	CICA, Arthur Andersen, Auditor General of Canada	<b>Yes</b>	No

Sources of data: CPAB Annual Report 2008; CPAB's website (January 2009); <http://www.fsco.gov.on.ca> (April 2010)

<sup>14</sup> Former President and CEO of the Institute.

<sup>15</sup> Director of Auditing and Assurance Standards at the CICA.

**Table 2**  
**Deficiencies found through CPAB's inspections**

	National audit firms			Non-national audit firms		
	2004	Average 2004 / 2007	2007	2004	Average 2004 / 2007	2007
Periodic inspections						
Number of files inspected	68	439	97	128	377	162
GAAS deficiencies	5.9%	7.5%	8.5%	14.8%	19.3%	29.8%
GAAP deficiencies	1.5%	3.0%	3.8%	10.9%	14.0%	16.6%

Source of data: Slide show presented in May 2008 at the Canadian Academic Accounting Association (CAAA) Conference, entitled "CPAB – Five Years On".

GAAS: Generally accepted auditing standards; GAAP: Generally accepted accounting principles.