

Audit Pricing Semiosis

A Case for an Alternative View To Audit Pricing

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Abstract

This study considers the validity of the determinants of audit pricing. Audit pricing research has always been approached from the traditional positivist research methodology which yields results that may not give a full account of what determines and influences audit fees. This *mainstream* approach gives the perception that the actors within the audit pricing discourse are *objective* and *rational* by nature during the course of their *interactions*. In addition, the researcher is also perceived to be unbiased and impartial. Such assumptions are not suitable for social science research, because they tend to oversimplify the way that people and organisations behave. *Interpretive* and *critical* paradigms are the traditional alternatives to positivist research. Interpretive researchers seek to reach an *understanding* of the phenomena being observed. While, critical researchers, in addition to seeking an *understanding*, may also *critique* such phenomena in respect to the morality and fair treatment of the parties involved who may have an unequal distribution of power. These traditional alternatives have their limitations and may subject the researcher to being accused of being too *subjective* or too *political*. From our research, the interpretive and critical approaches have never been applied to audit pricing research and *semiotics* is proposed as a viable alternative due to the *flexibility* offered in using the *Peircian* model. That is, the researcher can apply a semiotic approach in which they have the freedom to incorporate the key characteristics from both the interpretive and critical paradigms. Semiotics is applied to audit pricing with an objective of shedding new light on what factors determine audit fees. Stamper's Semiotic Framework was deployed in undertaking the analysis using six analytical levels, namely: the physical level, empirics, syntactics, semantics, pragmatics and the social level. The model was further extended through giving greater emphasis to the *interactions* between the parties. The traditional positivist approach, which explained audit pricing was mainly attributed to the *size* of the audit client and the audit firm. But an *in-depth* semiological analysis of the interactions between the parties within the discourse of audit pricing revealed a number of new ideas in addition to the 'size' variable. Such ideas include the influence of government intervention in the standard setting process, the audit profession's barriers to entry, risk of litigation from the client and the client's internal control function. These may be used, as the basis for further research into areas previously not considered by past literature.

I. Introduction

This is an *exploratory* paper, which applies a technique traditionally foreign in audit research. Its aim is to provide an explanation and demonstration of applying semiotics to the discourse of audit pricing. The discourse is concerned with the 'valuation' (or pricing) by interested parties in the intellectual work performed by auditors. Semiotics as an inter-subjective method, enables the researcher to engage in a process of inter-subjective deciphering (or accounting) of inter-subjective communications that take place between the different actors within the discourse of audit pricing.

The first few sections of this work discuss the *positivist* approach to accounting research as well as its traditional alternatives in the form of the *interpretive* and *critical* paradigms. Semiotics is then introduced as a viable alternative and is demonstrated through an application to the discourse of audit pricing. These sections show that semiotics focuses on the interactions between parties and subsequently provides additional ideas on audit fee determinants.

Firstly, the dominant paradigm of science and its traditional alternatives will be discussed. This section begins by describing what is called the positivist approach to accounting research. At face value, this approach appears to offer accounting researchers great hope because the positivist approach attempts to *explain* and *predict* phenomena and furthermore this mainstream approach carries *implicit* connotations of *rationality* and *objectivity*. But unfortunately, accounting is a social science, which deals with the complex cognitive processes of people and hence we cannot assume that people always act objectively and rationally. Moreover, the assumption that the researcher of accounting phenomena is a *passive* observer and takes a neutral value position is also criticised. Then, this will be followed with a discussion of the alternatives to the mainstream research methodology. The first alternative is the *interpretive* methodology, which takes a *subjective* view of the research phenomena in question and seeks to gain an understanding of the interactions involved. The *critical* methodology is the second alternative discussed and it takes a political approach to research and considers the well being of the weaker parties in a given discourse. This approach is highly opinionated and seeks to find a solution to the problems associated with the *status quo* in order to empower the weaker classes that need empowering. This will be followed by an outline of some of the limitations associated with the use of the interpretive or critical paradigms.

Secondly, a proposal for a semiotic alternative will be offered. Here, *semiotics* will be introduced as a viable alternative to the mainstream approach as well as the *interpretive* and *critical* methodologies mentioned in the previous section. The origins and the concept of 'semiotics' is considered and briefly explained. This section then considers the two major pioneers of semiotics: Saussure and Peirce. We look briefly at the contributions of these two theorists in that we consider Saussure and the *structuralists* movement that had followed, and Peirce and the movement of *symbolic interactionists* that had resulted. After a brief analysis of the ideas of Saussure and Peirce we assert that Peirce's model is superior because it has broader application as it steers away from the traditional focus on *linguistics* and moves to more flexible definitions of signs through Peirce's *triadic* model. The ending section of this section reconciles semiotics (influenced by the Peircian model) with both the *interpretive* and *critical* alternative methodologies. We conclude by asserting that semiotics is a very flexible methodology of research as it can overcome the limitations of the *interpretive* and *critical* approaches and simultaneously take advantage of their defining features.

Thirdly, a tentative proposal will be made of Audit Pricing. This section gives a critical review of the past research undertaken within the realm of audit pricing. This section introduces us to the audit

market as well as issues of *demand* and *supply* within the audit market. But this review mostly discusses the issue of *size* of the audit firm and the audit client and their influence on audit fees. This review also looks at the effects of some of the behavioural aspects performed by both the auditee and the auditor which includes low balling, price cutting, opinion shopping and audit switching as well *brand name* auditing. This section gives a criticism that most of the research is *positivist* by nature and questions why alternative methodologies, has not been applied to audit pricing research. We consider whether the editorial policy may be a factor and conclude that this is difficult to prove. This section then discusses semiotics where due to its flexibility, may be readily applicable to audit pricing as it may shed some new light on the discourse of audit pricing. The section closes by commenting that semiotics has never been applied to audit pricing before and hence this essay is largely a journey of discovery.

Fourthly, the communications and interactions between the different parties that take place within audit pricing will be outlined. This section takes on from the literature review conducted in the previous section. Firstly, this section considers what semiotics has to offer the discourse of audit pricing. We then have a change of pace and discuss the importance of communication is to our semiotic analysis of audit pricing. Communication is especially important because we are dealing with the interactions between a number of parties in which as a result of such interactions can induce *change* through shared meanings. The final section of this section gives a brief introduction of the six players in the audit pricing discourse. This introduction to these players is helpful before we undertake an semiotic analysis- especially for those people unfamiliar with the practice of auditing.

Fifthly, the reader will be introduced to Stamper's framework of semiotics and how it will be adjusted in order to analyse the discourse of audit pricing. The first part of this section looks at what may have influenced Stamper's framework and we conclude that the *Peircian* model would have had greater application to Stamper's model than the *Saussurian* model simply because the *Peircian* model is very flexible while the *Saussurian* model predominantly focuses on *linguistics*. We are then introduced to the six semiotic levels of Stamper's semiotic framework and elaborate on each level in turn. These levels are as follows: the physical level, empirics, syntactics, semantics, pragmatics and social signs. We then briefly discuss how our approach to the semiotic analysis will extend the framework of Stamper and focus on *interactions* between the parties in the social discourse across the different levels of semiotics. This section will come to a close by outlining the two reasons why Stamper's (1992) framework of semiotics is difficult to apply to the discourse of audit pricing. The first reason is that Stamper's framework is applied to *Computer Based Information Systems (CBIS)*. Audit pricing exists within an information system but it is not a CBIS and hence, a reconciliation between CBIS and audit pricing is difficult but not impossible. The second reason is that Stamper applied semiotics to microeconomic environments such as organisations, while the social discourse of *audit pricing* is macroeconomic in nature due to the fact that multiple organisations are analysed.

Sixthly, we outline the whole process that we had taken in the analysis and evaluation of the audit pricing discourse from a semiotic perspective. This section goes through the process of identifying the parties involved in this social discourse, through to analysing and evaluating the *interactions* of the six parties involved in audit pricing in order to shed some new *light* on audit pricing determinants that were ignored in past literature. To give a more in-depth analysis, *ontology* diagrams are constructed in order to provide structure to the interactions within the audit pricing discourse.

Finally, a conclusion will be drawn by reflecting on the use of semiotics as a research tool in respect to its relationship to the mainstream approach to research as well as the traditional interpretive and critical research methodologies. Stamper's (1992) framework of semiotics is also reconciled with the Peircian and Saussurian perspectives of semiotics. The literature review of audit pricing is reconciled

with semiotics in respect to the new ideas that semiotics has yielded in the analysis of the *interactions* between parties. This section ends by the comment that semiotics can offer social discourses new perspectives never thought of before.

II. The Scientific Paradigm & its Traditional Alternatives

This section begins by questioning why the dominant paradigm of the scientific methodology is so popular in accounting research. We then consider the traditional alternatives being the interpretive and critical approaches and the limitations they have as well. This section aims to set the scene of introducing a *semiotic* approach to accounting research.

II.A. The dominant paradigm of science

Accounting Research has been dominated by a scientific research methodology since the early 1970's. Science is held in high regard in society as it gives the perception of *rationality* and *objectivity*. The reason why the scientific method has been so dominant can be attributed to social influences such as the opinion of journal editors, research training in our universities and advances in technology (Gaffikin, 1988, p29).

The notion of science is very attractive. Gaffikin (1994, p8) observed that western culture considered science to be the 'ultimate in intellectual rigor and analysis'. Furthermore, to be labeled a 'scientist' carries with it connotations of *objectivity*, *rationality* and freedom from *value* judgments.

II.B. The positivist approach to social science and its limitations

The scientific method works on the traditional positivist basis of *observing* real world phenomena, formulating a hypothesis and ultimately drawing a general conclusion that will *explain* and *predict* the behavior of the phenomena being investigated. The positivist approach makes extensive use of sampling, probabilities, statistics and other mathematical techniques.

Science is traditionally suited to the *physical* sciences (such as chemistry, physics and astronomy) but science also has *prima facie* applications to social disciplines such as accounting. On face value, the rigorous, objective and rational techniques of the scientific method, has a lot to offer in explaining accounting phenomena. That is, if the scientific method can give the physical sciences a conceptual framework that can be agreed and relied upon by the wider community of that particular scientific discipline then perhaps a similar result would occur for social sciences such as accounting.

But this is not the case because we are dealing with *people*. Hence the scientific method becomes problematic when dealing with social sciences such as accounting. Blumer (1978) says that it is very hard to apply conventional scientific methods to the empirical social world because it:

... 'forces data into an artificial framework that seriously limits and impairs general empirical analysis.'
(p41)

The scientific method that deals with physical sciences is ontologically of the opinion that the world is an *objective* and *detached* reality and facts are there waiting to be discovered independent of people's behavior. Applying such a positivist approach to social sciences *assumes* that individuals are objective and rational where, the system is created by people to satisfy their needs (Stamp, 1981:p20). This is where the scientific method encounters problems when unrealistic and oversimplified assumptions are utilized in a scientific endeavor.

The positivist approach works upon the premise that the researcher is a passive observer in that they will only want a better understanding of the phenomena in question to the extent of *explaining* and *predicting* the phenomena in question. Since this mainstream approach is not normative in nature (Henderson *et al.*, 1978:p30), the research has little concern about injustices and other issues affecting the actors that may be relevant for solving the given research problem at hand. That is, mainstream accounting research will not attempt to change the institutional structure. It is irrelevant whether the accounting researcher exists in a capitalist, socialist or mixed economy or whether the market is a monopoly or perfect competition (Chua, 1986). The researcher maintains a neutral position as taking any stand may be perceived as being in breach of their implicit objectivity.

This so-called *neutral* value position runs into difficulties because the position that the positivist researcher takes is itself a *value* position. The value position taken by the positivist researcher lends support to the *status quo* and hence the researcher may be thought of as being a 'conservative' (Weber, 1949). Moreover the position taken by Tinker, Merino and Neimark (1982) asserts that such 'conservative' support helps *legitimise* market systems of exchange, production and suppressive regimes.

Mainstream research in *social* sciences is also limited due to the assumptions it makes about people and their interactions. Positivists have an implicit rationality assumption that actors are goal driven and rational and coexist within the structured and causal patterns of organisational life (Chua, 1986). This position is questioned (Cohen *et al*, 1972, Weick, 1979, and Mintzberg, 1979) who recognised the complexity within organisations, with regard to their rules and social interactions. Also there are power struggles between organisations and between the interest groups within the organisation (Chua, 1986) that ought to be acknowledged.

In essence, the scientific method only considers data that is accessible to our senses. Hence much of the empirical research relies upon observation, that is the observer makes generalisations based on the observations that were made. Theories based on observation can be most problematic, Chalmers (1978:pp23-32) believes that scientific knowledge is based on the objective and unbiased observer. The observer sees things based on their knowledge, past experience and expectations, hence we see things differently.

II.C. Traditional Alternatives

II.C.1. Interpretive philosophy

Simply explaining and predicting social phenomena is inadequate. An alternative is needed that seeks to *understand* the phenomena observed in order to properly *explain* it. *Interpretive* social science has surfaced as a result of the limitations of traditional positivist approaches when researching social phenomena. This methodology seeks to *understand* the behavior of people and how people understand each other's behavior (Puxty, 1993:p57). Hence this methodology openly admits its *subjectivity* and it opposes the (seemingly) *detached* and *objective* approach of the positivists.

Since the interpretive philosophers use a *subjective* methodology then no theory derived from interactionist studies are correct or incorrect. The philosopher is rather inclined to reason that there are interesting and less interesting ways of viewing the world, that is, interesting to the philosopher or to others (Walsham, 1993:p6). The researchers' interpretation is a result of his or her personal experience and insight, and additionally they cannot fall back on any verification procedure and hence they can only continue to offer alternative interpretations (Rabinow *et al.*, 1979:p7). These alternative

interpretations are tested, by exposing them to verbal and written discourse from which a broad variety of value judgments can be made (Walsham, 1993:p6).

Limitations of the interpretive philosophy

The limitation of interpretive philosophy is that there can be multiple and conflicting interpretations. There is not one 'correct' interpretation and thus much interpretive work may be discarded as being *subjective*. Consequently, the interpretive philosophy may be driven to case studies and ethnographies under strong anthropological influences. Another limitation is that the researcher cannot expressly pass an opinion on the state of affairs concerning the subjects within their defined area of research. Their role is to reach an *understanding* about the actors' activities in the specified social discourse.

II.C.2. Critical philosophy

In our opinion, critical theory is an extremely broad methodology and we fear that our description maybe somewhat oversimplified. Critical theory looks at the *social* element in a given research problem. Critical theorists make certain assumptions about the world we live in. In short, we live in a world where people have great potential to achieve their goals but they are *constrained* by dominating structures that exist in modern society (Burrell *et al.* 1979:p17). It is the desire of the critical theorist to highlight the injustices tolerated by the oppressed masses and to *empower* (Ellsworth 1992, p98) them to *transform* the system that has exploited them for so long (Laughlin, 1987:p482).

The background assumptions described above have implications on the way that the radical theorist would conduct their research. The radical sees *critique* as an important component in questioning the *status quo* and to determine how *transformation* could improve the interests of the oppressed. The radical theorist also views organisations and people in its *historical* and *societal* context (Laughlin, 1987:pp483-484). This approach has fewer limitations placed upon it than the *positivist* approach and hence could provide the social scientist with an *acceptable* means for *understanding* and *changing* our worldly structures and systems. (Laughlin 1987, p. 484). Some critical theorists are openly against the positivists, for example Frankfurt theorists: Horkheimer and Adorno feel that the positivist theory of science associated with their crude and detached research methodology perpetuates the survival of *capitalist* domination as critique is discouraged. (Agger, 1991:p109).

Limitations of the Critical Philosophy

Since critical theory is inter-subjective then it stands to reason that different theorists have different philosophical opinions for the position they take in the theories they evaluate. There is no 'right' position to take and as a result many critical theorists openly criticize each other. But such criticism between theorists also occurs within the *interpretive* and *mainstream* paradigms (Chua, 1986:p626).

Ellsworth (1992) openly criticizes the critical paradigm by arguing that critical theorists tend to hide behind theoretical jargon such as 'critical', 'social change' and 'revitalized public sphere' (ibid. p93) which hides the theorists political agenda. The literature might imply that it is 'political' but critical research rarely if ever investigates if the practice it prescribes actually alters power differentials in society.

The participants within a social system are forced to take sides on an issue and to question the *status quo*. But social change in the form of an acceptable solution that is socially acceptable may or may not occur (Dillard, 1991).

Radical literature may not appeal to the very interest groups that critical theorists are trying to reach. In effect, such literature may only interest those already prepared to question the basis of our social structures, thus critical theorists are merely ‘preaching to the converted’ (Mathews *et al.*, 1993:p352).

II.D. Conclusion

The traditional positivist approach has dominated the way accounting is researched for a long time. We are finally beginning to acknowledge the limitations of using positivist assumptions in a social science. That is, the people researched are not *objective* or *neutral* beings that can be observed so that we can explain and predict their future behavior, nor is the researcher a *passive* researcher. Alternatives such as the interpretive and the critical paradigms offer hope in rectifying the limitations of *positivist* research. But these approaches also come under criticism for being too subjective, too conflicting and too political. The interpretive and the critical methodologies may not be perfect but at least they have addressed the limitations of the mainstream approach.

III. A Proposal for a Semiotic Alternative

It would seem that there are serious doubts relating to the mainstream philosophy of science and its application to social sciences such as accounting. Some argue that without the reassurance of a *neutral* and *objective* reality, science in its *social* context is in a ‘state of flux’ (Barnes *et al.*, 1982) and as such leaves us open to *alternative* methods of research. An approach is needed that will accommodate the complexities that exists between people and organisations as well as to overcome the limitations of the *interpretive* and *critical* pedagogues. This section shall demonstrate that semiotics, the theory of signs is a viable alternative.

III.A. Origins of Semiotics

Semiotics is the study of the *science of signs* (Culler, 1975) and is derived from the Greek word ‘*semeion*’, meaning a “sign”. Modern semiotics had grown from *structuralism*, which is a technique of linguistic inquiry whose major contributors were Claude Levi-Strauss in anthropology and Jacques Lacan in psychoanalysis. Semiotics owes its roots to *linguistics* and borrows heavily from linguistic concepts. But what we must bear in mind is that semiotics is not an independent academic discipline and is frequently applied to linguistics, communication, anthropology, advertising and marketing (Chandler, 1994).

Signs

By ‘signs’, We are not referring to signs in an everyday sense (like street signs) but rather anything can be a sign as long as it can be *perceived* and *interpreted*. Hence *signs* include gestures, numbers, words, photographs and facial expressions. This list is not exhaustive and the successful interpretation of these signs results in information (Barthes, 1972:p111). Since we interpret such signs, the meaning of the signs is a result of social conventions (Culler, 1981). Hence *semiotics* explains how the meaning of objects, behaviors, or talk is produced, transformed and reproduced (Culler, 1975). But, to understand the theory of signs more deeply we need to consider two schools of thought that influence contemporary semiotic theory, one was led by the Swiss linguist, Ferdinand de Saussure and the other by the American, Charles Sanders Peirce.

Two opposing groups has resulted from the ideas put forward by Saussure and Peirce: the *structuralists* and the *symbolic interactionists* respectively. The *symbolic interactionists* stress the

ongoing process of the “situation” as the determinant of *meaning* and these thoughts can be traced back to the origins of pragmatism and C.S. Peirce. In support of Saussure’s ideas, the *structuralists* postulate that *meaning* is found at the deeper level of ‘system’ or ‘structure’ of signs rather than at face value (Rochberg-Halton, 1982:pp.455-457) We shall further elaborate the contributions of the two theorists in turn.

Saussure

Saussure’s interpretation of semiotics was based on the European efforts to reconfigure the study of language. Under the Saussurian regime, language was treated as part of an overall larger system whereby each component of language was no longer viewed as an independent component but was rather viewed in *relation* to other components within the system. The key concept of this relation is the formation of the relationship between the *signifier* (the actual sign) and the *signified* (the response triggered by the sign within the interpreter). The Saussurian approach to semiotics is generally referred to as *semiology*.

Such an approach is all about looking at the opposing relationship between the *signifier* and the *signified* and since the relationship is arbitrary, the underlying meanings of language can be easily analysed. Hence, language systems can be formulated for different occupations and cultural practices in which ‘codes’ can be developed where an interrelated set of signs allow us to better explain and understand our world (Saussure, 1959; Eco, 1979). That is, meaning of signs is produced through the ‘binary opposition’ within the *signifier* and *signified* system in which the very basis of meaning in the Saussurian model is *difference*. Thus, the factor that distinguishes one sign from another constitutes its *meaning* (Saussure, 1966:p121).

The Saussurian approach is limited since the *meaning* of signs is entrenched within the general language system and not the actual speech act. That is, communication owes its significance by its underlying language structure as opposed to the *social context* of the situation. Studying signs should be broader than this and should not be merely confined to *linguistic* analysis (Rochberg-Halton, 1982:p459). Hence the *diatic* model of Saussure would have limited application to accounting research since signs are produced and reproduced within a social discourse.

Peirce

The second pioneer of semiotics is Charles S. Peirce who was the founder of the *pragmatist* aspect of semiotics. Peirce’s work tends to steer away from the traditional linguistic focus on semiotics, rather he takes a broader approach and asserts that all intelligent behavior is *sign* behavior. Peirce saw a sign as a *triadic* structure as opposed to Saussure’s *dyadic* structure and furthermore viewed meaning in terms of *relation* rather than *difference* (Rochberg-Halton, 1982:p458).

To quote Peirce directly on this issue:

“A *sign*.... is something which stands to somebody for something in some respect or capacity. It addresses somebody, that it creates in the mind of that person an equivalent sign, or perhaps a more developed sign. That sign which it creates we call the *interpretant* of the first sign. The sign stands for something, its *object*. It stands for that object, not in all respects but in reference to a sort of idea, which we have sometimes called the *ground* of the representation” (Peirce, 1931-35:2.228).

In other words Peirce’s model is made up of a *sign*, an *object* and an *interpretant*. The sign is a particular physical or a conceptual entity, which is said to be the basis of the sign relation. The *sign* is the symbol, signal mark or trace, but a sign in itself is meaningless. The *object* is what the sign stands

for or represents and the *interpretant* is the effect of the sign on the receiver of the sign. This three way *triadic* model is represented in the following diagram:

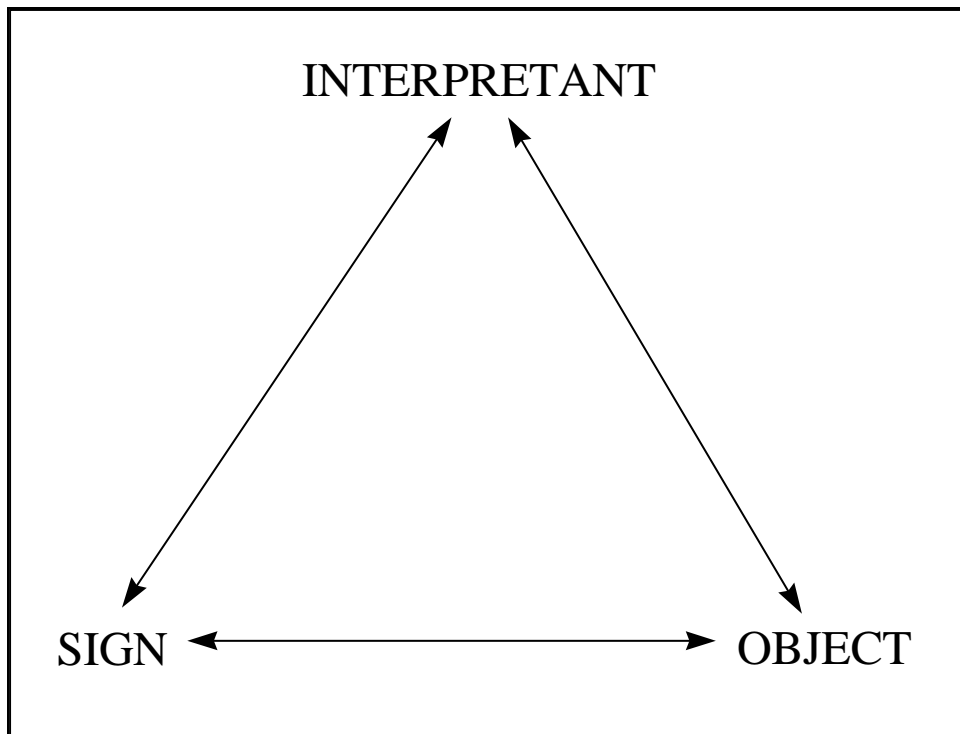


Figure 1 - Peirce's Triadic Model

Semioticians under Peirce's way of thinking refer to three kinds of signs:

- **iconic**- icons are signs that bears a close resemblance to the *signified*. That is, icons look like the objects to which they refer. Icons are easy to recognise and to learn, as they tend to be familiar to the interpreter from previous experience (Marcus, 1993:p102). Examples of icons include photographs, maps, x-rays and some paintings.
- **symbolic**- this sign does not necessarily represent the *signified* but is arbitrary or purely conventional. Symbols have no inherent meaning of their own as they may not resemble the signified object since they tend to be abstract and lack visual characteristics (Marcus, 1993, p102). For example, a 'stop' sign or a red traffic light to enforce people to stop their car.
- **indexical**- this sign is inherently connected in some way to the *signified*. That is, the index refers to that which caused the object to exist in the first place (Marcus, 1993, p102). For example, where there is smoke there is fire, and footprints represent the presence of people.

The Peircian model is much broader than the Saussurian model and later we shall provide a rationale for applying semiotics under the framework of Stamper (1992) who we feel was more influenced by the Peircian model as opposed to the Saussurian model. We shall also use Stamper's model of semiotics as the basis for a semiotic analysis of audit pricing.

Now that we have introduced the concept of semiotics, let us now reconcile semiotics with both the interpretive and critical philosophies.

III.B. Semiotics and Interpretive philosophy

Let us now reconcile the interpretive paradigm with *semiotics*- the theory of signs. People extract information from signs which forms the basis of message construction and the creation of *meaning* (Colon, 1995). But every sign has an *explicit* or *implicit* meaning as a result of interactions of the actors involved within the wider system of their values, ideas and beliefs. That is, the interpretation of signs is chiefly a result of the cultural experience of the reader draws upon his or her experience, attitudes and emotions (Fiske, 1982:p43). The creator of a given set of signs would be wise to pay close attention to the interpretive processes of the actors who interpret such signs. That is, the communicator ought to study the cultural background of his or her intended audience and formulate the right combination of codes, media, and contexts in order to make the transfer of information: fast, cost effective, accurate and most importantly, *meaningful* to the intended audience. Thus, the sign is only effective if the audience's interpretation of the meaning of the sign is in congruence with the sender's with the sender's *intended* meaning (Hughes, 1995).

At this point we can determine that the *ontological* position of semiotics is that *reality* is a social construction by human actors and this is assumed in all semiotic research. As such, semiotics holds that there is no *objective* reality that can be discovered by researchers and replicated by others but conversely we make sense of the world in our own way and share *inter-subjective* meanings of the signs we interpret.

Methodologically speaking, semiotics contrasts sharply with the traditional positivist approach outlined above. The main criticism was that the *positivist* paradigm works well with physical sciences but has no place in the realm of *social* sciences. Semiotics cannot overcome the limitation of *subjectivity* altogether. But as we shall demonstrate later, semiotic analysis provides a sensible balance between the *objective* and *subjective* extremes of interpretation. But overall, semiotics through *interpretivist* philosophy offers the social scientist an attractive alternative for research.

III.B. Semiotics and Critical philosophy

Semiotics is chiefly a technique entangled in *hermeneutics* but due to the flexibility of semiotics it can easily have critical applications. As communicators we constantly send signs. These signs can be anything and they cannot always be validated. That is, there is no 'correct' sign and as such *inter-subjective* interpretation result. Barthes held that radical theorists send signs that will hopefully inspire *change* (see Dyer, 1989). As such, this theorist cannot afford to compose signs and then have them decomposed by the reader in the *wrong* way. Instead the 'good' political text is written in such a way that will reduce the reader into a 'dumb acceptance or rejection' for the given issue discussed.

It is surprising how many objects in society, are a symbol which has great implications to the way we conduct our everyday lives. The way we interpret certain symbols governs the way we live our lives and if the symbolic meanings were changed in our culture then it stands to reason that our lives will also be affected. Dyer (1989) looks at *money* as an example of a *sign* that governs the way we lead our lives. Economists and the rest of society view money in terms of its *medium of exchange* function, that is, in a *semiotic* sense they share a common understanding of what money *represents*. Hence, objects are commonly represented in *monetary* terms of exchange value and thus, transform life and impacts the way we understand and live our lives. For example, money has a significant impact on Ford Motors' decision making process. That is, it can be said that the *sign* of money has induced Ford to act in an unethical manner, having disastrous and unjust effects on parties of lessor power. Hyde (1979) tells the story of Ford Motor Company's reaction to the Pinto's (a popular car model in the 1970's) alarming performance in rear end collisions. Ford conducted a *cost-benefit* analysis where it was found that the *cost* of modifying the Pinto outweighed against the *benefits* of saved lives. Both costs

and benefits were expressed in *monetary* terms and it was found that modifying the Pinto was economically not viable.

A semiotic analysis may suggest that this is a less than desirable situation as money symbolises a *meaning* that makes the world understood in a certain way. The critical semiotician would then argue that such an interpretation is morally wrong. The way to *transform* this situation into a more desirable state is to change the semiotic code and symbols so that new social actors and personalities are created (Rosenberg, 1983, pp. 36, 200-204). A new code of money may have greater emphasis on the rights of the consumer rather than the capitalist intentions of the producer.

Environmental activists could use semiosis in order to demonstrate the inadequacies of the state and corporations symbolising the environment as an (exploitable) *commodity* and take steps to symbolise the environment as a *gift* (Hyde, 1979).

III.C. Conclusion

Semiotics can definitely give a fresh perspective on the mainstream, interpretive and critical philosophies of research. It is clear that the interpretive, critical and semiotic alternatives will offer insight not possible with the *positivist* methodology alone. The use of interpretive and the critical approaches may also be limiting to the researcher. We must not forget that research has to be palatable to those who read it. Interactionalist studies by means of *hermeneutics* may not be the best method to take since it may be too *subjective* and too limiting since in some aspects of research we may require limited use of *positivist* methodologies. On the other hand, critical studies may be too *political* for the research we want to conduct because we will be forced to turn our research into a political opinion. Sometimes, we do not wish to take a political stance.

Therefore, semiotics is very flexible because it can overcome the limitations of the alternative methodologies outlined in the previous section and instead take advantage of both of the defining characteristics of each of the alternative methodologies. That is, we can take steps to reach an *understanding* of the actions taking place and in addition it is also possible to express an opinion if we wish.

IV. A Tentative Proposal to Auditing Pricing

Semiotics have had relatively little application to accounting. As far as commerce related disciplines are concerned, semiotics has only found application in management and marketing. This monograph shall demonstrate a novel attempt of applying semiotics to audit pricing. This section of the monograph shall undertake a literature review of past research into the field of audit pricing and will critically comment on the limitations of such research in light of the philosophies of science outlined in the previous sections. This section shall set the groundwork for a semiotic analysis in audit pricing which shall be addressed in the next section.

IV.A. The Audit Pricing Environment: a review of the literature

There have been a number of studies since the beginning of the 1980's that investigated what factors determine *audit prices* or *fees* charged by audit firms. These factors can be attributed to characteristics of either the *auditor* or the *auditee* and may be applicable to both *private* or *public* sector clients. The purpose of this *literature review* is to find the major factors that influence *audit pricing* in general. The review looks at the *supply* and *demand* forces that exist on the audit market and then moves on to

the determinants of audit fees. The literature has a great deal of emphasis on the size of the audit firm and the audit client as this has implications for the strategic games these parties play to further their interests.

IV.A.1. The audit market

In undertaking an analysis of the way audit fees operate, it is desirable to do so from a *macroeconomic* perspective. That is, to view not just the auditing firm in question who charges the fee but to have an overview of supply and demand issues from a wider societal perspective.

IV.A.1.1. Auditing: the commodity with a difference

Before we consider the supply and demand issues relevant to the audit market it is important at this point to stress that the auditing is different from most other goods and services because auditing (like other goods and services) is an economic good evaluated on the basis of *quality*. Consumers can readily appraise the quality of other goods and services, because they know what constitutes quality. But this is not the case for audit services, because the consumers (the shareholders and other stakeholders in the company) do not know what constitutes a 'quality audit' and consequently do not know what their company is paying for. External users cannot directly observe (let alone understand) auditing procedures, nor do they have knowledge about the contractual arrangements and resulting incentives that may exist between the auditor and the client (Wilson *et al.*, 1990).

IV.A.1.2. Supply in the Audit Market

Let us turn to the *supply* issues that may have an influence on audit fees. Large multinational accounting firms dominate the audit market. The *big six* accounting firms are KPMG, Coopers & Lybrand, Ernst & Young, Price Waterhouse, Arthur Anderson, Deloitte Touche Tohmatsu. These multinationals have offices dispersed across the globe. Research in countries such as the United States, Australia (Yardley *et al.*, 1992), United Kingdom (Moizer *et al.*, 1989) and New Zealand (Johnson *et al.*, 1995) agree with the assertion that the big six dominate the audit market and that there is market concentration. These large accounting firms have a number of characteristics that puts them in an advantageous position in relation to audit pricing policies.

Audit Market

As indicated before, the audit market is largely characterised by the increasing domination by large multinational accounting firms. Craswell and Taylor (1991) feel that regulatory agencies such as the Australian *Trade Practices Commission* are overly concerned that industry concentration will lead to a *monopoly* that may control the audit market in order to create *above normal* returns. These agencies tend to ignore the positive aspects of such a market structure in regard to its impact on audit fees and audit quality.

We must proceed with caution when dealing with market concentration studies because different researchers use different proxies to suit their own means so that we get a different perception of audit pricing. Previous studies may have misrepresented the extent of market concentration of the big six because indirect measures such as auditor size (number of clients), client size (sales revenue) were not perfectly correlated with audit fees. More recent studies have used actual audit fees as a proxy for market concentration (Moizer *et al.*, 1989; Tomczyk *et al.*, 1989).

Economies of scale

This follows the notion that a single large firm would have a comparative advantage over a consortium of smaller audit firms in regard to prescribing and coordinating audit procedures. The large audit firm has a greater ability to service large multinational clients as large audit firms have offices dispersed all over the world (Penno, 1996). The larger audit firms also has economies of scale in regard to the development and support of the *expertise* required for specialised services such as taxation, regulatory agency reporting, internal control systems and management services. The larger firms can more economically nurture the *expertise* of their professional auditors with training, library support and the latest technology (Benston, 1985). There has been little research done on economies of scale in the audit market, but at this point in time, research indicates possible scale economies in regulated industries and large client segments of other industries (Yardley *et al.*, 1992).

Product Differentiation

Different auditing firms offer different packages as a *differentiated* product from their competitors. Product differentiation in the market of audit services can result from the audit firms reputation (that is their brand name image), industry specialisation, technical expertise in a given area, geographic dispersion of offices, responsiveness to client needs and the provision of non attest services (Schwartz *et al.*, 1985, p249).

Given the advantage that the big six firms have over smaller audit firms due to their market concentration, economies of scale and product differentiation we could postulate that the big six could easily deliver a higher quality audit at a lower price. But as we shall demonstrate later in this section this is not the case.

IV.A.1.3. Demand in the Audit Market

Agency relationships

Early studies (Watts and Zimmerman, 1983) tended to discuss the *demand* for audit services arising from the conflict of interest between managers, creditors, and outside shareholders. Benston (1985) postulated that the demand for audit services is largely influenced by the desire to *monitor* the actions of agents for which have *stewardship* of the organisation's resources. Leaving regulative issues aside, the manager has the incentive to engage audit services because they want to monitor employee activities more effectively. Employee reports may not reveal the true state of affairs and management may want to *assure* outside investors that resources are not being diverted towards the manager's interests. But the level of assurance will vary given the extent of the financial stake the manager has in the organisation as well as the extent of the agency conflict that may exist in the organisation.

Demand and auditor size

It is difficult to discuss the demand for audit services (in terms of fees) in relation to audit size for two reasons. The first reason is that the size of the client is an important factor as big clients and small clients generally have different needs and requirements. The second reason is that *audit quality* is a powerful motivation for the demand of an auditor based on size since larger auditors have a higher reputation for quality (we shall expand on this point later). Subsequently, audit fee research is not incorporated into research of audit demand (Copley, 1994).

IV.A.2. The audit market and its implications for audit pricing

What we have covered so far are a number of *supply* and *demand* issues that are relevant to audit fees. The major limitation is that we cannot construct any *quantitative* model that will *explain* and *predict* audit fees in the audit market given any set of conditions. In other words, the supply and demand of audit services cannot be quantified and form an *equilibrium*. This positivist's dream cannot be realised because we are dealing with the complexities of social interactions within socially constructed institutions that cannot quantitatively operationalised. The next section will see how the positivists have tried to solve this problem in order to construct an audit model.

IV.B. The factors that influence audit fees: a review of past research

Previous research had revealed that there are a number of factors that are a function of audit fees. The first two factors are auditee risk and auditee complexity and are relevant notwithstanding the size of the audit firm, the client as well as the state of the audit market. We shall then take a closer look at the *size* of the audit firm and audit client, assuming that the audit market is competitive.

IV.B.1. Variables studies independent of size

Before we consider the significance of size of the auditee and the auditor, there are two characteristics of the auditee, independent of size that needs to be briefly explained. The characteristics include:

IV.B.1.1. Audit client complexity

The theoretical framework in Chan (1993) suggests that the audit fee will increase positively with the complexity of the audit task that the auditor has to undertake. Such complexity pertains to the nature of the business of the auditee, the state of the internal control system, the number of subsidiaries and the proportion of unusual transactions etc.

IV.B.1.2. Audit client risk

The greater majority of audit firms take into account audit risk when determining the audit fee. Audit risk is the perceived risk of audit failure and could relate to the nature of the client's business or the nature of the internal control system (Chan *et al.*, 1993:p769). It is expected that the higher audit risk associated with a higher audit fee is a direct consequence of more audit testing or an 'insurance premium' (Wallace, 1989). Such a premium for this risk exposure also takes into account the increased tendency for litigation (Palmrose, 1988).

IV.B.2. Variables studies dependent on size

If we consider size in its simplest terms then we can generally conclude that the *size* of the audit client has an impact on the audit fee charged. Hence the larger auditee has the more complex structure and enters into more transactions than a smaller auditee and therefore requires more audit hours (Rubin, 1988). The majority of the previous studies had used total assets to measure 'size', but sales revenue can also be used, and may be more suitable in a *transaction based* audit.

Rubin (1988) had undertaken a relatively easy task in looking at the level of fees and the size of the client, but researchers before Rubin had pondered something more difficult: why different audit firms charge different audit fees? Simunic (1980) was one of the initial researchers into audit fee determinant research using *regression* analysis between audit fees and the audit market, and he concluded that the market was indeed *competitive*. He was one of the first to see the significance of *size* in finding that the *big eight* audit firms charged lower fees than smaller audit firms for reasons of *economies of scale* larger firms enjoyed. On the other hand, Francis (1984) contradicted Simunic

(1980) in the finding that larger audit firms charged significantly higher audit fees compared to their smaller firm rivals which was consistent with the *product differentiation* hypothesis.

Francis and Stokes (1986) saw that it was a mistake to research audit fees based on the dichotomy of large versus small audit firms alone. Instead Francis and Stokes took this research further and concluded that in Australia, the audit market was split by company (client) size. Hence according to their research, in the large clientele sized market, there is no difference in fees charged by large and small audit firms. And in the small clientele audit market there are significant differences in fees charged by large and small audit firms, in that large audit firm charge higher fees than smaller audit firms.

There is no denying that all three factors: auditee risk, auditee complexity and the size of the respective auditee and auditor play an important role in determining audit fee outcomes. But the factor of particular interest is *size*, because this factor has the greatest potential in explaining the audit market and the behavioural strategies that occurs within the market that determines the fee.

IV.C. A new perspective: size influences behavior

It would seem the best approach to researching audit pricing is through an understanding of the audit market. As postulated before, it would seem that the *size* of the audit firm and the client has a significant influence on the audit price. The large audit firms are perceived to have a higher level of *audit quality* and product differentiation in a competitive market. These clients desire such attributes, but their needs usually differ according to their size.

This section moves from the *demand* and *supply* forces within the audit market structure and the description of size characteristics of the entities involved and *extends* our focus into the behavioural tactics used by the respective audit firms and the audit clients engage in to further their own respective interests. Behavioural games such as *price cutting*, *low balling*, *audit premiums* and *audit switching* has different effects and implications depending on the size of the auditee and the audit firm.

IV.C.1. Price cutting and low balling

Price cutting is a tactic practiced by audit firms where they offer relatively lower fees in the initial year or the first few years of the audit with the hope of recovering the initial loss in future engagements with the client (AICPA, 1978). The audit firm cuts fees in order to retain the audit client. Simon and Francis (1988) studied 226 firms and found an average discount of 24% in the initial year and continue at reduced levels for the next two years and then diminished.

There is no research to suggest that *size* of the audit firm or the client directly affect the extent of the price cut. Instead the small client has a reduced price (in relation to larger clients) due to small firm *diseconomies*. Since there is a *price premium* charged to smaller clients, the client's net price cut is significantly reduced (Palmrose, 1986; Simon and Francis, 1988). All things being equal, the smaller client is disadvantaged by their *size* as they are charged a *price premium* to engage the services of large auditors. These clients will have to rely on any of the three following factors in order to receive any price cut (Ettredge and Greenberg, 1990) and these include:

- *the client's financial health*- since audit firms cut their initial prices in the hope of retaining the client, the price cut or low ball for the initial year will be more for a financially sound client as opposed to a client who may not financially survive the next few years (see DeAngelo, 1981)

- *industry expertise*- there is no consensus on the issue of the auditor having expertise in a given industry. On one hand the expertise could indicate a faster and efficient audit indicating a greater price cut, and on the other hand the expertise could enhance the auditor's reputation and offset the price cut with a price premium (see Francis and Stokes, 1986).
- *Number of bidding auditors*- In a very competitive environment where there are a large number of bids for a particular audit engagement for tender, it is expected that the winning bidder will give the greatest fee cut (see Beck and Barefield, 1986; Fisher, 1987).

IV.C.2. Audit price premiums

The opposite action of *price-cutting* is *price premiums*. It is not *oligopolistic* profit from market concentration that causes price premiums but rather it is the firm's *brand name reputation* (Craswell *et al.*, 1996). Larger audit firms are able to charge premiums because they are said to give a higher quality audit than the smaller firms (Dopuch *et al.*, 1980; 1982), and are more independent than smaller audit firms (DeAngelo, 1981) and in order to maintain this reputation they undertake more powerful audit tests (Simunic *et al.*, 1987). As a result of such perceptions, these audit firms are able to charge a *premium* for their services as they realise that the client's best interests are served when their financial statements audited by a reputable firm (Firth, 1993).

Audit firms do tend to discriminate according to size. Studies conducted by Simon and Francis (1988) and Palmrose (1986) show that *big eight* firms command *price premiums* are charged to smaller clients. Such price discrimination is justified by research of Francis and Stokes (1986) who found that small client *diseconomies* were the reason for the premium. But it would not be unreasonable to speculate that the real reason of not charging larger clients the *premium* is to keep their business.

IV.C.3. Audit switching

It is the prerogative of the audit client to change auditors. The *size* of the audit client and audit firm does have an impact on audit switching issues, which are subsequently reflected in audit fees. If the audit client is large and growing then they may need to switch auditors who are more technically capable of conducting the audit (Francis and Wilson, 1988). This will lead to higher audit fees due to the *product differentiation* and audit fee premiums discussed above. On the other hand, if the audit client is financially distressed then regardless of its size it is most likely to *switch* auditors for the reason of reducing audit fees or gaining a favorable audit opinion (Schwartz *et al.*, 1985). Whatever the reason of why the client wants to switch auditors, studies by Ettredge and Greenberg (1990) show that audit clients experience an increase in audit fees if they switched to *large* audit firms (and vice versa).

IV.D. Implications- audit brand names!

What we have is a competitive market where there are the elitist big six audit firms who rely heavily on their *brand name* reputation to be able to charge audit premiums. Brand name reputation is so important to audit firms that a number of audit firms in New Zealand who were subsidiaries of the big six changed their names to the names of their parent owners in order to *free ride* off their brand name reputation capital (Firth, 1993).

IV.E. A comment on previous research on audit pricing

When sifting through the many journal articles that we have collected to conduct this literature review, the greater majority of the research used *positivist* methodologies. Such methodologies include the use of regression analysis to identify independent variables that attempts to explain the dependent audit fees, empirical surveys, or cross sectional analysis etc. Such techniques hope to *explain* why entities act the way they do in the process of setting audit fees. As explained in the first section of this section, *positivist* methodologies in audit pricing research are not, without their limitation. For example, the above literature review suggests that there are multiple variables that influence the dependent (fee) variable and this makes interpretation of the research confusing. The research may be able to indicate the *strength* of the relationship between the *dependent* and *independent* variables but we may not always be certain of what is the *dependent* variable. That is, we have two variables but how do we know which variable is affecting who? Moreover, *multiple regression* does not tell us which of the independent variables have the greatest influence on the (dependent) audit price. Additionally, there may be a strong correlation between the audit price and a given independent variable, but such a relationship may not be *plausible* because there is yet another unknown intervening factor that is causing this strong correlation. For example, it may appear that the auditor size has a strong positive influence on audit fees when in fact it is the poor economic climate that is making this relationship so strong.

Previous research into audit pricing is *reductionist*, because researchers over simplify the factors that explain an audit price. It would seem to a great extent, audit price is determined by the *size* of the auditee and the audit firm. But these models only distinguish between large (big 6) and small (other firms)- surely there are other *degrees* of size?

The previous literature has not yet been bold enough to provide a *model* that claims to have a formula where the independent variables can be imputed, subsequently manipulated in order to determine a quantitative value for the audit fee. The positivists recognise their limitations, as far as they can go in their analysis in multiple regression models. For reasons mentioned above, *multiple regression* is not adequate, this is because audit pricing may be more complicated than this.

There is a political environment that needs to be acknowledged here, and previous research has attempted to account for it. The literature had the auditor and the auditee play their own respective games such as ‘audit switching’, ‘low balling’ and ‘price cutting’ etc. in order to influence the audit price. But people need to be identified and understood. People in the various organisational structures that will be identified later in this monograph owe their livelihoods to the audit fee determined. Political players in the *auditing board game* all have political interests and ambitions that would be too difficult to express in quantitative terms. But an understanding of the way that the players who have a stake in the audit fee in addition to the positivist research discussed above would be more enriching and interesting from a research point of view.

In addition, the previous research has neglected to account for all the players within the audit pricing discourse. That is, there is more to audit pricing than just the audit firm and the audit client. How about considering the auditors, government agencies, audit profession and external parties? Do they have an effect on audit pricing that we have neglected to account for?

In this monograph, semiotics will attempt to apply techniques that may help the researcher gain a richer understanding of how the audit fee is *really* determined.

IV.F. Alternative Methodologies- why have they not been applied?

From our investigation, all the research undertaken in audit pricing has been from a *positivist* perspective. The references used in the literature review show journals such as *The Accounting Review*, *Auditing: A Journal of Practice and Theory* and *The Journal of Business Finance and Accounting*. There are many other journals of this nature and in our opinion such journals exhibit a *positivist* bias. These journals may publish articles which may discuss alternative methodologies (for example, Chua, 1986) but we are yet to see any alternative methodologies demonstrated in any research problem. It would seem that accounting research undertaken utilising alternative paradigms is scarce and the larger mainstream journals may avoid publishing such research for the fear of being labeled radical, subjective or left wing. This may be unfair and we cannot prove that such journals are systematically refusing to publish alternative methodologies. Other journals do publish alternative research methodologies (such as *Critical Perspectives on Accounting* and the *Accounting, Auditing & Accountability Journal*) but there is yet to be any application to audit pricing. The reason why the *positivist* approach is dominant in the literature review is because researchers tend to build upon the work of their predecessors who identify key variables and ideas that are expanded in future research under a positivist methodology. From a researching perspective, it is a risk to apply alternative research paradigms to audit pricing. That is, risking terms of being too radical or unscientific. But the alternative path, using semiotics as our guide is the passage that we wish to explore.

Therefore after considering the unacceptable research methodologies that were applied in the literature review we have outlined for audit pricing above, we plan to use semiotics to discover if any new light can be shed on the problem of audit pricing determinants. To our knowledge this will be the first time that semiotics has ever been applied to audit pricing.

V. A Semiotic Approach to Audit Pricing

This section follows on from the literature review conducted in the previous section. The first section of this section considers what semiotics has to offer the discourse of audit pricing. We then have a change of pace and discuss the importance of communication in our semiotic analysis of audit pricing. Communication is especially important because we are dealing with the *interactions* between a number of parties who as a result of such interactions can induce *change* through shared meanings. The final section of this section gives a brief introduction of the six players in the audit pricing discourse who interact and communicate with each other. Such an introduction to these players is helpful before we undertake a semiotic analysis- especially for those people unfamiliar with the practice of auditing.

V.A. What can semiotics do for audit pricing?

The literature review suggests that the audit firm and the audit client possess specific characteristics (size, risk and complexity) that determine the audit fee. This may be true to a certain extent, but there are also *interactions* that take place between these interest groups. There are negotiations, conversations, struggles for power, ambitions and egos that need satisfying. What a semiotic analysis hopes to do is reconcile the social processes and the more detached technical processes of audit pricing. As the semiotician is an interpretive theorist, it is not his or her intention to provide a clear set of answers of what actually determines audit pricing for the purposes of future prediction. Rather the semiotician will put forward a number of ideas that will be useful for those interested in audit pricing to develop an appreciation for factors that cannot be *quantified*. Hence what we are demonstrating is a methodology of researching the discourse of audit pricing. The answers put forward in the analysis are

possibilities and we do not assert that they are the right answer. Semiotics is not about finding the right answer it is about shedding some new light on a problem so that the right solution will eventually be found.

V.B. The importance of Communication

Communication is an integral aspect of semiotics and we could not discuss semiotics without including this section. The concept of communication is quite diverse as it involves a variety of behaviors, processes, and technologies by which its meaning is transmitted or derived from information (Strate, 1995). Communication involves a wide range of activities including conversation, electronic data transfer, emotional impact of a work of art, a gesture, a facial expression or whatever. Communication involves at least two parties: the *sender* and the *receiver* or rather the *addresser* and the *addressee*. The process of communication is best thought of as a set of activities involving a sender with the *intentions* to convey information, a medium to carry the information and a receiver who has the means to *interpret* the information (Liebenau *et al.*, 1990:p11).

This monograph will rest on the assumption that communication is a *social* discourse. That is, communication does not occur in a social vacuum because in addition to the physical or technical elements that may be involved, the communication process is also governed by social expectations and norms (Stamper, 1973). The *social context* of communication is important because a communication breakdown will occur if the sender's intentions do not correspond with the receiver's interpretation.

Communication takes place by using signs which has a number of properties which include physical signs, empirics, syntactics, semantics, pragmatics and the social level (Mikhail, 1996; Stamper, 1992). These levels will be discussed in turn over the course of this monograph. Communication is highly relevant to audit pricing since it is continuously demonstrated in the *interactions* between the physical entities in our audit pricing discourse.

V.C. The key players

It would be desirable to identify the key players we shall be dealing with in our semiotic analysis. The following key players are in their broadest terms, and they can easily be broken down into smaller players who are individuals who interact with other individuals from other bodies with the audit pricing discourse. But for the time being we shall discuss each key player and their role in determining audit fees as well as their interests they have in other players that play a part in audit fee determination.

V.C.1. Government Agencies

The Australian Securities Commission (ASC) administers Corporations law in Australia. It administers regulation pertaining to futures, securities, takeovers, company regulation and compliance to audit standards. The ASC has the power to take action to recover damages or property or to press criminal charges. The legislative interests of the ASC extend as far as the establishment of the *Companies Auditors and Liquidators Board* (CALB) who determines whether auditors have breached the corporations law. As such they have the power to enforce penalties such as cancellation or suspension of an auditor's registration, restrictions on their conduct or an admonition (Gill *et al.*, 1993).

The ASC provides this oversight function in order to serve the interests of external users. The role of the ASC has become increasingly important in the present regulatory environment as some would say that this body was established in response to the epidemic of corporate collapses during the 1980's. The auditors were held to be a major contributing factor to these collapses as their services could not reveal the warning signs the community expects to be detected (Walker, 1993). The ASC would only be interested in *audit fees* if the actions of the auditors breach the Corporations Law (Deis *et al.*, 1992).

The government also acts through parliamentary legislation, which can constrain the activities of auditors, audit firms and audit clients alike. Later in the semiotic analysis, the *Fair Trading Act (1987)* is used as such an example.

V.C.2. *The Audit Firms*

The audit firms are made up of auditors who sell audit services to clients. An engagement partner is appointed responsible for an audit and it is their signature, which goes on the engagement letter. The firm's services traditionally include auditing but presently include *non-attest* services such as taxation, management consulting and information technology. It is convenient to distinguish audit firms by *size*. That is, the audit market distinguishes audit firms into the *big six* and non *big six* audit firms.

The big six accounting firms were described in the literature review above. The big six accounting firms include: KPMG, Coopers & Lybrand, Ernst & Young, Price Waterhouse, Arthur Anderson, Deloitte Touche & Tohmatsu. All other firms are non-big six firms and will be referred to as the *smaller* firms.

V.C.3. *The Audit Clients*

The audit clients are the customers of the audit firms. They employ the professional services of the auditors of the audit firms because they may be required to by law to have their accounts audited. Moreover they want to give confidence to shareholders and other interested external report users that the accounts have been legitimately scrutinised by an independent professional. The audit clients have a direct interest in the audit pricing model and it is the company management's responsibility to employ an auditor at the *right* price. The audit market is very competitive and it is common practice for the audit client to open their audit for tender and hence subsequently selects the bid that meets their needs. If the audit fee is a major factor then it would be expected that the lowest bid will win the contract. In a large company it is common for the management of the company to establish an audit committee to deal with audit matters.

V.C.4. *The Audit Profession*

In Australia, the two professional bodies that exist for accountants (auditors) are the *Australian Society of Certified Practising Accountants (ASCPA's)* and the *Institute of Chartered Accountants in Australia (ICAA)*. This is what is referred to as the accounting profession. The mission of the society expressed in its 1991 annual report is

“...to support, protect and advance the character, status and interest of the accountancy profession generally and particularly of accountants being members of the society.”

The society and the institute provide a broad range of services to its members such as professional and technical statements, a code of ethics, an education program for professional development, a

member's handbook, libraries and a monthly journal. Furthermore the professional bodies also have disciplinary measures for those members who breach standards and professional conduct (Gill *et al.*, 1993).

The internal auditors also have their own professional body: The *Institute of Internal Auditors Australia* (IIAA). This professional body has similar features to that of the ICAA and the ASCPA's. For example the IIAA has internal auditing standards and a code of ethics for its members to follow.

V.C.5. *The Auditors*

The auditors are the individuals that appraise the financial statements of a company. There are three types of auditors: independent auditors, internal auditors and government auditors.

V.C.5.1. *Independent auditors*

In respect of the audit client, the independent auditor is generally referred to as the *external* auditor. These auditors can be sole practitioners or be employed by an audit firm. The external auditor is expected to be *independent* when conducting an audit of the client. External auditors have to be appropriately qualified in accounting or commercial law and be registered with the ASC (Gill *et al.*, 1993).

For the purposes of this monograph we will assume that independent auditors work for an audit firm and hence they are answerable to the engagement partner.

V.C.5.2. *Internal auditors*

Internal auditors are employees of the entities they audit. The internal auditor is involved in all phases of the audit cycle and their work generally supplements the work of the external auditor (Gill *et al.*, 1993). Internal auditors may be answerable to representatives from the *audit committee*.

V.C.5.3. *Government auditors*

The Australian National Audit Office (ANAO) employs government auditors as well as the offices of the Auditor-General of Australian states and territories. The ANAO has the task of auditing the government departments, government enterprises and their subsidiaries (Gill *et al.*, 1993). The government auditors will be excluded from the semiotic analysis conducted in this monograph.

Generally speaking, the auditors are interested in maintaining their *professional status* within the community and has been enacting a system of self regulation in order to prevent any possibility of an increase in regulation from the State (see Gaa, 1991; Walker, 1993). The profession must therefore be *seen* to have the society's interests at heart and to extinguish any suggestion that auditors are primarily motivated by audit fees.

V.C.6. *The External Parties*

We have chosen not to use the terms 'public interest', 'society' or the 'community' as there are sections of the wider community that would have no material interest in the disclosure of an audit report from any company. The term 'external users' is less misleading and it defines various interest groups who have an interest in the audit report from the company. If we are referring to audit reports *per se* then external users cover a vast number of interested parties. According to SAC 2, such parties include resource providers such as shareholders and creditors, recipients of goods and services, such

as: customers. Other interested parties may include the ASC (*Australian Securities Commission*-discussed separately), as well as other parties interested in the financial condition of the company such as suppliers, media and trade unions. If we are specifically referring to audit fees then the shareholders and creditors would be most interested as their resources are entrusted into the management's stewardship (Henderson *et al.*, 1994).

The wishes of the external users are served by the ASC to the extent that an independent auditor is required every year to audit the accounts of the company (client) as per sec 332 of the Corporations Law (1994) in Australia. A Company in accordance with its own subjective criteria nominates the auditors. Generally speaking, one audit firm is the same as another to external users who are confident that the audit profession is admitting auditors that are competent in undertaking the audit.

Hence, with regards to audit price, the interests of external users are that they are concerned with the opinion from competent auditors as this provides them with the assurance they need to rely on the financial statements to facilitate effective decision making. But they are also interested in the audit fees if they have a material effect on company profits.

V.D. Conclusion

This section has given us an introduction of the parties that interact with one another to determine audit fees. It is argued that a semiotic approach will shed some new light on audit pricing determinants by undertaking a semiotic analysis of the interactions involving these six parties.

VI. Stamper's Semiotic Framework

The basis for our framework in applying semiotics to audit pricing is strongly influenced by the work of Ronald Stamper. Stamper's work of semiotics revolves around solving problems in information systems in microeconomic environments. His work, *Information- in Business and Administrative Systems* published in 1973 was a major treatise in semiotics. This work saw semiotics split into four levels: pragmatics, semantics, syntactics and empirics. A work which adapted, the ideas of Stamper came from Liebenau and Backhouse (1990) who were students of Stamper at the London School of Economics and Political Science (LSE). Liebenau and Backhouse outlined the application of Stamper's levels of semiotics in their work: *Understanding Information*.

Stamper (1992) had introduced two additional levels to the semiotic framework in the form of the social and physical level, in order to fully account for the properties of signs.

The reason why Stamper's framework is chosen as the basis of a semiotic application is because we believe the sign properties theorised in his works can provide much insight and flexibility in analysing the *interactions* between the parties involved in the discourse of audit pricing.

VI.A. Influences of Stamper's approach

Stamper's approach is very interesting, but we would like to take this opportunity to discuss the influences of Stamper's approach on semiotics. In our opinion, Stamper has little use for Saussure and his thoughts on what role signs play in society and language. The Stamperian approach leans more towards Peirce's' model of semiotics which focused on the logical aspects of signs. This is to be expected since Stamper applies his model to information systems which encompasses a wide variety of systems which may include legal and administrative systems.

Recalling previous sections of this monograph, Peirce's definition of signs included three attributes:

- some *physical* representation,
- something to which it (the sign) refers,
- somebody able to *interpret* this relationship

Stamper may feel this *representational triangle* does not capture all the aspects of the semiotic framework and accordingly Stamper may have been inclined to create a semiotic framework by means of semiotic levels which may capture all such elements.

VI.B. The Semiotic Levels

Communication can only take place via the use of signs (Liebenau *et al.*, 1990:p13). These signs have a number of properties which are adapted from the ideas of Stamper (1992). According to Stamper, signs are best observed from a number of different levels from which we can apply a number of different analytical tools for the purposes of reflection and problem solving. These levels are as follows: physical signs, empirics, syntactics, semantics, pragmatics and the social level. Looking at signs at each of these different levels encompasses ideas from many different disciplines (Stamper, 1973:p18). Semiotics is not a subject in itself *per se* but rather it gives the researcher the opportunity to apply an interdisciplinary approach which we feel is a more effective and rewarding method of analysis.

Figure 2 below reveals the types of signs that exist relevant to each of the levels of semiotics. The properties stated in each semiotic level are not exhaustive, as this figure merely serves as a useful guide in establishing some idea of which sign property is indicative of the particular level in question.

<p>SOCIAL WORLD beliefs, expectations, commitments, contracts, law, culture, etc.</p> <p>PRAGMATICS intentions, communications, conversations, negotiations,</p> <p>SEMANTICS meanings, propositions, validity, truth, signification, denotations,</p>	<p>S O C I A L</p>
<p>SYNTACTICS formal structure, language, logic, data, records, deduction, software, files,</p> <p>EMPIRICS pattern, variety, noise, entropy, channel capacity, redundancy, efficiency, codes,...</p> <p>PHYSICAL WORLD signals, traces, physical distinctions, hardware, component density, speed, economics,</p>	<p>T E C H N I C A L</p>

Figure 2 - Socio-technical Semiotic Levels [Adapted From Stamper (1992)]

VI.C. An elaboration on the semiotic levels

The basis of the research of this monograph on *audit pricing* rests on the semiotic framework according to Stamper. Originally Stamper published his most influential work in 1973 that covered all the semiotic levels except for the social and the physical levels. The semiotic approach incorporated in this monograph shall address the physical and social levels that were later introduced in Stamper (1992). Stamper applied semiotics to computer based information systems (CBIS) because he was concerned with the technical aspects of the systems and felt that semiotics could give analysts insight into the information these systems signify.

Stamper asserts semiotics offers a whole new methodology for the analysis and design of information systems. Semiotics challenges the ‘classical methodologies’ (ibid. p22) which sees the world as an *objective* and *detached* reality which is represented by information. Stamper (1992) argues that it is the analyst’s job to move *beyond* the technical physical aspects of information systems and move toward establishing the *meanings* and the *purposes* of such information instead of leaving this task to end users. To achieve this, Stamper argues that the *objective* notion of reality should be abandoned and instead a *subjective* view of reality should be embraced. That is, we can no longer assume that information has passively entered the information system to be manipulated by software to turn this data into information but rather reality is constructed by informal culturally based information systems.

Stamper (1992) does not go into any great detail as to why he added the *physical* and *social* levels to his semiotic framework (this is because this was rationalised in his earlier works). But, Stamper does indicate that the physical level was added because it illustrates the physical means by which signs are represented and processed. The social level was added because signs ought to have explicit recognition of the social dimension of what these signs represent. Let us briefly elaborate on each of the semiotic levels in turn.

VI.C.1. The physical signs

The physical world attempts to model the *physical* means of representing signs. The physical world model identifies the physical properties of objects (marks) and events (signals). Signals and marks are often referred to as *tokens* and hence this level is concerned with the physical means of creating such tokens. Attributes of physical objects such as size, volume, cost, capacity and weight etc. are all relevant to inquiries at this level. The physical world is readily accessible to our senses and it is important to be aware of this in any semiotic analysis at this level.

At face value, this level is difficult to apply to audit pricing since Stamper (1992) has a focus on hardware configuration of computer information system design. For the purposes of our analysis, we have adapted Stamper's (1992) framework and altered it. We assert that each of the parties in the discourse of audit pricing is a *physical* entity - or to be more exact the representative or agent from each respective entity is the *physical* device.

VI.C.2. Empirics

Empirics, is concerned with *communication* issues relating to *signs* produced within an information system. That is, an issue that would be relevant to this level is that signs produced ensure clear and unambiguous communication from the sender to the receiver. Empirics considers the transmission of signals and their coding and decoding by interpreters (Stamper, 1973). Empirics is not concerned with the grammar an actor may use (or misuse) or the intentions behind a given act of communication, instead empirics is concerned with the design of efficient communication channels in which actors

may send or receive signals reliably. Hence it is most important that the levels of syntactics and empirics are not confused.

Empirics, considers such issues of how to encode and decode signals for use in communications. Empirical analysis is easily applied to routine, repetitive data handling tasks that needs to be encoded for faster and more efficient transmission. Associated issues are the channel capacity of the communication media, the speed of transmission as well as the presence of *noise* in the communication system.

Since we are not dealing with computer information systems we have to adapt the empirical level of analysis to the discourse of audit pricing. Stamper had outlined that empirics can be analysed from the perspective of pattern, variety, noise, entropy, channel capacity, redundancy, efficiency and codes. At face value it would seem impossible to apply such empirical aspects to audit pricing. But this is not true. As mentioned previously, semiotics is extremely flexible and hence the definitions of pattern, variety, noise etc. does not necessarily have to adhere to CBIS definitions. Instead if the researcher thinks long enough, such phases can adapt to the context of audit pricing with little difficulty.

VI.C.3. Syntactics

Assuming that the *physical* and the *empiric* levels are designed effectively, we can now move to the *syntactic* level. The syntactic level is concerned with the *formalising* of the way we represent information. By formalising we mean providing the rigor to the language in *signs* we use subject to the constraints of vocabulary, grammar and rules which govern the sign's use. *Syntactics* is concerned with the complexity and structural richness of the signs within the semiotic system and the constraints that govern the language of a given social discourse are indicative of the *complexity* of the sign system.

Languages are a central means of expression of the signs used in an information system and syntactics is used to assist the researcher in studying the design of the information system. Stamper (1973) looked at *natural* and *formal* language systems, recognising that both play an integral part in the analysis of information systems at a *syntactical* level. *Natural* languages are languages used for everyday communication and as such are complex in structure since they reflect cultural contexts. In addition, *formal* languages are much simpler constructs used in circumstances where *precision* is necessary and exhibit a finite set of vocabulary, grammar and syntax. A striking example of a *formal* language is the language of mathematics, more specifically the branch of algebra.

The version of syntactics that we will be utilising is different from the version outlined in the preceding paragraphs. The version we will be adopting does not emphasis the *linguistic* aspect of syntactics. Furthermore, since our model will steer away from the using CBIS as a metaphor to demonstrate syntactics, we will only use some of the syntactic indicators used by Stamper (1992). Hence, we will not be considering data or software but may be flexible enough to consider records or files in our analysis. In essence the version of syntactics applicable to audit pricing research is to consider the *rules* that govern the *relations* between the physical entities within a given social discourse. For example, if we look at an employee and an employer then the *syntactic* rules could include employment contracts, union awards, superannuation agreements and so on.

VI.C.4. Semantics

Since we are dealing with diverse signs and our own cognitive processes there cannot be any clear *right* or *wrong* answer. Instead we assess the signs we can identify and critically scrutinise these signs

(Stamper, 1973). That is, under the semantic level we analyse the *connections* that entities make between the signs they use and their subsequent behavior or actions.

Semantics is concerned with the *meaning* of acts of communication, hence we are looking at what signs *refer* to. Since semantics can be linked to *meaning* then the most desirable situation is when we can take signs and *consistently* know its meaning or to what the sign is referring to. But this situation would rarely (if ever) occur when dealing with ‘complicated’ situations. It is common for a communication ‘breakdown’ to occur at the *semantic* level because confusion occurs when trying to interpret the meaning of the sign. Good communication requires the receiver to consistently give the appropriate *signification* of any signs the sender utilises. A communications breakdown presents real problems for the interpreter in the physical world when such an interpretation is *crucial* to the success of the design of a computer based information system (Stamper, 1973). Despite the fact that audit pricing is not a CBIS, semantics still bears the same application to audit pricing. That is, in essence, semantics is the meanings associated with intentions- consistent with Stamper’s discussion.

VI.C.5. Pragmatics

Pragmatics takes into account the general *culture* and the broad *context* of communication. That is, *pragmatics* concerns the relationships between *signs* and *behavior*, thus at this level it is possible to draw upon social science and humanities disciplines (Stamper, 1973). This level would see the sender of information thinking about sending information to the receiver regarding policies, value judgments, rewards and sanctions and so on taking into account the *context* in which the information is sent and the sensitivity of the receiver to such signs (Stamper, 1973:p19). The Stamper framework sees pragmatics to include intentions, communications, conversations and negotiations and such terms can be applied to the interactions between the parties within the audit pricing discourse previously identified.

VI.C.6. The Social Level

The social level is looked at in Stamper (1992) and the existence of this level is justified since no sign can be properly understood without regard for its social consequences. The social world consists of rules, norms, beliefs, customs, values and traditions that shape a common social reality. The social level is concerned with the social consequences of signs produced by physical entities. The social level is an important component of an information system and the rules, expectations, norms and so on are continually evolving.

VI.D. An application of Stamper’s levels to audit pricing

The objective of applying semiotics to audit pricing is to determine if any new insight can be gained in respect of the determinants of audit pricing. As outlined in the literature review, the determinants of audit fees were generally dependent on the *size* of the audit firm and the audit client. It is hoped that a semiotic analysis will reveal additional determinants that the literature review did not consider. A semiotic approach is a very broad methodology and the analysis undertaken in this monograph is far from complete. Semiotics is an evolving process and changes in response to changes in the physical and social environment.

Let us visualize what the researcher can discover when he or she looks at the six entities in the context of a semiotic analysis in order to determine the determinants of audit pricing. The following diagram depicts a set of six boxes in which each box represents a sign property of Stamper’s semiotic framework. On top of this pile of boxes is the *social* box with the flag representing the *sign* of audit

pricing. The flag comes from the *social* box because audit pricing is a social discourse. Therefore, from this diagram we can derive that the six sign properties (or levels) contribute to establishing the determinants of semiotics. Each sign property is important and *interacts* with one another to contribute to describing the determinants of audit pricing.

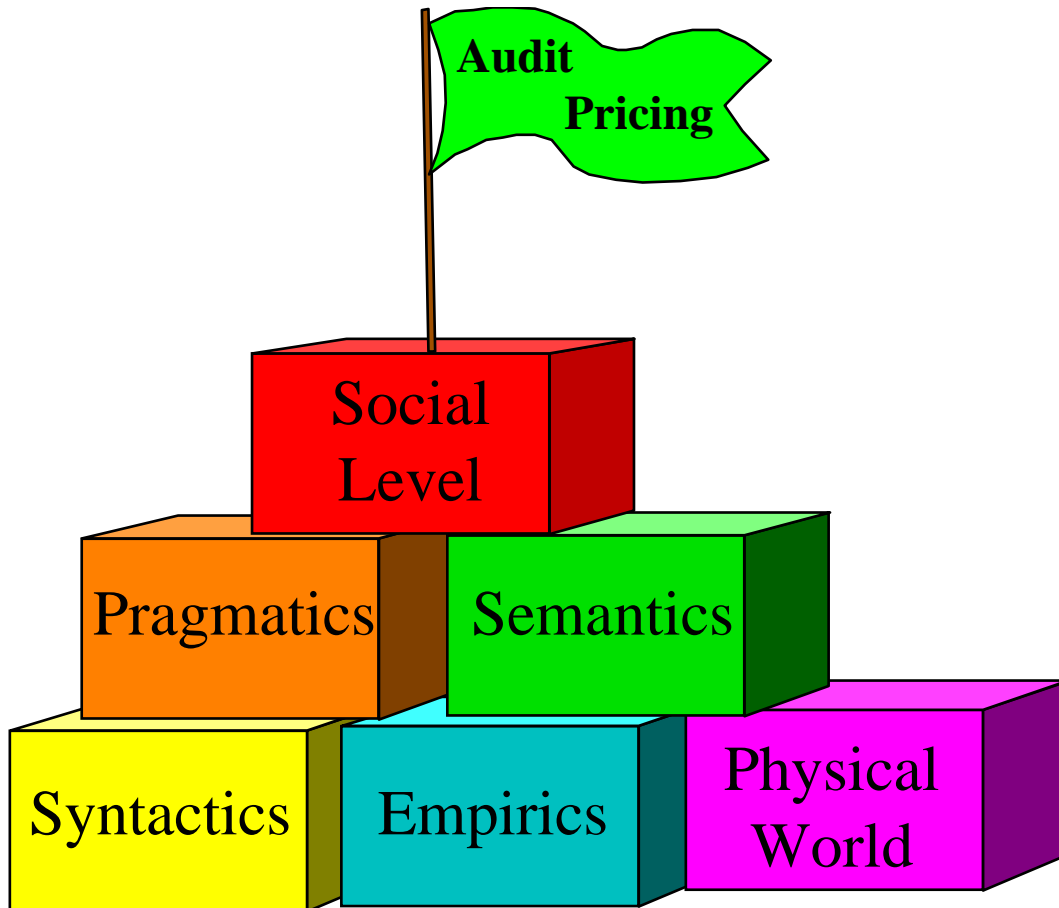


Figure 3 - Sign Properties Interactions and Audit Pricing Determinants

Stamper had used the levels of semiotics in order to reconcile the physical world and the social worlds of a CBIS. The approach that Stamper has adopted tends to ignore the *interactions* between the entities and it is in this aspect that we shall look at in detail in our analysis of audit pricing. The matrix diagram (table 1) below shows a template of how a semiotic analysis may be undertaken under Stamper’s regime. This analysis has the objective of reconciling the physical and the social levels for each entity in the audit pricing discourse. Notice how each party is independent and there is no opportunity for analysing *interactions* between the entities involved.

SOCIAL	↓	↓	↓	↓	↓	↓
PRAGMATIC	↕	↕	↕	↕	↕	↕
SEMANTIC	↕	↕	↕	↕	↕	↕
SYNTACTIC	↕	↕	↕	↕	↕	↕
EMPIRIC	↕	↕	↕	↕	↕	↕
PHYSICAL	↑	↑	↑	↑	↑	↑
	AUDIT FIRM	AUDIT CLIENT	AUDIT PROFESSION	AUDITOR	GOVERNMENT AGENCIES	EXTERNAL PARTIES

Table 1 - A Semiotic Analysis without emphasis on Interactions in between Parties

The ideas that will be proposed in our analysis will focus on the *interactions* between entities within the audit pricing discourse. The idea of focusing on the interactions between entities within a given discourse is directly inspired by the work of Mickhail (1996).

As we are not dealing with a CBIS, we are looking at the discourse from a human perspective. These entities have people, who interact and communicate with one another and hence pass on knowledge to one another. Such interactions between these entities is mediated by the sign properties in respect of the social, pragmatic, semantic, syntactic, empiric and physical levels. In turn we analyse these levels in terms of sign presentation and production so that we can reach an understanding of audit pricing.

VI.E. Reconciling audit pricing with Stamper's semiotics

Applying Stamper's approach of semiotics to the determinants of *audit pricing* is challenging for two primary reasons.

The first reason is that Stamper has projected his semiotic analysis to computer based information systems (CBIS). That is, this approach applies semiotics to the equipment, programs, data, and procedures necessary for the tasks performed on a computer system. The determinants of audit pricing is in essence a social discourse and could not be directly associated with CBIS's. But is the framework of audit pricing an information system? According to Cushing and Romney (1994) an information system is:

... "an organised means of collecting, entering, and processing data and of storing, managing, controlling, and reporting information so that an organisation can achieve its objectives and goals."

It can be argued that the entities within the discourse of audit pricing collectively achieve these functions. Although this discourse is not a microeconomic structure, the entities collectively undertake the functions of an information system that would contribute to audit pricing. Hence the audit pricing discourse does resemble an information system based on the definition above.

The second reason is that Stamper's approach to semiotics is applied to microeconomic perspectives such as an organisation. Audit pricing is a macroeconomic discourse since it involves a number of different organisations all playing a part in determining audit fees. Although the past research on semiotics refers to microeconomic structures, the principles can be transposed to macroeconomic structures.

Research is about trying new ideas and extending semiotics to a macroeconomic structure involving non computer based information systems is an area of the development of semiotic research that could be ventured.

VII. The Analysis and Evaluation

This section outlines the steps that we had taken to undertake a semiotic analysis of the discourse of audit pricing. The steps that we have taken are based on the semiotic levels from Stamper but as for the *sequence* of the steps and the idea of extending Stamper's framework by focusing on *interactions*, these were mostly from the work of Mickhail (1996). The steps see the researcher:

- (a) identifying the parties,
- (b) considering the sign interactions of *two way* combinations of parties,
- (c) constructing interaction tables,
- (d) performing *Party 1- Party 2* analysis,
- (e) evaluating this analysis,
- (f) searching for new determinants of audit pricing, and
- (g) constructing ontology diagrams in order to reconcile the *interactions* between the parties and the *ontological* structure they interact with at each semiotic level.

Over the course of this section we will expand on these steps and provide a rationale for undertaking these steps.

VII.A. The Proposed Analytical Steps

Step 1: Identifying the Parties

The first step is to identify the parties involved within the audit pricing discourse. This appears to be an easy step but the difficulty is to identify all the parties involved. If all the parties are not identified, then the semiotic analysis will not be as complete as it should be. The six entities that we can identify are:

- the audit firm
- the audit client

- the government
- auditors
- audit profession
- external parties

These parties listed above have been outlined in preceding sections of this monograph. We are confident that we have identified all the parties, but perhaps there are more. What also has to be born in mind is that each of these parties can be divided into smaller physical entities. For example, the audit client is made up of shareholders, the board of directors, audit committees and managers. And external parties can be divided into shareholders (of other companies), unions, creditors, suppliers, customers etc. A major limitation in identifying the parties listed above is that these parties are not mutually exclusive. That is, these parties tend to overlap somewhat because some entities are made up of other entities which are also under analysis. Such a limitation is seen in the *interrelationship* between the auditors, the audit firms and the audit professional bodies. The auditor is a member of both the professional body as well as an employee (or a partner) of the audit firm. We acknowledge that a semiotic analysis will be easier for a group of mutually exclusive parties but in this during some parts of our analysis we found this to be a difficult task.

Step 2: Considering the sign interactions between each two entity combination

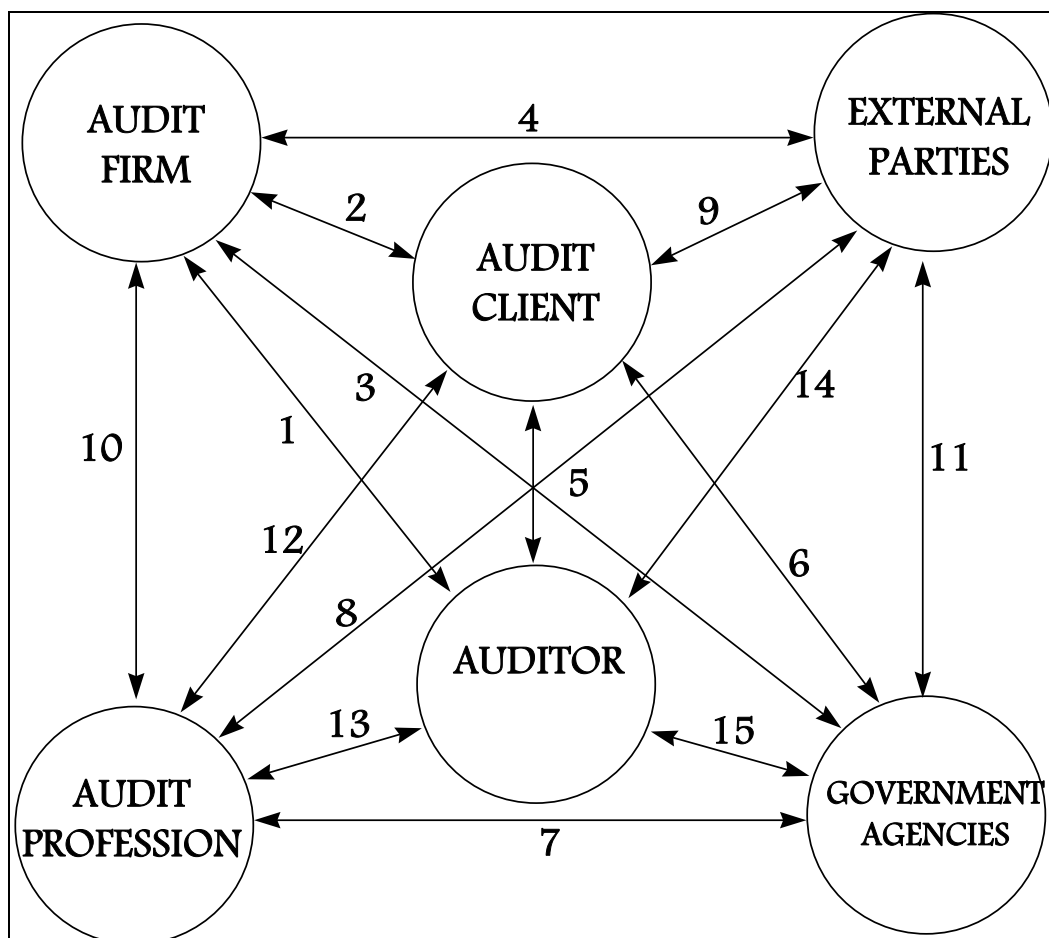


Figure 4 - Possible Interactions of the Parties within the discourse of Audit Pricing

Given that we have identified the entities involved in the audit pricing discourse we shall now consider the *interactions* between the parties at each of the semiotic levels. The study of these interactions may appear to be a cumbersome task, but this task is important because is the only way to gain any meaningful insight into the forces that drive audit fees.

We have already identified the parties that are going to be used in the semiotic analysis. This has implications for *figure 4* featured above. The six parties identified gives us fifteen combinations for interactional semiotic analysis. Figure 4 above shall be the template for the analysis of the following combinations of entities:

1. audit firm <----> auditors
2. audit firm <----> audit client
3. audit firm <----> government
4. audit firm <----> external parties
5. audit client <----> auditor
6. audit client <----> government agencies
7. audit profession <----> government agencies
8. audit profession <----> external parties
9. audit client <----> external parties
10. audit firm <----> audit profession
11. government <----> external parties
12. auditor profession <----> audit client
13. audit profession <----> auditor
14. auditor <----> external parties
15. auditor <----> government agencies

Step 3: Setting up the interaction tables

This is not a compulsory step but it may be a good idea to draw one as it can give the researcher a visual perception of some of the issues that may be covered in the in-depth analysis in step 4. A template of this table is displayed in *table 2* below and some examples of such tables that we had used are placed in *Appendix B*. The idea of this table is basically to ‘brainstorm’ for ideas. The table initially constructed may look completely different from the actual analysis subsequently completed.

PARTY TWO	PARTY ONE						
		Physical	Empiric	Syntactic	Semanti	Pragmati	Social
	Physical						
	Empiric						
	Syntactic						

	Semanti						
	Pragmati						
	Social						

Table 2 - A Semiotic Analysis Matrix Template for Interactions between Parties

Step 4: Party One - Party Two Analysis

The above step has outlined the *interactions* between each of the combinations of entities. This step will extend step three and will provide an analysis of the *interactions* at each of the semiotic levels. This step is labeled *Party One - Party Two Analysis* can be represented by *figure 5*.which sees the analysis of the interactions between both parties in terms of each of the levels of semiotics.

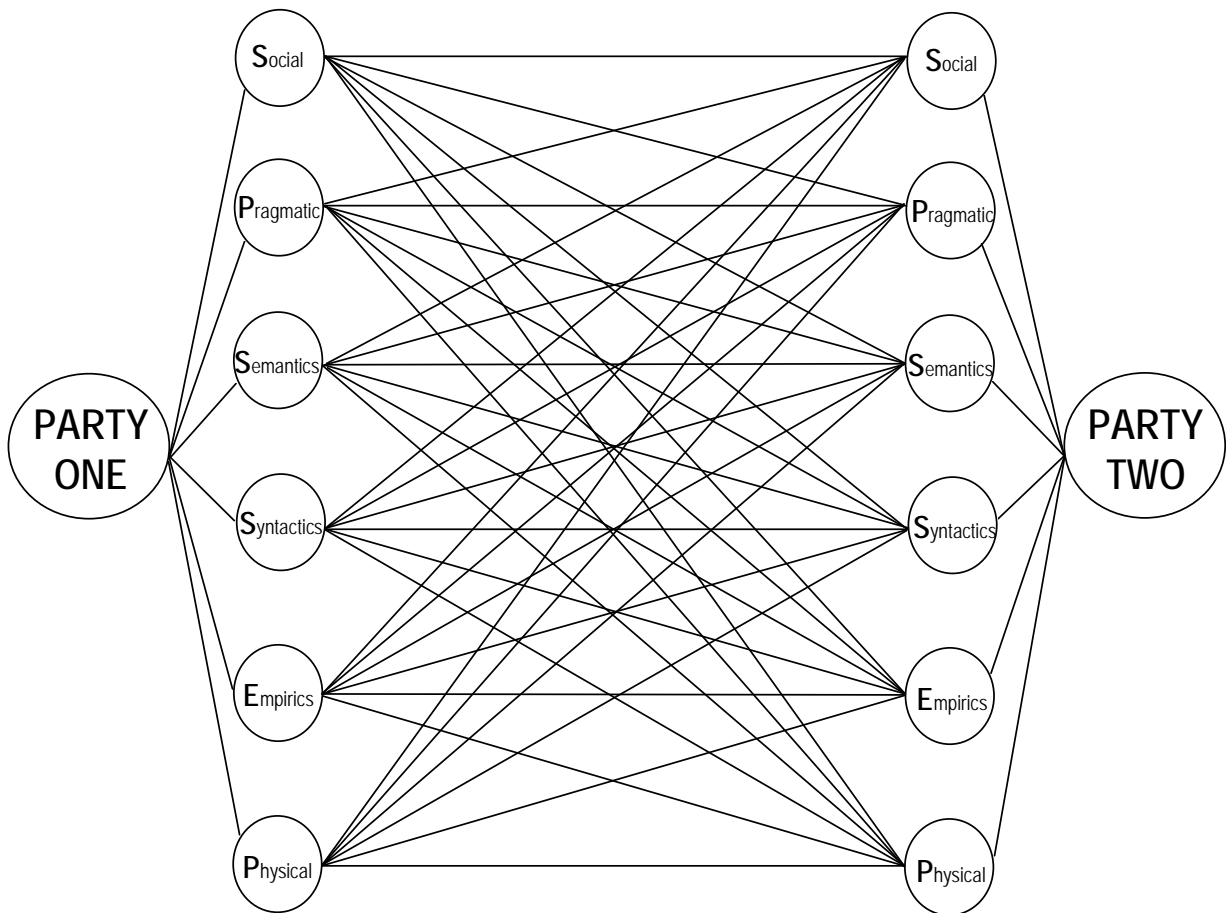


Figure 5: A Diagrammatical Representation of *Party 1 - Party 2* analysis

The above diagram sees the *analysis* of one party's semiotic level in terms of another party's semiotic level. For example, the *empiric* level of party one is evaluated in terms of the different levels of party two:

- Party One (empiric) - Party Two (physical)
- Party One (empiric) - Party Two (empiric)
- Party One (empiric) - Party Two (syntactic)

Party One (empiric) - Party Two (semantic)
Party One (empiric) - Party Two (pragmatic)
Party One (empiric) - Party Two (social)

An important factor that must be born in mind is that the analysis is conducted on a *two-way* basis. This is to ensure a more thorough and complete analysis is undertaken. Therefore, we have to conduct *Party 1 - Party 2* analysis and we also have to conduct a *Party 2 - Party 1* analysis. For example, the *empiric* level of party two is evaluated in terms of each level of party one:

Party Two (empiric) - Party One (physical)
Party Two (empiric) - Party One (empiric)
Party Two (empiric) - Party One (syntactic)
Party Two (empiric) - Party One (semantic)
Party Two (empiric) - Party One (pragmatic)
Party Two (empiric) - Party One (social)

The *social* level is considered at the end of analysis of each level of semiotics. It is in these levels where we may find answers to our quest of finding determinants of audit fees. The actual undertaking of the above 'party one - party two' analysis is too involved to be included as a section in this essay. This is because we have 15 interactions to study and within each interaction between two parties there is a study of their interactions based on five levels on a two-way analysis (with six interactions at each level). Hence the number of *interactions* that have to be considered is a product of the following:

15 combinations of parties x 5 semiotic levels x 6 interactions in each level x 2 (two way analysis) = 900 interactions to consider!!!!

The analysis will see the researcher considering one level of semiotics in terms of another. For example the researcher may be faced with the combination of:

Party One (empiric) - Party Two (pragmatic) [given that *party one* is the audit client and *party two* is the audit firm]

This combination will see empiric properties such as size (or noise, variety etc.) of the audit client being considered in terms of the pragmatic properties such as intentions or communications of the audit firm. Such a combination may yield a useful insight or it may not yield anything meaningful. But the analysis of each and every of the 900 combinations is bound to yield some new idea not yet considered. That is what semiotics is all about.

At this point it would be appropriate to point out that since we are looking at one level in terms of another then the evaluation of common levels [for example: **Party Two (pragmatic) - Party One (pragmatic)**] is meaningless and shall be labeled as 'not applicable throughout the analysis.'

Due to the sheer volume of this analysis, we shall only include the abridged analysis of the determinants we had found in doing such an in-depth analysis.

Step 5: Evaluation of the analysis

After the tedious and time consuming task of analysing the interactions of the parties at each of the semiotic levels then the researcher can evaluate the findings within the analysis. This involves sifting

over the interactions, between each of the 15 combinations at each of the semiotic levels. The ending social level is of great assistance in this task and often (but not always) directly gives the researcher the answer they are after: anything that may affect audit pricing! The analysis is a very slow and painstaking process and the researcher may not always spot all the findings on the first time evaluating the tables. But this labor is worth the effort because new and exiting answers, ideas and insights are extracted through the labyrinth of semiotic tables constructed.

The following paragraphs can be thought of as summaries of the issues, ideas, and ‘new light’ on the discourse of audit pricing.

Combination 1: audit firms - auditors

AN EVALUATION: PARTY ONE (SOCIAL) - PARTY TWO (SOCIAL)

On one hand we have the audit firms who are made up of professional external auditors who audit the accounts of the audit clients who may have internal auditors who perform audit tasks throughout the year and their work may supplement that of the external auditor. But let us focus on the audit firms. In respect to the external auditors, the audit firm (the engagement partner) may believe that they are competent, because of their professional qualifications and training. In addition, the audit firm may feel that the more experience career developed the auditor is, the better they will perform in generating revenue for the firm. The audit firm may believe in hiring the best external auditors, as they are more likely to turnover more fees. This is evidenced largely, by the quality and quantity of the working papers they produce, as these are the working records of the audit process. In respect of internal auditors, the audit firm may believe that part of the reason they are there is because the client may use them as a bargaining tool, in order to lower the audit fee. The audit firm realises that they will have to evaluate the internal audit function to establish whether they can use some of their work to supplement the external audit hence resulting in a lower fee because the external auditors work has been supplemented.

On the other hand we have the auditors: the external and internal auditors. The external auditors may believe that the audit firm is a place of belonging and employment. They may believe that they are in a relationship with the audit firm to *add value* to the firm. In addition, the external auditor realises that their bargaining power will be affected if the audit firm is small as this reduces the opportunities to generate more fees because the client can also take a stand and negotiate with another audit firms. The internal auditor may believe that they are employed partly because they have the potential of lowering the audit fee for the client they work for. The internal auditors may believe that their working papers have to be of a high standard because a favorable evaluation by the audit firm may mean lower audit fees. In addition the internal auditor may believe that the size of the internal audit function could have implications for the audit fee since a smaller internal audit function may not be a ‘quality’ internal audit function. Hence it could be asserted that the *size* of the internal audit function could affect the quality of the clients internal control system and hence may have an influence on audit fees.

Overall the audit firm has two different relationships with the internal and external auditors, and each relationship has different implications on audit fees. It is interesting that the external auditor is a *tool* used by the audit firm and the internal auditor is a *tool* used by the audit client to influence audit fees. Hence, the auditors (whether internal or external auditors) is the entity between the interests of the audit firm and the audit client.

Combination 2: audit firms - audit clients

AN EVALUATION: PARTY ONE (SOCIAL) - PARTY TWO (SOCIAL)

On one hand, we have the audit firms who sell their services to audit clients. There is an inter-play between the two parties that make for some interesting ideas on the effects on audit fees. The audit firm (the engagement partner) may believe that the audit client places great importance on the audit fee they pay the audit client and hence negotiates on the terms of the engagement letter even though there may be an imbalance of bargaining power between the two parties. The audit firm may also believe that the *size* and *complexity* (in terms of *structure*) of the client is relevant in deciding whether to cut fees in order to maintain the contract (see Simon *et al.*, 1988) with the client. In addition, the engagement partner may believe that their audit firm could be threatened with the client *switching* auditors in future engagements in which the fee may be dropped even further.

On the other hand we have the audit client who has their accounts audited by auditors from an audit firm. The management (or audit committee) from the audit client will negotiate with the engagement partner an audit price in which the client may take into account the *size* and *variety* of services offered by the firm (see Schwartz *et al.*, 1985). The audit client feels that the size of the audit firm is important because if the firm is too large then they may charge the audit client an audit premium (see Firth, 1993). Hence the client may believe that they have to be large and a lucrative client (in terms of fee turnover) in order to receive price cuts to fees).

Overall we are looking at a process of *negotiation* between the audit client and the audit firm who use their differences to reach a price mutually agreeable to both parties.

Combination 3: audit firms - government agencies

AN EVALUATION: PARTY ONE (SOCIAL) - PARTY TWO (SOCIAL)

On one hand, we have the audit firms who audit their client and charge them fees for their services. The audit firms (representative) may believe that government agencies such as the ASC are interfering with this process in order to gain some control over the activities of the firm in order to have some influence over audit fees. The audit firms may be fearful of the size and power of government agencies who, for example, operate the *Fair Trading Act* in which under sec 42 has the power to fine partners of an audit firm for 'misleading or deceptive conduct'. The ASC also has power over the auditors these firms employ, which affects their behavior in fee setting activities (more on this later). The audit firms may feel that they have to know in detail the laws that affect them in order they can find ways of avoiding or at least adapting to them as they go about their business. The audit firms have no choice but to comply with the laws of the government even though they may have a self-regulation program in place (especially the larger firms). The audit firms are aware that in response to public demand, future governments may in fact increase the powers of the ASC and hence the firms will be under tighter control.

On the other hand, we have government agencies (the government bureaucrat) which may feel that they have the public's interest at heart. They work in contrary to the *self interest* that the audit firms have in maximising their audit fees and hence set up legal provisions (FTA) that aim to ensure that the firms are not exploiting the client consumer and the wider community through their audit pricing practices. The government may not see the individual firm as a powerful force but rather may see a group of large firms with strong policies of firm regulation as a strong preventative measure of preventing further state intervention.

Overall, the audit firm does operate in an environment where they have government legislation to comply with as they go about their activities of auditing their clients and charging fees. The government may see their laws as an effective *weapon* to increase their control over the whole auditing discourse (which includes audit fees) in the name of the public interest.

Combination 4: audit firms - external parties

AN EVALUATION: PARTY ONE (SOCIAL) - PARTY TWO (SOCIAL)

On one hand, we have the audit firms who sell their audit services to audit clients. Many external parties are stakeholders such as shareholders (probably the most significant stakeholder), suppliers, employees, unions, creditors etc. who have some interest in the opinions of the auditors and the fees paid to the audit firms. The audit firm may believe that the *size* and *complexity* (of interests) of the external parties influence the way in which they engage in communicating with them. They use a variety of media forms aimed (directly or indirectly) at these external parties to assure them of an independent quality audit services, so that they are happier in paying (directly or indirectly) the fee. The audit firm needs the confidence of the external parties or else the external parties may directly lobby the audit client to review or to justify the fee paid to the audit firm.

On the other hand, we have the external parties who believe they are justified in questioning and lobbying the policies and fees charged by audit firms. They may believe that the *size* of the audit firm is important because they may be more powerful and influential and hence may have a greater effect on audit fees. The external parties may also believe that the *intentions* of the audit firms are not honorable and they will use a variety of means through various media resources in order to assure confidence in the external parties. The larger firms especially rely on their *brand name* image in which external parties may believe that it can be used to 'mystify' the weaker external parties into a reluctant acceptance of the *status quo* (see Dyer, 1989).

Overall, the external parties are skeptical of the audit firms, and the way that the firm fights back is to take steps to win the confidence of the external parties so that they will not lobby for change.

Combination 5: audit client - auditors

AN EVALUATION: PARTY ONE (SOCIAL) - PARTY TWO (SOCIAL)

On one hand, we have the audit client (management) who engages the services of the external auditor (engagement partner) and pays them an audit fee for their services. But the audit client realises that there is a way of reducing the audit fee, and this is achieved by having a competent internal audit function. This audit function will reduce the audit fee by doing some of the work that the external auditors (see Gill *et al.*, 1993:p15) would be otherwise contracted to do. The only contingency is that the external auditor has to evaluate and approve of the client's internal audit function. The client may believe that such an interaction between the internal audit function and the external auditors play a role in determining the audit fee. The client may believe that the *size* of the internal audit function as well as the 'quality' of the working papers they produce may contribute positively to the evaluation of the internal audit function hence (possibly) reducing the audit fee. The audit client may most likely see the internal auditor as a *tool* to reducing audit fees and would not hesitate in using the internal audit function in the negotiating process with the audit firm over audit fees.

On the other hand we have the internal and external auditors. The external auditors audit the accounts of the audit client and may charge a lesser audit fee if the client has an effective and competent internal audit function. The external auditor may believe that the internal audit function is important for determining audit fees. The external auditor may believe that the *size* of the client is indicative of the audit fee to be charged as it indicates the nature, scope, length and objectives of the audit service to be performed. And moreover the external auditor may also believe that the size of the client is also indicative of the internal audit function that they may have. That is, the larger audit client is likely to have a larger internal audit function in which a lesser fee may be charged. As part of the evaluation of the internal audit function, the external auditor will consider the cooperation and support given to them by the internal auditors. The external auditors are very likely to consider the internal audit

function in *negotiations* with the client when trying to determine a price. The internal auditors may believe that they are a ‘feature’ of the client company, which can yield a lower audit fee, if they are cooperative, and are of the ‘right’ size (according to the audit firm) and their working papers are of ‘good’ quality. The internal auditor may believe that their audit client (employer) uses them in negotiations with the audit firm (external auditors) in order to hopefully to convince the audit firm to lower the audit fee due to the effectiveness of the internal control function.

Overall we can say that the internal auditors are in the middle of the negotiating table between the audit firm (external auditors) and the audit client in determining an audit fee.

Combination 6: audit client - government agencies

AN EVALUATION: PARTY ONE (SOCIAL) - PARTY TWO (SOCIAL)

On one hand, we have audit clients who are required by virtue of the Corporations Law to engage the services of an external auditor on an annual basis. The *size* of the company is the contingent factor for this rule and in addition the audit client (engagement partner) is also told who can be an auditor and when an auditor can be appointed. This is by virtue of the Corporations Law, which requires larger disclosing entities to engage an external auditor [see secs 327-324 CL]. The audit client may believe that the ASC has a lot of power, which includes the power to suspend the registration of a company or appoint the company an auditor by virtue of a court order [see sec 327]. The audit clients may feel that such measures are in the public interest, but the clients may believe that this is contrary to their interests because they are forced to appoint and pay fees to an auditor they may not be able to employ. As such the audit client may question the intentions of the government in their ASC regulations on compulsory auditing. Is it because of the public interest? Or is it because they want some control of the affairs of both the auditors and the audit clients? (Perhaps in respect to fees?)

On the other hand we have the government through the ASC. The ASC may feel that the audit clients may be burdened with legislation but they may feel that this function in the community is too valuable to be left unregulated. The ASC may also feel that the larger clients are the ones who are most affected by its ASC regulation because they are the ones that are forced to pay the fees. The ASC may justify their position in appointing external auditors because they want the audit client to be accountable to their members and in addition these members form part of the external parties which the government may try to preserve their interests and rights. The ASC has such laws for audit clients because they wish to look after the public interest.

Overall, the relationship between the audit client and the government is one of control from the government. The government through the ASC forces the appointment of auditors and if these laws change then less clients may desire the use of auditors.

Combination 7: audit profession - government agencies

AN EVALUATION: PARTY ONE (SOCIAL) - PARTY TWO (SOCIAL)

On one hand, we have the audit profession. The audit profession in Australia is made up of two professional bodies, namely the ICAA and the ASCPA's. These professional bodies has the power over its affairs in respect to the admittance and the behavior of its members but they do not have the sole power over the standard setting process for auditing standards (see Miller, 1995). The profession develops standards (see Gill and Cosserrat, 1993) in cooperation with the *Australian Accounting Standards Board* (AASB). Due to this the profession is under significant control from this government agency (the AASB) in which the quality of the standards produced may ultimately affect the audit fees charged since there will be implications to how the audit is undertaken and billed. The profession

would see this as interference but they instead of lobbying and demanding full autonomy, they cooperate in this standard setting arrangement so no further public regulation may occur. In addition, the profession has also developed a number of Statements of Auditing Practice (SAPs), Auditing Guidance Releases (AuGRs), audit guides, monographs and ethical pronouncements. These are developed through the profession sponsored Auditing Standards Board (AuSB) and could be used to prevent further state intervention.

One the other hand, the government contributes to the standard setting process through the AASB. The system for the *due process* of standard setting may have been established as a reaction to the epidemic of corporate collapses during the 1980's and hence in the name of the public interest, the government is setting out to control the profession to some degree (see Walker, 1993). The government could see that the audit profession is very large and hence needs to be regulated in the name of the public interest. The government may not fully trust the audit profession and perceives their efforts for self-regulation as a means of preventing extra intervention. The government (through the AASB) may find their powers useful to influencing audit fee setting for reasons mentioned in the preceding paragraph thus maintaining an element of control over the profession.

Overall, the potential for influence of audit fees through the standard setting process is great and should not be ignored.

Combination 8: audit profession - external parties

AN EVALUATION: PARTY ONE (SOCIAL) - PARTY TWO (SOCIAL)

On one hand, we have the audit profession who is comprised of two professional bodies who are combined to create a large and powerful accounting (audit) profession. The primary interest of the profession is to its members but they also may believe they have a responsibility to interested external parties that may exist. The audit profession, recognises that the external parties have a stake in the client companies they audit. Hence, they are interested in audit pricing issues from the point of view of these external parties getting value for money for the audit fee they may directly (or indirectly) pay to the audit firms (who in turn have auditors belonging to the framework of the audit profession). The audit profession may see it as their duty to give these external parties, *confidence* in the duties their member auditors perform. The profession may reason that if the external parties do not have this confidence (see Walker, 1993) then they may push the client companies to review the fees paid to the audit firms (and their members). As such, the profession may engage in programs of advertising through the media giving messages to the external parties that the auditors are professional and highly skilled. Unfortunately this is a common message and not aimed at particular interest groups.

One the other hand, the external parties are made up of a variety of different groups such as shareholders (the main interest group), creditors, unions, customers and suppliers etc. The external parties may *use* the audit profession (in addition to ASC, audit firm and audit client) to express their grievances they have about audit fee issues. The external parties may justify lobbying the profession because the actions and policies of the profession affect many interest groups. The external parties differ in size as well as the agendas regarding audit fees may differ, hence it may be difficult to enact any change in fee policies. The audit profession does take the concerns of external parties seriously because they may engage (which they have done in the past) in communications through the media (TV adverts) to induce *confidence* in these external parties. But unfortunately, these external parties may remain skeptical and continue to lobby the audit profession to make sure they receive value for money (fees).

Overall, the audit profession needs the confidence of external parties to ensure that they do not put pressure on their clients to review fees.

Combination 9: audit client - external parties

AN EVALUATION: PARTY ONE (SOCIAL) - PARTY TWO (SOCIAL)

On one hand, we have audit clients who is the company owned by (or is under some other interest) by external parties. These external parties include shareholders (the most important and influential), creditors, unions and the wider community. The audit client may feel that they do owe an explanation to shareholders and other external parties of the audit fee they may pay. But, at the same time the client may feel that external parties such as shareholders cannot criticise the audit fee paid for an audit report if they did not read the engagement letter or observe audit procedures. The audit client may believe that they need the confidence of the external parties that they are getting the 'best deal' possible for the audit services they engage because the external parties like shareholders own the company and if they are unsatisfied then they can invest elsewhere. Hence the audit client may communicate such issues at events like the AGM or even more informal gatherings. The audit client as a result will engage in a number of practices (audit switching, opinion shopping) to get value for the audit fees they pay. The audit clients may believe that much of the negotiations (and conflict?) with the external parties is attributed to the separation of ownership and management. That is, if the client was a smaller company then the shareholders could be the management as well and much of this conflict over audit fees may have been avoided.

On the other hand we have the external parties who believe that they are justified in expressing their concerns over the audit opinion expressed and the audit fee paid. The external parties may believe that they are presented with an audit report to be reassured that the financial statements of the client company has been appraised by a professional independent party. But, the experiences of the corporate collapses of the 1980's have made some external groups skeptical of auditors. Therefore, these groups may lobby their company not only to justify the audit fee paid to the audit firm but to also require them to demand a higher standard of service from the firm without any great increase in the audit fees.

Overall, both parties: the management of the client company and the external parties both want is best for the company. And this may be a quality audit undertaken at a price that the external parties find acceptable.

Combination 10: audit firm - audit profession

AN EVALUATION: PARTY ONE (SOCIAL) - PARTY TWO (SOCIAL)

On one hand, we have the audit firms (engagement partner) who employ auditors who are members of professional accounting bodies such as the ICAA or the ASCPA. The audit firm may send representatives to communicate or negotiate with the audit profession on which skills the audit members need to have to best meet the firm's needs. If the firms believe that they have the greater bargaining power compared to the audit profession then the firm could reason that they could use this influence to manipulate audit fees in the long run. That is, the firms could demand higher standards from members of the professional bodies, which will raise audit fees due to these higher standards. This would be an advantage to the firm because these higher standards required by the profession would be of little cost to the firm.

On the other hand, we have the audit profession who are made up of two professional bodies: the Institute of Chartered Accountants in Australia (ICAA) and the Australian Society of CPA's

(ASCPA's). These two bodies combined make up a powerful profession. It is the profession that sets the *barriers to entry* to the members admitted into the profession. The profession may believe that the audit firms have an influence on the way they train and educate their auditors- after all they have to be a desirable product to the audit firms. Representatives from the profession are more likely to communicate with the larger audit firms since they are more noticeable and influential. In addition, the large audit firms have a three members on the board of the ASCPA's (see ASCPA annual report, 1992). Since the profession believes that the larger 'big six' audit firms have an influence (but not necessarily a controlling influence) over the *barriers to entry* into the audit profession, then they may question the motivation behind the interest in auditors qualifications. Is it because they want to give the most professional service to their clients or is it because they are after the types of auditor which would attract higher fees?

Overall, there is a cooperation between the audit firms and the audit profession. The audit firms may be after the auditor who can generate audit fees and the profession is after the best opportunities possible for their members.

Combination 11: Government agencies - External Parties

AN EVALUATION: PARTY ONE (SOCIAL) - PARTY TWO (SOCIAL)

On one hand, the government has a number of agencies with the most significant being the ASC. The government can really only believe it can address the problems of audit pricing through communication with the affected parties involved. In doing so, the government would communicate with agencies of different sizes and locations, which in turn will shed some 'new light' on their bad experiences with audit pricing. Such experiences could relate to false advertising, over pricing and the fee not complying with the engagement letter. The government in turn may believe that the legal remedies put in place (the CL and the FTA) are adequate to solve these problems. The government has a difficult task! They have no specific legislation on audit fees and the lobby groups are so wide and diverse that it would be hard to have common legislation and furthermore, each interest group is likely to have their own personal agenda to look after as opposed to the government's public interest policy.

On the other hand, the external parties may believe that it is the job of the government to look after the *public interest* so they may listen to any lobby group who express an interest in audit fee setting. External parties are made up of lobby groups of different sizes and hence it would be the larger lobby groups may have the greatest influence on government policy formation. The external parties may see the usefulness of the existing *Fair Trading Act* (FTA) and *Corporations Law* (CL) frameworks but these could be improved with further lobbying. Every external interest group can justify their own position and hence such interests may be in conflict leading to an unpredictable effect on audit fees.

Overall, the government would contribute to the standard setting process through the AASB, which is said to have the public interest at heart. The standards in which the audit fee is supposedly based on is assumed to be supported by the public. The external parties in turn give feedback to the government of their views on audit fee related policies. It is simply a political game between the government agencies and the external parties.

Combination 12: audit profession - audit clients

AN EVALUATION: PARTY ONE (SOCIAL) - PARTY TWO (SOCIAL)

NB: In this combination we are dealing with audit clients who in turn employ internal auditors for their internal audit function. This combination deals with the audit client's interaction with the audit

profession. So we are looking at the internal auditors of the client and their respective audit professional body (IIAA). Hence the audit profession and the audit client only interact with each other through the internal auditors- and this is the 'rationale' behind discussing internal auditors under this combination and not a combination strictly addressing the 'auditor' entity.

On one hand, we have the audit profession of the IIAA who are a relatively small professional body made up of internal auditors. The IIAA may feel that they have to engage into communications with the audit clients who employ internal auditors. Such interactions help the profession establish the best way to train the internal auditors to become *Certified Internal Auditors* (CIA's). The effect on audit price is to the advantage of the audit profession because they are the only source in Australia of CIAs and, hence, they monopolise the supply. The satisfaction of the audit client with the quality of the CIA is contingent on the favorable evaluation of the internal audit function by the external auditor (from an audit firm). A favorable evaluation means that the external auditors will use some of the work already done by the internal auditor (Gill *et al.*, 1993:15) in the audit thus, making the audit cheaper for the client.

On the other hand, we have the audit clients who may believe that the audit profession (the IIAA) is the only supplier of internal auditors in Australia. The clients may also believe that just because the IIAA is a small profession it cannot be influenced to any great extent because they are the sole professional body dealing with internal auditors. The audit client is after an (effective) internal audit system that may lower the cost of external audits. That is, an effective internal audit function of CIAs that meets the standards of the external auditors may induce the external auditors to use some of the work the internal auditors have already done and thus may lower the audit fee. The audit clients may also believe that the audit profession is not a neutral party. But, would rather act directly in the interests of its members by perhaps raising barriers to entry, restricting supply or making the requirements for the CIA more rigorous which would give a better quality internal audit function and thus generate higher salaries for the internal auditor.

The overall relationship between the IIAA (audit profession) and the audit client is an understanding, that the client demands quality internal auditors to lower the fee from external auditors. Hence, the profession will find out what exactly the client wants from an internal auditor (in response to the needs of the audit firm), and produces an internal auditor that fits this mold.

Combination 13: audit profession - auditors

AN EVALUATION: PARTY ONE (SOCIAL) - PARTY TWO (SOCIAL)

NB: In this combination, we are dealing with auditors and the audit profession. This presents a problem due to the fact that the auditors are members of the audit profession. In this combination we shall not be discussing internal and external auditors separately but rather will discuss the way auditors and their profession, interact with each other in general.

On one hand, there is the auditor who can either be an internal or an external auditor and are (usually) a member of a professional body. The auditor may believe that the profession looks after the interests of its members and because it is large and influential it can may more easily communicate with the audit firm and audit clients on issues relating to audit fees. The auditor may believe that they lead a comfortable existence within the audit profession. They pay a yearly fee to the upkeep of the profession and the profession provides them with a framework which incorporates audit standards and a code of ethics that that gives the auditor professional status which induce confidence in the community. The community has confidence in auditing standards and the auditors may believe that if the profession is seen to improve the quality of these standards then the community may be willing to

pay a higher audit price. In addition, the auditors may believe that, similar acts on part of their professional body such as higher education, harder examinations etc may heighten *barriers to entry* to the profession (higher fees due to less supply).

On the other hand, the audit profession may engage in a number of possible tactics in order to influence the level of fees that members are receiving. That is, the profession sees the individual auditor as being small and weak in themselves, and hence need representatives from the profession to negotiate and converse on audit pricing issues with representatives from the audit clients and the audit firms. The audit profession realises the implicit value that the professional certificate carries and hence may feel inclined to engage in a program of reducing the supply of these certificates in order to raise audit fees by making the requirements to obtain one much more difficult.

Overall, the audit profession dominates the auditors who support the profession. The profession will act in the best interests of its members by engaging in practices that affect the *barriers to entry* into the profession in order to maintain higher remuneration for its members.

Combination 14: auditors - external parties

AN EVALUATION: PARTY ONE (SOCIAL) - PARTY TWO (SOCIAL)

On one hand, the auditors believe that they have *professional status* which is granted by the community. Such professional status gives the auditor autonomy to express a professional opinion and to charge a fee for their services. This *professional status* is recognised by all sections of the wider community and will continue to be willing to (indirectly) pay audit fees. The external parties are willing to pay audit fees because they want to be assured that the financial statements that they have an interest in are true and fair and comply with the relevant accounting standards. In addition, the audit report is addressed to the shareholders (arguably the predominant external party) but the shareholders cannot directly negotiate fees with the individual auditors as any fee change may affect the *independence* of the auditor.

On the other hand, the external parties recognise that they may be more influential and powerful than the individual auditor, but they cannot directly *negotiate* fees with them. The external parties believe that they are in a position where they have to negotiate and communicate their concerns on audit fees with their company of interest, audit firm or ultimately the ASC. This may be perceived as being unfair when the auditor is the one who has done the work and in addition the auditor may have other goals from their duties apart from maximising audit fees! The external parties acknowledge the legitimacy of the auditors' professional certificate and may be willing to pay audit fees while they recognise the auditor's professional status. However, the external parties may feel that it is possible for the audit firms to misuse the *professional status* granted to its auditors and interfere with audit fees to the detriment of the clients bringing the auditor and the audit profession into disrepute.

Overall, auditors and external parties are not directly related even though the audit report is addressed to the shareholders themselves. The interactions between the auditors and external parties is vague because these two parties do not directly have any contact with each other relating to audit fee setting. Rather it is the actions of the ASC, and the audit firm that facilitates the relationship between the auditor and external parties since the audit firms and the ASC are readily accessible to many external parties. For example, the shareholders cannot directly contact the auditor but can contact representatives of the audit firm, the client company or even the audit profession.

Combination 15: auditors - government agencies

AN EVALUATION: PARTY ONE (SOCIAL) - PARTY TWO (SOCIAL)

On one hand, the government (ASC) believes that the auditors are a *tool* that they can use to implement their public interest policy. They realise that the government cannot directly influence an auditor, they can only influence the standard setting process of the professional body, which may have a flow on effect on audit fees. In addition to this the government realises that the auditors are forced to comply with the ASC provisions in order to remain in employment.

On the other hand, the auditor may believe that the government cannot be directly dealt with (unless it is through the *Companies Auditors and Liquidators Disciplinary Board* [CALDB]) since the professional body would be more effective in any communications with the government. Additionally the auditors may feel that the ASC is too big and powerful and places constraints on the activities of their revenue generating activities. For example, the ASC only communicates to the auditors by means of disciplinary action from the CALDB. This group keeps a list of auditors who they feel are guilty of minor breaches of the Corporations Law (see Boreham, 1992). Such a list could ruin an auditor's reputation and a list of auditors' names could give the entire auditing profession a bad reputation which could see audit prices fall. Alternatively, the auditor may aspire to give a better quality service in order to prevent any complaints made against them.

Overall, there may be an uneasy relationship between the auditors and the government agencies primarily because both these groups have different objectives. That is, the government aims to look after the public interest and protect these external parties from the activities of the auditing profession. The auditors may be more profit motivated, wanting to stay employed and do the job they were trained to do without having their fees affected by government interference.

Step 6: Finding key ideas for the determinants of audit pricing

This step involves listing the key points from the analysis, which could warrant further research in finding the determinants of audit pricing. From our analysis and evaluation conducted in this monograph, we have come up with the following ideas, which could need further investigation in future research:

- the impact of the audit client's *Internal Audit Function* (IAF) on audit fees
- the relative *sizes* of the audit firms and audit clients and the effect of behavior such as *price cutting, low balling, audit switching* and *opinion shopping* etc. on audit fees (nothing new here since it was covered in the literature review in section 4)
- the impact of government legislation such as the *Corporations Law* and the *Fair Trading Act* on the freedom of the audit firm to charge audit fees
- the effect of community *skepticism* of the audit firms and/or the audit profession on audit fee determination
- the effect of the government's stance on upholding the *public interest* on audit fees
- the effect of the government's role (through the AASB) in the development of auditing standards on audit fees
- the external parties view of what the company (of interest) should be paying for audit services

- the impact of a high risk of litigation (from the audit client to the audit firm) on fees
- the impact of the audit profession's *barriers to entry* on the level of audit fees
- the impact of corporate *confidence* in the standard of auditors who are members of the profession on audit pricing
- the role of the *professionalism* of the auditor in charging audit fees

The issues above are very broad and diverse and cover a more issues than the positivist mainstream research reviewed in section 4 of this monograph. Any of the topics above could be rich grounds for further research into audit pricing determinants. In addition to the above, we can focus on the *interactions* between these parties to solve any problems these parties may have with one another. Such problems can occur at any of the semiotic levels (Mikhail, 1996). And, it is the task of the analyst to take a given problem or issue from the above list, and consider it from each of the semiotic levels (or the levels that are relevant) given the *interactions* that may occur between parties. With audit pricing in mind some problems that may occur between parties may include:

Physical- Is the engagement partner competent enough to administer a given audit engagement?

empiric- Should the *engagement letter* be sent to the audit client by post or facsimile?

syntactic- Does the engagement letter cover all the details necessary to complete the audit. That is, does it adequately cover the scope, nature, objectives and price of the audit engagement.

semantic- What is the *significance* of the public interest to the government and the audit firms? That is, does a differing significance induce different behavior from both these respective parties?

pragmatic- Is there an even *balance* of bargaining power between the audit firm and the audit client? A difference in bargaining power may induce the audit firm to reduce fees or the audit client may be induced to *switch* auditors.

Social- To what extent does the social context, affect a transaction between the audit firm and the audit client? That is, the culture, norms and ambitions etc of a given organisation should be taken into account.

Step 7- Reflecting back on the semiotic structure

We have already gone into great detail on the *interactions* between the six parties identified for the purpose of the analysis of the audit pricing discourse. This step reconciles the *interactional* analysis outlined above and the *structure* of the audit pricing discourse from each of the semiotic levels. This can be achieved by constructing *ontological* diagrams, which in a sense are a construction of *reality* of the workings of the discourse of audit pricing. The template and ideas for the ontology diagrams that, we will construct is directly derived from the work of Stamper (1992). In this work, *ontology* diagram templates are constructed for each of the semiotic levels with the exception of the social level. Such diagrams are applied to CBIS's but we shall use the templates of Stamper (1992) and apply them to the audit firm and their use of the engagement letter within the social discourse of audit pricing. To achieve this, we decided to be flexible with the terms used in the diagram and adapt them to audit firms and their use of engagement letters in audit pricing.

The structure of the physical level for audit firms and engagement letters

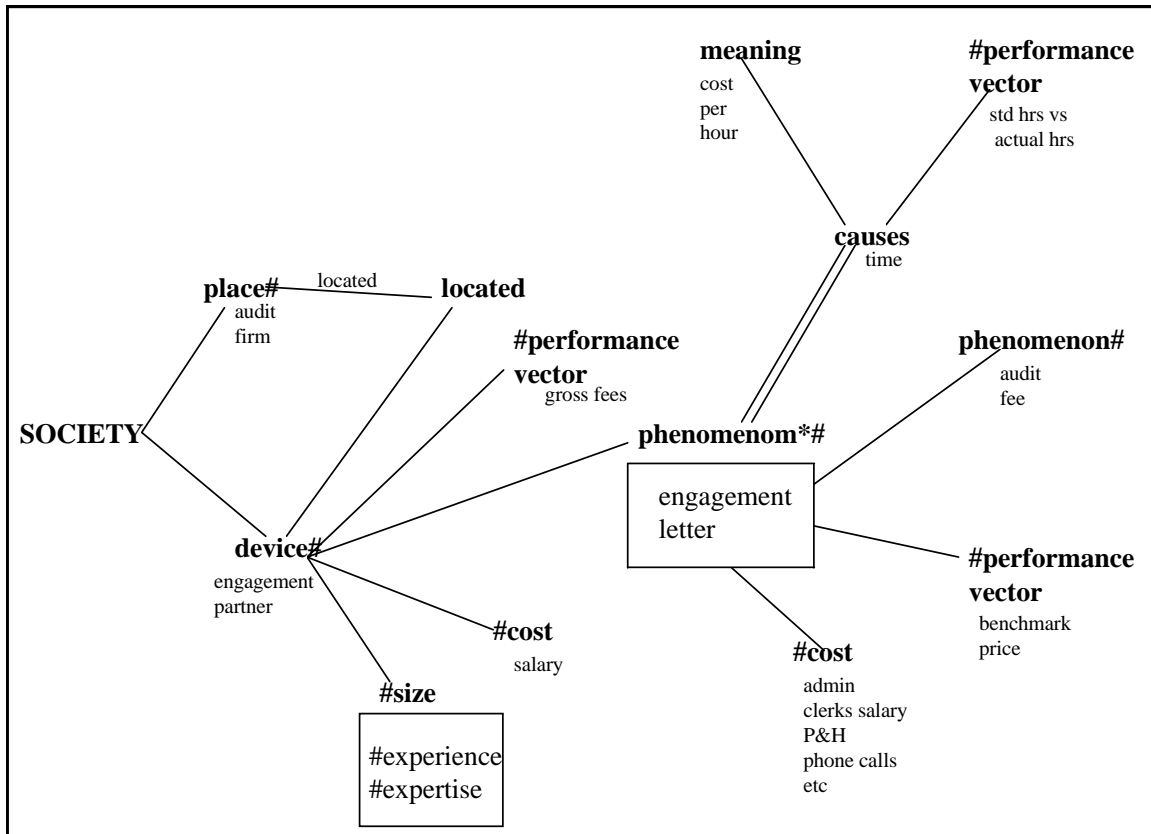


Figure 6 - Ontology diagram of Audit firms at the *physical* level

In *figure 6* above, we are concerned with the physical means of creating *tokens* (signals or marks) which can be used as *signs* (Stamper, 1992, p50). This diagram shows the engagement partner (*device*) being used by the audit firm (*place*) to create an engagement letter (*phenomenon*) which in turn creates a further phenomenon by means of the *audit fee*. The engagement partner (*device*) has his/her size measured by their experience and expertise, their cost is their salary (salary multiplier) and their performance is measured by gross fee turnover (*performance vector*). The engagement partner is located within the audit firm which is *rooted* in society. The phenomena of the engagement letter is *caused* by the amount of *time* spent on the engagement and its performance is measured by standard hours and standard costs as a benchmark of past performance.

The structure of the empiric level for audit firms and engagement letters

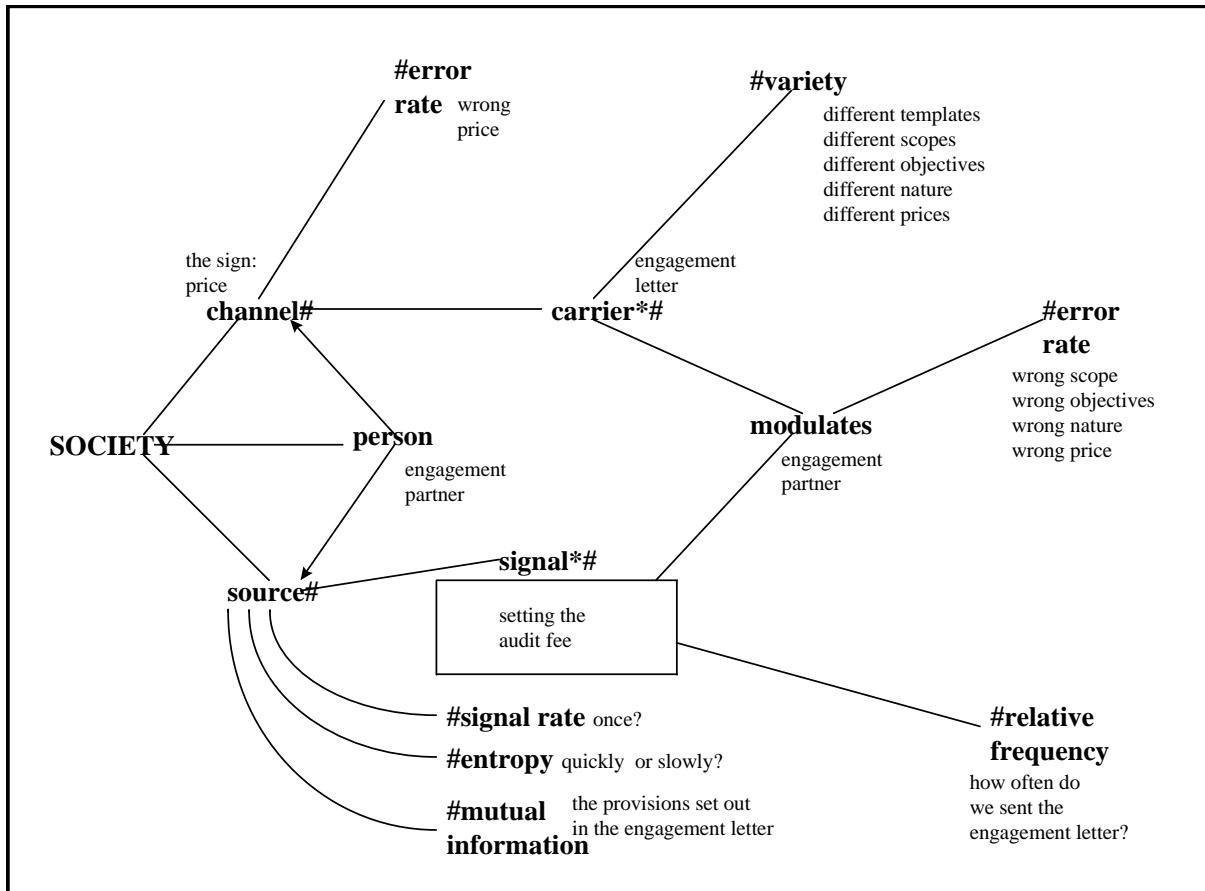


Figure 7 - Ontology diagram of Audit firms and the *empiric* level

In *figure 7* above, we are concerned with *communication* issues of audit firms in the discourse of audit pricing. Again the whole discourse is *rooted* in society which sees the engagement partner (*person*) who is from an audit firm (*source*) *channeling* and *modulating* the *signal* being the ‘setting’ of the audit price. The engagement letter is the *carrier* of this *signal* in which it can be subject to a *variety* of errors if the engagement partner is not careful in its construction. In addition, when generating an audit price sign, the partner ought to realise that there is a *variety* of different versions of the engagement letter that may be used which may represent different scopes and objectives. The audit firm who employs the engagement partner sets out the general form of *mutual information* within the *engagement letter* and is usually set at a *signal rate* of one because there is only one engagement letter. But this may vary if the conditions of the client change (new management, new direction of business etc.).

The structure of the syntactic level for audit firms and engagement letters

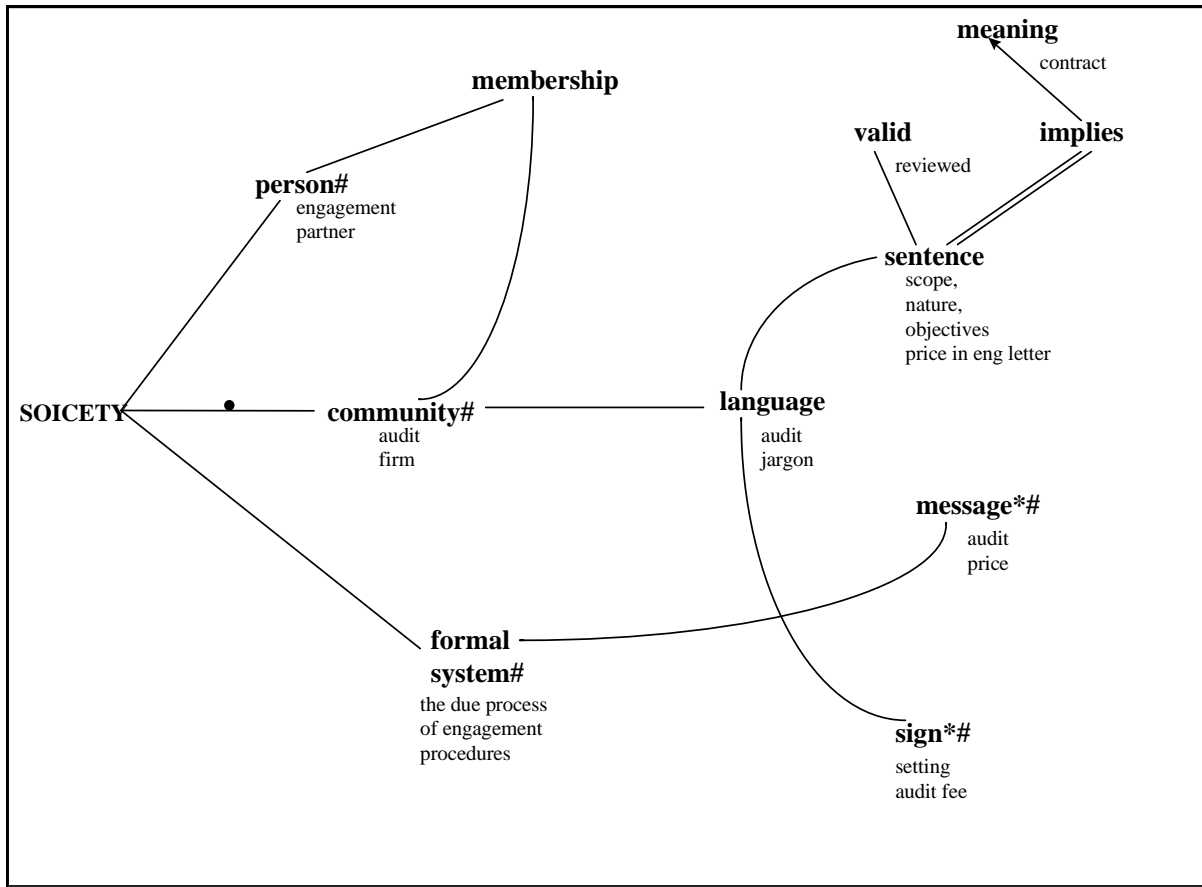


Figure 8 - Ontology diagram of Audit firms at the syntactic level

In figure 8 above, we see the engagement partner being a member of a *language* community where they have *membership* in the audit firm. On the basis of a *formal system* of engagement procedures, the engagement partner utilises the *language* of ‘accounting jargon’ to create *sentences*, which may imply *meaning* of a contract between the audit firm and the audit client. The *sign* that gives the means to constructing an engagement letter is the need to set audit fees and carries the *message* of the audit price.

The structure of the semantic level for audit firms and engagement letters

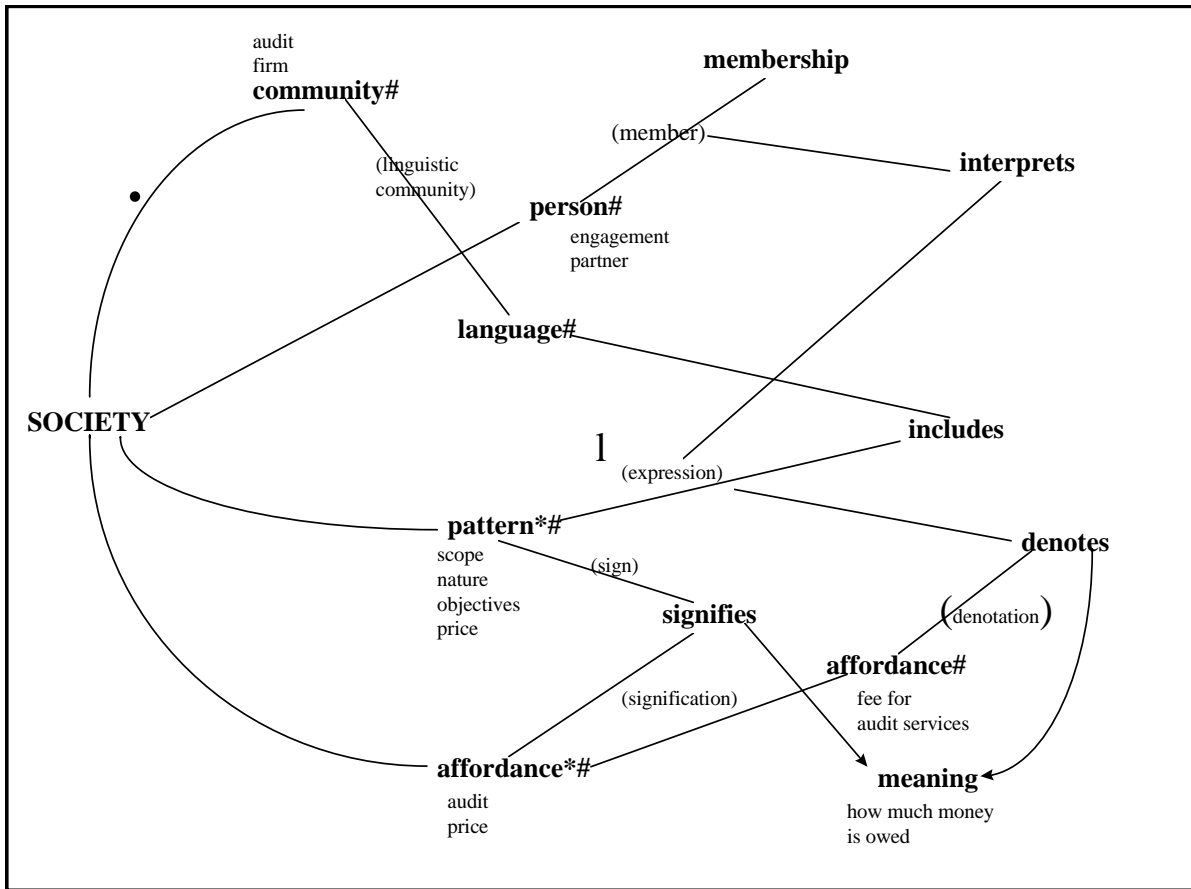


Figure 9 - Ontology diagram of Audit firms and the semantic level

In figure 9 above, we see the engagement partner who is a *member* of a *linguistic community* being the audit firm which shares meaning and *interprets* the common *language* of accounting jargon which creates the engagement letter that shares a common *pattern* pertaining to its scope, nature, objectives and price. Such a pattern in turn *signifies* an audit price (*affordance*) which *denotes* a fee for audit services (a further *affordance*).

The structure of the pragmatic level for audit firms and engagement letters

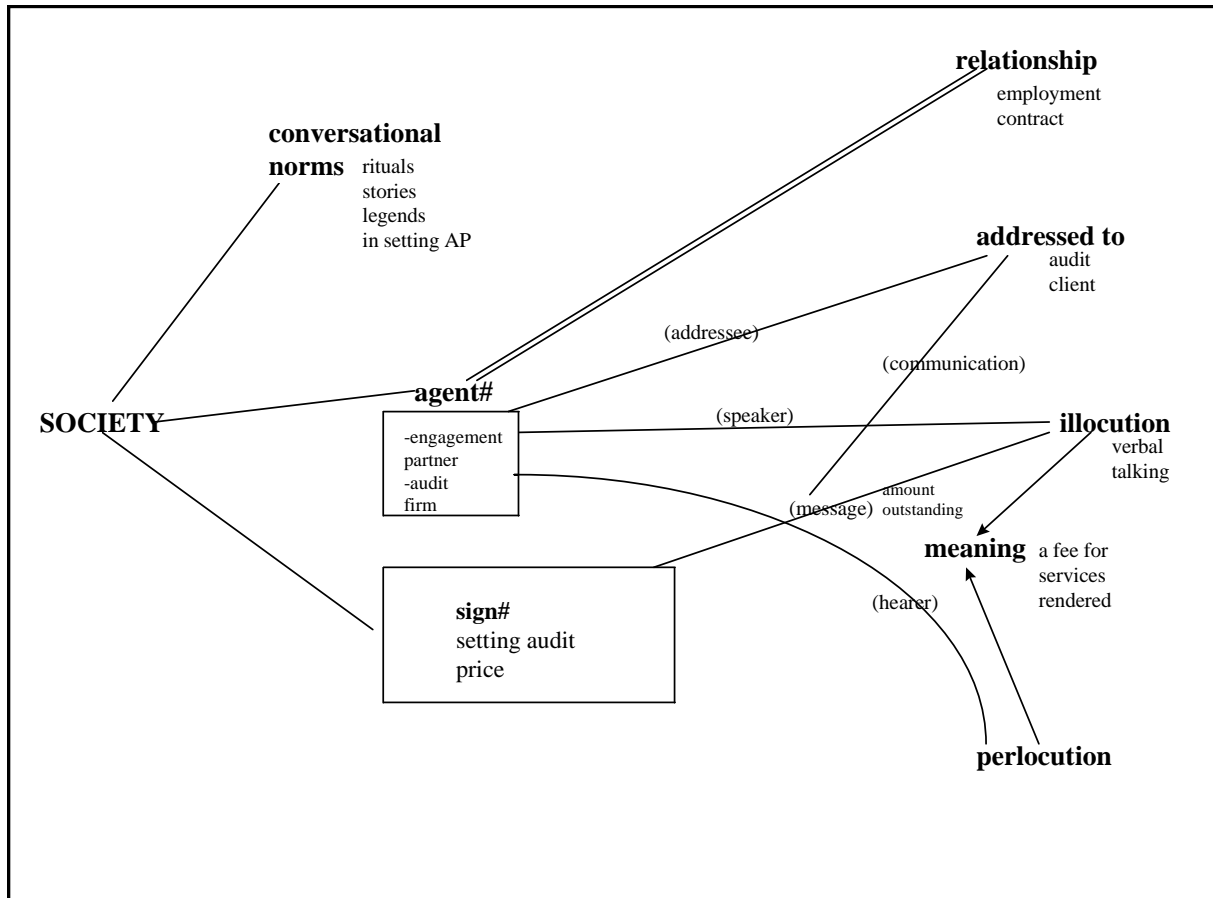


Figure 10 - Ontology diagram of Audit firms and the *pragmatic* level

In *figure 10* above, we see that the engagement partner has a relationship with the audit firm in their capacity of being an ‘agent’ for the interests of the audit firm. Then they would engage in communications and negotiations with representatives of the audit client’s (audit committee) in determining an audit fee. The engagement partner undertakes the task of setting an audit fee (*sign*) by drawing upon the *conversational norms* in the form of the stories, rituals, and legends in setting audit fees. These may have been heard over the length of their career. Assuming that the whole process of setting an audit fee is rooted in *society*. Then, we can move from here and say that the *sign* of *setting the audit price* is uttered by the engagement partner via using the engagement letter as a means of *communication* being addressed to the audit client. The engagement partner may have the intention that the message of the balance (fees) outstanding is *heard* by a representative of the audit committee. This member of the audit committee may also share the *meaning* of the message that a fee is owed for the balance outstanding for the audit services performed (or about to be performed).

VII.B. Limitations of the analysis and evaluation

The analysis that we have undertaken is all about shedding some ‘new light’ on the discourse of audit fee determinants, it is not about finding the ‘right’ answers. Much of the contents of the analysis are ideas and thoughts that can never be ‘complete’ because we live in a dynamic environment in which new ideas can be added to the analysis and other ideas already part of our analysis may become obsolete. For example, what if dramatic developments in respect of the laws concerning key audit activities occur in the next six months? There would have to be some change to our analysis or else it

will become outdated. Thus, we would like to note that any semiological analysis occurs at and is relevant to, a certain point in space and time.

In addition, within the analysis and the evaluation when we use an expression such as the *audit client* deals with the *audit firm* then we are referring to the representatives of each party dealing with each other. We neglected to mention this in every interaction in the analysis and evaluation for reasons of simplicity. And lastly, during our analysis we did not go into any great details into of internal auditors. We could have split every ‘auditor’ entity into their *internal* and *external* auditor components but instead we merged the internal auditor with the audit client when convenient. This was to simplify the analysis.

VII.C. Conclusion

Since semiotics has never been applied to a social discourse such as audit pricing before (according to our research) then we can enjoy the freedom of experimenting with the way the analysis and evaluation are going to be performed. The above steps take time and with constant attention can be refined and improved upon. Our analysis is no exception. We make no claims that our analysis is complete, We are sure that there are additional points and ideas that we have not yet thought of that may improve our analysis. In essence, what this section has achieved is an analysis and evaluation of both the *interactions* and the *structure* that the actors coexist within the social discourse of audit pricing.

VIII. Conclusions and Reflections

This section will briefly review and sum up some of the insights that semiotics has given as a method of research.

Semiotics and the philosophy of science

The semiotic analysis that has been employed in this monograph may be reconciled with the positivist approach as well as the *interpretive* and *critical* paradigms. Our analysis has steered away from the traditional positivist approach of *quantitative* research in order to *explain* and *predict* the audit fee phenomena. The research conducted in this monograph has been about *interactions* between organisations and people. Since we are assuming that the audit pricing discourse should be treated as a *social science* as opposed to a *physical science* then as a researcher this will affect the way we view the world. Hence we will not hold the determinants (which are merely ideas) of audit pricing that we found in the world we researched as being the ‘right’ answer because they are not. There is no ‘right’ answer as we have just presented a possible answer from our *interpretation*, which may be of interest to those wishing to conduct further research in audit pricing. We have already established that this semiotic analysis into audit pricing is an *interpretive* methodology but can it have applications to the *critical* paradigm? Of course! The very ideas that we found in the analysis can induce our audience in certain ways of thinking. For example, we could have taken the angle that the audit firms perpetuates the continuation of *capitalism*, whereby the profit maximising audit firm audits the accounts of their lucrative client which in turn induces *confidence* in the shareholders while the client continues to exploit *surplus value* from its workforce. Therefore in respect of the research conducted in this monograph, semiotics had been used as a *lens* used to search for new ideas for future research as opposed to being used as a political *tool* to express political opinions.

The Pioneers of Semiotics

In applying a semiotic approach through Stamper's framework on the discourse of audit pricing, it would have to be argued that the Peircian model has had a greater influence than the Saussurian model. Although we did not *explicitly* relate Peirce's triadic model to setting audit fees during our analysis, it would seem that such a model could have a direct application. This is because of the inherent flexibility, of the *triadic* model in asserting that the:

- (a) *sign*, is the setting of an audit fee,
- (b) the *object*, is that the sign stands for a fee for services rendered, and
- (c) the *interpretant*, is the party that receives the 'sign' and may react in a certain way.

Hence to study audit pricing from a semiotic point of view, it is advantageous to adapt the thoughts of Peirce who asserts that any intelligent behavior is a *sign* (Rochberg-Halton, 1982, p458) as opposed to being entrenched in *linguistic* reasoning as the Saussurian model seems to be.

Semiotics and the Positivist Views of Recent Literature

A semiotic approach has certainly shed more light on audit pricing determinants than the positivist approach. Our analysis is essentially a technique to find new avenues for further research. Unlike the positivist approach, we do not make any claims on having the answers that will *explain* and *predict* audit-pricing behavior. We have suggested ideas that may extend audit pricing research from the traditional focus of *audit firm - audit client* studies based predominantly on size. Our ideas draw upon other parties and the laws, communications, negotiations, meanings, files, commitments, culture, conversations and physical characteristics that may contribute to determining an audit fee. The critics of semiotics may label it as too *subjective*. We have no problem with this because semiotics is an interpretive technique and the researcher seeks to gain an understanding of the audit pricing discourse. We would suggest that by considering the interactions between the parties involved we would gain a much broader overview and appreciation of the determinants of audit fees as opposed to measuring correlations between fee and size variables.

The Semiotic Methodology Itself

The technique of semiotics is very involved, very time consuming but yet it is also very rewarding for the researcher. When looking at 900 interactions involving six parties, we liken the technique of semiotics to panning for gold. That is, many of the *interactions* at different levels will be meaningless and yield no inspiration whatsoever. But occasionally, the researcher will find an idea or a 'nugget of gold' (as it were) that will lead to an area of research or further investigation never considered before. And as researchers, we feel that this is a healthy attitude to have.

The Future of Semiotics

As mentioned before, semiotics has had very little application in commerce related disciplines and has had no application in audit pricing. As researchers begin to recognise the limitations of positivist research, they may begin to look for alternatives. Semiotics may very well be an alternative they may consider. It will be unfortunate if semiotics remains entrenched in the field of linguistics because it can offer some very creative and innovative ideas never before thought of in solving problems and perhaps even finding new problems to solve. And as this monograph has demonstrated, semiotics

offers accounting research great potential as a possible alternative to the traditional *positivist* regime due to its innovative and flexible nature.

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