CURRENT ISSUES IN AUDITING
Vol. 16, No. 2
Fall 2022
pp. P39–P50

American Accounting Association
DOI: 10.2308/CIIA-2021-021

PRACTITIONER SUMMARY

Financial Auditing as an Economic Service

Matthew W. Driskill
Texas State University

W. Robert Knechel
University of Florida

Edward Thomas
Georgia College & State University

SUMMARY: This article summarizes Knechel, Thomas, and Driskill (2020), conceptualizing financial auditing as an economic service. In contrast to the production of tangible goods, a central characteristic of economic services is substantial customer/client participation in the production process. Financial auditing is an intensive collaborative network service due to the multiple parties involved in the production and consumption of the resulting output. This introduces significant heterogeneity and complexity into the planning and conduct of the audit, the resulting audit output, and perceptions of audit quality. While the independence of the auditor is necessary, ignoring the essential nature of auditor-client cooperation may generate unexpected costs which impair audit quality. The multitude of parties involved in an audit creates tension between audit quality and audit efficiency and makes objective definitions of audit quality difficult. Excessive standardization of the audit process may not increase audit quality.

JEL Classifications: G18; G28; G34; G38.

Keywords: audit quality; audit process; service science; regulation; corporate governance.

Matthew W. Driskill, Texas State University, McCoy College of Business, Department of Accounting, San Marcos, TX, USA; W. Robert Knechel, University of Florida, Warrington College of Business, Fisher School of Accounting, Gainesville, FL, USA; Edward Thomas, Georgia College & State University, J. Whitney Bunting College of Business and Technology, Department of Accounting, Milledgeville, GA, USA.

Editor's Note: Accepted by Denise Dickins.

Submitted: September 2021
Accepted: February 2022
Published Online: February 2022

I. INTRODUCTION

Practitioners, regulators, and academics tend to treat an audit as akin to the manufacture of a tangible economic good produced solely by the auditor. As a result, audit quality is often framed as a function of auditor competency—the likelihood of the auditor detecting a breach—and auditor independence—the likelihood of the auditor reporting the breach (DeAngelo 1981). Knechel, Thomas, and Driskill (2020) explore the implications of conceptualizing an audit as an economic service.[1] An economic service perspective formally incorporates the client firm into the audit production process, emphasizing the interaction of collective auditor and client competencies in the joint production of the audit—a characteristic acknowledged in early audit research, but often forgotten in more recent work.[2] As a result, quality is not determined by the auditor alone, and each auditor-client service relationship is unique. The introduction of auditor-client collaboration generates additional complexities, inefficiencies, and opportunities in audit production (and consumption) relative to economic goods.

A service perspective also provides a variety of new insights—and further justification for existing insights—regarding our understanding of financial auditing. For example, a service perspective suggests that better working (i.e., cooperative) relationships between auditors and clients should produce higher-quality audits, in contrast to the idea that auditor-client cooperation is simply a threat to auditor independence.[3] A service perspective also highlights the tension between audit quality and audit efficiency; due to the idiosyncratic nature of services, increased service quality can come at the expense of service efficiency.

Knechel et al. (2020) apply a service perspective to identify the following general insights about auditing:

1. **Auditing meets the general conditions of an economic service.** Unlike the manufacture of economic goods, the production of economic services involves significant cooperation between service provider and the service customer/client.
2. **Auditing is a collaborative network service**. While auditors must clearly take responsibility for their work, audit quality is affected by the efforts of other parties who participate in the audit process, such as managers and audit committees.

[1] As we discuss later in the paper, there are multiple recipients of the audit service. The audit client can be described as the *customer* of the audit service, receiving the benefit of enhanced credibility of financial disclosures, while the user of the financial information is the ultimate *consumer* of the audit service, receiving the benefit of more credible information. Audit services are therefore akin to other business-to-business services where the ultimate beneficiary (a financial statement user) is downstream from the service customer (the client firm).

[2] Congruent with a service perspective, Demski and Swieringa (1974) model audit production as cooperative and jointly determined and note limits to auditor independence: "this elementary and innocuous form of *cooperation* in selecting their respective decisions ensures that *the auditor is not strictly independent*. The auditor and auditee *jointly share* in the consequences they *jointly produce*; and *they coordinate* these choices *to the extent of*, other things being equal, *not compromising each other*" (Demski and Swieringa 1974, 509–510; emphasis added). DeAngelo (1981) similarly notes the joint nature of audit production: "Defining audit inputs and output in this manner [i.e., in terms of the auditor alone] simplifies the analysis at the cost of *bypassing* some interesting *auditor-client interactions caused by the jointness of the production process*" (DeAngelo (1981, 185, footnote 6; emphasis added).

[3] It is important to acknowledge that regulations intending to protect auditor independence, e.g., limits on non-audit services that can be provided to audit clients, often have the effect as well of constraining the service (i.e., collaborative) potential of the audit.

3. **Audit quality depends upon perceptions within the cooperative network**. While audit standards are intended to promote a uniform (i.e., high) level of audit quality, quality ultimately depends upon how well the audit service meets various audit consumer expectations (e.g., the assurances that financial statement users, regulators, audit committees, etc. expect from the audit).
4. **Excessive standardization in the audit process may undermine audit quality**. Standardization may make audits more efficient and easier to pass regulatory inspection, but high levels of standardization may undermine the value that arises from auditing's service characteristics.

These general observations are presented in Table 1 in the form of propositions on audit as an economic service which we reference in the following discussion.[4]

II. AUDITING IS AN ECONOMIC SERVICE

Proposition 1

The defining characteristic of a service is the participation of the client/customer in the production process, known as "co-creation of value" (Sampson 2010; Spohrer and Maglio 2008; Vargo, Lusch, and Akaka 2010). Auditing is a service because of the critical role of the client in making the service possible: an organization's financial reporting depends upon several parties playing specific roles in the audit process, including management, the board, audit committee, internal audit, and external auditor.[5] Quality financial reporting depends upon the distinct activities of all parties and involves cooperation to achieve shared goals related to financial reporting.[6] For example, auditors draw upon their familiarity with accounting and auditing standards and their experience with other clients within the same industry, and client personnel have knowledge about the operations and transactions of the company. The "co-creation of value" in the audit process depends upon all parties making their respective contributions to the process.[7]

In a typical service context, the service *customer* and service *consumer* are one and the same. This means that the consumer has input into the service process and the outcome depends

[4] The propositions in this paper are identical to the propositions enumerated in Knechel et al. (2020). Some propositions receive proportionately more attention in the original paper.

[5] Research on audit quality over the last two decades has increasingly focused on the roles played by the various parties *within* the client firm which contribute to audit production (e.g., see DeFond and Zhang [2014] for a review).

[6] The various parties involved in or affected by the audit may have some conflicting goals. Audits exist as a solution to agency problems that arise from goal misalignments between management and shareholders. Part of the challenge auditors face is to motivate sufficient cooperation from the client firm by responding to goals that are shared, while maintaining professional independence.

[7] We do not mean to suggest that the participation of managers, the audit committee, and other members of the audit client means that the audit client co-manages the audit or has the same responsibility as the auditor for the conduct of the audit. These parties "co-create" the audit with the auditor—as part of the collaborative service network (Section III)—but the auditor has ultimate responsibility for the success of the audit.

TABLE 1

Propositions on Audit as an Economic Service[a]

Proposition 1: The more an audit involves the participation of the client and other parties, the more the audit should be characterized as a service process.

Proposition 1-1: The less (more) that end users are separated from the collaborative audit process, the more (less) able the audit process is to meet their expectations.

Proposition 2: The value that any participant in the audit process brings to the audit will be a function of (1) the competencies and resources of the participant and (2) how successfully those competencies and resources are integrated into the audit process.

Proposition 2-1: The extent and nature of cooperation in the audit process will depend on (1) the goals of the audit participants and (2) the stage of the audit process where cooperation is needed.

Proposition 2-2: The greater the number of participants in the audit process, the greater the likelihood of (1) goal misalignments and (2) communication limitations between participants.

Proposition 2-3: The audit committee should be evaluated by the competencies and resources it brings to the process and by how well those competencies and resources are integrated into the process.

Proposition 3: An audit failure is a network failure and does not necessarily imply that the performance of the auditor was deficient.

Proposition 3-1: Auditor knowledge specialization and service co-investments can increase the client's reliance on the auditor, leading to an increase in auditor independence.

Proposition 4: There is no universal standard of audit quality since a stakeholder will judge audit quality by comparing the performance of participants in the audit process against the stakeholder's performance expectations.

Proposition 4-1: Insofar as there is an inherent variation in the level of assurance demanded by stakeholders across audits and by the various stakeholders within a given engagement, there should be a corresponding variation in the level of assurance provided by the audit network to the various participants in each engagement.

Proposition 5: The relationship between audit standardization and audit quality is non-linear. Very low levels of standardization risk inconsistency in audit performance; very high levels of standardization ignore the idiosyncrasy of the client and the client's stakeholders.

Proposition 5-1: Auditors can pursue service efficiency through (1) standardizing "back-office" processes, (2) changing the timing of client demand, and (3) economies of scope and resource integration.

[a] Propositions 1 through 5 are considered foundational based on the theory of service science, while the other propositions are either positive or normative propositions that follow from the related foundational proposition.

on effectively integrating each party's competencies and other resources into the service process (Grönroos 2011). However, audit services are different from the typical service context in that a primary consumer of the audit is not typically involved in the audit process.[8] This lack of participation from financial statement users in the audit process is a common criticism of the audit

[8] This distance—between financial statement users (e.g., investors and other external stakeholders) as primary audit consumers, and auditors and client firms as audit co-producers—significantly complicates actual and perceived audit quality (Section IV). While external users of financial statements are the primary consumers of financial auditing, the client firm itself benefits from the audit. This variety of consumers makes it difficult to develop a single objective definition of audit quality.

profession (e.g., Kingman 2018; Brydon 2019). While financial statement users do not currently participate directly in the audit process,[9] the logic of professional services suggests that audits would be improved by greater and more effective participation.[10]

III. AUDITING IS A COLLABORATIVE (COOPERATIVE) NETWORK SERVICE

Proposition 2

Auditors presume their clients will cooperate with them, but the extent of that cooperation can vary considerably. Managers committed to financial reporting quality might actively support information flow from the organization to the auditor (Hellman 2006). At the other extreme, managers might act to frustrate auditor efforts, perhaps to keep the auditor from discovering fraudulent reporting. A third possibility is that managers may provide perfunctory cooperation because they perceive the audit as a nuisance which provides little value to the organization. Accordingly, auditors may need to find ways to encourage managerial cooperation while maintaining professional independence.[11]

Auditors should not overly rely on management representations, but managerial cooperation is vital for all stages of an audit. Audit planning requires auditors to update their understanding of the client and much of this information comes from discussions and interviews with client personnel. Audit testing requires significant managerial cooperation as well. While auditors should not consider management's representations to be sufficient audit evidence, auditors rely on their clients to obtain and interpret a great deal of audit evidence. Cooperation is particularly important at the completion of the audit. Auditors meet with management and the audit committee to discuss findings related to accounting misstatements and control deficiencies. These discussions can be characterized as negotiations influenced by the nature of the relationship between auditor and client (Gibbins, McCracken, and Salterio 2010). The quality of the client's cooperation with the audit influences the quality of the audit itself by potentially affecting: (1) the quality and timeliness of the information the auditor receives, (2) the auditor's ability to interpret the information received, and (3) the willingness of management to consider the auditor's positions.

[9] To the extent that audit committees (and boards of directors generally) are representatives of the interests of shareholders, then shareholders participate in the audit indirectly. We discuss the value that audit committees can bring to the audit process in our discussion of Proposition 2-3.

[10] The U.K. Brydon Report (Brydon 2019) has a number of proposals for engaging shareholders in the audit: (1) the auditor developing publicly reported risk assessments using input from the audit committee and interested shareholders, and (2) having auditors available to answer questions during shareholder meetings. For practitioners working within the current audit institutional setting, communicating with shareholders and other stakeholders as part of risk assessment might help adapt the audit to meet the specific needs of the firm's stakeholders (Hall 2021).

[11] Guénin-Paracini, Malsch, and Tremblay (2015) describe how auditors make significant efforts to limit their intrusions on their client's time. Auditors also endeavor to maintain a constant friendliness and agreeableness, even under stressful conditions.

It is common to think of auditing as a monitoring activity. Like the Hawtch-Hawtcher Bee Watchers from Dr. Seuss,[12] auditors monitor managers, while others (audit committees, PCAOB) monitor auditors. Viewing audit as a monitoring activity leads to an emphasis on formal controls (e.g., audit standards, audit inspection processes) to properly guide and motivate audit participants. The service perspective, however, encourages us to think of the audit network in terms of a collaboration where each party's competencies and other resources are integrated collectively into the audit process.[13,14] This alternative view of audits leads to an emphasis on informal relations and leveraging collective actor competencies across the network. Research indicates that social interaction between service participants improves trust and communication (Havila, Johanson, and Thilenius 2004) and that informal social agreements are more important for developing cooperation than the terms of formal contracts (van der Valk and van Iwaarden 2011).[15]

While we tend to think of the audit in binary terms of "audit client" and "auditor," auditors can find themselves operating as relationship managers integrating the competencies of a number of parties in the audit process and satisfying their different expectations. The audit committee, for example, participates in the "co-creation" of the audit process across the network of audit participants.[16] Rather than just serving as an additional monitor, the audit committee functions best when it brings its own unique competencies to the process by being actively involved in agenda setting, reviewing management's choice of accounting policies and management's accounting estimates, considering fraud risks, and taking responsibility for the internal audit function (Beasley, Carcello, Hermanson, and Neal 2009).[17]

[12] "Out west near Hawtch-Hawtch, there's a Hawtch-Hawtcher Bee-Watcher, his job is to watch. Is to keep both his eyes on the lazy town bee, a bee that is watched will work harder you see. So he watched and he watched, but in spite of his watch that bee didn't work any harder not mawtch. So then somebody said 'Our old bee-watching man just isn't bee watching as hard as he can, he ought to be watched by another Hawtch-Hawtcher! The thing that we need is a bee-watcher-watcher!'. Well, the bee-watcher-watcher watched the bee-watcher. He didn't watch well so another Hawtch-Hawtcher had to come in as a watch-watcher-watcher! And now all the Hawtchers who live in Hawtch-Hawtch are watching on watch watcher watchering watch, watch watching the watcher who's watching that bee. You're not a Hawtch-Watcher, you're lucky you see!" (Dr. Seuss [Theodor Geisel] 1973).

[13] The more parties there are in a service network, the greater the likelihood that there will be goal misalignments between parties (van der Valk and van Iwaarden 2011). Auditors may have to contend with the reality that some members of the audit client have a higher commitment to quality financial reporting than others. For example, a CEO might be more concerned about missing analyst forecasts than the CFO or the audit committee (Beattie, Fearnley, and Brandt 2001).

[14] Having more participants increases the costs of integrating the competencies of all parties that participate in the audit. One obvious cost would be in the time needed to bring the audit to completion. We thank the reviewer who provided this observation.

[15] Agency theory (Jensen and Meckling 1976) frames the relationship between client firm (principal) and auditor (agent) as contractual and formal, with strategic actors motivated by coldly rational economic incentives. A service perspective emphasizes that auditor and client firm must work together to jointly produce the audited financial report. Maximizing effective collaboration requires building trust, communication, and relationship management.

[16] Audit committees have the role of working with the board of directors, management, external auditor, and internal auditors. From a service perspective, the audit committee improves the audit by bringing its unique competencies but also by assisting the auditor in integrating the competencies of all the other parties in the audit network.

[17] The audit client's internal auditors are another party that contributes to the audit. Audit research has tended to focus on the extent to which the external auditor can reduce effort by relying on the work of the internal auditor, but the internal auditor can also work *with* the external auditor in identifying potential weaknesses in controls or financial reporting. Lin, Pizzini, Vargus, and Bardhan (2011) provide evidence that the collaboration of external and internal auditors leads to greater detection and disclosure of material weaknesses.

Proposition 3

Since audits involve a network of actors, an audit failure may be less the failure of the auditor and more a failure of the network.[18] Managers who obstruct or minimally contribute to the audit, or audit committees that are merely ceremonial, might undermine the audit in ways that make it difficult for the auditor to overcome. While research shows that auditors increase substantive testing when dissatisfied with "the tone at the top" (Cohen and Hanno 2000; D. Sharma, Boo, and V. Sharma 2008), it is unclear whether the auditor's response fully mitigates the audit risk incurred by weak governance. Ultimately the success of the audit is the responsibility of the auditor, but audits might fail because of poor performance from parties other than the auditor.[19]

Naturally there are concerns about whether close cooperation between the auditor and client personnel undermines auditor independence. The AICPA identifies a "familiarity threat" to auditor independence, which is "the threat that, due to a long or close relationship with a client, a member will become sympathetic to the client's interest or too accepting of the client's work or product" (AICPA 2014, section 1.000.12). While the service relationship may generate potential threats to auditor independence, it also creates potential safeguards. Service providers develop an understanding of, and relationships with, their clients that increase the clients' dependency on the service providers. Providing better service can strengthen the auditor's hand when working with the client, thereby increasing an auditor's ability to remain independent in fact (i.e., skeptical). Knechel et al. (2020) identifies two examples of how auditors can strengthen independence within the audit service network: (1) auditor specialization of knowledge[20] and (2) extensive co-investments between the auditor and the client.[21]

Efforts to reduce the familiarity threat to auditor independence in appearance, such as audit partner rotation or audit firm rotation, might undermine these safeguards. Creating distance can have the effect of decreasing the client's dependence on the auditor. The more standardized and

[18] As noted in the introduction, audit quality is typically framed as a function of the auditor alone: the likelihood of the auditor detecting and reporting a breach (DeAngelo 1981). A service perspective broadens determinants of audit quality to include the role of the client firm, and the resulting working relationship between auditor and client firm.

[19] Auditors are required to provide reasonable assurance due to "inherent limitations of an audit" (see AICPA AU-C 200.06, AICPA 2011; ISA 200.18, IAASB 2007). The quality of cooperation from other parties can be considered part of those inherent limitations, although these inherent limitations should not prevent the auditor from providing "reasonably" high assurance. We thank the reviewer who provided this observation.

[20] One source of independence in a professional service organization is specialization of knowledge (expertise), also referred to as "knowledge intensity" (von Nordenflycht 2010) or "knowledge power" (Sharma 1997). An imbalance in knowledge intensity can make the other members of a collaborative network dependent on the specialized expertise of a professional. Research on auditor-client negotiations suggests that auditors who bring more expertise to the final discussion of accounting adjustments can obtain improved results (Ng and Shankar 2010; Gibbins et al. 2010). Knowledge intensity and professional status can also partially insulate a professional against the loss of objectivity (independence) that might accompany economic dependence.

[21] The longer the working relationship between a service provider and customer, the harder it is for another service provider to step in and provide an identical service, i.e., a long working relationship creates supplier differentiation (de Brentani and Ragot 1996; Eriksson and Vaghult 2000; Sharma and Patterson 2000). This is true of audit services as the time required for a client to replace an auditor can be substantial (Fiolleau, Hoang, Jamal, and Sunder 2013). In general, client retention is a very important factor for service quality because longer relationships promote cooperation (Boström 1995). Audit research indicates that shorter auditor tenures may result in less client-specific knowledge (Stice 1991), weakened influence over audit adjustments (Iyer and Rama 2004), and less sharing of important information (Bell, Causholli, and Knechel 2015; DeFond and Zhang 2014).

homogenous audits are, the easier it is for audit clients to change auditors when the auditor is telling them things they would rather not hear.

IV. AUDIT QUALITY DEPENDS UPON PERCEPTIONS WITHIN THE COOPERATIVE NETWORK

Proposition 4

In the manufacturing of goods, quality is commonly considered objectively in terms of how often a process or output deviates from established parameters.[22] With services, quality is often measured subjectively as the difference between what the customer/client expects and what is experienced (Parasuraman, Zeithaml, and Berry 1985).[23] Service researchers use a "gaps model" to describe the different ways that a customer/client experience might deviate from expectations (Parasuraman et al. 1985).

In the context of audit, the "expectations gap" describes financial statement users' expecting a level of assurance that audits are not designed to provide,[24] as if an audit is established without the concern or involvement of relevant stakeholders. Accordingly, the accounting profession commonly assumes the expectations gap is a misunderstanding of financial statement users that should be addressed by better explanations of the assurance audits provide (Reinstein and McMillan 2004). From a service perspective, however, stakeholder expectations develop through the interaction of the auditor and audit stakeholders, as they mutually determine the nature of their specific audit relationship.

Service science theory predicts that auditors will provide assurance responsive to the specific demands of relevant stakeholders, rather than uniform assurance based solely on standards. This point is captured to some extent by the concept of "qualitative materiality." If an audit client has debt covenants, for example, the auditor should adjust materiality thresholds to provide assurance that the debt covenants are not being violated (PCAOB 2010). Audit research also indicates that companies will seek higher-reputation auditors when stakeholders demand higher levels of assurance (Abdel-Khalik 1993; Knechel, Niemi, and Sundgren 2008). From a service perspective, variation in assurance provided by audits is a natural response to market demand and is not necessarily evidence of auditors performing improperly. A variation in audit quality does not mean that an audit does not satisfy auditing standards if the expectations of various stakeholders exceed a standards-compliant audit (Knechel 2013).

22 Producing goods more efficiently (through standardization) generates increased quality (through minimization of defects). We return to this idea in Section V.

23 The fact that audits are "consumed" by many stakeholders (e.g., investors, but also the client firm, etc.) further complicates perceptions of audit quality. Further, it is difficult to assess audit quality even after audit completion, suggesting that audits meet the criteria of a credence good (service) (Causholli and Knechel 2012). This uncertainty about (actual) quality is another reason why perceptions of quality are so relevant in an audit context.

24 This could be stakeholders expecting perfect assurance rather than reasonable assurance, or stakeholders expecting assurance on matters that are beyond the design of a financial statement audit.

V. EXCESSIVE STANDARDIZATION IN THE AUDIT PROCESS MAY UNDERMINE AUDIT QUALITY

Proposition 5

The accounting profession and its regulators often treat auditing more like a manufacturing than service process, with audit quality being measured by perceived deviations from standards.[25] The provision of services is distinct from that of goods, however, because service efficiency (i.e., standardization) can be negatively associated with service quality. The service science literature emphasizes the heterogeneity of the service process and its costs, which follows from the close interaction with the service customer (Chase and Apte 2007). In an audit context, heterogeneity arises from: (1) variability in client and environmental characteristics, (2) the nature of the collaborative audit network, and (3) possible variation in audit demand, e.g., a private company audited to obtain a bank loan. Audit quality depends upon respect for these idiosyncrasies. Through the interaction with the network participants, service providers tailor their services to the needs of the stakeholders. Efforts to make the audit process more uniform might improve efficiency but can impair audit quality.[26]

VI. PRACTICAL IMPLICATIONS

The theoretical conclusions of this paper suggest that auditors might conduct higher-quality audits and provide better value to their clients by embracing the idea that auditing is an economic service. Possible practical implications of this viewpoint include:

- *Audit standards are means, not ends*. Audits are heavily structured by the requirements of audit standards and regulators. Nonetheless audits are not intended to *serve* standard-setters or regulators. Audits benefit clients and users of financial information by providing assurance on historical financial information. Audit standards should be followed in order to appropriately satisfy the specific needs of the client and those who rely on the client's financial information.
- *Take audit planning/risk assessment procedures seriously*. Ironically, thinking of auditing primarily in terms of compliance with standards can lead auditors to follow audit standards more in form than in spirit by rolling forward their audit programs from prior years, or using nearly identical audit programs for different clients, and then "back into" the risk assessments consistent with those programs. A quality audit depends upon a respect for the idiosyncrasies of each audit client.

---

[25] The heavy reliance on standards in auditing is justified because, unlike many services, the primary consumers of the audit are separate from the audit client firm who pays for and assists with the audit. Auditing standards are intended to protect the users who are remote from the audit process itself.

[26] Knechel et al. (2020) discuss Proposition 5-1 in more detail. In brief, service researchers distinguish elements that require direct customer contact/input ("front office") from those that do not ("back office"). Back office activities can be standardized much more than front office activities (Sampson and Froehle 2006). Audit information technologies, audit client platforms, technical departments, and the offshoring of routine audit procedures are examples of "back office" activities that may be standardized. Service researchers also distinguish "economies of scope" (spreading costs across services), efficiencies that service firms can achieve, from "economies of scale" (spreading costs across clients), which is more associated with manufacturing environments (Normann and Ramírez 1998). Non-audit services (NAS) are an example of "economies of scope" for audit firms.

- *Include assessments of the extent and quality of client cooperation when forming audit strategy*. The audit risk model states that material misstatement risk in audited financial statements is a product of inherent risk, control risk, and detection risk. While the auditor has ultimate responsibility for reducing detection risk to an appropriately low level, detection risk is also affected by client cooperation in the audit. Clients who cooperate begrudgingly or actively deceive make it more likely that auditors will fail to address "unknown unknowns," i.e., inherent or control risks not encountered in previous audits. Auditors might explicitly consider and document the quality of client cooperation when determining which audit team members to assign and which audit procedures to perform.
- *Develop an understanding of the needs of financial statement users*. Auditors might consider formal assessments of financial statement user needs (and other audit stakeholders) during audit planning, either through direct communication or planning analytics modeled on techniques that investors and creditors use to evaluate the audit client. Materiality is fundamentally about what matters to financial statement users. Determining financial statement user needs can affect audit procedures performed and the content of the audit report, e.g., critical audit matters, emphasis of matters, and other matters.
- *Provide value to the audit client*. Regulations and professional ethics put limits on services that auditors can provide for their clients, but auditors still provide much value to audit clients beyond the issuing of an audit opinion. Providing value to the client and its stakeholders helps the auditor create a unique service that reflects the nature of the collaborative network (e.g., the management letter). Providing value to the client may strengthen an auditor's independence, as managers may be more cooperative when they perceive the audit service as something more than a necessary evil.[27]

Framing financial audits as an economic good has profound implications for how relevant stakeholders think about auditing. A service perspective introduces new complexities to our understanding of auditing—highlighting the variety of producers and consumers of the audit, the idiosyncrasies of each audit engagement, and the inefficiencies generated therein—but also offers roads to possible solutions. We hope that the ideas proposed in this paper provide an initial foundation which encourages relevant stakeholders to begin thinking about financial auditing from a service perspective.

REFERENCES

Abdel-Khalik, A. R. 1993. Why do private companies demand auditing? A case for organizational loss of control. *Journal of Accounting, Auditing & Finance* 8 (1): 31–52. https://doi.org/10.1177/0148558X9300800103

American Institute of Certified Public Accountants (AICPA). 2011. *Overall objectives of the independent auditor and the conduct of an audit in accordance with generally accepted auditing standards. AU-C Section 200*. New York, NY: AICPA. Available at: https://us.aicpa.org/content/dam/aicpa/research/standards/auditattest/downloadabledocuments/au-c-00200.pdf

American Institute of Certified Public Accountants (AICPA). 2014. *AICPA Code of Professional Conduct*. New York, NY: AICPA. Available at: https://us.aicpa.org/research/standards/codeofconduct

[27] Research on auditor-client negotiations indicates that auditors use reciprocity-based strategies to improve managerial cooperation (Hatfield, Agoglia, and Sanchez 2008; Hatfield, Houston, Stefaniak, and Usrey 2010). An auditor's careful evaluation of the design and operating effectiveness of client controls, for example, might be seen by the client as a benefit and a reason to actively assist the auditor in the audit.

Beasley, M. S., J. V. Carcello, D. R. Hermanson, and T. L. Neal. 2009. The audit committee oversight process. *Contemporary Accounting Research* 26 (1): 65–122. https://doi.org/10.1506/car.26.1.3
Beattie, V., S. Fearnley, and R. Brandt. 2001. *Behind Closed Doors. What Company Audit Is Really About*. Basingstoke, U.K.: Palgrave.
Bell, T. B., M. Causholli, and W. R. Knechel. 2015. Audit firm tenure, non-audit services, and internal assessments of audit quality. *Journal of Accounting Research* 53 (3): 461–509. https://doi.org/10.1111/1475-679X.12078
Boström, G.-O. 1995. Successful cooperation in professional services. What characteristics should the customer have? *Industrial Marketing Management* 24 (3): 151–165. https://doi.org/10.1016/0019-8501(94)00042-U
Brydon, D. 2019. *Assess, Assure and Inform: Improving Audit Quality and Effectiveness. Report of the Independent Review into the Quality and Effectiveness of Audit*. Cheshire, U.K.: APS Group. Available at: https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/852960/brydon-review-final-report.pdf
Causholli, M., and W. R. Knechel. 2012. An examination of the credence attributes of an audit. *Accounting Horizons* 26 (4): 631–656. https://doi.org/10.2308/acch-50265
Chase, R. B., and U. M. Apte. 2007. A history of research in service operations: What's the big idea? *Journal of Operations Management* 25 (2): 375–386. https://doi.org/10.1016/j.jom.2006.11.002
Cohen, J. R., and D. M. Hanno. 2000. Auditors' consideration of corporate governance and management control philosophy in preplanning and planning judgments. *Auditing: A Journal of Practice & Theory* 19 (2): 133–146. https://doi.org/10.2308/aud.2000.19.2.133
de Brentani, U., and E. Ragot. 1996. Developing new business-to-business professional services: What factors impact performance? *Industrial Marketing Management* 25 (6): 517–530. https://doi.org/10.1016/S0019-8501(96)00066-1
DeAngelo, L. E. 1981. Auditor size and audit quality. *Journal of Accounting and Economics* 3 (3): 183–199. https://doi.org/10.1016/0165-4101(81)90002-1
DeFond, M. L., and J. Zhang. 2014. A review of archival auditing research. *Journal of Accounting and Economics* 58 (2–3): 275–326. https://doi.org/10.1016/j.jacceco.2014.09.002
Demski, J. S., and R. J. Swieringa. 1974. A cooperative formulation of the audit choice problem. *The Accounting Review* 3: 506–513.
Dr. Seuss (Theodor Geisel). 1973. *Did I Ever Tell You How Lucky You Are?* New York, NY: Random House.
Eriksson, K., and A. L. Vaghult. 2000. Customer retention, purchasing behavior and relationship substance in professional services. *Industrial Marketing Management* 29 (4): 363–372. https://doi.org/10.1016/S0019-8501(00)00113-9
Fiolleau, K., K. Hoang, K. Jamal, and S. Sunder. 2013. How do regulatory reforms to enhance independence work in practice? *Contemporary Accounting Research* 30 (3): 864–890. https://doi.org/10.1111/1911-3846.12004
Gibbins, M., S. McCracken, and S. E. Salterio. 2010. The auditor's strategy selection for negotiation with management: Flexibility of initial accounting position and nature of the relationship. *Accounting, Organizations and Society* 35 (6): 579–595. https://doi.org/10.1016/j.aos.2010.01.001
Grönroos, C. 2011. Value co-creation in service logic: A critical analysis. *Marketing Theory* 11 (3): 279–301. https://doi.org/10.1177/1470593111408177
Guénin-Paracini, H., B. Malsch, and M. S. Tremblay. 2015. On the operational reality of auditors' independence: Lessons from the field. *Auditing: A Journal of Practice & Theory* 34 (2): 201–236. https://doi.org/10.2308/ajpt-50905
Hall, H. 2021. *How to identify and manage audit stakeholders*. Available at: https://cpahalltalk.com/audit-stakeholders/
Hatfield, R. C., C. P. Agoglia, and M. H. Sanchez. 2008. Client characteristics and the negotiation tactics of auditors: Implications for financial reporting. *Journal of Accounting Research* 46 (5): 1183–1207. https://doi.org/10.1111/j.1475-679X.2008.00302.x
Hatfield, R. C., R. W. Houston, C. M. Stefaniak, and S. Usrey. 2010. The effect of magnitude of audit difference and prior client negotiations of proposed adjustments. *The Accounting Review* 85 (5): 1647–1668. https://doi.org/10.2308/accr.2010.85.5.1647
Havila, V., J. Johanson, and P. Thilenius. 2004. International business-relationship triads. *International Marketing Review* 21 (2): 172–186. https://doi.org/10.1108/02651330410531385
Hellman, N. 2006. Auditor-client interaction and client usefulness—A Swedish case study. *International Journal of Auditing* 10 (2): 99–124. https://doi.org/10.1111/j.1099-1123.2006.00345.x
International Auditing and Assurance Standards Board (IAASB). 2007. *ISA 200: Overall objective of the independent auditor, and the conduct of an audit in accordance with international standards on auditing*. Available at: https://www.ifac.org/system/files/meetings/files/3393.pdf

Iyer, V. M., and D. Rama. 2004. Clients' expectations on audit judgments: A note. *Behavioral Research in Accounting* 16 (1): 63–74. https://doi.org/10.2308/bria.2004.16.1.63

Jensen, M. C., and W. H. Meckling. 1976. Theory of the firm: Managerial behavior, agency costs, and ownership structure. *Journal of Financial Economics* 3 (4): 305–360. https://doi.org/10.1016/0304-405X(76)90026-X

Kingman, J. 2018. *Independent review of the Financial Reporting Council (FRC)*. December 18. Report prepared for the Department for Business, Energy and Industrial Strategy, United Kingdom. Available at: *https://www.gov.uk/government/publications/financial-reporting-council-review-2018*.

Knechel, W. R. 2013. Do auditing standards matter? *Current Issues in Auditing* 7 (2): A1–A16. https://doi.org/10.2308/ciia-50499

Knechel, W. R., L. Niemi, and S. Sundgren. 2008. Determinants of auditor choice: Evidence from a small client market. *International Journal of Auditing* 12 (1): 65–88. https://doi.org/10.1111/j.1099-1123.2008.00370.x

Knechel, W. R., E. Thomas, and M. Driskill. 2020. Understanding financial auditing from a service perspective. *Accounting, Organizations and Society* 81: 101080. https://doi.org/10.1016/j.aos.2019.101080

Lin, S., M. Pizzini, M. Vargus, and I. R. Bardhan. 2011. The role of the internal audit function in the disclosure of material weaknesses. *The Accounting Review* 86 (1): 287–323. https://doi.org/10.2308/accr.00000016

Ng, T. B., and P. G. Shankar. 2010. Effects of technical department's advice, quality assessment standards, and client justifications on auditors' propensity to accept client-preferred accounting methods. *The Accounting Review* 85 (5): 1743–1761. https://doi.org/10.2308/accr.2010.85.5.1743

Normann, R., and R. Ramírez. 1998. *Designing Interactive Strategy: From Value Chain to Value Constellation*. Chichester, U.K.: Wiley.

Parasuraman, A., V. A. Zeithaml, and L. L. Berry. 1985. A conceptual model of service quality and its implications for future research. *Journal of Marketing* 49 (4): 41–50. https://doi.org/10.1177/002224298504900403

Public Company Accounting Oversight Board (PCAOB). 2010. *The Auditor's Responses to the Risks of Material Misstatement. Auditing Standard No. 13. PCAOB Release No. 2010-004*. Washington, DC: PCAOB. Available at: https://pcaobus.org/oversight/standards/archived-standards/pre-reorganized-auditing-standards-interpretations/details/Auditing_Standard_13

Reinstein, A., and J. J. McMillan. 2004. The Enron debacle: More than a perfect storm. *Critical Perspectives on Accounting* 15 (6–7): 955–970. https://doi.org/10.1016/j.cpa.2003.08.006

Sampson, S. E. 2010. The unified service theory: A paradigm for service science. In *Handbook of Service Science*, edited by P. P. Maglio, C. A. Kieliszewski, and C. James, 107–131. New York, NY: Springer.

Sampson, S. E., and C. Froehle. 2006. Foundations and implications of a proposed unified services theory. *Production and Operations Management* 15 (2): 329–343. https://doi.org/10.1111/j.1937-5956.2006.tb00248.x

Sharma, A. 1997. Professional as agent: Knowledge asymmetry in agency exchange. *Academy of Management Review* 22 (3): 758–798. https://doi.org/10.5465/amr.1997.9708210725

Sharma, N., and P. G. Patterson. 2000. Switching costs, alternative attractiveness and experience as moderators of relationship commitment in professional, consumer services. *International Journal of Service Industry Management* 11 (5): 470–490. https://doi.org/10.1108/09564230010360182

Sharma, D. S., E. Boo, and V. D. Sharma. 2008. The impact of non-mandatory corporate governance on auditors' client acceptance, risk and planning judgments. *Accounting and Business Research* 38 (2): 105–120. https://doi.org/10.1080/00014788.2008.9663324

Spohrer, J. C., and P. P. Maglio. 2008. The emergence of service science: Toward systematic service innovations to accelerate co-creation of value. *Production and Operations Management* 17 (3): 238–246. https://doi.org/10.3401/poms.1080.0027

Stice, J. 1991. Using financial and market information to identify pre-engagement factors associated with lawsuits against auditors. *The Accounting Review* 66 (3): 516–533.

van der Valk, W., and J. van Iwaarden. 2011. Monitoring in service triads consisting of buyers, subcontractors and end customers. *Journal of Purchasing and Supply Management* 17 (3): 198–206. https://doi.org/10.1016/j.pursup.2011.05.002

Vargo, S. L., R. F. Lusch, and M. A. Akaka. 2010. Advancing service science with service-dominant logic. In *Handbook of Service Science*, edited by P. P. Maglio, C. A. Kieliszewski, and C. James, 133–156. New York, NY: Springer.

von Nordenflycht, A. 2010. What is a professional service firm? Toward a theory and taxonomy of knowledge-intensive firms. *Academy of Management Review* 35 (1): 155–174.