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A genealogy of accounting materiality

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ABSTRACT

This study explores the relevance of the historical dimensions of the materiality concept and its past role. Metaphors applied to materiality provide insights into conditions and traces of power that have shaped its discursive configuration. Rather than viewing materiality as the gradual development of a technical idea over time, metaphorical discourses suggest that it has been constituted as multiple categories of knowledge, with divergent roles, as: a moral responsibility; a solution to the problem of over-auditing; a solid epistemic foundation for financial reporting; a scientific technique; a quantitative rule of thumb; a risk management concept; and a mysterious shield. The malleable nature of the concept has allowed the profession to realign and reinvent it to meet shifting priorities and challenges. Divergence in the trajectories of materiality discourses is relative to certain conditions, events, actors and financial scandals. The paper draws on the metaphor of performance, to interpret materiality as a performative activity at the crux of truth games about making visible, controlling, taming, managing and hiding translation errors in accounting inscriptions. The extent to which a genealogical analysis identifies different styles of reasoning that have shaped its meaning over time has implications for debate about its future development.

1. Introduction

Materiality is a fundamentally important accounting concept (Messier et al., 2005), generally understood to involve the determination of the importance of a matter for financial reporting purposes (FASB, 1975). It also has a fuzzy ontology that has persistently evaded precise codification in professional guidance (Power, 1997, p. 36 Ling Lee, 2004). Decisions about materiality are a matter of professional judgement and no set of rules can be applied to determine thresholds in all circumstances (Gray and Manson, 2008; IFAC, 2010a,b). Nevertheless, it is a *seemingly* time-honoured concept (Lackritz, 2004; Wilcox, 2007), familiar to agents involved in the preparation, audit, analysis and regulation of financial statements (European Securities and Markets Authority – ESMA, 2012).

Scholarship has explored the nature and operationalisation of materiality. Detailed literature reviews have been conducted by, amongst others, Iskandar and Iselin (1999), Messier et al. (2005) and Brennan and Gray (2005). Yet, scant information exists about its beginnings. Little was written about materiality until after the Second World War (Hicks, 1964) and the importance of its past role, in a social and professional context, has perhaps been overlooked.

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The current study seeks to address this gap by exploring materiality's historical ontology (Hacking, 2004). Historical ontology is a form of enquiry that considers how concepts retain traces of the influence of their historical dimensions.[1] To this end, the paper undertakes a genealogical analysis, drawing on Foucault, to investigate conditions that have shaped our knowledge of materiality. Foucault developed genealogy as a tool to query what lies beneath the emergence of discourses. His ambition was to fragment and de-familiarize beliefs that "we tend to feel are without history" (Foucault, 1980, p. 139). Concepts are not the gradual, seamless, teleological development of ideas over time (Foucault, 1970) but are configured through discourses (Macintosh, 2009). Therefore, truths provided for us by our discourses have a history contingent upon certain past events, happenings, ruptures and struggles between power blocs (Foucault, 1986; Kearins and Hooper, 2002; Macintosh, 2009). By power, Foucault was referring, not to a specific authority, but to anonymous arrangements that exercise control over systems of thought (Hacking, 2004). Our beliefs change, relative to systems of domination that are powerful enough to influence ways in which we think about the world (Macintosh, 2009; Jones et al., 2011).

The objective of this historical analysis is therefore not to ask what materiality '*is*' or unveil misconceptions or hidden truths in discourses but to question how others have sought to construct it (Foucault, 1986; Bartleson, 1995; Hacking, 2004). The focus is on the constitutings of materiality (Hacking, 2004), particularly on the conditions, events, traces of power and expert discourses that have shaped its existence.

As a precedent for this type of critical history, prior scholarship has investigated the past of other key accounting concepts and practices. Miller and O'Leary (1987) interpreted standard costing and budgeting as an apparatus of control over the performance of individuals. Sikka and Willmott (1995) explored the power of independence in building and defending a professional accounting jurisdiction. Maltby (2000) identified links between prudence and the practice of the social regulation of capital. Power (2012) explored fraud risk as a system of intense organisational governance and discipline. The current study reflects on the role of materiality as attempts by competing powers and expertises (Samiolo, 2012) to make visible, mediate, control, tame, manage, ignore, hide or downplay errors and ambiguities in the process of translating the elements of an organisational context into accounting inscriptions (Robson, 1992).

The specific contribution of the paper lies in developing two, related ideas. First, different expertises and metaphorical discourses have constituted materiality as a multiplicity of knowledge objects including: a moral responsibility; a commercial solution to over-auditing; a solid 'thing' and epistemic foundation for reporting; a scientific technique; a rule of thumb, a risk management tool, a mysterious professional lens and shield. Second, the paper explores how assemblages of factors, actors, powers and events have shaped the trajectories of materiality discourses.

The paper attempts to adopt a novel method. Discursive figures of speech are used, as a linguistic tool, to unearth clues about relevant genealogical factors. Metaphors and similes complement a genealogical approach because they provide an insight into traces of power, systems of thought and truth games that underlie meanings. Themes within metaphors applied to materiality and modes of use (whether strategic, reflective or critical) demonstrate how its construction has not been the product of any single, dominant, primary logic. Multiple factors have sculpted its complex ontology. The study also builds on the seminal work of Carpenter et al. (1994) who were amongst the first to explore materiality as a social and behavioural rather than a technical or cognitive phenomenon.

The findings of the current study seek to contribute to the accounting literature. Materiality is often referenced, as if its meaning, technical discourses and expertises that have constructed it, are solid and timeless. This critical analysis questions such assumptions. The paper may also have a practical significance for practitioners in understanding how materiality has historical dimensions, shaped by different, at times conflicting, expertises. Viewing materiality decisions as a performance by a group of actors, where expertises are drawn upon and ranked, may broaden horizons within which materiality decisions are reached.

Section 2 of the paper contextualises the study and begins with a review of the materiality concept in accounting and auditing. Section 3 explains why a Foucauldian methodological approach provides a relevant framework for an analysis of materiality and discusses the method of analysis adopted. Section 4 evaluates themes in metaphor applied to materiality to probe factors that have underpinned the development of materiality discourses, with a discussion of findings in Section 5. Concluding remarks summarise the paper in Section 6.

2. Materiality in accounting and auditing

The following section provides a context for the current study. First, the obscure beginnings of materiality and early references to the concept are considered. Problematics associated with inconsistencies and vagueness in definitions are discussed. Second, themes in scholarship on the subject are explored. Sections 3 and 4 attempt to suggest that a genealogical analysis may assist reflexivity about materiality by considering its historical dimensions and systems of thought that have shaped it as an object of knowledge.

[1] This term was originally put forward by Michel Foucault, concerned with truth through which we constitute ourselves as objects of knowledge, with power, through which we constitute ourselves as subjects acting on others and with ethics through which we constitute ourselves as moral agents. Ian Hacking expands this term to examine all manner of constitutings and the relevance of the historical dimensions of concepts. Some problems with concepts may be traced back to their past (Hacking, 2002, p. 37).

2.1. Background

Materiality is a pluralistic term (OED, 2010) representing, in a simple sense, the stuff of the world (Dale, 2005). As a metaphysical construct, it refers to an abstract notion of materiality, relative to ideas about immateriality (Miller, 2005). Metaphorically, the term denotes substance or importance in evaluating criteria and reaching judgments (in the OED, 2010; Bentham, 1789; Kennedy, 1860; Stephen, 1824). A related notion of a *test* of materiality (or significance) has spread into professional discourses such as law and accounting.

In accounting, the term *material*, as an adjective, first appeared in accounting and auditing texts at the turn of the twentieth century and in US guidance, issued by the American Institute of Certified Public Accountants (AICPA) (Newman and Mellman, 1967). Accounting historians have assumed that the concept was legalistic in origin, as a sense of obligation[2] in setting out material facts (Holmes, 1972; Lee, 1984). References to material facts have been traced back to UK legal cases in the 1860s and the Companies Act 1985[3] (Holmes, 1972, p. 46). The word material has also been used, in a simplistic sense, to refer to the importance of instructions for auditors (Dicksee, 1892).[4] The term was probably introduced to the US in the late 19th Century by emigrating British accountants. It was not formally defined at this time although legal definitions existed (Holmes, 1972).[5]

As the accounting profession began to develop formalised guidance in the US, particularly from 1938 onwards (Dyckman and Zeff, 1984; Zeff, 2009), a discursive shift took place. Definitions of a technical understanding of materiality materialised. From the outset, different ways of thinking about materiality were apparent. For example, Kohler's dictionary for accountants in the US defined materiality as:

> "the characteristic attaching to a statement, fact, or item whereby its disclosure or the method of giving it expression would be likely to influence the judgment of a reasonable person," (Kohler, 1952, p. 317).[6]

A few years later, the American Accounting Association (AAA) produced the following definition,

> "An item should be regarded as material if there is reason to believe that knowledge of it would influence the decisions of an informed investor," (AAA, 1957, p. 8).

Kohler defined materiality as a characteristic *attaching* to an item. In contrast, the AAA linked the concept *with* professional judgement, under an "*if*" condition. Furthermore, the notion of Kohler's reasonable person signals different information needs compared to an informed investor. Such differences raise important questions about broader genealogical and not just technical factors that lie beneath divergences in discourses, which this study seeks to examine.

Many subsequent definitions of materiality have been produced, by professional accounting bodies, the Securities and Exchange Commission (SEC), common law and statute but none have been in complete agreement (Brennan and Gray, 2005). This heterogeneity is specifically mentioned in International Standard on Auditing (ISA) 320, "financial reporting frameworks may discuss materiality in different terms." ISA 320 no longer attempts to define materiality but states:

> "they (financial reporting frameworks) generally explain that: misstatements, including omissions, are considered to be material if they, individually or in the aggregate, could reasonably be expected to influence the economic decisions of users taken on the basis of the financial statements; judgments about materiality are made in light of surrounding circumstances and are affected by the size or nature of a misstatement, or a combination of both," (IFAC, 2010a,b, para 2).

Brennan and Gray (2005, p. 4) have identified shared characteristics of materiality. Companies are required to disclose a true and fair view in law but this is subject to uncertainty. Materiality allows a degree of flexibility. First, materiality decisions are a matter of professional judgement. Second, information is considered material if its omission or misstatement could influence the economic decisions of users, for whose benefit the concept operates. However, no source of guidance has, to date, codified the concept precisely (Power, 1997), with variations around the subject of the definition and the degree of uncertainty involved (Brennan and Gray, 2005).

The concern of this paper is with an examination of factors that have underpinned different discourses about this elusive concept. In scoping the study, it is important to mention that materiality is relevant in both accounting and auditing. These meanings are related but distinct (Thomas and Krogstad, 1979; Flint, 1988). Initial decisions about accounting materiality are made by management in preparing financial statements. Where a financial audit is undertaken, independent decisions about thresholds are reached by auditors (Gray and Manson, 2008). The focus of this paper is on materiality in auditing

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[2] "The public accountant is *bound* to see that all material facts are set out in his certificate," (Dickinson, 1908, in Holmes, 1972, p. 46). Holmes suggested that a sense of legal obligation is implied in this context by the term *bound*.

[3] Holmes (1972, p. 46) mentioned the following examples "In any prospectus no misstatements or concealment of any *material* fact ought to be permitted," *Central Railway of Venezuela v Kisch* (1867), in addition, Lord Davey's committee in updating the Companies Act 1985 reported "every contract or fact is material which would influence the judgement of a prudent investor."

[4] "The printed instructions cannot be more than a mere outline of an Auditors duties but they can be so framed as to be of *material* assistance to the audit clerks," Dicksee (1892, p. 19).

[5] Holmes (1972) did not provide any examples but legal definitions did certainly exist. For example, Wharton's (1883) legal dictionary explained the term material as "the subject matter of the statement (or concealment) related to a fact or circumstance which would be important to the decision to be made as distinguished from an insignificant, trivial or unimportant detail."

[6] Kohler was the editor of the Accounting Review, the Journal of the American Association of University Instructors (Dyckman and Zeff, 1984).

because it is through financial audit that the concept is linked to ideas about fair representation and quality in reporting (Lee, 1984; Brennan and Gray, 2005).

2.2. Prior scholarship

Not surprisingly, materiality has attracted academic interest. Scholarship has sought to explore what materiality is and how it is operationalised. Empirical research, in the 1950s investigated quantitative variables involved in decisions. Early studies, using case study questions and questionnaires, identified the percentage effect of an item on net profit as a dominant determinant in judgments (Woolsey, 1954). Later studies confirmed this finding but significant variations in materiality thresholds were observed (Bernstein, 1967). Concerns about divergence led to numerous calls for more detailed professional guidance and case studies (Reininga, 1968; Frishkoff, 1970).

Later research, from the 1970s and 1980s onwards, queried the circumstances of auditor materiality judgments, especially cues and factors influencing decisions. Findings varied because of the different items and contexts studied but a number of themes were apparent (Messier et al., 2005). First, materiality was a relative notion where the size of an item relative to net profit was a primary cue in decision-making (Iskandar and Iselin, 1999; Holstrum and Messier, 1982; Messier et al., 2005). Second, qualitative factors influenced judgments, particularly experience. Although auditors were homogenous in their beliefs about materiality as a significant error, they scaled variables differently at various levels of management (Ward, 1976). Experienced individuals applied more scrutiny in non-routine transactions and experience was influential in less structured tasks (Messier, 1983; Carpenter and Dirsmith, 1992). Firm size and industry factors were further factors that affected auditor judgments (Pattillo and Siebel, 1974; Krogstad et al., 1984; Wright and Wright, 1997). Higher materiality levels were observed amongst partners of large audit firms (Messier, 1983; Chewning et al., 1989). Personal characteristics, such as age and place of employment could also affect materiality decisions (Estes and Reames, 1988). Moriarty and Barron (1976) found divergence in auditor judgments in evaluating quantitative and qualitative factors.

Third, materiality judgments varied between management, auditors and users. These heterogeneous groups demonstrated different thresholds because of their divergent motivations (Firth, 1979; Holstrum and Messier, 1982; Messier et al., 2005). Differences were also apparent in thresholds between auditors and the courts (Jennings et al., 1987). Variation in judgement amongst preparers, auditors, information users and accounting enforcers remains a concern amongst practitioners, academics and lawyers and has been described as a dilemma and a source of insecurity (Reininga, 1968; Jennings et al., 1984–1985, 1987; Ling Lee, 2004).[7]

Interdisciplinary, qualitative research has investigated materiality not as a technical or cognitive phenomenon but in a social and organisational context. Carpenter et al. (1994), in their seminal study, adopted a cultural anthropology approach to exploring materiality, viewing human thought as a culturally coded product. Differences were observed in the number of cues used by less structured, organic firms *versus* highly structured mechanistic firms. Individuals became differentiated by their hierarchical position suggesting that materiality is a social, behavioural phenomenon and the consequence of social interaction in the context of firm culture.

Critical studies have highlighted a lack of transparency in the concept of materiality. The term is not well specified or applied consistently, leaving the profession open to charges of mystification and paternalism. Auditors reach authoritative judgments about thresholds for the benefit of users but without any responsibility to disclose the criteria that underpin decisions (Roberts and Dwyer, 1998; Brennan and Gray, 2005). The institutionalisation of the concept in accounting and auditing standards, with a focus on processes rather than truth telling, has resulted in a view that auditors are being materialistic, calculating consequences rather than considering duties (Shaub, 2005).

Materiality is thus an enigmatic problematic. On the one hand, it is linked to the concept of a true and fair view and quality in financial reporting (Chastney, 1975; Lee, 1984). Contrarily, it is criticised for being secretive, paternalistic and materialistic, only nominally serving the interests of users of financial information (Brennan and Gray, 2005). Section 3 suggests that a genealogical analysis may assist reflection on the concept.

3. A genealogical approach to exploring accounting materiality

The following section attempts to explain why a genealogical approach facilitates a critical history of materiality. Macintosh (2009) has drawn attention to the effectiveness of analysing accounting concepts through a Foucauldian lens. Foucault distrusted histories that rationalise concepts as the gradual refinement of ideas over time. Instead, he viewed history and the production of knowledge as a struggle between powers attempting to impose systems of domination (McNay, 1994). Certain belief systems prevail and influence ways in which we see the world whilst others are overpowered (Hook, 2001). According to Foucault, we acquire knowledge through the medium of discourses. Knowledge therefore operates as a form of power that exercises control over how we construct ourselves, interpret the world and act. Our beliefs may seem familiar but on investigation are logically dependent for their existence on certain *a*

[7] Materiality remains a topical and controversial subject. A recurring theme within recent discussions at the European Enforcers Coordination Sessions has revolved around the divergence in views between preparers, auditors, information users and accounting enforcers about its application. The European Securities and Markets Authority (ESMA) has been charged with seeking and evaluating views on materiality in financial reporting (ESMA, 2011, 2012).

priori conditions, words, events, actors and foundations (Jones et al., 2011). These conditions that underpin the possibility of knowledge were referred to by Foucault, as an episteme or in his later work, an apparatus (Foucault, 1981; Power, 2012).

For Foucault, the task of the historian is to unearth the foundations of every day concepts, a process he termed archaeology (Foucault, 2002). He focussed his analysis on discursive statements, as a network of rules, through which concepts become meaningful. An archaeological approach probes disruptions and investigates how the apparent "continuous development of meaning is crossed by discontinuous discursive formations" (Dreyfus and Rabinow, 1983, p. 106).

Foucault, in his later work, developed Nietzsche's idea of genealogy as an archaeological tool to investigate concepts as a form of social power (Dean, 1994).[8] A genealogy evaluates the significance of rhetorical battles that underlie meanings where the past may reveal traces of the influence that power has had upon truth games (Rabinow, 1984). Foucault used similar methods to practice archaeology and genealogy. Both focus on the same conditions or elements that provide a foundation for knowledge (O'Farrell, 2005). Archaeology queries how forms of knowledge and meanings are created by networks of statements. The focus is on gaps and ruptures in archives (Macintosh, 2009). A genealogy probes the influence of power upon knowledge and ideas about truth (O'Farrell, 2005). This involves exploring knowledge, and its operation, as a form of dispersed power that permeates micro-practices. The analysis is on connections and discontinuities between discourse and practice (Burrell, 1998). "The genealogist is a diagnostician who concentrates on the relations of power, knowledge," (Dreyfus and Rabinow, 1983, p. 105). A genealogical approach to exploring materiality thus seeks to investigate the influence of power upon discursive truth games.

To conduct the current study, professional accounting guidance, journals and literature, textbooks and academic papers about materiality were sourced, extending to law and social science literature and landmark cases on materiality in the US and UK. Electronic search engines were used to locate academic papers.[9] A vast (although not exhaustive) body of data was collected covering cases and discourses from mid nineteenth case law and emerging discourses around the beginning of the twentieth century onwards to the present day. It is inevitable that material has been overlooked, especially information that has not been digitalized. However, a sufficient quantity of data was gathered that is broadly representative of different networks of statements about materiality, for conducting a genealogical analysis.

A mechanism was needed to filter and analyse the data in a meaningful way, consistent with a genealogical approach. Foucault was careful not to prescribe specific methods but a genealogy should consider traces of organisational arrangements and events (Dean, 1994, p. 35). Given a striking abundance of rich figures of speech applied to materiality in discourses, metaphors and similes were used as a scoping mechanism to unearth clues about relevant genealogical factors. Metaphors can be viewed as a transference in meaning where we think of one thing in terms of another (Walters and Young, 2008). They can take divergent forms (grammatically as a noun or adjective) and may be cognitive, allegorical, paralogical or even contradictory. Similes also make associations but allow ideas to remain more distinct (as a comparison).

An analysis of metaphor complements a genealogy by unearthing underlying conditions and events through which meanings are assigned to objects, concepts and discourses. Nietzsche specifically linked critical discursive analysis with metaphor, "there is no real expression, and no real knowing apart from metaphor," (Nietzsche, 1872/1999, 149, p. 50). All language and therefore all truth and error is metaphoric in origin (in Gibbon, 2012, p. 204). Lakoff and Johnson (1980, p. 103) explain that metaphorical concepts provide a way of conceptualising a pre-existing reality, structuring what we perceive and how individuals relate with each other. Metaphors point to systematic underlying thoughts and hidden meanings. They influence our beliefs and define our perceptions and experiences as "implicit images or cognitions about our perceived realities," (Suddaby et al., 2011, p. 242).

Metaphor has been used extensively in scholarship because it provides an insight into perceptions of reality. Metaphors can be strategic or tactical. They may be employed to highlight certain features of an object or idea, whilst suppressing others (Lakoff and Johnson, 1980, p. 109). The use of metaphors can create new ways of thinking about objects (Lakoff and Johnson, 1980, p. 110). New modes of description can consequently bring about new possibilities for action (Hacking, 2002).

In accounting, the benefit of asking how metaphors represent cues (signalling thought processes, values and/or cultural changes) has been noted by Dirsmith and Haskins (1991), Amernic and Craig (2009)[10] and Gibbon (2012). Robson (1992) has emphasised the importance of asking not just "what" but "how" and "why" metaphor draws attention to processes of organisational behaviour and control. Metaphors may construct reality from a particular point of view and be selectively employed (Walters and Young, 2008). Competing metaphors have been observed to provide an insight into truth games over contested meanings of audit, embedded within social relations of power (Sikka et al., 1998).

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[8] In his genealogy of morality, Nietzsche called into question the value of values and conducted a history of morality. Foucault developed these insights into a critical problematisation, where truth has a history (Dean, 1994; Jones et al., 2011). A genealogy, as a critical history, is opposed to the search for origins but focuses in a meticulous manner on factors that have shaped beliefs (Kearins and Hooper, 2002).

[9] The method used was simple but effective, using search engines such as ABI inform. The content of individual academic journals was also searched, especially those with long a publishing history including the Journal of Accountancy, The Accounting Review, The Journal of Accounting Research, Accounting Organizations and Society and Critical Perspectives on Accounting amongst others. These papers in turn provided references to other useful data and publications.

[10] "Examining how metaphors are used in various accounting contexts can be productive and illuminating,"(Amernic and Craig, 2009, p. 882).

Methodological approaches to metaphor analysis are varied and controversial. Some claim that analysis should be subject to a form of scientific measurement, whilst others suggest that classification is a matter of interpretation, which is often the case in the humanities (Steen et al., 2010). This study intentionally adopted the latter, interpretative approach. Metaphors or transferences were identified in discourses, whether used strategically, descriptively or unconsciously and were grouped according to subject matter. Themes were evident amongst these metaphors (where materiality has been thought of in terms of people, physical objects, scientific ideas, techniques or abstract concepts). Groups of metaphors and their manner of use could be linked to distinct metaphorical discourses, styles of reasoning (Hacking, 2004) and expertises that have shaped materiality as categories of knowledge.

The term expertise refers to discourses through which members of a professional community demonstrate expert knowledge in professional writings. Through expertises, members align themselves with the aims of their professional community. Expertises thus play a role in discursive truth games in the production of knowledge through promoting the beliefs and tacit values of the relevant disciplinary culture (Bhatia, 2004). In accounting, expertises describe technologies of discovery and techniques involved in the measurement, calculation and classification of data (Robson, 1991). Expertises are therefore relevant to an examination of truth games in shaping beliefs about materiality. In addition, the study attempted to probe the fluid assemblages[11] of factors, actors and events that have underpinned the emergence of different discourses on the subject.

4. A Genealogy of accounting materiality through metaphorical discourses

The findings discussed in this section suggest that materiality is not a term, with a core meaning. Rather, distinct themes within imagery and metaphorical discourses imply that materiality has been constituted as multiple categories of knowledge with divergent discursive trajectories and roles. The paper classifies these knowledge objects as: a social responsibility; a solution to the problem of over-auditing, a solid epistemic foundation for auditing; a tolerable error; a rule of thumb; a risk management technique; and a mysterious professional lens and shield. The assemblages of actors, factors, events and expertises that have shaped these heterogeneous discourses are explored.

4.1. Materiality and socio/legal imagery – a responsibility

A strong theme within imagery is humanistic, where materiality has been objectivised as a moral responsibility to protect investors. The figure of mysterious, mythical man for whose benefit materiality should operate, as a safety test, is deeply embedded in discourses. This humanistic imagery is socio-legalistic and draws attention to a legal apparatus, as an arm of the state that has shaped materiality as an ethical responsibility. A capitalist rationale and a need to protect the material wealth of investors from the damaging consequences of misleading information underlie this construction.

A striking metaphor that provides an insight into the constitutings of materiality as a knowledge object in relation to a moral responsibility, personified the concept as a "child of law. . .and at most, a foster child of accounting," (Holmes, 1972, p. 49).[12] Two observations about power games are relevant here. First, materiality has been fostered upon the Profession. Second, it is a vulnerable concept requiring due care but institutional and hierarchical boundaries are clearly drawn. A foster child is a ward of court, in the day-to-day care of guardians but ultimately the courts make all the important decisions and remain *in loco parentis*.

This image accords with observations about early (and continuing) legal influences on the profession. As accountants began to establish themselves as providers of validation services, informality and inconsistencies in approach between practitioners, led to widespread criticism of the profession and scandals in the UK and US (Loft, 1986; Zeff, 2009). It was following the catastrophic Wall Street Crash in 1929 that a federal power, the US Securities and Exchange Commission (SEC) stepped in to protect investors. Materiality was configured as a regulation imposed upon the work of accountants (Rutherford, 2007),

> "The term "material", when used to qualify a requirement for the furnishing of information as to any subject, limits the information required to those matters as to which *an average prudent investor* ought reasonably to be informed before purchasing the security registered," (SEC, Regulation S-X, Rule 3-06, 1933).[13]

Through this rule, the SEC gave visibility to, and empowered the mysterious image of the "average prudent investor."[14] Materiality should operate as a test, for his safety, to leave him impartial, unbiased and objective in his actions (Hewitt, 1977). The idea of materiality as an ethical responsibility to protect the *mythical investor* was rooted in economic and political policy objectives at the time, concerned with rebuilding investor confidence, economic recovery and the continuing growth

[11] The term assemblages refers to flexible heterogeneous connections between people, organisations, events, happenings and words, drawing on the work of Deleuze. The appeal of an idea of assemblage is that it does not attempt to privilege the importance of any one level of organisation (at a macro or micro level) over another (DeLanda, 2006).

[12] Holmes was an influential US academic historian and a practitioner. He was a manager of Peat Marwick Mitchell and Co. in Boston, a member of the American Institute of Certified Public Accountants and British member of the Association of Certified Chartered Accountants. He was also a historian, on the editorial board of the Journal of Accountancy.

[13] Regulation S-X set out the form and content for financial statements to be filed under the Securities Act of 1933 and the Securities Exchange Act of 1934.

[14] An image that can be traced back to the common law of fraud and cases at the turn of the twentieth century (Hewitt, 1977).

of capitalism. Rule 3-06 was issued to respond to strong calls for enhanced disclosures and to address public concerns about investor vulnerability.[15]

Legal discourses and the courts have continued to play an influential part in codifying and socialising an idea of materiality, amongst practitioners, as a safety test for the mythical investor. These constitutings have been episodic, triggered by disputes about items that could be construed as a *peril*[16] for the mythical man, if not given visibility. The traditional association in professional accounting guidance between materiality and significant errors and omissions for the safety of the reasonable investor, can be traced back to judicial discourses in a landmark UK case, *Rex versus Kylsant* (1932).[17] At the heart of the dispute, was the practice of supplementing profit measurement through undisclosed transfers from secret reserves. Reserve accounting was considered prudent (and useful for management) by eminent practitioners[18] (Edwards, 1976). The court viewed the matter from an investor's perspective, where non-disclosure could imply that an investment was safe, when the position was otherwise. In the Court of Criminal Appeal, Mr. Justice Avory stated,

> "the document as a whole may be false not because of what it states, but because of what it does not state, because of what it implies," (p. 92).

Although the company auditor was acquitted, the ruling highlighted serious flaws in practitioner judgement (Ashton, 1986). The impact of the case, which Camfferman (1998) has compared to a bomb that disrupted the accountancy world, was interesting in two respects. First, accountants were thereafter expected not just to comply with the law but to use ethical and moral judgement in making materiality decisions. The case reportedly had a greater subsequent impact on audit practices than all previous case law and legislation (Camfferman, 1998). Second, the idea of a material item was extended to omitted data and not just errors (Edwards, 1989). This style of reasoning underpinned the future development of materiality in professional guidance.

The image of the mythical, mysterious investor has permeated accounting discourses and has encouraged practitioners to reflect on the workings of materiality decisions,

> "Who is this beholder, or prudent man, or reasonable person? We must identify him, *for our materiality decisions ultimately depend upon how we perceive him*. In effect, we have to assume his position in order to judge how financial statements or particular items therein will influence him. At best, this is no easy task," (Hicks, 1964, p. 159).

An important element in decision-making therefore involves finding credible evidence to justify an approach, in a type of guessing game as to "what and how much influences the judgement of a reasonable person" (Rose et al., 1970, p. 139).

Not surprisingly, truth games have been played in debating the mythical man's identity and his needs. Discursive shifts in his profile are traces of battles between practitioners and the courts. The courts have at times used the term "reasonable man"[19] instead of "prudent investor" (Jennings et al., 1984–1985). However, the *reasonable man test* implies a lower materiality threshold because knowledge about capital markets is not assumed (Jennings et al., 1984–1985). The American Accounting Association (AAA) re-characterised him as an informed investor, "An item should be regarded as material if there is reason to believe that knowledge of it would influence the decisions of an informed investor" (AAA, 1957).

This move towards an informed investor signals a growing expertise among users but also a desire by the profession to tailor judgments to the needs of experienced users, as a rational collective (Young, 2006). Individual perceptions of materiality amongst uninformed investors may be unreasonable, with resource and legal liability implications for practitioners:

> "The possible effect of misstatements on specific individual users, whose needs may vary widely, is not considered," (IFAC, 2010a,b, paragraph 2).[20]

Over the course of decades, battles over the boundaries of materiality as a moral responsibility have produced a maze of black letter law (Jennings et al., 1984–1985; Bean and Thomas, 1990).[21] Viewed through a Foucauldian rather than a legal lens, this body of judicial expertise operates loosely as a form of dispersed power/knowledge that encourages practitioners to reflect upon the way in which they organise themselves as willing, moral agents. Where practitioners have tended to view materiality in quantitative terms, the courts have considered qualitative and performance issues (Bean and Thomas, 1990).

[15] Changes in the organisational control of companies had been taking place (Berle and Means, 1932), with an increasing separation between management and ownership. This, combined with a growing appetite amongst the public to speculate in purchasing stocks, resulted in widespread calls from prominent academics and contemporary authors, for the SEC to expand disclosure requirements and protect investors (Weiss and Schwartz, 1977).

[16] A term used by the Attorney general, Sir William Howitt in Rex v Kylsant (p. 87) see note 20 below.

[17] Rex v Kylsant [1932] 1 KB 442.

[18] Evidence supporting this opinion was provided during the hearing by an influential and prominent member of the profession, Lord Plender, ex President of the ICAEW and a partner with Deloittes, as an expert witness.

[19] As cited in Kohler's early dictionary definition (1952).

[20] Judgments about the extent of auditor legal liability have widened and narrowed over time. The important ruling in *Caparo Industries plc v Dickman* [1990] 1 All ER 568 would suggest that the courts in the UK, view the duty of care of an audit firm as being to shareholders as a group.

[21] The attention of interested readers is directed to Karmel (1978), Bean and Thomas (1990) and Ling Lee (2004).

For example, the ruling in the landmark US case, *Escott versus BarChris Construction Corp*. (1968)[22] linked materiality with a performance imperative for all practitioners within a firm to observe internal as well as professional guidelines in reaching materiality judgments. *TSC Industries Inc.* v. *Northway Inc.*[23] provided knowledge of materiality as a likelihood that an omitted fact would be viewed as significantly altering the "total mix" of information made available. It was therefore important for practitioners to ascertain whether investors were sufficiently empowered by information to vote responsibly. Viewed through humanistic imagery, legal expertises socialise practitioners into framing materiality judgments in a prescribed manner, mediated by an external authority (Rabinow, 1984). The conditions for materiality are thus dependent on the needs of the mysterious, mythical man, as a prominent member of the SEC declared, "Although materiality has been defined differently in different contexts, all of these definitions are grounded on the legitimate expectations of the reasonable investor," (Karmel, 1978).[24]

The accounting profession has been socialised into shaping practices to respond to legalistic expectations:

> "In the end, however, auditors may be answerable for the quality of their work in a court of law and therefore the level at which they set the materiality level is highly likely to be highly influenced by what they can believe can be justified in court," (Gray and Manson, 2008, p. 411).

As Dreyfus and Rabinow (1983) explain:

> "To understand power *in its materiality*, its day to day operation, we must go to the level of the micro-practices, the political technologies in which our practices are formed," (p. 185).

An extensive network of statements about materiality has therefore been constituted through a legal apparatus. However, accounting and legal definitions have not fully converged, despite calls that the courts might be more likely to abide by a universal materiality standard if a specific accounting definition could be developed (Bean and Thomas, 1990). In the US, where a clearer judicial codified discourse on accounting materiality has emerged than in the UK (Sherman, 2010)[25] lawyers still comment on the vagueness of accounting definitions (Ling Lee, 2004). This lack of a complete agreement between legal and accounting understandings is partly to be explained by the existence of competing metaphorical discourses that have shaped materiality as multiple categories of knowledge.

4.2. Materiality – a cost/benefit idea and a solution

Other metaphors promoted by practitioners have positioned materiality as a category of commercial knowledge and a cost/benefit solution to the problem of over-auditing. As providers of a service and commodity, practitioners have an interest in securing the material value of their labour (Sikka et al., 1998; Power, 1997). A central question linked to financial audit has always been how much testing should the auditor do (Power, 1992). The economics of auditing in the early Twentieth Century forced auditors to be selective about audit work (Power, 1992) and notions of efficiency were influencing business practices (Miller and O'Leary, 1987).

A group of US academics, with links to the profession, interpreted materiality as an effective, practical filtering mechanism for trivia, "Materiality means simply this: *if it doesn't really matter, don't bother with it*," (Hicks, 1964, p. 158). A lens that facilitated expediency within audit was considered vital (Frishkoff, 1970).[26] Bernstein agreed:

> "The concept of materiality is part of the wisdom of life. Its basic meaning is that there is no need to be concerned with what is not important or with what does not matter. Man's work is burdensome enough without his having to pay attention to *trivia*," (Bernstein, 1973, p. 68).

Expertises linked materiality with the competent, efficient organisation of practitioner time:

> "A lack of understanding of the **materiality** concept can result in over-auditing by the conscientious professional," (Fritzemeyer and Carmichael, 1973, p. 3).

In the UK, the materiality concept was deemed incompatible with a true and *correct* view of financial statements (De Paula, 1948). A shift to a true and fair view, introduced in the UK Companies Act 1947 (Evans, 2010) allowed an idea of materiality to develop that complemented a more flexible audit opinion (Lee, 1984). Both in the UK and US, materiality was strategically linked with utilitarian and efficiency logics:

[22] Escott v. BarChris Construction Co. 283 F. Supp. 643.

[23] *TSC Industries, Inc. v. Northway, Inc.*, 426 U.S. 438 (1976). The case concerned the omission of certain facts from a proxy statement. This later became known as the Basic v. Levinson test (Basic, Inc. v. Levinson, 485 U.S. 224, 1988) of whether the magnitude of the event and the probability of it happening are high enough that the information becomes material under the foregoing standard.

[24] Roberta Karmel, was a Commissioner of the SEC. This quote is from a national speech to the investor relations institute, New York, 1978.

[25] In the UK, materiality is a pluralistic term in law, extending to the materiality or significance of a crime in criminal law or the significance of a fact. In the US, in fraud statutes, the core definition of material information is the well-recognized "total mix of information" test. Under the total mix test, courts ask whether there is a substantial likelihood that a reasonable investor would have viewed the misrepresented information, or disclosure of omitted fact(s), as having significantly altered the "total mix" of information available to the investor (Sherman, 2010).

[26] Assistant Professor, University of Oregon.

> "if financial statements are to be prepared and examined with anything approaching reasonable economy. . .without such a rule, unwarranted amounts of time would almost certainly be spent on insignificant matters, and financial statements would undoubtedly be cluttered with useless or unimportant information, obscuring the necessary and important facts and relationships they are intended to convey," (Hicks, 1964, p. 158).

To legitimise the term, it was suggested that materiality was widely used in business:

> "To help keep the subject in perspective. . .the concept is widely and frequently used. For example, when a business executive, applying the technique of "management by exception", cuts through to the matters of significance, he is recognizing materiality. When the president of a corporation, presenting non-financial data in reports to stockholders, prunes away details, he is recognizing materiality," (Hicks, 1964, p. 159).

Practitioners portrayed materiality as a form of knowledge that balanced good judgement with value for service and clarity in reporting. Over-auditing was a burden and over-disclosure was pessimistic (Jennings et al., 1984–1985). Such views have become mythologised over time,[27]

> "When we (all of us: the press, companies, lobbyists, Congress) talk about the level of burden that *accounting* firms have been placing on corporations these past five years. . .due to the significantly increased amount of time that audits are taking. . . trying to tease out exactly why they are taking longer and why more people are involved is difficult. . .When I ask, I get a host of different but related answers. . .They appear to have lost any sense of the *time-honoured accounting* concept of "*materiality*", (Wilcox, 2007).

A network of statements, where the visibility of a material item resembles "an index of time and trouble in relation to the amount in question," (Jeffries, 1981) has a focus on the material value of the audit and its role as an organising concept. Two logics appeared to underpin expertises promoting this role. First, materiality constituted a solution to inefficiency, reducing time wasting in relation to unimportant details. Second, it enhanced the quality of financial statements for users by eliminating clutter. The melding of these two logics echoes observations that firms are caught between two logics, commercialism (a need to develop their economic capital) and professionalisation, maintaining the traditional cultural and symbolic capital of the profession, in the public interest. Although these logics are diametrically opposed, they depend upon each other for success (Malsch and Gendron, 2013).

4.3. The reification of materiality as expert knowledge, a solid object and technique

Other conceptual metaphors, employed by the profession, have portrayed materiality as a thing of substance, a technical term, a solid object and a doctrine. Given the weak knowledge base upon which the craft of audit has developed (Power, 1997, pp. 6–28), an understanding of materiality as a solid object or authoritative technique has helped to convey an impression of substance to auditor judgement.

This role, which perhaps resembles impression management, is strikingly visible in the rhetorical entrenchment of the term *material* in professional guidance in the UK from the 1940s to the early 1980s. In response to concerns about a lack of clarity in accounting principles and calls for guidance (interestingly, not from leading audit practitioners but from accountants outside the profession) the ICAEW issued the 'N' Series of Accounting Principles, between 1942 and 1969 (Zeff, 2009). Amongst 192 pages of guidance, there were 175 references to the word material. This repetition rhetorically positioned materiality as a technical term, implying importance or substance but scant detail was provided about its meaning.

In the early 1970s, following a series of critical reports about auditor performance (Humphrey et al., 1992), the Auditing Practices Committee (APC) was established. Its outputs, which included the first set of auditing standards, have been deemed protective, rhetorical and overly concerned with appearances and public reassurances (Hopwood, 1990; Humphrey et al., 1992). There were 126 references to materiality peppered throughout these standards (Lee, 1984), which, along with the frequent repetition of other vague technical terms such as adequacy, relevance, reliability, sufficiency and judgement did more to standardise presentation than provide useful detail (Humphrey et al., 1992, p. 48).

Materiality has also been discursively depicted as a solid structure and has materialised as "one of the cornerstones of accountancy," (Frishkoff, 1970; Lee, 1984).[28] A cornerstone is the first stone set in the construction of a building. It determines the position of all other stones and the entire structure. This metaphor reified materiality as an epistemic foundation for the entire audit process and disclosures. The image was used by the Advisory Committee on Corporate Disclosure in its 1977 report to the SEC, "The materiality concept is the cornerstone of the disclosure system established by the federal securities laws."

[27] For example SEC Staff Accounting Bulletin 99, refers "a great deal of the time might be spent during the accounting process considering insignificant matters. . . If presentations of financial information are to be prepared economically on a timely basis and presented in a concise intelligible form, the concept of materiality is crucial," (SAB 99, note 50).

[28] In a review of the significance and implications for audit of materiality published by the ICAEW.

It was assigned two reporting functions as a principle and a standard,[29] at a time when investors were concerned about ethics in reporting (Weiss and Schwartz, 1977). Other metaphors of authority, in the form of a doctrine and rules, have helped to configure materiality as a code, that underpins the quality of information:

> "if financial statements are. . . to be meaningful and useful, such a doctrine (of materiality) is indispensable. Without such a rule. . .," (Hicks, 1964, p. 158)

Reification and rhetorical positioning of materiality as a matter of expertise and professional knowledge have enabled the concept to emerge, in a Foucauldian sense, as a sculpted, product of professional power (Power, 1997). Promoting the idea of materiality as a solid, guiding foundation for audit helps the profession and similarly, regulatory agencies, such as the SEC, to reassure the public about the quality of financial reporting and the substance of professional judgement.

4.4. Materiality – as an object of scientific knowledge

Another theme amongst metaphors, linked to science and standardisation, reveals how the profession has objectivised materiality as an acceptable level of error in reporting. Scientific metaphors have depicted materiality as a technique that measures, calculates and determines the visibility of errors. With the rise of systematic audit processes, such as statistical sampling, from the late 1950s onwards (Power, 1997, p. 72) calculative logics were increasingly used by practitioners to compute materiality thresholds. As the profession promoted its expertise in providing a neutral, technical point of view (Sikka and Willmott, 1995), it began to enhance the scientific authority of audit processes and judgement (Power, 1992),

> "Let us define materiality in accounting thus: the relative, *quantitative importance* of some piece of financial information, to a user, in the context of a decision to be made," (Frishkoff, 1970, p. 116).

Materiality was associated with a tolerable or acceptable error, based on scientific, systematic sampling processes. This picture persists in current auditing texts and professional guidance:

> "When testing amounts, *a tolerable error* is equal to the materiality level set by the auditor," (Gray and Manson, 2008, p. 419).

Calculative logics have assisted the profession in trying to transcend a subjective view of decision-making, by embedding judgments in neutral criteria (Samiolo, 2012). Scientific processes added credibility but more importantly, calculability to the technical formulation of materiality judgments. To control errors within accounting inscriptions, numbers and statistical methods provided a code, backed by scientific process.

Even after statistical sampling methods lessened in popularity in the auditing community, guidance setters in the US and UK have continued to use metaphors associated with measurement,

> "Materiality judgments are concerned with screens or thresholds. Is an item, an error, or an omission large enough, considering its nature and the attendant circumstances, to pass over the threshold that separates material from immaterial items?" (FASB, 1980, paragraph 126).

Materiality was represented in SFAC 2 as a pervasive, base constraint, underpinning all other concepts (FASB, 1980). This involved a consideration of materiality as a buttress for other related concepts, particularly relevance and reliability.[30]

In contrast, the ASB represented materiality, diagrammatically, as a supra threshold, positioned above other concepts. Materiality constituted "the final test" of what information should be included in financial statements (ASB, 1999, paragraph 3.28). The concept was also portrayed as a cut-off point (IASB, 1989) which is a term associated with capital budgeting, risk appraisal and capital investment decisions.

This distinct, scientific territory in discourses has emphasised the importance of an understanding of materiality, as a standardised process, where a foundation for decision-making is neutral. The appeal of science in shaping materiality discourses was probably engendered by auditors as a means of providing evidence to support judgments, rebut criticism and deflect possible problems with litigation.

4.5. Rules of thumb, magic numbers and legitimacy

Amidst shifting configurations of materiality, the most prevalent metaphor in the audit field, amongst practitioners, has been that of a rule of thumb (Fang and Jacobs, 2000; Brennan and Gray, 2005, p. 16; Gray and Manson, 2008; Vorhies, 2005)

[29] As a principle for the inclusion and exclusion of information in investor oriented disclosure documents and as a standard for determining whether a communication omits or misstates a fact of sufficient significance that legal consequences should result (Advisory Committee on Corporate Disclosure, 1977).

[30] There was a perceived 'trade off' in SFAC 2 between reliability and relevance. If data were not reliable, whether or not this was a material error might dependent on its relevance in a specific context, with all qualities subject to a materiality threshold.

and a closely related image of magic numbers (Hicks, 1964, p. 170). Rules of thumb or magic numbers are pragmatic, assist decision-making and generally position materiality within a range of 5–10% of net income.[31]

Truth games have been played between practitioners, guidance setters and regulatory bodies in debating the legitimacy of magic numbers. Under certain conditions, quantitative thresholds have been promoted by expertises. At other times, their validity has been qualified or refuted in the strongest terms.

Shifts in discourses about the legitimacy of magic numbers can be traced back to certain events and happenings. Illustrating this point, in the US in the 1970s, the fallout from a series of financial scandals[32] and the SEC's Watergate Related Enquiry in 1973/1974 (investigating secrecy and undisclosed payments) ruptured traditional beliefs about the value of a "fixed and easy" objective standard of materiality (Karmel, 1978). The SEC concluded that a sharper understanding of the materiality concept was required. Financial matters alone should not be the sole criteria for the determination of materiality. Views about the information needs of the average prudent investor also changed (Hewitt, 1977). The SEC re-constituted a new, *intelligent* idea of materiality that extended to matters of social significance and management integrity (Karmel, 1978). Around the same time, the newly formed FASB, which had been in the process of publishing a discussion memorandum on materiality, concluded that it was impractical to produce quantitative materiality guidelines that applied in all situations (Thomas and Krogstad, 1979; Iselin and Iskandar, 2000). Policy makers positioned materiality as a qualitative concept (Karmel, 1978) and these changes were signalled to practitioners in SFAC 2,

> "Magnitude by itself, without regard to the nature of the item and the circumstances in which the judgment has to be made, will not generally be a sufficient basis for a materiality judgment," (FASB, 1980, p. 7).

In the UK, reporting problems of a different nature, rooted in concerns about inconsistencies within accounting rules, encouraged the configuration of quantitative thresholds for materiality. To reduce divergence in judgments, the Accounting Standards Committee (ASC) defined materiality as a percentage, in specific standards (Rutherford, 2007). In Statement of Standard Accounting Practice (SSAP) 3 (ASC, 1972) a percentage threshold of 5% in the computation of earnings per share was established. Thresholds were introduced in other SSAPs.[33] However, fixed rules, in seeking to reduce divergence in judgement, created new problematics. Rules appeared to encourage the manipulation of thresholds in calculating the materiality of an error (Blakemore and Pain, 1998), amidst growing concerns about a wave of creative accounting practices amongst large listed companies in the 1980s (Shah, 1996).

Views about the value of fixed thresholds were disrupted. The Auditing Practices Board, shifted towards a dual quantitative and qualitative understanding:

> "an expression of the relative significance or importance of a particular matter in the context of financial statements as a whole... Materiality is not capable of general mathematic definition as it has both quantitative and qualitative aspects," (APB, 1995, paragraph 3).

In the US, concerns about creative accounting and the use of benchmarks to manipulate materiality judgements, led to the SEC to condemn rules of thumb in the strongest terms:

> "Certain registrants, over time, have developed quantitative thresholds as "rules of thumb" to assist in the preparation of their financial statements... The staff reminds registrants and the auditors... that exclusive reliance on this or any percentage or numerical threshold has no basis in the accounting literature or the law," (Staff Accounting Bulletin (SEC) 1999).

Commissioner Levitt (1998), the Chairman of the SEC, rejected rules of thumb as a blatant "numbers game" where practitioners "sheepishly" argued, when challenged, that the bottom line effect of identified errors was immaterial.

Interestingly, a new concept of performance materiality has been introduced in the recently clarifies ISA's. ISA 320 recognises that some account balances or disclosures might be affected by misstatements that are less than the materiality level for the financial statements as a whole. This is where performance materiality should be applied, with the intention of reducing the probability that the total of uncorrected misstatements exceeds financial statement materiality. ISA 320 refers to the use of benchmarks in calculating materiality which perhaps finally recognises that metrics are widely used in practice (Collins and Laudato, 2010). However, the guidance is vague,

> "The concept of performance materiality does seem to have thrown confusion amongst professional auditors... there is no guidance on how auditors should calculate it... As the concept becomes more established, standard setters, software providers and Continuing Professional Development (CPD) providers could well come up with calculations

[31] More recently, a percentage of 5% of net income has been used in the US. IFAC has suggested that 5% of profit before tax is often used. Implicit therefore within a rule of thumb is a simplistic assumption that fluctuations of less than 5 percent of net income would not influence investor decisions (Vorhies, 2005).

[32] Scandals including for example the collapse of the Equity Funding Corporation in 1973. The failure of the organisation's auditors to detect a significant fraud, perpetrated by staff over a decade, raised concerns at the time about tunnel vision in professional judgement.

[33] As well as the UK, the Australian Accounting Standards Board (AASB) also issued a quantitative definition. Accounting Standard 1031 suggested that 10% of a base amount was material while 5% or less was not (AASB, 1995).

on how to arrive at performance materiality. I suppose back in the days when the concept of materiality was first introduced, auditors then had the same issues we face now with performance materiality," (Accountingweb, 2010).

This observation signals a preference amongst practitioners for an understanding of materiality based on benchmarks and rules of thumb. Such approaches are straightforward, pragmatic and are of practical assistance to the practitioner in reaching a judgement about an item's importance.

4.6. Materiality – a technique linked to the management of audit risk

Another historical development has constructed materiality as a risk management technique that manages uncertainty and reduces audit risk. Following a series of economic crises and scandals in the mid 1970s and 1980s (Sikka and Willmott, 1995), a risk-based approach to audit emerged amongst firms in the 1990s (Power, 2004). Statistical sampling dwindled in popularity and analytics began to drive audit planning and practices. Materiality was reinvented in professional guidance as a category of knowledge that complemented a risk management approach. A theoretical relationship was established between materiality and audit risk, with the objective of reducing audit risk to an acceptable level:

> "There is an inverse relationship between materiality and the level of audit risk, that is, the higher the materiality level, the lower the audit risk and vice versa," (IFAC, 2008, paragraph 10).

Textbooks depicted materiality as "a subset" of risk (Millichamp and Taylor, 2008, p. 151). This relationship was represented as a Venn-diagram, placing materiality in a logical relationship with evidence and audit risk (Cosserat, 2000, p. 215).

Materiality guided the entire audit process, from planning through to the audit opinion. A notion of planning materiality was introduced (APB, 1995, paragraph; Big Five Audit Materiality Task Force, 1998) to assign materiality levels to each component in the financial statements (Cosserat, 2000; Porter et al., 2008). The extent of audit evidence gathered was theoretically linked to identifiable audit risks and materiality thresholds. Finally, at the evaluation stage, the materiality of actual and *potential* errors would be evaluated, referred to as evaluation materiality (Gray and Manson, 2008, p. 411). Materiality judgments thus responded systematically and logically to audit risk assessments. The focus of the audit was directed towards systems as the auditable object rather than the reality of underlying transactions (Power, 1997). At the same time, the overall responsibility for detecting material errors and the governance of fraud risk as a future possibility was increasingly been emphasised as a management responsibility (Power, 2012).

4.6.1. Materiality and risk management – post Enron

The extensive regulatory fall out in the US following the collapse of Enron triggered a reconstruction of the materiality construct. The recommendations that followed strengthened the links between materiality and risk management as a category of knowledge. Misrepresentations in Enron's financial statements were aggressively intended to overstate profit and the company's auditors, Arthur Andersen, and the wider profession, were criticised for adopting a mechanical focus of materiality[34] (Shaub, 2005) instead of challenging management (Cullinan, 2004).

In response to internal control failures at Enron, the Sarbanes-Oxley Act 2002 assigned a "new importance" to materiality that placed a greater emphasis on the governance responsibilities of management to detect material errors,

> "If you think you understand materiality and its uses, think again. The Sarbanes-Oxley Act of 2002 has put demands on management to detect and prevent material control weaknesses in a timely manner," (Vorhies, 2005).[35]

A re-construction of materiality linked the concept with four categories of misrepresentation: (1) misstatements or errors; (2) internal control deficiencies; (3) accounting estimates; and (4) frauds. The emphasis of the Act has been on the responsibility of management to implement a control risk reporting process to ensure the timely identification of material issues, where the practitioner's role is one of assistance (Vorhies, 2005). Cullinan (2004) has suggested that in responding to the symptoms of internal control problems at Enron, with a focus on management responsibilities, the Act has missed an opportunity to reflect more widely about rationales underpinning materiality in financial audit.

4.7. Materiality – a mysterious shield and shooting target

Another metaphor combination, drawing on abstract, fictional and mythical objects, has positioned materiality as a mysterious, protective shield but also as a shooting target. The foundation of this metaphorical discourse is rooted in vague definitions of materiality, its fuzzy workings in the field, debate about uncertainty in reporting and contested meanings of financial audit (Sikka et al., 1998).

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[34] The impact of the fraud on net assets was a reduction in shareholders' funds from \$11.5bn to \$10.3bn. Commentators have suggested that this adjustment was bordering on immaterial, measured in quantitative terms. However, in qualitative terms, there were multiple oversights and points of break down in decision-making (Cullinan, 2004; Shaub, 2005; Chabrak and Daidj, 2007).

[35] With four types of key control exceptions, including misstatements or errors, internal control deficiencies, accounting estimates and fraud, where materiality is applied by management to evaluate each one.

Bernstein (1967, p. 90) famously characterised materiality as a black box where the workings of professional judgement are hidden. Materiality has been described as a "mystery concept" and "part of the art of accounting," (Rose et al., 1970) and like beauty, as being "in the eye of the beholder," (Hicks, 1964, p. 159). Brennan and Gray (2005) referred to the concept as "accounting's best kept secret."

The secrecy about materiality (Ling Lee, 2004) is strategically advantageous and operates, in a tacit sense, as a mysterious shield. A definition lacking precision, where the criteria that underpin auditor materiality decisions are not transparent or disclosed, allows flexibility and shields judgement from public scrutiny:

> "The question of what is material has puzzled a great many people over a great many years, yet nobody is prepared to define it so that it does not ultimately rest on someone's judgment," (Blough, 1949, p. 13).

However, this shield also manifests as a knowledge object that auditors are able to manipulate or hide behind to give authority to unprofessional practices. Griffin (1959, p. 298) warned about the dangers of standing behind the "aegis" of materiality, "for it will undermine the significance of precision as a mental discipline and instead encourage inexactitude and approximation." The aegis, in Greek mythology, is a mythical shield and form of protection from a powerful, knowledgeable higher authority. Latitude in judgement afforded by a vague definition of materiality has been described as hazardous,

> "Materiality is used to justify practices and procedures which we recognize as wrong, or at least as questionable. . .there exists a real danger of opening a *Pandora's box* in the accounting world because materiality is not well defined and its applications not defined at all," (Hylton, 1961, p. 63).

Negative discourses concerned about secrecy have constructed materiality as a type of target for critics to shoot at. The Wall Street Journal described materiality as an Alice in Wonderland judgement, with accountants scurrying around like white rabbits, never quite getting to grips with the subject (Holmes, 1972, p. 44). Thirty years later, the absence of a clear definition was still being lamented, "Companies are required to tell the public 'material information,' but 'what's frustrating about 'materiality' is that there is no *clear definition*", says Paul R. Brown, chairman of the *accounting* department, New York University's Stern School of Business. Policy makers have literally avoided defining *materiality*" (Wall Street Journal, 1999).

Vague, qualitative understandings of materiality have been described as a "murky world" (Miller, 2000–2001). In the recent Senate Banking Securities Subcommittee investigation into the Accounting and Auditing Profession, following the Financial Crisis, in 2011, it was reported that "accountants and auditors need to quit hiding behind materiality," (Valukas, 2011).

Materiality as a shooting target is prevalent again in the media in the US. US investors are concerned that vague disclosure guidelines[36] encourage less information to be divulged instead of more (Henning, 2011). At the same time, materiality is increasingly being associated, by investors, with softer issues that influence share prices. A lack of disclosure for example about the deteriorating health of a CEO may now be considered grounds for litigation (Davidoff, 2011).[37] There is a growing public perception that practitioners too easily defend their decisions in court by raising reasonable doubt about the materiality of an item relative to the "total mix" of information available to investors. The implication is that that materiality judgments increasingly lie, "like beauty, in the eye of the jury," (Henning, 2011).

Calls for a review of what materiality really means, greater transparency and detail still abound (Chewning and Higgs, 2002; Ling Lee, 2004; Brennan and Gray, 2005; Sherman, 2010). Concerns about vagueness and cries for certainty about materiality however are ultimately linked to wider debates about uncertainty in financial reporting and audit quality. As such, these calls are rooted in the impossibility of eliminating the expectations gap (Sikka et al., 1998).

5. Discussion

Our understanding of accounting materiality today is built upon assemblages of historical conditions, events and ongoing battles over its meaning. Materiality is not a reporting concept that has developed in a continuous, linear manner. On the contrary, metaphorical discourses indicate that it has been constituted as multiple categories of knowledge. The inherent, malleability of the concept has facilitated its re-alignment and re-invention to meet reporting priorities and challenges. Its shifting configurations have been episodic, mirroring and strengthening changes in the craft of audit.

Through a Foucauldian lens, materiality operates at the crux of truth and power games about making visible, managing or hiding errors or ambiguities that arise in the translation and materialisation of information into accounting inscriptions (Robson, 1992). These inscriptions manifest as financial statements that need to be fit for purpose and show a true and fair view. Materiality determines the importance of a matter in processes of translation. However, a genealogical analysis suggests that under different conditions of possibility, it has been constituted as multiple categories of knowledge as: a moral responsibility to protect the material capital of investors; an organising, de-cluttering concept but with a focus on the material value of the audit; a technology and solid foundation for audit to reassure the public about quality in reporting; a

[36] American securities laws do not require, as they may do in other jurisdictions, that all material information be disclosed on a continuous basis. Instead, companies must periodically file reports with the SEC disclosing all material information. Certain categories of such information, like director resignations, are required to be reported within two business days. But most information is allowed to be reported quarterly or yearly. New York Times Davidoff (2011).

[37] The medical issues of Apple's chief executive, Steve Jobs, led to calls for protocols about when issues related to an executive's health should be revealed to shareholders (Henning, 2011).

scientific technique to standardise decisions and deter litigation; a risk management tool with a focus on systems and governance; a pragmatic rule of thumb to assist decision making; and a shield to allow flexibility in decisions which also manifests as a shooting target for critics.

Implicit within all these understandings, is the metaphor of materiality as a performative activity that determines what is included or lost in translating data into inscriptions,

> "The assumption that the item in question is in some sense material is implicit in every decision to render some event into a financial datum, to classify a transaction, to dispute some controversial accounting treatment. Thus, for every decision made in accounting there is a prior, often subconscious decision that the item in question is material." (Frishkoff, 1970, p. 116).

Materiality resembles an enmeshing of material and social processes, or a type of performance involving complex interactions within actor networks,

> "*other notions* of materiality are relevant in analytical review, in evaluation of internal control strengths and weaknesses in compliance testing, in selection and application of audit procedures in personnel assignments and even to time budget allocations to various aspects of the audit and in judging the sufficiency of evidence gathered. *The nuances of materiality judgements extend well beyond professional guidance*," (Thomas and Krogstad, 1979, p. 77).

Interpreting materiality as a performance amongst actors and a performative activity potentially opens up new avenues for research. Decision-making could be explored as the enactment of metaphors and truth games amongst groups of actors and shifting configurations of materiality. A material item becomes visible only in the context of the socio-material arrangements in which it is enacted (Latour, 1987; Law and Mol, 1995) where boundaries between the material and the immaterial, in an audit engagement, are constructed through micro dynamics.

For practitioners, the value of this analysis may lie in unravelling a familiar concept, to reveal its shifting configurations and multiple histories. There are two key observations. First, new metaphors open up possibilities for new actions and practices (Hacking, 2004). Second, metaphorical discourses and expertises may conflict, triggering epistemological battles in the way the materiality of an item is evaluated (Samiolo, 2012). Where there is ambiguity, an item cannot be both material and not material at the same time. Different understandings have to be resolved especially in the context of an audit, where there is a process of *drawing a line* in decisions (Olson, 1968)[38] which may need to be justifiable in court. The mode in which ambiguity is resolved may involve the ranking of certain expertises over others or a negotiation where a new understanding is formulated or through suppression (Latour, 1987; Mol, 2002). Certain expertises may exist outside the socio/material setting in which a decision is reached and may be overlooked (Foucault, 1981). Future research into the resolution of ambiguity may be relevant for practitioners.

6. Concluding remarks

This study has attempted to explore genealogical conditions that lie beneath the emergence of materiality discourses and its past roles. An analysis of imagery applied reveals that the meaning of the concept has been influenced by different, at times conflicting, styles of reasoning. Expertises have constituted materiality as a multiplicity of knowledge objects: as a moral responsibility; a solution to over auditing; a solid foundation for audit; a scientific tool; a professional lens; a rule of thumb; a risk management process; and a mysterious lens. These knowledge objects cannot be understood in isolation from expertises that have responded to challenges, objectives, priorities, threats and constraints within the work of accountants. Its meaning has not developed continuously over time but has been episodic, contingent on changes in the craft of audit, perceptions of investor needs, economic conditions and financial scandals.

Many different powers have played a part in the materialisation of this construct, including legal apparatuses and the courts, professional accounting and regulatory bodies, professional technologies (such as statistical sampling, and risk management approaches) and practitioners through the way in which they construct and organise themselves and their practices.

The variety of figures of speech apparent: as a child of law, a safety test, an index of time and trouble, part of the wisdom of life, a cornerstone and doctrine, a tolerable error, a screen or threshold; a subset of risk; or a mythical shield, demonstrate the malleability of the concept and its multiple roles. Its flexibility has enabled its alignment and reinvention to meet socio/legal and professional objectives and priorities, either externally imposed or strategic. Vestiges of legal power and shifting concepts and technologies in developing systems of professionalisation are all reflected in its construction. Underpinning these constitutings, the concept is legalistic and rooted in a capitalist ethos, with a focus both on protecting the material capital of the mythical man and the material value of the audit, rather than the interests of a wider audience of stakeholders.[39]

Viewed through a Foucauldian lens, materiality operates at the site of truth games about making visible, controlling, taming, managing or hiding errors and subjectivities in the translation of accounting inscriptions. Accounting materiality is one of the most iconic and important concepts associated with audit judgement. The concept is so familiar that its rich

[38] Executive Vice president of the AICPA.

[39] Although the idea of moving towards a more stakeholder orientated understanding of materiality in financial reporting was briefly considered in the UK, during the Company Law Review in the early 2000's, the committee reverted to a traditional shareholder focus (Company Law Steering Group, 2001).