

THE AUDIT PHILOSOPHY, DETERMINANT FOR FIRM PHILOSOPHY*

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ABSTRACT

The main aim of this paper is that of creating an integrate vision, a holistic one, regarding the existence and contribution of audit activities. In fact, it's about the inclusion of the auditing theories and practices in the general philosophy of the entity. The methodology consists of a survey and positivistic approach regarding the meaning of philosophy of an entity, both from Romanian case and international one. Also, I tried to highlight the importance of audit as main part of the managerial function of evaluation, control and correction of errors, or of activity's gaps or not fulfillments. Auditing must be objective, independent, professional and a very reliable tool for the present and future of the firm. The contents comprise a part of firm presentation and its philosophy of existence, the audit activity and its philosophy and, finally, how auditing matter supports in a beneficial mode the complex system of functioning.

Keywords: Economic Philosophy, Audit, Management Functions, Well-Functioning.

JEL Classification: M40, M42

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İŞLETME FELSEFESİNİN BELİRLEYİCİSİ, DENETİM FELSEFESİ

ÖZ

Bu çalışmanın temel amacı, denetim faaliyetlerinin uzmanlık gerektiren hizmetler veya departmanlar dahilinde, varlığını ve katkısını dikkate alan, bir bütüncül vizyon ve bütüncül bir bakış açısı yaratmaktır. Aslında, bu çalışma, işletmenin genel felsefesine denetim teorilerinin ve uygulamalarının dahil edilmesine ilişkindir. Çalışmanın metodolojisi, Romanya açısından ve uluslararası açıdan bir işletmedeki felsefeyi dikkate alan anket ve pozitivist yaklaşımdan oluşmaktadır.

Çalışmada, denetimin önemini, hataların ya da faaliyetlerin boşluklarının ya da yerine getirilmemesinin değerlendirilmesi, kontrolü ve düzeltilmesinin yönetsel işlevinin ana parçası olarak vurgulamaya çalıştım. Denetim, firmanın bugünü ve geleceği için tarafsız, bağımsız, profesyonel ve çok güvenilir bir araç olmalıdır. Çalışmanın içeriği, firmanın ortaya konuşunu ve onun varoluş felsefesini, denetim faaliyetini ve onun felsefesini ve nihayetinde denetimin, işletmenin karmaşık sistemini, nasıl faydalı bir biçimde nasıl desteklediğini kapsamaktadır.

Anahtar Kelimeler: İktisat Felsefesi, Denetim, Yönetimin Fonksiyonları, İyi İşleyiş.

JEL Sınıflandırılması: M40, M42

1. INTRODUCTION

In this paper there are two aspects in a straight interdependence:

a. The philosophy of the existence of an entity (firm, corporation, organization);

b. The Auditing action and philosophy, supporting the well-functioning of the entity and entity's functions towards a balance between home environment and external environment of the entity.

The literature in the field includes both Romanian theories and specific practice and European or international studies and researches, in order to understand the complex activity in this domain, but also the necessity to harmonize the norms and regulations in the Audit activity around the world.

It is true that for a long time few literature was available in this field, in what we call now Auditing theory. This one, unlike the accounting theory, has received a little attention, even its roots are considered to being in 1930s (Soltani 2007).

It is considered, by the the specific literature, that the theory od Internal Auditing was

conceived, primarily, by Lawrence Sawyer (1911-2002), often referred as “the father of modern Internal Auditing. His outstanding book, *The Internal Audit* (2003 edition) is considered a top selling college textbook, as well as the reference source for practitioners (Goza 2005).

Generally speaking, a research/study philosophy (as it is in the present case) means to put in work a set of beliefs concerning the aspects from practice which are under investigation (Bryman 2015). Furthermore, the philosophy provides the background in conducting research or survey (Flick 2015). Therefore, it is good to be understood the philosophy of research in order to explain the assumptions inherited in the research process and shows the appropriateness of the methods used!

Philosophy is considered an attitude towards knowledge, but not in a static manner and Auditing has its roots in logic.

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The task of accounting is to make clear the situations of a firm/corporation/organization, i.e. to reduce the huge mass of information to manageable and understandable proportions. On the other hand, Auditing is to review the activities and measurements of accounting and to be analytical, critical, investigative as the theoreticians of Auditing affirmed (Mautz & Sharaf 1961).

According to another author, Pickett (2005), Auditing is now a fully developed profession. It is important to understand the roots and the ways of developing over recent years. In fact, the authors speak about the situation of the Internal Audit as an extension of the external one, which role is in testing the reliability of the accounting that contribute to financial statements publishing. Cascarino and Van Esch (2005) consider that the Auditing (in its internal form) has its roots in the era of the Industrial Revolution of the 19th century.

And one more theory regards the Internal Auditing as a management-oriented discipline that rapidly evolved since the WW II. The development is due to the increased size and complexity of the organizations, all these aspects requiring for an independent, objective means of evaluation and improving their risk management, control and governance processes (Gleim 2004).

As methodology used, first of all the positivisme of the survey and, secondly, the deductive method. This approach is better to be used in the case related to confirm whether the observations and analyzed facts are based on previous researches or not (Wiles, Crow & Pain 2011). The interconnetion with the positivisme is illustrated in the cases when questions are formulated, after brainstorm session and litterature reviewed Kothari (2004) highlights exactly the idea that deductive method means an approach developing assertions from general aspects to specific.

The analytical descriptive methodology is used, searching for previous works in the field and reports and good practices in this domain.

2. THE CREATION OF A FIRM PHILOSOPHY

As a truism in business, what makes the difference between several producers or services providers, with goods of the same range, or very close, in the same field, is exactly the firm/company philosophy.

It derives from owner (s) ideas and vision about the business, mixed with the organizational culture and the use of all the managerial functions towards atingerea scopurilor and gaining profits.

So, it must be highlighted that there are 2 (two) reasons of the existence of a business, of a firm/company:

- a. The own philosophy;
- b. The profit pursuing.

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In practice, having a strong and adaptable philosophy is very good for the atmosphere within the firm/company/organization, for the employees motivation and training, which might be decisive when it counts, for a better decision-making process and avoidance, as much as possible, of the crisis and conflicts situations.

A suggestive example, “Performance with Purpose” is considered the philosophy of acting and existing for Pepsi Company (PepsiCo). This one emphasizes the medium and long term sustainable growth, and impact pozitiv asupra societatii si mediului. The scope and focus are the transformation of the portfolio, providing healthier food products and, hence, more prosperous communities. “Performance with Purpose” means, at the same time, gaining top financial performances by integrating sustainability within the business strategy of the firm. Everything is starting from what is being produced, i.e. food products and soft drinks, then to those who produce these things on behalf of customers and communities (see www.pepsico.ro).

A very interesting situation is represented by the freelancers, or so-called working places without bosses. A report by FreshBooks (a cloud-based accounting company), recently published, reveals the fact that the number of American people working for themselves could reach 42 million persons. Furthermore, about 97 % of self-employed workers have no intention to return to traditional job/work (Kline 2018).

For the present analysis, about 45 % of the respondents (about 3,000 full-time workers surveyed) express the feel that becoming self-employed will give them more control to their career and activity. In today’s splintered economy, it is considered that self-employment is an increasing alternative, based on CEOs, employees, workers opinions, offering benefits like flexibility of the work and adaptation, even autonomy and creativity. But, taking into account the own philosophy of the self-employed person and his intentions, forecasts, it is better to know, from the beginning, which are the trade-offs involved in the business.

In fact, the problem is the people don’t want a boss, or don’t like to be bossed ? It is

remarked an increase of the persons wishing to be their own boss and, therefore, to not depend on CEOs with less culture, less skills, less knowledge in the field. But, when the time of taxes comes, these persons have additional responsibilities beyond those of the conventional workers. The tax audit and verification of state of activity is done by specialized external institutions, such as the IRS, in order to avoid tax evasion and financial fraud.

The philosophy of a firm is considered at a level between that of the mission of the firm and the code of ethics of that entity. The philosophy should be simple, memorable and not reductive. Furthermore, the principles attached to the philosophy must come from the ideas and thinking of the owner (s) or CEO (s).

This philosophy should not be put off and must be crafted in each entity to cover all the activities and situations which might occur. In a completion to this assertion, it is necessary to use either focus group interview method, or questionnaire method, for employees, clients, suppliers, in order to apprehend (from the part of ownership or of CEOs) what are the strengths and weaknesses points, especially, and what to do further.

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3. THE AUDIT PHILOSOPHY

The main fact and, at the same time, the feedback from employees, customers and potential clients, is that these ones to be able to rely on the professionalism of Audit conducting, most preferable in an independent, unbiased, suitable manner. This aspect is realized both by internal Departments, Divisions, or Audit compartments (Internal Audit) and by specialized firms in the field (External Audit), which offer even non-stop Audits to a variety of standards.

Even in the specific literature there are presented a different number of steps (stages) of an Auditing process within an entity, like a modus in rebus, six steps are considered sufficient and understandable for this issue, ensuring a successful audit (Penn 2018).

It must be started with the assertion that an Audit is a formal check of financial situation (accounts) of a business, organization (such our case). This activity is conducted by specialized members of the same entity (internal audit), or by specialized agencies, institutions or from governmental system. The steps required are the following:

- a. Documents to be presented, included in a preliminary checklist, together with the last Audit report;
- b. Preparation of an Audit plan and the information needed;
- c. Meeting and scheduling the tasks, altogether with general management and key administrative staff to inform possible evaluated/verified persons about the scope and means of the Audit;
- d. Fieldwork activity by discussing with the staff and to see if the procedures and the

information recorded are adequate with the law frame, regulations and internal norms and decisions;

e. Draft the report detailing the findings of the Audit. All errors observed, of mathematical nature, payments authorized and not paid, other discrepancies or failures are included in the report.

f. The conclusions, the management responses, terms given that all mistakes and errors to be remedied and the plan to eliminate faults and to correct the trend of the entity.

On the other hand, this work, this task of Auditing is done, from internal point of view, by specialized bureaus, departments, services. For example, the Division of Audit Services is an independent and objective assurance and consulting activity that is guided by a philosophy of adding value to improve the operations of the entity consistent with the entity's strategic directions. It provides a systematic and disciplined approach to evaluate and improve the effectiveness of the institution's risk management, systems of internal control and governance structures processes, including the manner in which the first and second lines of defense achieve risk management and control objectives (see www.usask.ca/audit/documents).

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In the literature in the field, the most known and used work is that of Mautz and Sharaf (1961) in which the authors conceive the auditing as a field of knowledge built on a central core, considered as being abstract including mathematics, logic and even metaphysics, because Auditing has its roots in logic.

In this respect, Mautz and Sharaf drawn a hierarchical scheme, consisting of:

- a. Philosophical foundations
- b. Postulates
- c. Concepts
- d. Precepts
- e. Practical applications.

In fact, the authors believed this scheme in order to obtain a comprehensive view of the concept of Auditing. The first three levels: the basic philosophy, the postulates and concepts produce the precepts that guide the practice. Practice is considered being concerned directly with the precepts and, if precepts are based on the other three levels, clearly results that practice is resting on a sound theoretical foundation.

Continuing the ideas of Mautz and Sharaf, Flint (1988) introduces other postulates regarding the Auditing activity, for its development as theory, as follows:

1. The primary condition for an audit is that there is a relationship with accountability.

2. Essential distinguishing characteristics of audit are the independence of its status and its freedom from investigatory and reporting constraints.

3. The subject matter of audit, for example conduct, performance or achievement or record of events or state of affairs, or a statement or facts relating to any of these, is susceptible to verification by evidence.

4. The meaning, significance and intention of financial and other statements and data which are audited are sufficiently clear that the credibility which is given thereto as a result of audit can be clearly expressed and communicated.

5. An audit produces an economic and social benefit.

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It is a reality that not every company needs to have one of the pillars of a sound functional and existential background. We are referring to a mission statement, philosophy and a code of ethics.

But, the most important, valuable and cost-effective companies, such as Google (in the virtual world) have all three elements. So, the mission statement, included in a Business Plan, summarize what the owner (s), CEO (s) intend to do. A business' mission clearly defines its purpose and reason for existence. This mission, in order to support this existence has to be lofty, ambitious and, in some cases, audacious.

A high-performance leadership instills the passion for company's purpose and targets and considers the mission as an asset to be used to empower management and staff to quality, competitiveness and profitability, altogether.

Secondly, the philosophy (exactly the issue of our study) which fleshes out the mission statement and ensures the company and its members to adhere to in the business dealings. For example, Google includes such principles (philosophy) as "fast is better than slow" (Spira, www.inc.com/guides). And a Code of ethics is a normal continuation of the previous two elements and reglement specific types of situations and behavior within the firm/organization.

But, until the existence of a body of Auditing theory and, hence, to speak about a philosophy of Auditing, the problem is whether Audit is considered a science.

In its independency, professionalism and objectivity characteristics, Internal and External Auditing have as clients the senior (general) management of the firm/corporation for providing special services on behalf of the normal activity of the entity and elimination of disturbances and errors.

The both philosophies have to be convergent towards the general interest of the entity and not on behalf of owners, CEOs or shareholders narrow interests.

4. THE IMPACT OF AUDIT PHILOSOPHY ON THE WELL-FUNCTIONING OF A FIRM

Audit became an intrinsic part of the today's business environment. In many cases, it happens that the results or the general functioning of a firm/corporation/organization not to be expected. The CEOs or departments' heads don't find visible proofs of something would go wrong, but there are suspicions regarding a mismanagement in the system. And, in this moment, Audit activity (especially financial one) is required.

In this chapter, it is the matter of the Internal Audit, mostly, but also the impact of the External one. It is mandatory to emphasize the fact that the Internal Audit must be considered, if not a function, rather a sub-function of the control function of a firm/corporation/organization (the last of the fifth functions). This action (of Auditing) is an element of the control of the infrastructure of the entity and has to be capable inspecting and finding out any abnormal activity or operation of the entity and to determine, at the same time, whether policies, tactics and procedures are adequate and in compliance with the established plans and rules, or if an analytic control is needed in order to close loopholes or correct errors and misleadings (see Joksimović 2017).

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This activity, considered as being objective, independent and of consulting nature, well organized and in terms of professionalism, adds value and improves the efficiency and quality of the firm's/companies' operations. It is mandatory once a year, or as many times as needed, especially when it exists suspicions of something goes wrong.

This is the spirit in which the Auditing activity, as a whole, is acting in order to prevent, to discover and to recover the damages produced (see Deaconu 2003).

5. CONCLUSIONS

The internal Audit activity is considered by some authors, a function, by others a sub-function of the fifth function of a firm/organization, the control and evaluation. For the well-functioning of the entity this activity is one of the most important within a firm/organization, meaning to enhance controlling and monitoring what is happened within it and to design and develop the internal control system, in order to prompt detection of the errors and failures and, therefore, supporting, at the same time, corporate governance.

Continuing, this sensitive and complex activity is seen in a manner of revision, guidance and control, evaluating competence and performances in order to eliminate disturbances and to get quality and meet the goals of the entity, i.e. to fulfil its philosophy.

In fact, the existence of a possible conspiracy or a reasonable doubts or suspicions regarding negative financial aspects implies the necessity to make the detection of a fraud by the senior (general) management or through the specialized departments or institutions of Auditing.

Also, it must be considered that the philosophy of Auditing is manifesting between liberalism and professionalism, between the international and national laws and regulations, within the liberty of profession and firm rules, based on the skills, knowledge and synthesis and analysis capacities of the specialists in the field.

It is clear that the success of every firm/corporation/organization depends on its financial status, in good performances, profitability, but also on monitoring and evaluation.

The profitability, solvability, proper atmosphere and the union of material, financial and human resources towards reaching the main scope/philosophy of existence of the entity, depend on the quality and professionalism of Auditing compartments, both internal and external.

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