

The Human Side of Internal Control

By Tim J. Leech, FCA·CIA·IT, CCSA, CFE, MBA

I began my career as an auditor and risk and controls specialist with, what was then called, Coopers & Lybrand in May of 1979 over 25 years ago. In September of this year my 23-year-old daughter, Lauren, will write her exams with the goal of becoming an accredited chartered accountant with PricewaterhouseCoopers, a descendant of Coopers & Lybrand. Last fall, I was 10 feet up a ladder that was perched precariously on an uneven surface, cleaning leaves from my eaves trough. I fell and broke my nose and narrowly escaped splitting my skull wide open. Last week, I was playing golf and launched an impressive but somewhat errant drive in to a grove of trees. To advance the ball I would have to hit my ball through a very small opening in the trees or, alternatively, take my medicine, as the expression goes, and just chip backwards on to the fairway and try again to advance my ball to the hole. I elected to try and advance my ball through the trees wherein it hit a tree and went out of bounds for a two-stroke penalty. I am using these unrelated bits of my personal life to illustrate that auditors and risk and control specialists are people that have families, sometimes raise children and generally have the same human aspirations and failings common to the human race.

I don't think this observation is likely to come as a big revelation to any of you. What has become very clear to me over my 25 year career is a related and interesting fact. The fact is that many specialists in the field of risk and control, although they are people themselves, often forget that the risk and control systems they are assessing are designed and maintained by human beings with all the same strengths and failings that come with being a human.

Each year I give many presentations and speeches to auditors and risk and control specialists. In those presentations I sometimes poll my audience to determine how they have been approaching their work of assessing and reporting on risk and control, most recently, I have polled on how they have been tackling SOX assessments. Questions I have asked include:

1. How many of you start your risk and control assessments by requesting and reviewing the performance and bonus

criteria and the overall reward system that motivates the behaviour of management and staff in the area you are assessing?

2. A well-known adage is what gets measured, gets done. How many of you working on Sarbanes-Oxley projects systematically track where the accounting errors and misstatements are actually happening that have been a) detected by your company's external auditors and b) detected by controllership staff? And, even more importantly, did you take the time to really understand why the errors/misstatements happened? Was it negligence? Was it a conscious effort to manipulate profits? Was it decisions to cut controls and save money to hit bonus targets? Was it that staff didn't possess the necessary knowledge and skills?
3. How many of you come from companies where at least 10 percent of your management's reward system

relates to doing a good job on some form of risk and control assessment? Is it a big surprise that only the people that think their day job is formalized risk and control assessment actually do it?

4. When you identify a control deficiency do you ask the fundamental question, why have the people in the area been OK with this until now? Was it because they didn't know it existed? Was it because they didn't see fixing it as a priority?
5. How many of you have written down the number one risk that resulted in Congress passing SOX, CEO/CFO manipulate earnings for personal gain and/or fame, and then described specifically what controls are in place in your company, if any, to mitigate it?

The questions above are all focused on what I call the human side of risk and control management. The answers I have been given by thousands of risk and control specialists all over the world regularly indicate that, in a frighteningly high percentage of organizations, the human dimension of internal control is being overlooked and/or underemphasized.

Back in the early '70s I took a psychology course in college. That course included studying experiments with mice and how they reacted to rewards (tasty food pellets) and punishments (small electrical shocks). What those experiments showed, not surprisingly, is that people repeat behaviours that they are rewarded for and avoid behaviours that produce pain and punishment. The work of Peter Senge at MIT clearly shows that many human beings don't much like really seeing their current reality and often try and avoid processes that force them to examine it. The problem according to Senge is that understanding your current reality is a critical prerequisite to creating learning organizations.

As I advance in my career as an auditor, forensic accountant, risk and control specialist I more and more frequently spend time studying and thinking about what motivates people to want do things and also to not do things that are considered bad, inappropriate, against policy and/or illegal. The major scandals that caused SOX were all about human beings and what motivates them. They were not about whether password controls were maintained, bank accounts reconciled or purchases authorized and approved.

My suggestion in today's column is that you give some serious thought to whether the work you do everyday as auditors or risk and control specialists gives adequate attention to the human dimension of risk and control management. Overlooking the human dimension frequently leads to reporting symptoms of a control problem but not identifying and understanding the real root cause. On a personal level, trying to understand what motivates and influences the way people behave is a lot more interesting than flowcharting yet another process or mechanically testing controls, especially controls that your own staff could have told you weren't done or done properly if they were asked. Give the human side of internal control the priority and attention it deserves.

About the Author

Since joining Paisley Consulting as Principal Consultant, Chief Methodology Officer, Tim Leech has been instrumental in the development and implementation of the company's risk and assurance methodology framework. With over 25 years of experience working with organizations around the world Tim has earned a reputation as a thought leader.