

Behavioral Ethics for Auditors

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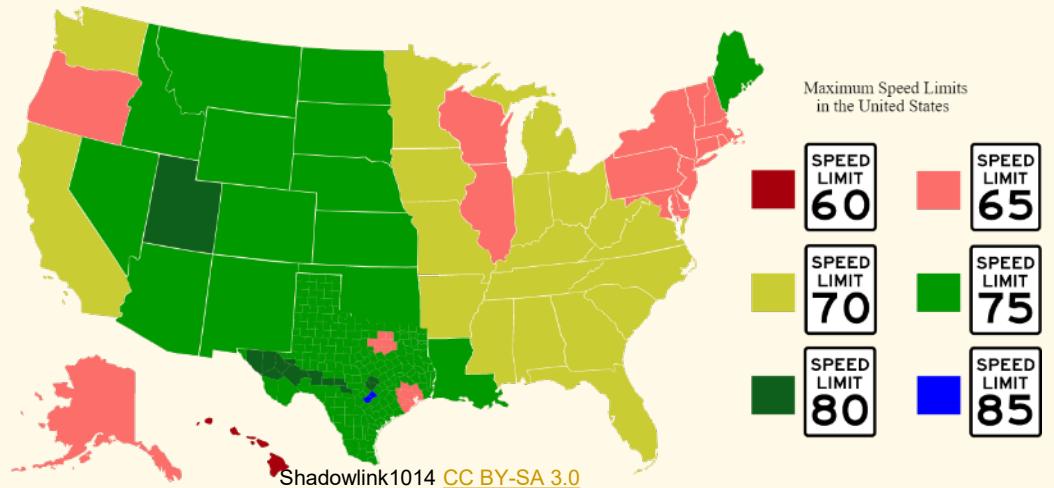
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U.S. GOVERNMENT
ACCOUNTABILITY OFFICE



Do rules and laws work?



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Behavioral Ethics

We irrational humans:

- ✓ Usually succumb to cognitive biases
- ✓ Lack self-control to do the right thing
- ✓ Allow social norms, even in professions, to influence our decisions



All human behavior runs through psychology

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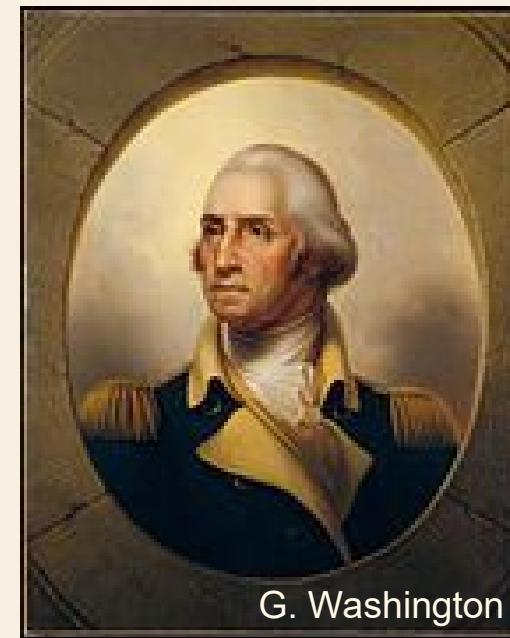
Behavioral Ethics

Examines how real people make real decisions in real-life situations

Behavioral ethics examines the cognitive, social, and emotional factors influencing behavior. It combines insights from psychology, sociology, and neuroscience to understand how ethical decision-making actually occurs.

Real people with strengths and weaknesses

Real decisions in the context of their situation



G. Washington



B. Arnold

In real life, you should not rely on good character and integrity

Fraud and Rationality?

Perceived Pressure:

Almost everyone in a workplace is under pressure

Rationalization:

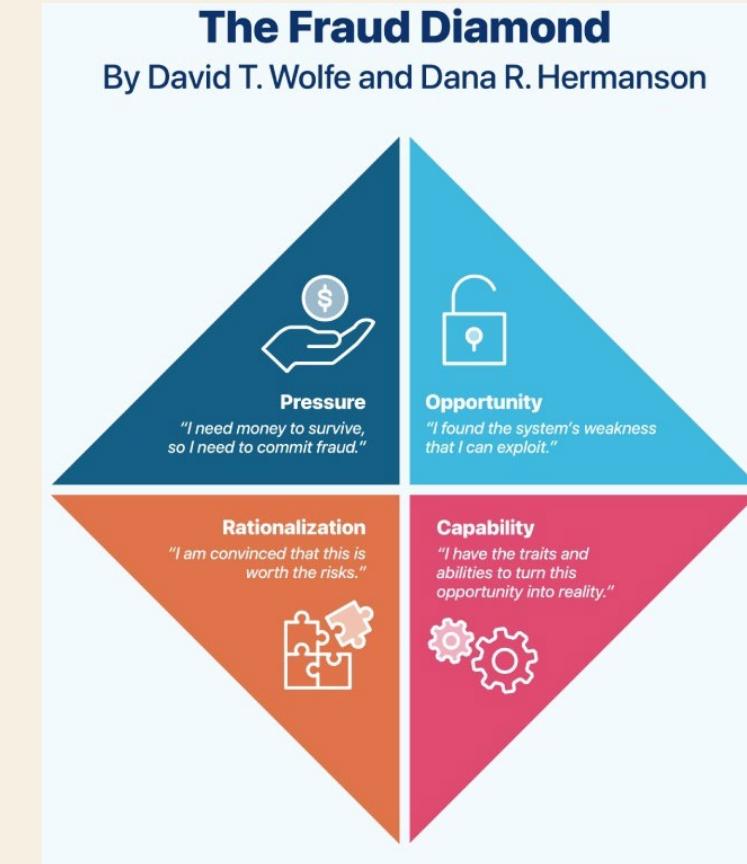
Ethical judgment is always a rationalization of automatic thinking and unconscious bias

Perceived Opportunity

Committing fraud is correlated to the risk of getting caught

Capability

Whether a person has the skills or traits to take advantage of the opportunity





PRESSURE MAKES

◆ DIAMONDS ◆

Pressure Makes Diamonds

- ❖ Motivates performance
- ❖ Increases efficiency
- ❖ Drives innovation



Photo by Bas van den Eijkhof on [Unsplash](#)

Building Blocks of a Strong Foundation



High-Quality Work



Strong Reputation
with Public

Pressure Can Also Crack Foundations

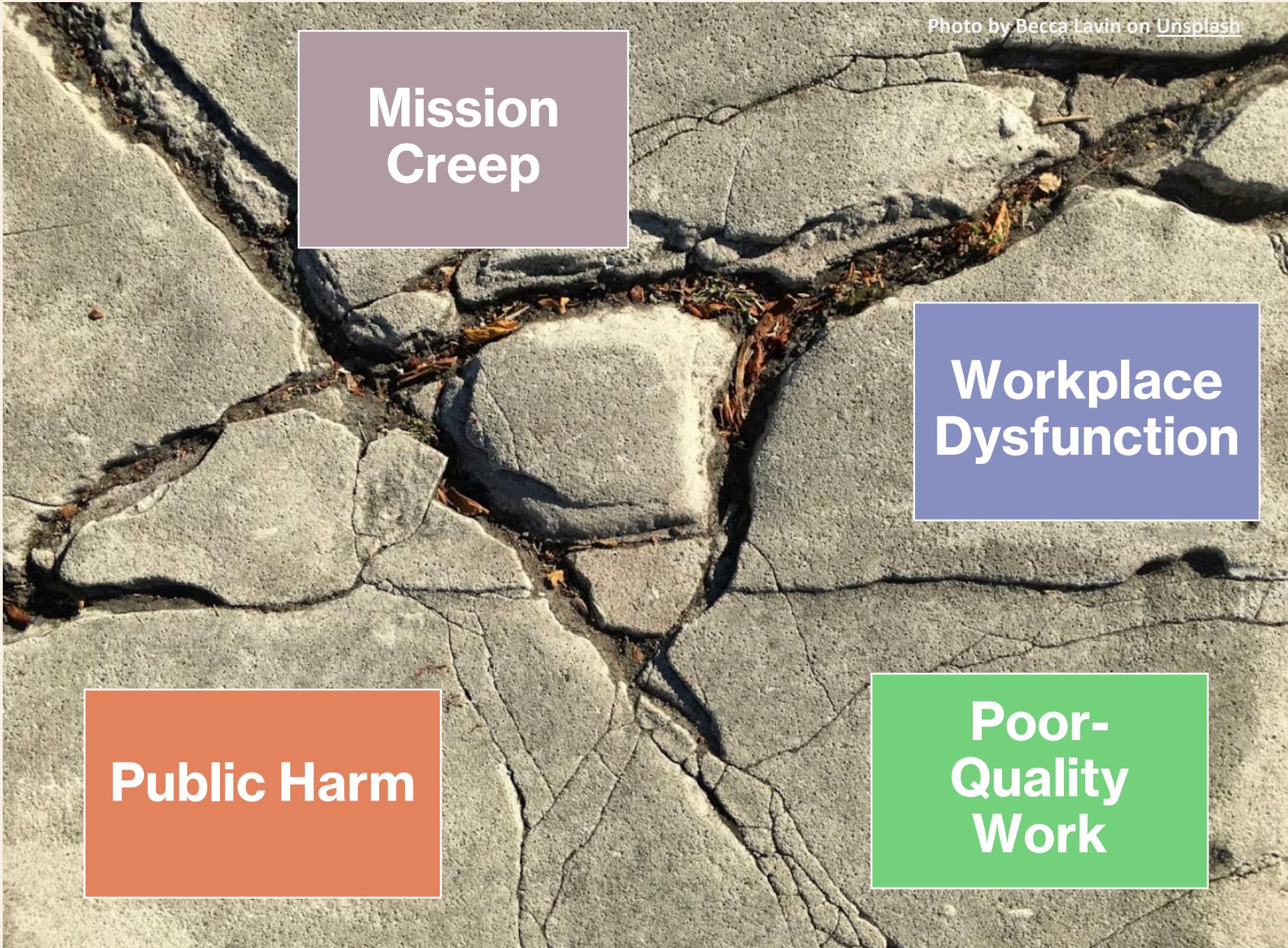


Aligned Mission and
Vision

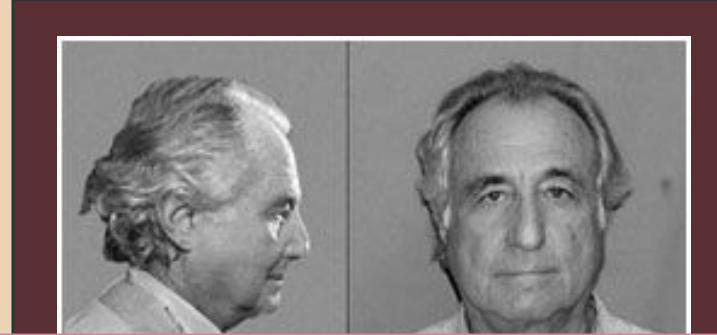
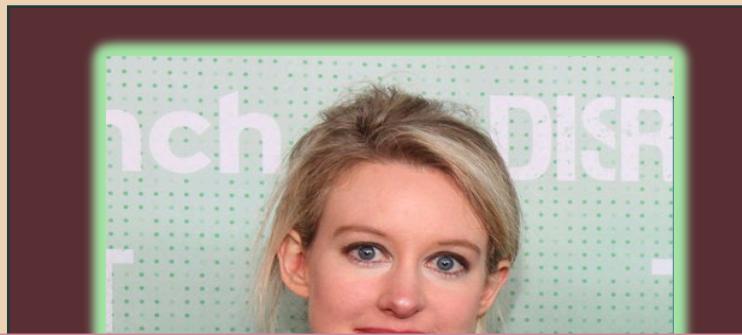


Satisfied and
Engaged Workforce

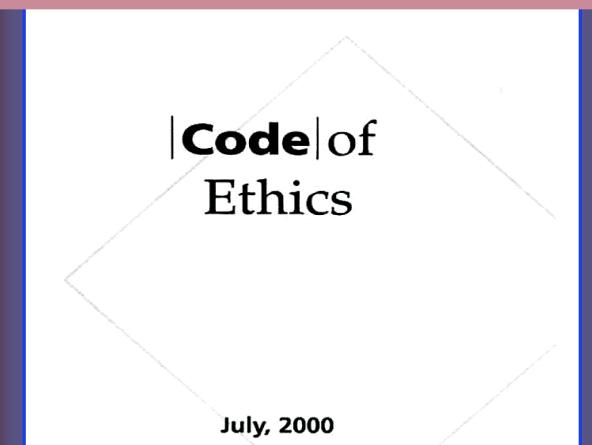




Public Harm & Consequences



Pressure Breeds and
Incentivizes Bad Behavior



Under Pressure to Perform

SINGLE-OUTCOME PERFORMANCE MEASURES

- A compensation system that rewards bank employees for the number of new accounts they open begs for fraud.

THE REWARD
SYSTEM ALWAYS
AFFECTS BEHAVIOR

“A REWARD SYSTEM
THAT ENCOURAGES
RESULTS IS
INDISTINGUISHABLE
FROM A SYSTEM
THAT ENCOURAGES
FRAUD.”

PROF. ROBERT
BLOOMFIELD

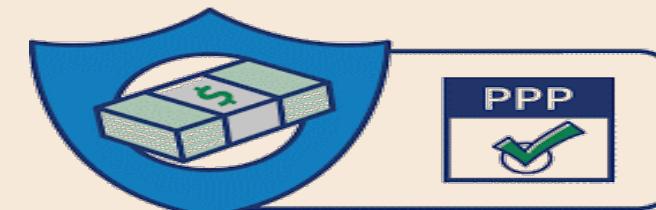
- A compensation system that rewards government officials who reduce wait times for service begs for fraud.



- A compensation system that rewards financial institutions for processing forgivable government “loans” with little or no penalty for bad lending practices.



U.S. Department
of Veterans Affairs



It might be hard to admit, but these pressures also appear in auditing

Almost all parties involved in auditing can distort measures to their own benefit and have reason to do so, at the expense of the public and anyone who relies on the audit.

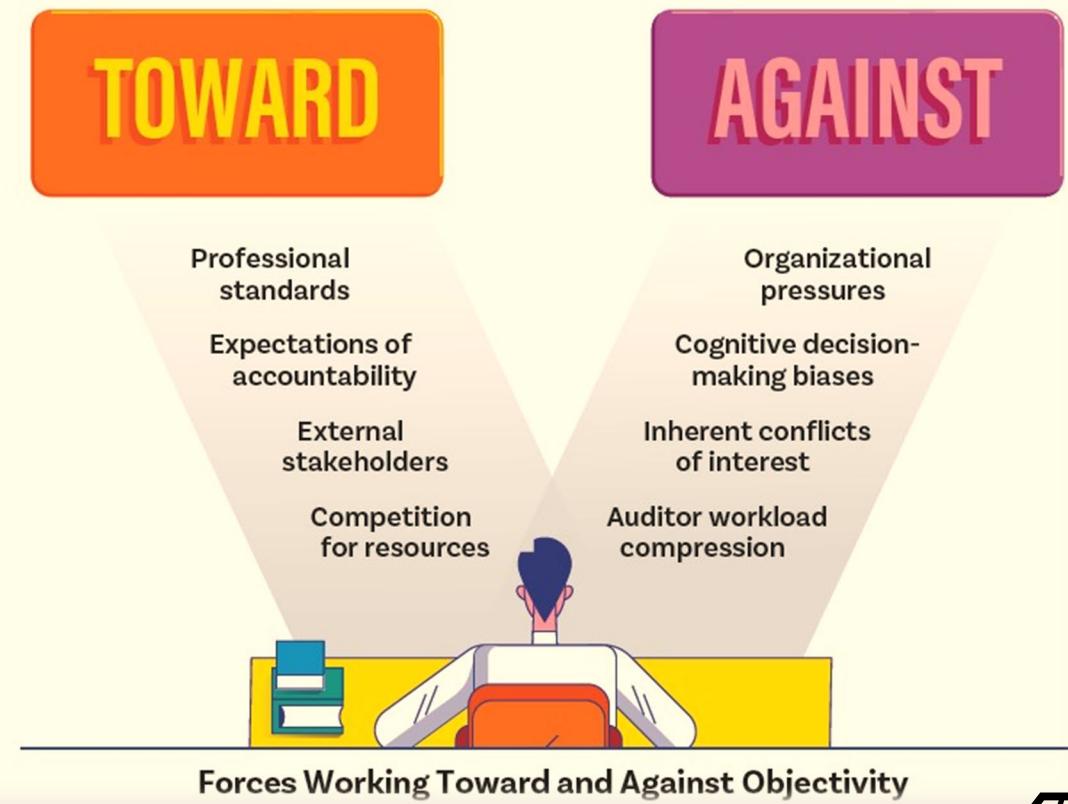
There are embedded incentives for bias:

- What does the audited entity want?
- What does the firm want?
- What pressures are pushing on the auditor?
- What does the reward system encourage?

These affect day-to-day work *unconsciously*

People usually *think* they are doing the right thing

Even good people succumb to unconscious bias



AICPA'S LIST OF BIASES THAT COULD AFFECT PROFESSIONAL JUDGEMENT

"[B]e aware of the effects of conscious or unconscious bias that could affect your professional judgment. Seeking advice from experts . . . and training *may* help mitigate the effects of bias."



Anchoring bias

- Using an initial piece of information as an anchor against which subsequent information is inadequately assessed

Confirmation bias

- Placing more weight on information that corroborates an existing belief than on information that contradicts or casts doubt on that belief

Overconfidence bias

- The tendency to overestimate one's own ability to make accurate assessments of risk or other judgments or decisions

Understanding behavioral ethics can help auditors:

Be more objective

Debias your work

Measure the right thing

Reward good process not good outcomes

Adjust systems pressures to make ethical behavior easy

“Ethics is not a belief problem; it’s a design problem.”

Prof. Nick Epley,
University of Chicago

