The importance of culture and behaviour

People are at the heart of every organisation, and it is human error which often results in non-compliance. Stimulated by the recent global financial crisis, regulatory interest in culture and behaviour has increased over the last few years. As a result, internal audit (IA) functions are being faced with both challenges and opportunities. They are uniquely positioned to bring value to the organisation by auditing culture and behaviour.

Auditing culture supports the delivery of stakeholder value by enabling organisations to proactively manage risk and correct internal control failings before things go wrong.

Culture is a complex aspect of business. Many companies are unfamiliar with how to quantify or measure it. However, a company’s inability to audit and monitor culture consistently and continuously can send a clear – and most likely, unwelcome – message to its stakeholders about its priorities.

Why the ‘soft stuff’ matters

- The International Standards for the Professional Practice of Internal Auditing stipulates that the internal auditor must pay explicit attention to soft controls.1
- It is fundamental to risk management and employee conduct.
- Increasing regulatory attention is being paid to (risk) culture and conduct.
- In the Institute of Internal Auditors (IIA) surveys, over 50% of chief audit executives (CAEs) see organisational culture as an inherent high risk; however, 58% state that they do not audit organisational culture.2
- Integrity is positively related to financial performance.3
- Over 90% of CEOs and CFOs believe that improving culture would improve the value of their company. Only 15% believe their culture is where it needs to be.4

How can culture and behavioural controls be audited?

Our approach to auditing culture and behaviour is primarily focused on three aspects:

1) **Entity-level controls**: These include governance, organisational set-up, tone at the top, risk awareness and openness, and training (also called behavioural controls instruments).

2) **Process-level controls**: We scrutinise the quality of behavioural controls that are conditional for the operational effectiveness of hard controls.

3) **Root cause analysis**: A thorough behavioural controls root cause analysis enables you to not only discover the root cause of audit findings, but also enhance the recommendations to improve the quality of controls.

Core beliefs that drive implicit and explicit prioritisations influence organisational behaviour and can be grouped into five categories. These aspects can be used as the starting point of our analysis.

---

2 'IIA Financial Services Audit Center poll' and 'IIA Audit Executive Center poll', The Institute of Internal Auditors Hong Kong, North American Pulse of Internal Audit, 2016, https://theiiahk.org
How can KPMG help?

We can help you audit culture on a consistent and continuous basis by implementing culture and behavioural controls auditing in your IA methodology. The first step is to determine your organisation’s stage of maturity. KPMG can support you at any stage of maturity.

KPMG’S MATURITY EVALUATION MODEL FOR INTERNAL AUDIT

**Initial ‘uncontrolled’**
- Culture and behavioural controls are **not included** in audit methods.
- There is **no model** for culture and behavioural control auditing.
- Culture and behaviour are included in existing techniques.
- Management may discuss but does not act on the auditing of culture and behaviour.
- Culture and behaviour are not considered to be key business issues.

**Infrastructure ‘root cause’**
- Culture and behavioural controls are included in the audit year plan and **described in parts** of the audit methods.
- A **basic culture and behavioural model** exists as part of the root cause analysis.
- Leaders seek to punish and blame when things go wrong.
- **Standardised** culture and behavioural control audit techniques are used regularly, including interview questions, surveys and observation protocols.

**Integrated ‘system-driven’**
- Culture and behavioural controls are a component of long-term audits.
- A **tailored culture and behavioural controls model** is **integrated** into audit methodology.
- Tailored culture and behavioural audit techniques are used regularly.
- Knowledge and skills about culture and behavioural controls are part of **permanent training and education**.
- Culture and behavioural controls are an integral part of written reports.

**Managed ‘proactive’**
- Culture and behavioural controls and a tailored model are part of the **audit vision** document and an integral part of every audit and work programme.
- Continuous culture and behavioural control auditing techniques are used, such as real-time data analysis.
- Knowledge and skills about culture and behavioural controls will be evaluated.
- Leaders understand that most risk events stem from behaviour.

**Optimising ‘values-driven’**
- Culture and behavioural controls and a tailored model are integrated into the organisation’s governance, risk management and controls.
- Culture and behavioural control self-assessments of businesses are audited.
- There is a varied mix of audit techniques depending on the situation, with **room to innovate and experiment**.
- Multidisciplinary auditors maintain diverse and culture- and behaviour-specific knowledge and skills.

### Include specific soft controls tests in each audit
- Each audit team can obtain a view on culture and behaviour.
- All IA personnel can be trained to do these audit tests.
- Potentially limited information compared to a more focused review or audit.

### Soft controls audits
- An internal audit focused purely on the testing of soft controls.
- Potential to target specific areas, but could also give a wider view.
- Client functions can be benchmarked against each other.

### Data & analytics testing to identify instances of inappropriate culture
- Continuous monitoring of culture and behaviour in the trading function.
- Regular reporting to identify potentially inappropriate behaviour.
- Action can be taken in response to identified concerns.

### ‘Deep dive’ culture review
- Targeted on areas or functions with specific risks regarding culture and behaviours.
- Involves interviews, staff focus groups, and review of policies and leadership communications involved.

---

**Contact us**

**Paul McSheaffrey**
Partner, Risk Consulting
KPMG China
T: +852 2978 8236
E: paul.mcsheaffrey@kpmg.com

**Jeffrey Hau**
Director, Risk Consulting
KPMG China
T: +852 2885 7780
E: jeffrey.hau@kpmg.com

**Alva Lee**
Partner, Risk Consulting
KPMG China
T: +852 2143 8764
E: alva.lee@kpmg.com

**Dagmar van Steenbrugge**
Manager, Risk Consulting
KPMG China
T: +852 2847 5060
E: dagmar.vansteenbrugge@kpmg.com

**Jianing Song**
Partner, Risk Consulting
KPMG China
T: +852 2978 8101
E: jianing.n.song@kpmg.com

---

kpmg.com/cn
The information contained herein is of a general nature and is not intended to address the circumstances of any particular individual or entity. Although we endeavor to provide accurate and timely information, there can be no guarantee that such information is accurate as of the date it is received or that it will continue to be accurate in the future. No one should act on such information without appropriate professional advice after a thorough examination of the particular situation.

© 2017 KPMG Advisory (Hong Kong) Limited, a Hong Kong limited liability company and a member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative (“KPMG International”), a Swiss entity. All rights reserved. Printed in Hong Kong. The KPMG name and logo are registered trademarks or trademarks of KPMG International.