

Dynamics of Authority Influence and the Impact on Risk

In [*Generalized Problems with Metric-Based Incentives*](#), we discuss the issue of moral neutrality in incentive schemes and its importance for ensuring desired outcomes. Moral alignment, or moral neutrality, of the incentive scheme may, however, not be sufficient to avoid unintended consequences of poorly framed incentive plans unless the influences of management in the organization are clearly understood. We note four connected implications for considering how authority and social processes in organizations drive behaviors.

1. Workers view those higher in the organizational structure than them with a deference that can drive behavior
2. Board or senior executive communications about true corporate objectives are often incomplete
3. Incentives drive behavior
4. Organizations often default to corporate codes of conduct to drive ethical behavior, communication about which might clash with other authority influences

Of all the modes of influence, authority is the one that can most easily lead to a negatively distinguished behavior by individuals inside of an organization versus that in which they engage outside of the

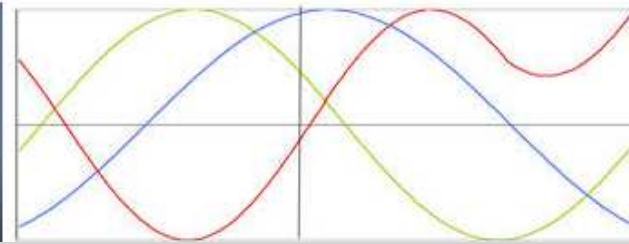
organization. In other words, verbal or nonverbal commands are almost always assumed to be legitimate if they come from superiors in an organization. This may take one to the point of engaging in behavior which might be morally objectionable to the individual, but is nevertheless engaged in because it has the implicit blessing of authority within the organization.

While risk management checks and balances on authority may well interrupt such an influence from becoming pervasive, if the communication about the overall corporate morals is incomplete, or if the authority is removed from oversight through complacent assumption of knowledge about corporate morals throughout the organization, these checks may not be engaged.

Corporate authority, communicated through incentives (money), will have more authority than policy (words), and may more strongly

About Us

Ductibility is private advisory service. We provide benchmarking research through our Research Circles. We design risk education and risk-awareness-building programs. We review and analyze compensation and incentive structures for alignment with corporate objectives.



indicate true corporate intent to employees, especially where communication is wanting. Incentive systems have an elevated status for communicating what the organization “really wants”.

The idea that some people might do bad things or things that are not in the interest of the organization is not a novel idea. Management that is well aware of the possibilities of unethical behavior by employees may create a corporate code of conduct policy to instruct employees on what the organization thinks is good behavior and what is bad. This leads to probably the most dangerous aspect of these codes: the assumption by managers that they are actually on the minds of employees. The complacency that is a byproduct of misplaced confidence increases the likelihood that business-ethical awareness is assumed to be more pervasive than is the case. Such can effectively relieve the manager from a degree of oversight in which they might otherwise engage.

In a February 2008 benchmarking study by Ductibility, more than 70 major corporations, most having well-developed risk management programs, were surveyed. Nearly 90% responded that their company had developed a risk management policy. Of those with such a policy in place, nearly half of respondents said that they could not agree with the statement “We have a regular training program for new employees that includes a focus on the risk management policy”. Similarly, nearly half of respondents with a risk policy indicated that they do not regularly update employees’ awareness of the risk policy.

This complacency is exactly what the literature in this area warns us about. There is a perception by the authority that a risk policy is well-understood by employees, but insufficient effort made to ensure that is the case.

See our case studies of where these influences have combined to produce unintended and infamous consequences.

Review of Key Points Regarding Control Systems and Authority Influences

- Overly objective systems may increase risk by attracting concentrations of personalities who prefer such to subjective systems
- Correct framing of incentive plans, particularly objective ones, thus becomes even more critical
- Objective systems may not be morally neutral and can stimulate gaming, cheating and the placing of self-interest above corporate interest
- Corporate authority, particularly when expressed through monetary incentives is the most pervasive influence
- Management may exacerbate risks through complacent oversight, brought about by a misunderstanding of how well corporate morals are understood by employees