Soft Controls in Internal Control Framework D&I

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Combine Accountability with Culture: Integrate soft controls in your Internal Control Framework (ICF)

In today's dynamic and complex business environment, the demand for transparency and accountability has never been greater. Organizations worldwide face mounting pressures to implement a robust ICF that not only address compliance but also foster a culture of trust and integrity.

Recent regulatory developments emphasize the importance of a strong ICF:

- The Dutch Corporate Governance Code (CGC) 2025 highlights the Verklaring omtrent risicobeheersing (VOR) principle, stressing the need for accountability in reporting.

- The UK Corporate Governance Code mandates declarations on control effectiveness, further underlining the importance of transparency.

- The Corporate Sustainability Reporting Directive (CSRD) and International Corporate Social Responsibility (ICSR) regulations reflect the growing need for sustainable and transparent operations.

- The increasing complexity of the legal and regulatory landscape, including frameworks like the AI Act, Digital Services Act (DSA), and Digital Markets Act (DMA), calls for innovative and adaptive ICF.

A robust control environment needs an ICF that is transparent, accountable and strong and integrates hard and soft controls.

A *transparent* ICF ensures that decision-making processes and organizational activities are visible and understandable to stakeholders, fostering trust and confidence.

Accountability within the ICF demands that individuals and teams take ownership of their responsibilities, creating a culture where errors and risks are addressed proactively, and effectively learned from them rather than concealed.

A *strong* ICF not only ensures compliance with regulatory requirements, but also enhances the organization's adaptability to change, enabling it to navigate complex challenges such as technological advancements, evolving business models, and global uncertainties.

When transparency and accountability are built into an ICF, they help the organization improve continuously, ensuring that control processes remain robust, efficient, and aligned with organizational objectives.

Combine hard and soft controls for a robust ICF

A robust ICF requires the seamless integration of hard controls (policies, procedures, and technology) with soft controls (culture, behavior, and leadership).

Adding more and more rules and procedures to encourage desired employee behavior makes no sense if people do not understand the rules, managers set the wrong example or people do not feel engaged in the organization. Together hard and soft controls create a cohesive framework that better detects and mitigates risks.

The role of soft controls - the human and cultural elements within an organization - remains underexplored but critically important. Elements such as organizational culture, leadership behavior, and ethical climate form the backbone of effective internal controls, influencing compliance, decision-making, and overall corporate integrity.

This article explores the intersection of soft controls and traditional ICFs, demonstrating how the eight pillars of KPMGs soft controls model can complement and strengthen ICF.

Regular Design & Implementation (D&I) of an Internal Control Framework (ICF)

A regular approach to design and implement an ICF of 6 steps from risk assessment to monitoring of the effectiveness of the system.

Communications

Step 1:
Assessment and Planning

Step 2:
Documentation of Key Processes, Systems and Controls

Planning

Engagement Project Management

Step 6:
Continuous Monitoring and Evaluation

Step 3:
Walkthroughs

Execution

Step 5:
Control Testing and Remediation

Step 4:
GAP Analysis and Remediation

Communications
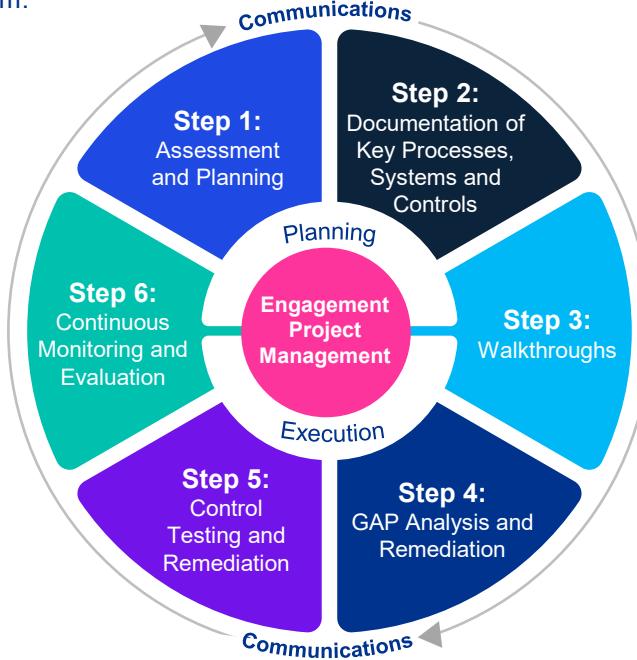
Step 1:
Assessment and Planning

Conduct a risk assessment by identifying and evaluating risks, materiality, and significant accounts in line with the organization's objectives. Assess risks at both the entity and process levels to determine areas of potential misstatement or operational risk.

Step 2:
Documentation of Key Processes, Systems and Controls

Document critical processes, systems, and control activities, ensuring a clear understanding of how these processes address identified risks. Map controls to specific risks, document the roles and responsibilities for execution, and highlight any risk points within the processes to support effective control D&I.

Step 3:
Walkthroughs

Perform walkthroughs of processes to verify the design and understanding of control activities, ensuring alignment with documented processes.

Step 4:
GAP Analysis and Remediation

Analyze gaps between the existing control framework and identified risks. Design and implement actions to address missing or inadequate controls to ensure risks are effectively mitigated.

Step 5:
Control Testing and Remediation

Evaluate the design and implementation of controls (TOD) to ensure they are appropriately designed to address identified risks. Subsequently, test the operating effectiveness of these controls (TOE) to confirm they are functioning as intended and consistently mitigating risks. Validate any changes or improvements made during the process to ensure the control framework remains robust and aligned with organizational objectives.

Step 6:
Continuous Monitoring and Evaluation

Establish ongoing and periodic monitoring activities to assess the effectiveness of the ICF. Ensure feedback from monitoring activities is integrated into the control framework to continuously improve its design and operating effectiveness, supporting the achievement of organizational objectives.

Enhancing Internal Controls: The Role and Benefits of Soft Controls in D&I of an ICF

Understanding the existing internal control culture is a crucial initial step when enhancing internal controls. Soft controls, which include aspects such as corporate values, ethical guidelines, and team behaviors, play a pivotal role in ensuring internal controls are seamlessly woven into the fabric of the organization. By integrating regular validation sessions and implementing continuous feedback mechanisms that focus on these soft controls, organizations can significantly enhance their control environment. These sessions allow for the periodic assessment and reinforcement of the organization's values and ethical practices, fostering a culture of trust and accountability. Moreover, this approach helps the ICF remain responsive and evolve in the face of new risks and organizational changes. Such dynamic adaptations contribute to the robustness and effectiveness of the entire internal controls system.

Below is an outline of how soft controls integrate with each step:

Step 1:
Assessment and Planning

Evaluate the organization's control culture to identify gaps in soft controls (e.g., accountability, leadership tone) that influence risk management. If the process is triggered by a specific failure or issue, conducting a thorough root cause analysis at this stage is critical.

To enhance this assessment, include a soft controls survey and organize one or two validation sessions to identify hindering and enhancing soft controls relevant to any identified gaps. This approach not only provides clear direction for addressing weaknesses but also fosters comprehensive stakeholder support by aligning implementation efforts with organizational needs and priorities.

Practical example:

In evaluating the organization's control culture, a soft control survey reveals that there is a lack of accountability among managers in overseeing financial transactions. To address this, the organization conducts validation sessions to identify hindering and enhancing soft controls. One specific control could be implementing a system where managers have to approve all financial transactions above a certain threshold, enhancing accountability.

Step 2:
Documentation of Key Processes and Controls

Incorporate insights on human behaviour and cultural factors into process documentation to address how leadership, communication, and ethical practices affect controls.

Practical example:

Within the financial reporting process, there is a section outlining the responsibility of the CFO to review and approve financial statements, highlighting the importance of leadership involvement in ensuring accuracy and compliance.

Step 3:
Walkthroughs

Assess not just the technical design of controls but also employee adherence to ethical standards and leadership's role in embedding these controls into daily operations. As part of this process, identify relevant aspects of soft controls that influence the effectiveness of the designed controls. This includes evaluating how accountability, communication, and leadership behaviours align with the organization's objectives and support the successful implementation of controls.

Practical example:

In a procurement process walkthrough, the focus is not only on the procedures in place but also on how employees handle conflicts of interest, emphasizing the importance of ethical behaviour in procurement decisions.

Step 4:
GAP Analysis and Remediation

Identify and address behavioural and cultural gaps (e.g., unclear accountability or weak ethical practices) alongside technical control deficiencies.

Practical example:

In conducting a gap analysis, the organization identifies a cultural gap related to unclear accountability. To address this, leadership implements a clear delegation of responsibilities and roles within departments, enhancing accountability and reducing the risk of errors or fraud.

Step 5:
Control Testing and Remediation

During testing, evaluate whether controls are designed to encourage ethical behaviour and consistently executed in line with organizational values. Remediation should include strengthening soft controls, such as training and leadership involvement.

Practical example:

During control testing, it is observed that employees do not consistently follow established procedures due to a lack of understanding. As part of the remediation, the organization conducts training sessions to reinforce the importance of adherence to controls, thereby strengthening soft controls related to employee behaviour and knowledge.

Step 6:
Continuous Monitoring and Evaluation

Embed soft controls into monitoring activities to sustain control effectiveness. Regularly assess leadership tone, employee morale, and communication to ensure continuous improvement.

Practical example:

In continuous monitoring activities, the organization assesses leadership tone through regular feedback sessions with employees. If feedback indicates low morale in a particular department, leadership implements communication sessions to address concerns and improve morale, thereby enhancing soft controls related to communication and employee engagement.

D&I cycle steps	Key Focus on Soft Controls
Step 1: Assessment and Planning	Control culture, leadership tone, stakeholder support
Step 2: Documentation of Processes	Human behavior, ethical practices
Step 3: Walkthrough	Ethical Standards, accountability
Step 4: GAP Analysis and Remediation	Behavioural gaps, accountability
Step 5: Control Testing	Ethical behavior, Leadership involvement
Step 6: Monitoring and Evaluation	Leadership tone, employee morale

KPMGs Soft Controls model

The starting point of the internal control journey is to assess how the organization's current internal control culture is. By assessing the strengths and weaknesses of the current internal control culture, this will help emphasize what the organization need to do as part of the D&I. One proved methodology to assess the current (internal control) culture is by applying the KPMG soft controls model.

KPMG's soft controls model, developed through extensive research by Prof. Dr. Muel Kaptein of KPMG Netherlands, highlights the critical role of human behavior and organizational culture in ensuring the effectiveness of internal controls.
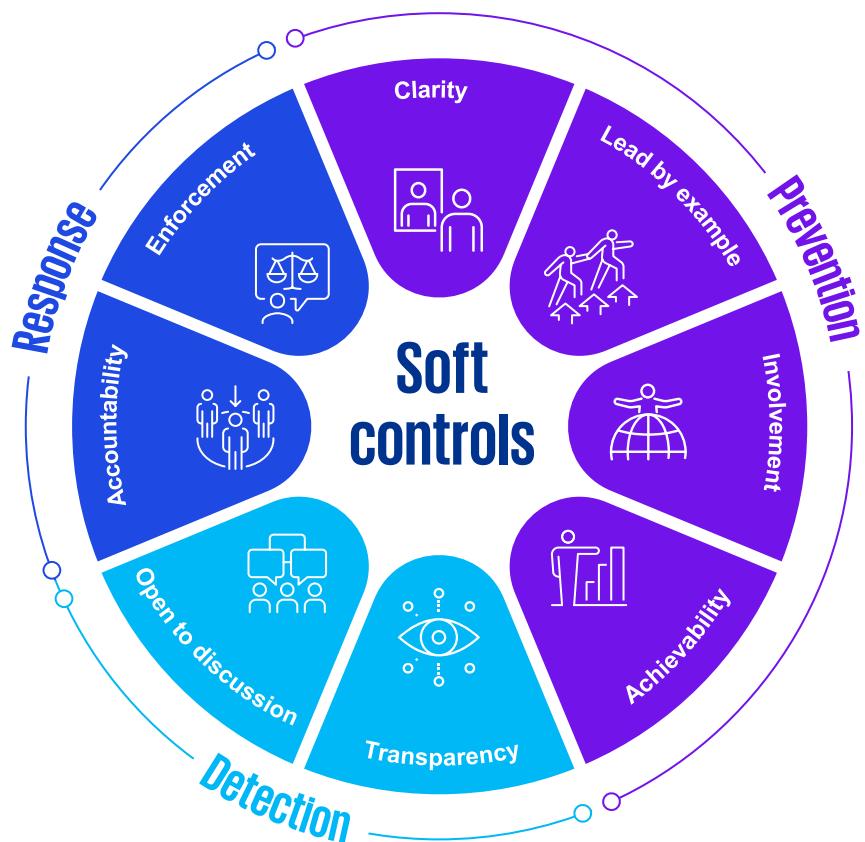
The 8 pillars of soft controls play a vital role in enhancing the effectiveness of an organization's ICF. While traditional internal controls focus on hard controls, such as segregation of duties, authorization, and compliance processes, soft controls address the behavioral and cultural aspects of governance. When implemented alongside hard controls, the 8 pillars of soft controls serve as a catalyst to strengthen the internal control system by fostering a culture of transparency, responsibility, and proactive risk management, thereby ensuring that the organization's objectives are achieved effectively.

Methodology

Interview and survey

The proposed methodology is to develop a clear scope of the organization who will be involved into developing the ICF. For the relevant addressed departments, interviews with several key stakeholder persons will be scheduled whilst a tailored soft control survey will be sent throughout the entire organization. By doing this, the departmental culture will be identified as well as organization wide culture assessment. This provides insights into the similarities and differences between the departments and the concerning organization.

Utilizing the assessment results

After assessing the current state of the organization's internal control culture, it is imperative to use the insights gained to fine-tune the D&I of internal controls. The results of the assessment can highlight specific areas within the organization that require more focused attention while also acknowledging aspects that are functioning effectively. These results offer a blueprint for planning changes, anticipating resistance, and understanding the behavioral adjustments needed to strengthen the control environment.

Integration into D&I

Incorporating the soft controls culture assessment into the standard approach to D&I ensures that the features of the internal control system are tailored to the organizations and departmental unique culture. This integration leads to a more personalized set of control activities that are relevant and attainable across different departments and geographic locations. Recognizing cultural diversity within the organization enables more effective change management, as different regions and/or specific departments may require varying approaches

The 8 pillars of soft controls within internal control environment

Clarity 01

For internal controls to be effective, they must be clearly defined, communicated, and consistently applied. The Responsible, Accountable, Consulted, and Informed (RACI) chart is an indispensable element in the field of clarity. Clear communication ensures employees understand their roles, while achievability of the tasks (including training) helps them implement controls properly. Consistent execution of work processes is crucial to detect and mitigate risks, preventing gaps due to ambiguity.

Lead by example 02

It might sound like a cliché, but it is important that management "walks their talk." Their behavior builds trust and credibility in the internal control system. By adhering to the controls themselves, management enhances their own credibility and demonstrates commitment to compliance. Employees are more likely to follow procedures when they see their leaders doing the same. The better the desired example is shown, the more the desired behavior will occur within the organization. Also, congruence of messaging from management is key because this sets the tone on top to reflect their point of view on internal control.

Involvement 03

Not all employees are familiar with internal control, and as the Dutch saying goes, "Unknown makes unloved." It is essential for management to explain the expected changes with the (new) internal control system and listen to their employees. The more management shows commitment to their employees, the more likely employees will cooperate with the system. On top of that, workers who are motivated by the purpose behind controls are more likely to identify control gaps when those controls are not functioning as intended.

Achievability 04

When designing a (new) internal control system and its procedures, achievability is key. Controls must be realistic and achievable to be effective. Overly ambitious or complicated controls may be bypassed or ignored by employees, which in turn reducing their effectiveness. Other important elements here are enough resources (time and employees) and mandate to strengthen the empowerment.

The 8 pillars of soft controls within internal control environment

Transparency 05

Transparency is pivotal in fostering visibility and granting insight into processes across the entire chain of control-related activities. It nurtures an environment of open communication where employees are not only informed about the rationale, testing procedures, and anticipated results of control activities but also understand the importance of both monitoring and being monitored. This continuous loop of feedback enhances the effectiveness of control testing, as it ensures that control testers and stakeholders are well-informed and equipped with all the necessary data for making well-informed decisions. Through increased transparency, all parties can actively engage in the oversight process, resulting in better governance and improved outcomes.

Open to discussion 06

Openness to discussion encourages employees to ask questions, seek clarification, and express concerns about internal controls. This dialogue helps identify control weaknesses, testing deficiencies, and potential improvements, fostering continuous improvement and leading to more thorough and insightful testing processes.

Accountability 07

Accountability is a critical responsive mechanism that involves calling individuals to account when they deviate from established policies and procedures. It ensures that every member of the organization is not only aware of their specific roles and duties but also recognizes their obligation to strictly follow testing protocols and to respond proactively to findings from control testing. By emphasizing the need for personnel to answer for their actions, accountability strengthens the reliability and efficacy of control testing. It acts as a catalyst for the prompt resolution of any issues uncovered, reinforcing the organization's commitment to maintaining high standards of performance and integrity in its control systems.

Enforcement 08

Soft controls that emphasize enforcement play a crucial role in reinforcing compliance with established control standards, policies, and procedures through a system of proportionate rewards and sanctions. By embedding these enforcement mechanisms within the ICF, the organization creates a clear set of expectations regarding acceptable and unacceptable behaviors. This approach not only ensures that individuals adhere to prescribed protocols but also promptly and effectively addresses any deviations through appropriate consequences. As a result, these soft controls contribute to more reliable testing outcomes by promoting a culture of accountability and discipline. They serve to complement the hard controls already in place, creating a comprehensive strategy that helps mitigate control-related risks and enhances the overall integrity of the organization's control environment.

The 8 pillars of soft controls within internal control environment

Benefits

The integration of soft controls into the ICF yields numerous benefits for an organization. By blending the human and cultural elements with traditional control mechanisms, companies can achieve a more holistic and effective approach to risk management and compliance. This method enhances trust and accountability among stakeholders, improves adaptability in a rapidly changing business environment, and ensures that ethical decision-making permeates all levels of the organization. Moreover, a culture-driven ICF enhances employee engagement and motivation, as individuals understand the value and impact of their actions within the corporate structure. The implementation of soft controls supports continuous improvement practices and creates a robust environment for internal controls that is both responsive and sustainable.

Manage Change

In managing change, soft controls are particularly vital in ensuring that transitions are smoothly integrated within the organization. By recognizing the importance of cultural adaptability, leadership can tailor change management strategies to align with existing values and behaviours, thereby reducing resistance and promoting acceptance. Clear communication and involvement empower employees to be agents of change, facilitating the adoption of new processes and controls. Moreover, accountability and enforcement ensure that changes are not only implemented but also sustained over time. The iterative process of assessment, feedback, and adjustment helps to refine approaches, ensuring change initiatives remain effective and aligned with the organization's strategic objectives. Soft controls underscore the principle that successful change management is not just about introducing new systems, but also about nurturing an environment that is receptive and favorable to change.

Summary

Starting the internal control journey with an assessment of the organization's internal control culture enables a tailored D&I strategy that directly addresses the identified strengths and weaknesses. This effort leads to improved change management, ensuring that the internal control environment is not only designed effectively but also embraced and upheld by the organization's members.

Key Questions to consider

Clarity 01

- Is it clear what the company expect from you with regards to your role in the ICF? How is it made clear?
- Are there sufficient training sessions conducted on the ICF?
- Are you familiar with the rules, policies, work instructions and guidance's relevant to your role in the ICF?
- Do you know where to access the rules, policies, work instructions and guidance's that apply to your role in the ICF?
- Do the conduct rules, policies and work instructions provide sufficient guidance on know how to perform your role and behave within the organization?

Lead by example 02

- How often do you observe senior management and leaders upholding the company's values and ethical standards?
- How often do you observe the reviewers adhering to the internal control procedures?
- How does your manager demonstrate how he/she deals with difficult situations or dilemmas related to internal controls?
- Is there enough room for you to provide input or ideas to improve the internal control processes?
- Do you have the feeling that your manager also does what he/she says when it comes to internal controls? 'Walk the talk'?

Involvement 03

- How committed do you feel to the organization's ICF?
- Do you feel that your contributions to ICF are recognized and valued?
- Do you feel personally invested in the success of the ICF and its goals?
- Are there aspects of the internal control process that you find draining or unmotivating?
- To what extent is compliance with conduct rules, policies and work instructions seen as a 'tick the box exercise'?

Achievability 04

- Do you feel that the targets and goals set for you regarding your role in the ICF (as preparer/reviewer/control owner/process owner) are realistic and achievable?
- Can you give examples of where shortcuts may be taken at some point? What causes this?
- To what extent are the tasks distributed among team members in the internal control process?
- How would you describe the level of detail in the internal control processes (too high-level, well-balanced, or overly detailed)?
- To what extent do you feel you are learning and developing new skills within the ICF?

Key Questions to consider

Transparency 05

- Do you think it would be noticeable if conduct rules, policies and work instructions are not followed within the ICF?
- To what extent the deviations or shortcuts would be noticed by management?
- To what extent does your supervisor/manager have enough insight into the actual processes on the work floor?
- To what extent do you receive regular feedback about your work?

Open to discussion 06

- How encouraged do you feel to speak up about ethical concerns or uncertainties related to ICF?
- Is there a formal forum or channel where you can discuss ethical dilemmas you face in your role within the ICF?
- To what extent is your manager approachable when you have questions or want to discuss difficult situations/dilemmas related to internal controls?
- To what extent are mistakes discussed within the team to improve internal controls?
- How frequently do healthy discussions or constructive disagreements take place within the team?

Accountability 07

- To what extent do you feel comfortable addressing a colleague or manager who does not adhere to rules, policies or work instructions?
- To what extent do you feel safe to report an incident or misconduct related to the ICF?
- To what extent do you trust that, if you were to report misconduct/incidents related to internal controls, the organization would handle it appropriately?
- How effectively do you believe your colleagues and/or manager handle criticism or feedback?

Enforcement 08

- To what extent are there clear consequences if someone does not follow the internal control policies and procedures?
- How confident are you that the organization enforces rules and standards related to ICF consistently?
- How strictly is compliance with internal control policies enforced? How does this impact your work?
- To what extent is it appreciated if you consistently follow internal control policies?

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