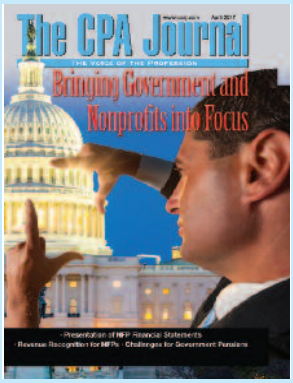
Serving the Public Interest

I enjoyed Richard Kravitz's article in the April issue of the *CPA Journal* ("Serving the Public Interest," p. 14). The message's import deserves some comment.

Kravitz mentioned CPAs' "critical fiduciary responsibility." I agree. Every time a company issues a restatement, it injures all CPAs and the system for which they serve as the watchdog. Some do not like to use the word "fiduciary," since it may mean more and higher legal responsibility for error. The larger picture, though, is that the public trusts the profession's audit opinion accuracy. "Unmodified opinions" support investors' belief in the profession's "good housekeeping" standard of reliable corporate financial statement reporting. The worldwide economy depends in large part on this intangible trust. That is the reason why the word "public" is in the middle of the CPA title—it indicates to which stakeholder the duty is paramount. It is naive to believe that lawyers or regulators can maintain a standard of financial statement accuracy without CPAs' professional support. That is why many enlightened CPAs and accounting organizations see the auditor's role as a fiduciary for the public, worldwide capital market that in large part holds this society together.

Jim Rigos, JD, LLM, CPA
Seattle, Wash.



There Is No Financial Fraud Personality Type

Sridhar Ramamoorti and Barry J. Epstein have written two articles published in *The CPA Journal* ("Today's Fraud Risk Models Lack Personality," March 2016, http://bit.ly/2m7UUoX; "When Reckless Entrepreneurs Become Dangerous Fraudsters," November 2016, http://bit.ly/2m7SVkD) claiming that there is a "dark triad" of personality types who, as business executives, are more likely than others to commit financial statement fraud. The "dark triad" consists of individuals who are narcissistic, Machiavellian, and psychopathic. Based on various other articles, these authors claim that "the overall incidence of these personalities is relatively small—2% or less in the general population—the incidence on Wall Street and in corporate America seems to be in the 10–20% range." The authors suggest that corporations, "before anyone is promoted to senior executive positions [sic] there should be assurance that their personalities are not deviant" and that for outside auditors "senior management personality types should be first be assessed and used to impact … audit procedures."

We strongly disagree with the authors, on many grounds. The personality types referred to have disparate traits, which do not necessarily lead to criminal behavior. While an individual with antisocial personality disorder will frequently have a failure to conform to social norms, not all people who engage in criminal activities have this diagnosis, and not all people with this diagnosis engage in criminal activities. People with narcissistic personality disorder may well have a pattern of grandiosity, need for admiration, and lack of empathy, but such a person is not considered by the psychiatric profession to have a higher risk of criminal behavior. Lastly, Machiavellian personality is not a disorder included in the Diagnostic and Statistical Manual of the American Psychiatric Association. We know of no reliable studies indicating that a confluence of these traits in one individual would materially increase the risk that

such an individual is significantly more likely to perpetrate a financial fraud.

There is a long history of society trying to find ways to define criminals by their physical characteristics, which have proven to be utter failures. We believe that the search for dark triad individuals is equally doomed to failure. There is a great deal of neurological research taking place currently that may or may not tie personality characteristics to genetic makeup someday, but we are far away from that understanding. Until the brain is better understood, we believe that trying to define dark triad individuals is another step in the failed attempt to define criminals based on non-experiential information.

In addition to the above generalities, we have specific disagreements with the positions taken in these articles:

■ We do not have faith in the statistics the authors cited, referenced above, as

to the proportion of persons in the general population and in executive positions having personality characteristics that would classify them as being part of the dark triad. While such personalities exist, this type of disparity in their incidence is questionable. The authors also refer to "the apparent prevalence of psychopaths in corporate management"; we have not seen such a prevalence.

■ Our business, political, military, and social leaders have many of these characteristics. While we do not know if our leaders and heroes have dark triad personalities, many of them clearly have some of the personality characteristics included in the dark triad.

■ Our most creative, interesting, and profitable clients are frequently those who are building business empires. Such individuals are not shy, retiring, or anxious to follow all social norms. Would the elimination of individuals who exhibit some of the dark triad characteristics from business eliminate the creators of Apple, Google, or Facebook? Enron was a very creative company and did many very creative things. We do not believe that, since they went astray, we should carefully try to eliminate such creative individuals from our clients.

■ There is no support we know of for the idea that personality issues are a significant cause of financial dishonesty. The author of a recent book on creators of financial frauds, *Why They Do It: Inside the Mind of the White Collar Criminal* (Eugene Soltes, Public Affairs, 2016) states his belief that many of the criminals that he interviewed were good people who made mistakes, either out of their inadvertence or finding themselves in a poor position from which they did not know how to recover. In general, they did not exhibit any of the three characteristics of the dark triad. Examining companies for dark triad personalities would not have discovered these individuals.

■ A professional psychiatrist's diagnostic conclusions about personality characteristics require input from a cooperative person; the types of behaviors and characteristics of the people described in the triad can easily be hidden during such an evaluation. In addition, the authors would require auditors and board directors to simplify what is a very complex and subjective matter.

> Until the brain is better understood, we believe that trying to define dark triad individuals is another step in the failed attempt to define criminals based on non-experiential information.

■ An auditor trying to follow the authors' recommendation would be perplexed as to how to proceed. The authors suggest that "perhaps psychologists or psychiatrists should interview client management and make assessments" for new clients. We do not believe this type of procedure is reasonable, as the individual would most likely strongly object. Alternatively, the authors believe that an auditor should make his own determination as to whether a prospective client is a member of the dark triad. If a psychiatric professional cannot do that, one cannot expect an auditor to make such an evaluation.

■ The authors suggest that "accounting students … should strive to become educated about abnormal personalities and their potential impact on audit risk." We do not believe that such educational emphasis would be productive.

■ It is possible that a trained psychiatric professional could make a reasoned judgement from peripheral information about the potential client or employee. We note, however, that the American Psychiatric Association specifically forbids members from making such evaluations of public figures, where much more information is available.

There are certainly serial predators that can endanger investors; auditors have been aware of this risk for many, many years. Firms have adopted requirements for searches for new clients not personally known to members of the firm. Internet-based search engines such as Google or Yahoo have made such searches inexpensive, and we absolutely believe they should be made whenever a firm gets a new client with personnel unknown to the firm.

As stated above, we believe that the percentage risks of either dealing with a person from the dark triad or the risk of such an individual committing a financial fraud are highly suspect. The risks involved are completely non-quantifiable, and therefore it is not possible to make any cost-benefit evaluation of following the authors' suggestions.

Jeffrey Borenstein, MD
Psychiatrist
President, Brain & Behavior Research Foundation
New York, N.Y.
Arthur J. Radin, CPA
Treasurer, Brain & Behavior Research Foundation
New York, N.Y.

The Authors Respond

We thank Jeffrey Borenstein and Arthur Radin for reading our articles carefully and preparing their response. We believe, however, that they have substantially misunderstood our argument and have underestimated the risk dark triad (DT) personalities pose to corporate America and society. Specifically, they assert that we have postulated that DT personalities are the necessary condition for the occurrence of business fraud.

We made no such claim, however. We only suggested that the Cressey Fraud Triangle is incomplete and that those exhibiting any of the DT personalities are more likely to commit or condone fraud. On the other hand, even a DT personality confronted by effective internal controls would be prevented or dissuaded from attempting fraud, as such controls reduce or eliminate the "opportunity" vertex of the Cressey Fraud Triangle and increase the probability of being detected. Besides underscoring the importance of controls, our thesis is that the auditing profession should do more to educate auditors, plan and review audits, and possibly engage specialists, in order to reduce the audit risks exacerbated by the presence of DT types in management and leadership positions.

Furthermore, we never claimed there exists a specific "financial fraud personality type"—not every white collar criminal is a DT type, and every DT type does not necessarily commit white collar crime. Rather, by citing proliferating research on the risks posed by DT personalities, we merely contend that auditors should consider the "DT personality risk" in the same way that paragraph 85 of SAS 99/AU-C 240, *Consideration of Fraud in a Financial Statement Audit*, requires auditors to consider "domineering management behavior in dealing with the auditor" and other personality risk factors.

Determining audit risk is a central element of any audit, constrained neither by laws of libel nor standards of the psychiatric profession. If personality assessments can be useful in more accurately assessing audit risk, then they must be pursued, not only to protect the audit profession's reputation, but also to benefit society.

Machiavellianism

Borenstein and Radin claim that because Machiavellianism is not formally defined as a personality disorder in the American Psychiatric Association's (APA) *Diagnostic and Statistical Manual*, it should not be considered relevant. It is, however, very much part of the DT specification, as well as the empirical findings supporting the existence of this personality type. The specific traits that constitute Machiavellianism have been well elucidated and, even more importantly, can be observed or measured by extant interview schedules and other means. It makes eminent sense to make efforts to detect Machiavellians in our midst (particularly in positions from which fraud or asset theft could be perpetrated) and makes no sense to ignore it.

Whether the psychiatric profession considers the DT personalities to have criminal predispositions is beside the point, for if the auditor concludes that their presence heightens fraud risk in any way, that conclusion must be factored into the fraud risk assessment according to professional standards. After all, the assessment of risk factors is the auditor's prerogative. Auditors cannot, after the fact, cite the APA's position as a valid defense for ignoring the behavioral characteristics of DT types if fraud occurs.

Response to Dark Triad Personality Characterization

Risks flowing from the presence among client management of DT personalities have not gone unnoticed by others, even if auditors have not previously addressed the topic. A Federal Bureau of Investigation Bulletin from 2012 carries the title, "Psychopathy: An Important Forensic Concept for the 21st Century." Clive Boddy, in his 2011 paper in the *Journal of Business Ethics*, lays the blame for the global financial crisis squarely on DT personalities. The incidence of psychopathy among males is between 1 and 2% in the general population, but once "almost-psychopaths" are also included, Harvard psychiatrist Ron Schouten, relying on research by Paul Babiak and Robert D. Hare, argues that the proportion among corporate

executives may well exceed 10%, in part because they are attracted to thrill-seeking, extreme risk-taking, and money. If indeed 10% of corporate executives share any such traits, the audit profession can scarcely afford to ignore this fact.

We recognize that grappling with DT issues will be challenging for auditors, who first must become educated in matters never previously addressed, and then deal with the likely contentiousness of clients in order to extract insights necessary to making the related risk assessments. DT personalities can be very difficult, which may necessitate departing from such typical practices as the commonly observed assignment of junior auditors to conduct rote internal control interviews. Fundamental changes to audit planning and staffing actions may well be needed. One does not send the lamb to question the lion.

Even accounting academic research is becoming curious about how DT personalities may potentially exert a pernicious influence on financial reporting and auditing; several studies posit that CEOs and CFOs may possess DT personalities, with one finding that psychopathy was the trait most strongly linked to bullying behaviors, followed by Machiavellianism and narcissism. There is evidence of CEOs pressuring CFOs to cook the books, and the Miller & Rittenberg 2015 study on the politics of internal auditing reported in the *Wall Street Journal* suggests that internal auditors are frequently pressured not to audit risky scenarios. Whistleblowers frequently talk about having been bullied into silence or threatened with retaliation. Furthermore, the Sarbanes-Oxley Act of 2002 (SOX) and the Dodd-Frank Act of 2010 contain provisions making retaliation against whistleblowers illegal. Lying to auditors is another concern, which is why SOX section 303 explicitly makes it illegal.

> To presume that white-collar crimes are random or accidental, thus rationalizing the continuing failure to deal with DT personality risk factors, is to tolerate the present incidence of audit failures and to bet against the likelihood of further instances.

The Dark Triad is about Personality and Behavioral Characteristics

Borenstein and Radin draw an incorrect analogy when they state that past efforts to link criminal activities with physical characteristics have been unsuccessful. We are well aware of the shameful episodes in the history of psychology of "trying to find ways to define criminals by their physical characteristics." We never mentioned "physical characteristics" in our articles, however, but instead focused on "personality and behavior characteristics." We aren't proposing using phrenology or any other similar discredited mechanisms or measures. On the other hand, several empirically tested personality scales are already in use and have been validated, and others could be developed once the significance of DT personality risk is better appreciated.

Why They Do It

Borenstein and Radin assert that there is no support they know of for the idea that personality issues are a significant cause of financial dishonesty. They cite Eugene Soltes, author of *Why They Do It: Inside the Mind of the White Collar Criminal*, as expressing the belief that many of the white collar criminals that he interviewed were good people who made mistakes, either inadvertently or by finding themselves in a difficult position from which they did not know how to escape, and that, in general, the perpetrators did not exhibit any DT characteristics.

Soltes in fact cites Ramamoorti's research twice in his book, discussing dark triad personalities, especially psychopathy, with the statement, "To the extent that corporate misconduct harms both investors and employees, it would not be entirely surprising to find a correlation between having *a lower level of empathy* and an individual's propensity to engage in corporate misconduct" (p. 61, emphasis added). Borenstein and Radin selectively quote from the book, ignoring that Soltes accepts psychopathy as a relevant construct; they again imply that we claimed that an ironclad linkage exists between DT personalities and the occurrence of fraud, which we did not do. We talk about probable cause and correlation, not certainty.

Corporate Psychopathy and its Consequences

Several positive traits (e.g., communication skills, persuasiveness, displaying greater strategic thinking) of successful leaders are also possessed by DT personalities. In addition, as reported by U.K. journalist Brian Basham, investment banks (and perhaps other types of businesses) have aggressively been recruiting DT types for several years now. Specifically, Basham quotes a

senior U.K. investment banker as saying, "At one major investment bank for which I worked, we used psychometric testing to recruit social psychopaths because their characteristics exactly suited them to senior corporate finance roles." DT types are hired because of their nature, then nurtured and incentivized to take reckless risks; should we then be surprised at the bad behavior that sometimes results? This is the key point made in our November 2016 *CPA Journal* article.

We agree that drawing an empirically justified correlation between DT personalities and white collar crime is difficult and may not be feasible in the short term. Nevertheless, many research papers seem to concur that psychopathy is much more prevalent in corporate management than among the general population. Certainly, the Wall Street financial crisis was not brought about by executives who, as Soltes says, "were good people who made mistakes, either out of their inadvertence or their finding themselves in a poor position from which they did not know how to recover." To presume that white-collar crimes are random or accidental, thus rationalizing the continuing failure to deal with DT personality risk factors, is to tolerate the present incidence of audit failures and to bet against the likelihood of further instances of such crimes in the future. For example, the potentially DT personalities in Enron's leadership ranks (e.g., Andy Fastow, Jeff Skilling) should have been screaming red flags. The auditing profession can and must improve its performance by making use of the most up-to-date tools and techniques, including risk assessments that are responsive to DT personality factors.

Sridhar Ramamoorti, PhD, ACA, CPA, CIA, CFE, CFF, CFSA, CGAP, CGFM, CGMA, CITP, CRMA, MAFF
Associate Professor
School of Accountancy
Kennesaw State University
Kennesaw, Ga.
Barry Jay Epstein, PhD, CPA, CFF
Principal, Epstien + Nach LLC
Chicago, Ill.

Note: The authors have provided a list of references for further reading, which can be found on our website (http://www.cpaj.com).