

Conference Paper

The Development of Risk-Management Techniques in order to Improve the Quality Control- Supervisory Activities

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Abstract

Quality control-supervising activity based on a risk-based approach (RBA), especially the Executive branch of Government, is now urgently pressing challenge, requiring further scientific and methodological developments. The concept and essence of the terms "risk" and "risk-based approach" are considered in the article, a semantic relationship of the concepts danger-threat-risk are proposed, alongside with risk management methods taking into account theorem about the ratio of the levels of risk and uncertainty in the organization.

Keywords: risk-based approach, supervisory activities, the risk, the threat, the danger in organizations

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1. Introduction

Improvement of control and supervisory activities based on a risk-based approach (RBA), particularly by the executive authorities, today is an urgent task requiring further scientific and methodological development. In practice, we use a variety of different systems, models, interpretations and approaches to the implementation of oversight activities. Even one of the most rigorous in the methodological attitude of Supervisory organizations – the FATF does not prescribe the organizations to use a particular Supervisory model. However, whatever the Supervisory system we choose for selected organizations, it should ensure the effective identification and reduction of risks of different nature, corruption, money laundering and terrorist financing in the financial sector and other offences, and not reduce the content of RBA only to the number of inspections in the organizations, as is sometimes even enshrined in the methodical developments on RBA.

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The concept and content of a risk-based approach is set out in the requirements of the FATF standards (recommendation 1, "Risk-based approach") for the need to assess policies, procedures and controls of companies and organizations to identify and manage risks, and, if necessary, to apply corrective measures, i.e. the formation of the risk management system [1]. It should be emphasized that standards for risk management, other normative documents, for example, "Methods of anti-corruption" of the Ministry of Labor, also include the same set of methods, measures and actions.

This approach requires individual risk assessments and understanding of the characteristics and situations of each organization. In the case of identifying deficiencies in the risk management program, or violations of laws or regulations, the Supervisory authorities should apply proportionate corrective action to correct identified deficiencies.

For effective work of risk management in organizations, we examine the understanding of risk as an object of regulation. The question is not idle, because the experiences of the regulatory and Supervisory agencies in various organizations showed significant differences, as will be shown, in understanding threats, vulnerabilities, hazards, risks in their activities depending on the prevailing practices. This issue is dedicated to the main contents of this article.

2. Material and Theoretical Bases of Research

The development of a theory and practice of risk management led to the recognition of the need to develop a clear guidance in the conceptual apparatus of this science and practice.

Two far apart countries, the USA and Australia and New Zealand almost simultaneously developed and adopted documents, which have become a guideline for professionals in many other countries. In 1992, the USA developed "Internal Control – Integrated Structure, ICIF", and in 1995, Australia and New Zealand worked out the standard of risk-management of the enterprises "Risk management". Many scientific and academic centers have contributed to the study of problems of risk management and promotion of this field of knowledge for already two or three decades [2, 5].

Considerable scientific and factual material allows determining the main development trends. According to the authors of "Risk Management Firm. Program of Interactive Management," [3] the world and society are in the beginning of the era of dramatically accelerating changes in general, and in business features. Among the

main reasons for these changes are increased price volatility, globalization of markets, increased competition, increase in tax and legislative regulation, the increasing availability of databases and other factors. This historical overview emphasizes the urgency and relevance of addressing issues of theory and practice of risk management at the present stage, without which, apparently, it is impossible to increase further the effectiveness of risk management as a comprehensive management concept.

Still unresolved problem is a scientific definition of the concept of "risk" that is not particularly surprising. The history of the interpretation of this term is the history of finding out the fundamental quality of the relationship of man and nature, the development of the relations of nature and society. As for the concept of "risk" being quite a long discourse, in various scientific sources and documents (guidelines, methodologies and standards for risk management) there are quite different points of view and approaches to the interpretation of the concept of "risk". The most common definition is the following, given in the already cited "Risk Management Firm" [3]: "risk is understood as life with the possibility that some future event may cause, but not necessarily harm." Further, on in the same publication (p. 40) the authors state: "in fact the risk as a phenomenon is much deeper than the mundane-application definitions". We emphasize that, nevertheless, applied understanding of risk is important for practitioners of management of the organization (business and management). They have little interest in the historical evolution of interpretations, but are interested in the practical assessment of the possible implementation of those or other methods of decision-making in the various possible circumstances of the probability of events, deviations from expected results, possible impacts, adverse impacts, etc.

Considering risk as a person's choice in the category of utility, the proposed definition of "risk" as "... a feeling of satisfaction with respect to expected changes in the quality of life in the future and the corresponding expected change in the prevailing quality of life, which an individual may have expected to sacrifice for the sake of the future." This definition is useful. In that it, firstly, introduces the person (organization, as a product of human activity) in the system of relations (the risk of that human activities). Secondly, we have significantly expanded the range of goals of the human (organizational) activities. Nevertheless, as it was shown in their works, the winners of the Nobel Prize in Economics R. Thaler, D. Kahneman say that an individual often makes his choice in spite of its use. In this case, the risk as a satisfaction is difficult to identify and measure the results of its possible manifestations. However, the dimension of risk (more precisely, the results of its implementation) is one of its distinguishing features, according to one of the first developers of this theme F. Knight.

Risk is a basic feature of human activities, and thus, the basic property of economic relations. This is the understanding of risk as an economic category, i.e. characterization of the relations concerning production, accumulation, distribution and consumption of the products of labor. In this sense, the enterprise, according to Th. Schumpeter and the authors already quoted, is "... a conscious assumption of risk in expectation of obtaining anything desired (the influence of status, profit, winning the election over competitors, etc.)", but not only because it will cause economic losses.

But, from our point of view, this formulation is not sufficient to define and implement the program of action for the management of risks in the organization. Let us consider the concept through the study of the essential part of the risk as a phenomenon of human relations. This will specify that our consideration has a more specific focus, namely risk management and management decisions at all levels of the organization. However, the concept of "risk management" has become not only convenient and widely accepted in theory and in practice, but also useful to justify the selection policy of risk management strategy. Apparently, either we cannot talk about controlling (or regulating) risk in its understanding as the possibility of damage, or we need to change the object-subject relationship. The subject is an observer and the controller remains the same, therefore, the object must be specified more carefully, accurately and in details. Trying to remove this contradiction by introducing the possibility of fixing quantitative risk parameters, a number of works complement the interpretation of "risk" by reference to its probabilistic nature. In a number of standards of risk management, for example, in the first version of the standard developed in Australia and New Zealand the notion of risk is revealed as "... the combination of probability and outcome." Though it often persists the previously mentioned pessimistic "down to earth-hands-on" approach to risk as probability of negative and undesirable effect for the economic entity of deviations (variance) of the possible implementation of a risk event in reality from those projected in the future. In our opinion, there is a substitution of concepts of risk and risk events that are not the same.

The contents of risk in our understanding can only refer to the person acting, the seeker, making his choice or just living and trying to realize his purpose (as he understands it). Risk management in such a setting as one of the mechanisms of conflict resolution and their harmonization is not only of socio-economic but also legal nature. The risk is realized under condition of interaction of elements of a complex system, comprising: operating from their point of view of the subject; managing and changing in time; the external environment of functioning of the subject, also changing in time, as the system of higher order.

3. Results

The risk, therefore, lies in management actions (decision-making process and its implementation). Nevertheless, the given definition is only part of the concept. The other part of this definition is that in order to take action, you need to identify, describe, estimate or measure the consequences of these actions (risk consequences), to rank the seriousness of the consequences. Otherwise, managing the risk will be very difficult (if it is possible in general to control unidentified object). Management methods may be different, but the general approach is aimed at overcoming conflict and lowering uncertainty of future events.

Thus, we can offer the following definition, which expands the understanding of economic risks in the activities of the economic entity through its three complementary essential components [4]. Risk is:

1. the existence of a situation of uncertainty, risks and threats to the external and internal environment;
2. the presence of the subject and awareness of the situation of threat (risk and its quantitative and qualitative assessment);
3. decision (purpose and method) based on risk perception and its implementation in order to reduce the uncertainty of realization of future events.

This definition also has an important limitation related to the fact that the activity of the subject is managerial in nature, but differs from the management of the organization as a whole. The difference is primarily in the ratio of levels of management: risk management is a subsystem in the control system of the organization providing the information component of top management. The second difference relates to the scope of analysis and evaluation. Risk management deals with uncertainty of future results, of course, important and significant for the organization, but not exhaustive of all management tasks. The next difference is the risk management is using an independent methodological and instrumentation unit of analysis as any other special model of management analysis. It is also important to emphasize that the subsystem of risk analysis is not isolated from the whole system of control, and is immanently present in all management processes within the organization and outside, permeating into all processes in the organization, but affecting only those matters that are specified in the definition of risk.

Concluding the consideration of the contents of "risk" as an economic category we should correlate the concepts of "danger", "threat", as semantically related to the

concept of "risk" as they are often considered as synonyms, or similar in contents. Nevertheless, these terms have different meanings:

- danger characterizes undefined deviation from the normal state of the environment or situation,
- the threat is a direct factor or cause of unwanted (uncertain) impact on the processes,
- risk is a controlling activity in the conditions of threat of external and domestic environment under the influence and endangering its activities threats.

Thus, the risk as variety of threats, if implemented, would result in operation of undesirable consequences for organization. The risk is adoption and implementation of decisions for future in a threatening uncertainty environment. Risk assessment is the evaluation of the consequences of a possible realization of a risk situation due to the adopted solutions.

The contents of the term "risk" we propose, allows you to build a logical relationship between three meanings mentioned above (danger, threat, and risk): the transition from environmental hazards to the threats of possible versions of the future development of events (risk, i.e. associated with solutions) and the need of responsible choice-making in these conditions of uncertainty.

Based on a complex model of a synergistic sense, the socio-economic system, considering risk management (activities to decrease uncertainty) and the uncertainty of the environment of functioning of business entities as parameters of the order of the system the theorem was formulated about the ratio of levels of risk and uncertainty of complex socio-economic system.

Any socio-economic regulated system corresponds to a certain level of risk, as a condition of its development. Uncertainty is a characteristic of the market complexity and instability that is a factor of a plurality of path selection of a development, but not a feature of development. With this correction, we can formulate the theorem on "Ratio of limits of uncertainty and risk complex economic system" [4], based on the following provisions describing the evolving socio-economic system:

1. Any socio-economic process has a specific value (measure) of uncertainty of the environmental conditions in which this process occurs and the amount (measure) of risk of functioning, and which acts as control parameters of synergetic system – characteristics of the complexity of the evolving system;

2. Any socio-economic process is characterized by a certain appropriate stability of functioning of system of interval (range) risk management (controllability, based on their measurement, assessment, regulation, monitoring) i.e. characteristics of controllability of the evolving system;
3. Socio-economic process characterizes both minimum and maximum levels of uncertainty of the environment and risks of the operation (handling) within which it is cost-effective and safe operation of the underestimation leads to the termination of the development (negative dynamics), and the excess of maximum level - to the destruction of the system – the characteristic stability of the evolving system.

Based on the theorem we can draw some specific conclusions and make recommendations, including assessment of the current socio-economic situation in Russian economy.

First, the narrower the range of uncertainty levels, the less risk of any nature from criminal and corruptive to public socio-economic.

Further, you can also predict that the minimum levels of risk (e.g., corruption, social) may not be the same in different countries, with their intervals of uncertainties and risks. Therefore, the comparison of indicators, such as corruption, financial crime in different countries is not quite correct, if you do not take into account the characteristics of the environment (context) of the operation.

Further, it is possible to note an inverse relationship with the growth of the level of risk (e.g., social), you can talk about the growth of uncertainty (the range extension threshold). Thus, the growth of social unrest, for example, in Ukraine, USA, and France may indicate increasing uncertainty on the level of choice of strategy of the development of a particular country.

4. Conclusion

In conclusion, it should again be emphasized that whatever Supervisory system is chosen by the organization, it should ensure the effective identification and reduction of risks of different nature, finance, corruption, money laundering and financing of terrorism and other offences. Moreover, accurate understanding of the content of basic concepts, in particular risk, threats, and hazards in the functioning of organizations will enhance the effectiveness of risk-based control method.

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