
Regulation of risk management system

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Abstract

The degree of risk is influenced by the following factors: knowledge of accounting by an auditor; general conceptual approach to the audit; changes in the regulatory system; level computerization; internal control system in the object of audit; frequency of change of managers upper and middle level and, as a consequence, their bad knowledge of the existing management system; evaluation of the obtained results and their completeness.

Experts are inclined to believe that the quality of external control largely depends on the professionalism, experience and objectivity of external controllers. The opinion of experts is based on numerous cases of unprofessional, biased attitude of some executives of audit, tax and other bodies to the management and employees of audit legal entities.

Keywords: audit, control, audit risk, management, accounting information, fraud.

JEL Classification: M40, M41, Q01.

Introduction

Audit, like any other type of business, is subject to risks. The nature of audit determines the occurrence of specific risks that are not inherent in other professional activities. They are, in particular, related to the drawing by the auditor of conclusions based on the results of the work performed.

The problem of audit related risks acquires higher topicality in the context of the economic crisis, when the probability of financial problems among business entities increases, and the society shows an increased interest in financial information that is subject to control by stakeholders, as modern scientists turn to the issue of control more often [2 ;3 ;4].

1. Literature review

The issues of risk assessment of audit activities have been studied by the following Ukrainian and foreign scientists: S. Bychkova [3], O. Razborska [4], V. Rudnitsky [5], V. Sopko [6], and others.

However, despite certain experience gained so far in the field of auditing, some issues call for more thorough consideration. In particular, certain aspects of the organization of audit in the agricultural sector, quality ensurance of audit services, use of effective methods of practical audit in the context of specific features of agricultural production and determining audit risks are insufficiently studied.

Works of scientists mostly consider the assessment of audit risk only and restrict to the presentation of a model of the relationship between the components of audit risk, the determination of an acceptable level of risk, and the characteristics of factors affecting risk. International audit standards contain definitions of audit risks. They define audit risk as that, when the auditor may express an inappropriate auditor's opinion if the financial statements are significantly distorted. This is due to the fact that the basis for the auditor's opinion is the auditor's reasonable confidence that the financial statements as a whole do not contain significant distortion due to fraud or error. Reasonable confidence is achieved if the auditor receives acceptable audit evidence in sufficient volume to reduce audit risk to an acceptably low level.

Based on the interpretation of the new version of the Law of Ukraine "On audit of financial recording and auditing activities", the requirement of mandatory audit for most agricultural enterprises is not fixed, except, of course, those that are of public interest. However, this does not diminish the relevance and importance of conducting an audit, even when it is rather proactive than mandatory [9]. The methodology for assessing audit risk and other risks of audit activity was studied only in the works of the following authors – V. Rudnitsky (2019) and M.Bychkova (2015), where methods of assessing audit risk based on expert assessments are considered [3;4].

In his scientific works V. Sopko (2015) considers the assessment of the level of audit risk as "determining the amount of audit risk, reflecting the auditor's predisposition to risk, his vision of the economic environment in which the object under study is located" [6].

O. Razborska and O. Krymets (2018) note that this is “the study and analysis of both the accounting system itself, which is used at the enterprise, and the process of accounting and reporting, familiarization with all business operations carried out by the enterprise” [5].

Thus, it suggests the conclusion, that the vast majority of domestic auditors adhere to a unified calculation of audit risk, without taking into account two extremely important components: the risk of non-detection, the risk of control, which would induce more comprehensive information about the sources of risk and directions for adjusting the activities of the enterprise itself, as well as its accounting and control in order to minimize the level of audit risk in subsequent reporting periods.

The analysis of this issue once again substantiated the need to highlight all the features, advantages and flaws of methods developed by various scientists.

2. Research methodology, data and hypotheses

Suffice it to note, that risk– is an economic phenomenon that is a combination of possible adverse events and their consequences in the form of losses or damage. Economic risk arising in the course of economic activity can be classified as follows: risks associated with the main business processes; risks associated with auxiliary business processes; environmental risks that do not depend on the company’s activities; corporate management risk. Unfortunately, corporate management risks are not yet sufficiently taken into account by enterprises in practice in the decision-making process.

It should be noted that audit risk is the risk of the auditor expressing an inappropriate auditor’s opinion in case of significant distortion of financial statements. Most common misrepresentations of financial statements occur as a result of fraudulent actions, so the issue of identifying the level of abuse and fraud is also extremely relevant and important.

In December 2020, PricewaterhouseCoopers (PwC) conducted a survey of Ukrainian companies as part of the world study of economic crimes and fraud [10]. PricewaterhouseCoopers (PwC) is an international network of companies offering professional consulting and audit services. “PricewaterhouseCoopers” is part of the global network of companies PricewaterhouseCoopers International Limited, each an independent legal entity. The company has been around for more than 160 years and is one of the “Great Four” audit companies. The network is headquartered in London [10].

For the past 20 years, PwC’s world study of economic crimes and fraud has remained one of the world’s leading analytical publications on economic crimes.

The aim of the study is to assess attitudes to fraud and economic crimes and their impact on organizations around the world. The growing volume of fraud and economic crimes has increasing consequences for Ukrainian companies and forces them to ask complex questions: is our risk management program flexible enough to overcome the dynamic challenges that arise in a globalized business environment. Fraud cases committed directly by management account for 56%, while those committed by a third party account for 36%. Almost half of respondents in Ukraine admitted not to doing any or only informal verification or constant monitoring of the integrity of their counterparties.

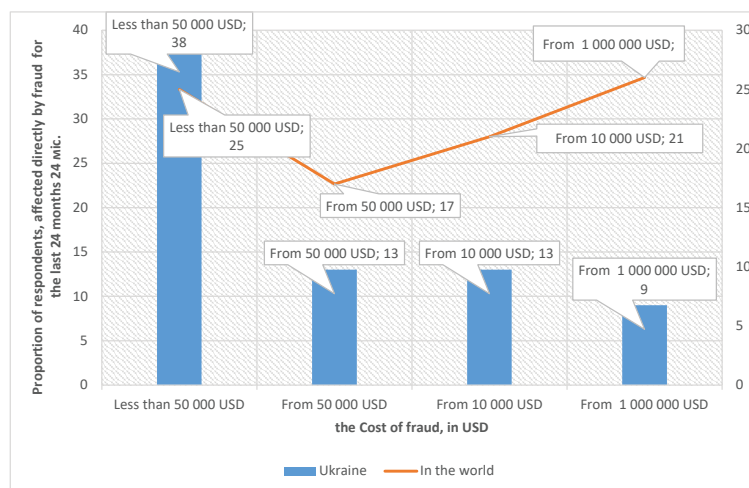
It should be noted that 51% of respondents in Ukraine have suffered from fraud in the last 24 months (period 2018-2020).

The study identified top 5 most common types of fraud in Ukraine for the period from 2018 to 2020. Suffice it to mention, that 26% of Ukrainian companies have suffered fraud losses in the amount of 50,000 to 1 million US dollars over the past 24 months (Fig. 1).

Besides, out of the 9% of Ukrainian respondents who suffered direct fraud damage of more than 1 million USD, –3% reported fraud losses of more than 5 million USD.

The cost of fraud in Ukraine and the world for the period 2018-2020

Fig. 1



Source is built by the authors basing on the source [10].

Every fourth organization in Ukraine does not have a special risk management program, and 22% of respondents in Ukraine have not conducted any risk assessment in the last two years.

It should be noted that risks are often called by the lacking information, which at enterprises is most commonly accumulated and processed in the accounting system. Risk in its common sense is the possibility of obtaining any negative or unfavorable results and failure to achieve the expected result. Its existence, primarily is associated with the inability to be certain, to anticipate the onset of certain events. So, the main features of risk are, firstly, its industry affiliation and, secondly, the specification of the object to which this risk is directed, i.e. production [7].

To fulfill the terms of Article 23 of the Law of Ukraine “On audit of financial statements and auditing” dated 21.12.2017 No. 2258-VIII, it is advisable to formalize the risk assessment methodology as an internal document [9]. For instance, it can be a “Regulation on the risk management system”. Each audit firm determines the format of such a document independently, however, we offer the following chapters:

I. General provisions (to describe the approval of this document, amendments to it, and regulatory documents to guide the implementation of the risk management process).

II. Strategic goals, objectives of the risk management system (to describe the goals and objectives of risk management system functioning).

III. Participants of the risk management process (interaction with company’s employees from different structural divisions to exchange information on risk identification, interaction with external stakeholders).

IV. The main stages of risk management (identification of risks, their sources and response method).

V. Assessment of the effectiveness of the risk management system (procedure for documenting the assessment, transferring the assessment to stakeholders). Assessment of the effectiveness of a risk management system can be carried out as self-assessment, internal assessment, or external assessment.

The issue of audit risk assessment is closely related to the risk management service of the audit firm. After all, auditor’s level of competence and responsibility depends on the level of detection of distorted information, and thus, on the audit risk itself.

Among the factors that most affect the quality of external control risk (REC), suffice it to highlight the following: qualifications and practical experience of external controllers (15,5%); changes in legislative and regulatory acts (12,8%); competence of the external controller about the objects verified (11,2%); objectivity in assessing the objects of verification and the actions of managers and other officials (10,1%); list of control procedures that are used in External Control (8,5%). Thus, experts are inclined to believe that the quality of external control largely depends on the professionalism, experience

and objectivity of external controllers. The opinion of experts is based on numerous cases of unprofessional, biased attitude of some executives of audit, tax and other bodies to the management and employees of audit legal entities [1].

Conclusions

Every practicing auditor should strive to achieve such quality of his/her work that can ensure a minimum level of audit risk. The fact that an auditor cannot provide an absolute level of confidence indicates that the audit risk can never be zero. In order to adhere to the established level of audit risk when performing a specific auditing, it is necessary to study the components of audit risk and analyze what factors may affect its size.

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