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Comprehensive Approach to Risk Management as an Essential Process of the Entire Enterprise Management

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ABSTRACT: A company's activities are inseparably associated with the risks whose sources of danger or conditions of manifestation are uncertainty and opportunity. Uncertainty is associated with incomplete and inaccurate information and implies the presence of factors the impact of which is unknown. Uncertainty can lead to both a reduction and an increase in the value of the enterprise for stakeholders. On the one hand, uncertainty is fraught with risk, and on the other, it opens wide opportunities. Therefore, the opportunities can be regardedas a risk with positive consequences.Risk characterizes the uncertainty associated with the likelihood of occurrence of adverse situations (threats) that hinder the implementation of the enterprise's strategy. In order to perform successfully, the enterprises should learn to manage risks, this implies building up (implementing) a risk management system (RMS).This article deals with the basic issues of risk management using a comprehensive approach at modern enterprises.

KEYWORDS: risk, risk management, comprehensive approach, risk classification, risk mitigationJEL classification: M10, M19, M20

I. INTRODUCTION

Risk is a potential event that can have a negative effect on the achievement of set objectives [1]. In other words, risk is the effect of uncertainty on objectives [2]. Risks can be both inherent, specific to the enterprise, and related to the environment. Usually, risk is assessed in terms of damage from a potential risk event and probability of its occurrence. A materialized risk can have both negative and positive consequences.

II. LITURATURE REVIEW

The history of the risk management practice development is shown in Figure 1.

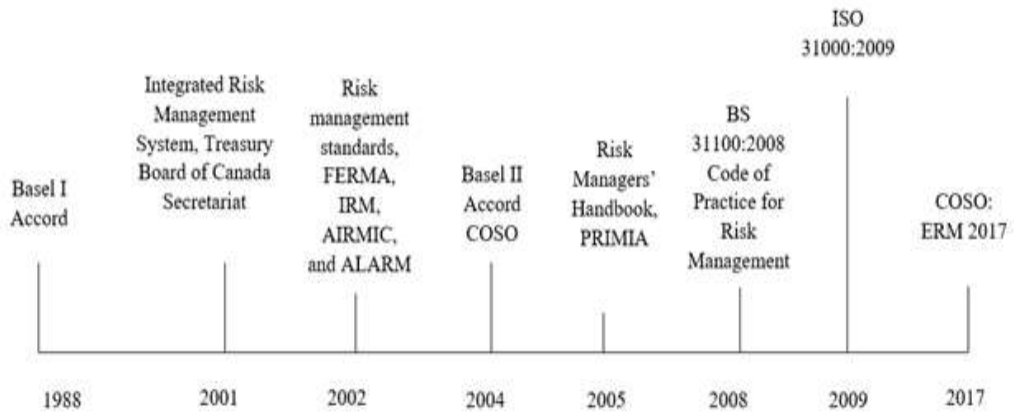

Figure 1: Risk management practice development history

The evolution of risk management is as follows: in the 90's the functions of risk management were to transfer risks to insurance and to settle losses, whereas today the functions of risk management are to identify risks,

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assess economic losses, manage risks through improving internal control and ensuring business continuity, to retain a large volume of risks, and to provide insurance.

Enterprise risk management is a process carried out by the board of directors, managers and other employees, which starts in the development of the strategy and impacts all company activities.

It focuses on:

1)Identification of potential events that may affect the company;

2)Management of the risk associated with such events;

3)Control to ensure that the risk appetite of the enterprise is not exceeded;

4)Provision of reasonable guarantees to achieve the goals of the enterprise.

The enterprise's operation goals are different; therefore, the risks should be managed subject to each goal of the enterprise operation [1]:

1)Strategic goals are high-level goals, they relate to the mission of the enterprise;

2)Operational goals imply efficient and effective use of resources;

3)Reporting goals imply preparation of reliable and timely reporting, accordingly;

4)Compliance goals imply the application of legal and regulatory requirements to the enterprise activities;

5)Resource conservation goals.

Subject to the goals of the company's activities, the risks may be classified as follows:

- Strategic risks (the most significant risks for the enterprise) are the risks that can adversely affect the successful implementation of the enterprise's strategy and achievement of the set goals;

- Financial risks are the risks associated with the capital structure, reduction of profitability, fluctuations of exchange rates, credit risks and fluctuations of interest rates (hedging is used to transfer the risks);

- Operational and technological risks include the risks associated with the interruption of production, systemic failures and reliability of the technologies used or implemented (including information), data loss risk, risks associated with logistics and sales / supplies, as well as accidental risks (insurance is used to transfer the risks);

- Company's compliance risk;

- Risks affecting the company's reputation.

Competition, changes in the consumer market, industry changes, legislation, culture, suppliers, contracts, and environment are external factors of potential risk manifestation. Research, intellectual capital, commercial services, personnel, property, products and services, accounting, information technology, recruitment, cash flow and liquidity are internal factors.

For example, business process risks in production may be as follows: the existing equipment will not enable to manufacture products that are in demand or the old equipment will not be replaced in time.

There is no single mandatory model of risk management because different countries and corporations employ different approaches and methods to regulate this process.

Regardless of the selected risk management model, the following principles must be observed:

1)Risk management is an integral part of all processes that take place in the organization;

2)Risk management is a part of the decision-making process;

3)Risk management should be systematic, well organized and implemented in a timely manner;

4Risk management should be based on information that is meant to be the most accurate at a given time;

5)Risk management is specific in nature;

6)Human and cultural factors shall be considered in risk management;

7)Risk management is a dynamic, regular process sensitive to changes.

The traditional approach to risk management implies that each risk is considered at its own level in the organization rather than a set of interrelated elements, i.e. the components of the enterprise's activities, such as finance, operations, technology, communications, personnel, property, environment do not add up into a whole. And the responsibility for risk management is somewhat blurred. The comprehensive approach to risk management implies that this task should be a part of managers' responsibility and should be an integral part of all organizational processes.

In The Book of Risk, Dan Borge wrote [3]: "The purpose of risk management is to improve the future, not to explain the past"; "The future may be uncertain but it is not unimaginable and what I do can shift the odds in my favor"

III. RESULT AND DISCUSSION

Based on the foregoing, the RMS reality is as follows:

- The RMS should start with addressing the key risks faced by the enterprise and enable operating at all levels of the organization;

- The RMS seeks to manage risks rather than to eliminate them; most enterprises have been in business precisely because they take risks, i.e. RMS is not a solution to transfer all risks to a safe zone;

Automation is an important tool for the RMS implementation, it will help to facilitate the collection, processing and reporting of risks, but the risk management culture first and foremost requires to address human problems and ensure a sound understanding of the requirements;

- The RMS implementation is a change in the enterprise culture, which enables to obtain many quantitative and qualitative benefits;

- Internal audit cannot be responsible for the RMS, it is an important part of the process, but the RMS should be controlled by the risk management and implemented by everyone.

Risk management is a central part of the company's strategic management. This is the process following which the company systematically analyzes the risks of each type of activity in order to maximize the effectiveness of each step, and, hence, the entire activity as a whole. Risk management should become an integral part of the corporate culture. Here it is also important to pay attention to human resources management.

Pursuant to the international standard ISO 31000:2009, risk management process covers the following activities [2]:

1)Establish the Context of Risk Management;

2)Risk Identification;

3)Risk Analysis;

4)Risk Evaluation;

5)Risk Treatment;

6)Communication and Consultation;

7)Monitor and Review.

Conditions, structure, environment and business processes at the enterprise form the RMS. Components of the enterprise's activities, such as the organizational structure of the enterprise, distribution of powers and responsibilities, risk management philosophy, risk appetite, history and culture of the enterprise, competencies and qualifications of the personnel should be considered as a whole, as the enterprise's internal environment which is the basis for all other RMS components.

Human resources management is important here: recruitment procedures, training, motivation, and regular assessment of performance, career advancement and remuneration, disciplinary actions, the enterprise's expectations regarding employee honesty.

Risk recognition (as the next RMS stage) involves identification of risks. Risk identification is the process of identifying the enterprise's exposure to uncertainty. Risk identification implies the availability of full information about the organization, market, legislation, social, cultural and political environment of the

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enterprise, as well as its development strategy and operational processes, including information about threats and opportunities to achieve the set values.

Various methods and tools are used to identify risks, such as seminars and discussions, internal analysis, brainstorming, interviews, analysis of competitors, questionnaires and surveys, process analysis, statistics on the events associated with losses. The events are identified both in terms of the past experience and in terms of potential future events.

The stage of risk analysis includes: analysis of causes of the risks and circumstances that characterize such risks; analysis of potential damage caused by risk in terms of financial, operational and human and reputational indicators; documentation of information obtained during the analysis.

Risk assessment is performed based on the following key indicators: degree of risk impact and likelihood of risk occurrence.

Risk management is the process of development and implementation of actions to reduce the negative effect and probability of losses or to receive financial compensation in the event of losses associated with the risks of the company’s business. The risk management stage includes: approval of employees that will be responsible for the management of significant risks; development (together with designated employees) of actions required to manage or eliminate significant risks. Risk management is inseparably associated with the risk response methods. The risk mitigation options are as follows:

1)Avoid: eliminate, prohibit, stop, limit, observe, and remove;

2)Accept: retain, consider in the price, insure by yourself, compensate;

3)Reduce: control, react, diminish, isolate, improve, shift, redesign, diversify;

4)Share: insure, reinsure, hedge, indemnify.

And it is important to know that risk management solutions can be a source of risk themselves.

Communications and consultations are one of the key stages of risk management. Exchange of information between business units should be performed at each stage of risk management. One example of communication is risk report. The approximate content of such report may be as follows: risk description; risk location, risk owner; risk-contributing factors; possible consequences of risk; risk assessment (likelihood, risk impact magnitude, final significance); answer to the question whether the risk is manageable; interrelated risks; action plans.

The last stage involves monitoring the status of risk-contributing factors and the progress of mitigation activities.

The stage of monitoring and revision includes monitoring of the status of risk factors. The following should be monitored: assessments of the likelihood of risk; the expected risk magnitude; other factors that may affect the risk significance; and drawn up mitigation plans and resources available. Based on the monitoring results, a decision should be made to introduce the necessary changes in the organization of the work, timeframes, and resources if required by the risk situation.

In conclusion, the advantages of the comprehensive approach to risk management should be highlighted as follows:

- Improvement of the decision-making process, reasonable guarantee of achievement of goals and objectives;

- Reduction of contingencies and losses in business activities;

- Total risk management in business activities;

- Timely identification and use of opportunities is a source of competitive advantage;

- Rational use of the enterprise’s resources;

- Improvement of the enterprise’s reputation;

- Borrowed capital cost reduction.

A typical sequence of the RMS implementation steps may be as follows (Figure 2).

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Figure 2: Typical sequence of the RMS implementation

Risk management should be introduced as an element of the enterprise's culture.

The objectives of risk management culture development are as follows:

- Understanding of risk management as a valuable element of the overall corporate governance system;

- Understanding of risk management by each employee as a significant and integral part of his/her functional responsibilities. Employees understand the priority of risks and how their functional responsibilities are related to the overall structure of the optimal risk management;

- Each employee understands how risks can be identified, managed and transferred to a higher level;

- Implementation, maintenance of the RMS at the enterprise and actual benefits;

- Continuous training, maintenance and development of the risk management knowledge, skills and potential, professional development and knowledge exchange throughout the entire structure of the enterprise;

- Development of understanding, competence, potential and knowledge.

At present, there is a need for effective implementation of risk-oriented management of the modern enterprise, and, in this connection, the issues of automation of risk management are intensively addressed [4].

Let us discuss the risk management process by the example of an educational organization in accordance with the stages described above. Let us take poor quality of classes (lectures, practicals) as such risk.

When identifying a risk situation, one can imagine the presence of incompetent teachers hired based on kinship ties, for example. (It should be noted that the existence of kinship/friendship ties does not exclude the employment of a professional teacher, however let us imagine a situation associated with risk). The identification of the risk enables to define a high degree of exposure of the organization to uncertainty in the event that personnel are selected in such a manner. The analysis of potential damage (risk analysis stage) presupposes that students fail to master the necessary knowledge, that no appropriate skills and abilities (hence, no required competencies) are acquired; these result in dissatisfaction of both the students and other parties concerned (management of the educational organization, parents and employers).

When assessing the risk, it is obvious that the likelihood of such risk is high if the teacher lacks the necessary qualifications. The process of development and implementation of the corrective actions (at the risk management stage) enabling to reduce the negative effect is the improvement of the personnel selection system, avoidance of selecting non-professional personnel based on personal liaisons (i.e. risk mitigation option: avoid). Given that the proposed recommendations have been implemented, the likelihood of occurrence of such risk will be significantly reduced.

IV. CONCLUSION

To sum it up, one can formulate the main conclusions on risk management as follows:

- Risk management should be considered as a standard management process rather than a separate line of business;

- An enterprise (organization) must assess to what extent it can see the picture of all the risks taken by each dpartment and by the enterprise as a whole;

- The enterprise should focus on developing a number of important actions that will enable it to monitor and manage risks within the area of its competence.

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