TOOLS OF ACTIVE AND PASSIVE MANAGEMENT OF FINANCIAL-ACCOUNTING RISKS

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Abstract:
The dynamic of the business environment continuously generates various risks, among them there are both the financial and accounting ones, risks affecting the entity's results, mostly negatively. In this context, the increase of the economic performance, the presentation of a true image and the carrying out of effective activities is strictly related to implementing a risk management system. Thus, identifying the tools for managing the financial-accounting risks is essential in knowing those risks that can be partially or fully accepted, evaluated or transferred.

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1. Introduction

"The objective of financial statements is to provide information about the financial position, financial performance and changes of the financial position and financial performance of the entity, information that is useful to all users" [F.C. Dima, p 57].

In case of inadequate presentation of the financial information financial and accounting risks are highlighted. Therefore, increased attention should be given to removing hazards from the activities developed in an entity.

Management or financial and accounting risk management refers to all processes defined and implemented by an entity in the financial and accounting department, whose main aim is to reduce the existing or the potential risks.

In this context, the aim of this paper is to identify the financial-accounting risks that entities are facing and to propose a set of tools for managing them.

To achieve the purpose set, a series of specific objectives was followed, namely:
- theoretical grounding of the risk concept;
- presentation of the financial-accounting risks;
- highlighting the key tools for managing the financial-accounting risks.

2. Financial and accounting risks of the entity

The literature attributes many definitions to risk, as follows:

Risk can be seen as "the threat that an action or event will adversely affect an organization's ability to achieve its objectives and to successfully perform its strategies" [P. Griffiths, p 17].

Risk is "the uncertainty of an outcome taking the form of a positive probability or a threat, of certain actions and events and it should be managed in terms of a combination between the possibility of something happening and the impact that the materialization of this possibility would cause." [H. M. Treasury, p 9].

The Dictionary of Economics defines risk "as an uncertain and likely event or process which can cause a loss, a loss in an activity, operation or economic activity" [N. Dobrotă, p 36].

The definitions presented emphasize the fact that risk is perceived as a threat, which generates a negative impact on the entity. Therefore, on the one hand the entity must identify the threats that jeopardize the orderly functioning and the presentation of a true and fair view, and on the other hand to implement a series of measures to limit them.

The specific operations within the financial and accounting department of an entity generate a number of risks.

The main financial risks that should be considered include:

a) risks arising from the usage of the basic financial instruments:

- losses incurred by the shareholder, under lower price stock market trading;
- lack of profitability expected by the issuer;
- material liability to the amounts invested;
- the interest rate risk;
- the credit risk;
- the risk of inflation.

b) risks arising from the usage of the derivative financial instruments:

- the risk that the losses suffered by the holders of these instruments may exceed the existing amount in the margin account;
- the risk of position, generated by the market developments in another direction than expected by the investor.

c) risks associated with the investment decisions:

- the risk of bankruptcy arising from the expenses incurred in making investments that may affect the solvency of the entity;
- the operational risk associated with uncertainty arising from investment activities and results;

d) risks arising from the financing activities:

- the risk of foreign currency arising from the exchange rate fluctuations;
- the risk of interest rate;

– the risk of non-payment arising from the entity's inability to honor its obligations to creditors.

With regard to the accounting risks, their analysis must be based on objective financial statements related to present a true and fair view of the entity.

The challenge of true image can be overshadowed by various risks arising from:

a) the misapplication of the accounting principles:

- the risk of presenting a misleading image of the financial position and financial performance which can influence the economic decision of the users of financial statements;
- the risk of false recognition of the balance sheet items and the risk of assessing and

presenting the entity's results may not reflect a real image;

- the risk of assessment;
- the risk of presenting the annual financial statements of a higher or lower performance in accordance with registering in accounting or not their income and expenses;
- the risk of generating unnecessary expenses that affect the entity's financial performance.

b) the erroneous classification of assets, liabilities and equity:

- the risk of erroneous estimation of the degree of certainty of the future economic benefits flows existing in records;

- the risk of erroneous classification of the elements of the balance sheet structures;

- the risk of non-recognition;
- the risk of wrong assessment.

c) Incorrect performance of the different activities specific to the financial and accounting department:

- the incorrect organization of the accounting records;
- poor management of the accounting department;
- poor management of the financial activity;
- wrong elaboration of the balance sheet;
- incorrect elaboration of the account of budget execution;
- the improper organization of the financial and accounting data reporting system to the internal and the external users;
- poor operating system;
- incorrect filing of financial and accounting documents.

3. Tools used to manage financial and accounting risks

The main components of the risk management process are:

- identification;
- evaluation;
- control;
- monitoring of risks.

The range of risk management tools will thus be differentiated according to the stage where they are used. On the other hand, a classification of these management tools can be based on the management style that can be pro-active, which will involve the predominant use of active risk management tools, or reactive, and then the major share will be owned by the tools of passive risk management.

In the risk identification stage, the main instrument used is to self-evaluate risks, to which they add the constitution of working groups or using experts.

Using the self-evaluation made with the help of the staff directly involved in the financial and accounting activities presents the advantage of a detailed analysis of the risk sources incurred by those responsible for managing risk activities, allowing their accountability both to risk sources and obtain a detailed list of risks.

Although the self-assessment activity requires a high degree of subjectivity, or offers irrelevant risks, these disadvantages can be minimized by directly involving the manager who can analyze the lists obtained.

The constitution of a working group (internal or external) may be another way, less subjective, to identify risks and can provide more detailed information about the interdependencies between various factors risk. On the other hand, using a work group may disadvantage of non-identifying some specific risks, known by the operational staff. Therefore, an optimal strategy in risk identification stage is the usage of both methods.

The stage of risk evaluation requires the use of qualitative or quantitative mathematical tools with the help of which it aims to determine the probability of risks and the size of their consequences in correlation with the objectives of the organization or of the department, and the evaluation of risk exposure which is the size that quantifies the two previous sizes. If the evaluation of the probability can be achieved using the methods derived from the classical theory of probability, with the help of the risk matrix or with the help of the method of circumstances analysis (similar causes determine similar effects), evaluation of the impact or of the consequences of risk can be a difficult task, which requires impact studies. The evaluation of the consequences of risks can be done both quantitatively and qualitatively, depending on the specific of the risk. A modality to evaluate the size of the impact is due to a specific risk is the impact

decomposition in the components that define it, and can be defined by quality, budget, time or effort.

The next stage of risk management is the one of risk control, which like the risk management tools have active control (risk avoidance, risk mitigation or risk diversification) and passive control tools (risk prevention or transfer).

To determine the most effective tools of management control exercised within risk management, it is necessary to determine risk tolerance, depending on which one can divide risks into: partially controllable risks and uncontrollable risks. Risk tolerance is a quantity that quantifies the amount of risk that can be accepted by the entity or the entity may be exposed. Evaluation of risk tolerance varies according to how risk is perceived either as an opportunity or as a threat. Also, according to the size of risk tolerance one can evaluate the exposure to risk, which is not relevant in absolute size but as a deviation from risk tolerance. Such control measures are required only if the risk exposure value is superior to the size of risk tolerance, the opposite situation regarding the acceptance of risks.

Determining a threshold of risk tolerance is not an easy task due to the need to quantify the costs of control activities and those arising from the exposure to risk. One of the tools used for this approach is cost-benefit analysis and the determination of the qualitative scale for the size of risk tolerance.

Knowing the size of risk tolerance and the amount of risk exposure, control measures can be established and their intensity will be determined by the exposure deviation compared to the accepted tolerance.

The main strategies of risk control are those related to acceptance, permanent monitoring, avoidance, transfer or mitigation.

The last step in the process of risk management, monitoring involves both tracking the way in which risk management takes place and monitoring the way in which the risk profile undergoes various changes due to exercising control actions. At this stage, one can use self-evaluation as a self-specific tool, but also different types of reports or records (risk register) determined according to the specific activity. Another specific tool is internal audit independently evaluating the entity's activity providing reasonable insurance of risk management.

4. Conclusions

Providing a clear, objective image of the entity requires the observation of the processes performed and their correct reflection in accounting. The assessment of the economic-financial records helps identify the risks generated by conducting operations specific to the financial-accounting department. The identification of the threat reduction methods represents the fair practice in order to achieve the goal of a loyal image. The management of accounting-financial risks refers to all the processes defined and implemented by an entity within the financial-accounting department, whose main purpose is to reduce the existing or potential risks. These processes aim to: identify, assess, control and monitor the threats, in the first phase, and then to suggesting some strategies to contribute to their reduction.

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