



**ACCOUNTANCY
EUROPE.**

SME RISK MANAGEMENT

How can your accountant help?

Briefing paper

VIEWS.

**SMES
FEBRUARY 2020**

HIGHLIGHTS

SMEs (small and medium size enterprises) play a crucial role in people's daily lives and the economy. Managing the risks they face is essential for the EU's economic resilience. As SMEs' closest business advisors, accountants are well-placed to help SME owners with their business risks.

This paper launches our SME risk management publication series that explores the accountancy profession's role in developing a robust risk management culture among their SME clients. It makes the case for SMEs to start discussing risks to be able to tackle these in practice.

For further information, contact [Paul Gisby](#) or [Johan Barros](#).

INTRODUCTION

SMEs are crucial for the EU economy and citizens, not only in terms of pure job creation and innovation but also to reinforce the economy's resilience.

However, not only are SME owners struggling with day-to-day challenges in running their business (i.e. financing, managing cashflows, complying with legislation, ensuring business transition from one generation to another) but they are also facing new challenges arising from global megatrends. This makes managing risks increasingly difficult; but ever more important.

SME accountants – whose practices are often small businesses themselves – are among SMEs' closest business advisors¹. Most small businesses in Europe rely on services provided by a professional accountant and meet with their accountant regularly. The accountancy profession is thus well-placed to inform SME owners about new emerging risks as well as long-standing challenges.

Accountancy Europe is launching this new project, consisting of a series of publications, to explore some of those risks and the accountancy profession's potential for managing them.

LAUNCHING A PUBLICATION SERIES

This set of publications will look into different areas of risks that SMEs are facing or may increasingly face in the near-future, with particular focus on those risks that the accountancy profession is well-placed to address. Our project series aims to:

- raise awareness among Europe's SMEs on some of the main risks and challenges that their businesses may face, and on the potential of their accountants to help them
- stimulate a discussion within the accountancy profession on what further could accountants do to help SMEs thrive, and how the profession's services for SMEs could evolve towards tailored and proportionate risk management in a cooperative, multidisciplinary SME risk management ecosystem²
- promote cooperation between different relevant professions, experts and stakeholders

This project series will cover the following risk areas:

- cashflow and insolvency
- family business succession
- IP
- cyber
- fraud and corruption
- supply chain and sustainability
- tax

For each risk area, we will discuss the nature of the risks, what SME owner-managers should take into account and what role the professional accountant could play in mitigating the risks. Depending on the area of risk, the accountant can be involved in different ways. Probably the most important of these is to act as a sounding board or provide an early warning, making the SME owner aware of risks. Accountants may also assist with implementing or monitoring business controls. Additionally, accountants can put their clients in touch with other

¹ ACCA, (2019). *Scale-up: What do SMEs need to supercharge their growth?* [online] available at: <https://www.accaglobal.com/content/dam/ACCA/pi-scale-up-success-SMEs.pdf>

² A combination of SMEs and relevant professions (such as accountants, certified risk managers, IT professionals, lawyers and insurance brokers) who have a complimentary and mutually supportive roles in fostering SME risk management.

relevant and trusted experts such as an IT expert or a certified risk management professional³, or to choose another model to provide specialized services by cooperating with or hiring an expert in their own practice.

WHAT CHALLENGES ARE SMES FACING?

Many SMEs struggle with day-to-day survival. For example, fewer than half of SMEs created in 2011 were still 'alive' in 2016⁴. This trend is further reinforced by a constantly evolving economy with new emerging challenges, where it is increasingly difficult to be aware of all relevant and existential issues. New global megatrends such as climate change, digitalisation, and the resulting societal and regulatory expectations for businesses inevitably impact SMEs – often in a disproportionate manner.

Being aware of the challenges and threats facing one's business is essential. With appropriate care and preparation, businesses can at least be more resilient and better plan for their future. Failing to recognise and address possible challenges can lead to business failure. For example, according to the US National Cybersecurity Institute, 60% of SMEs that have been subject to a cyber-attack go out of business⁵.

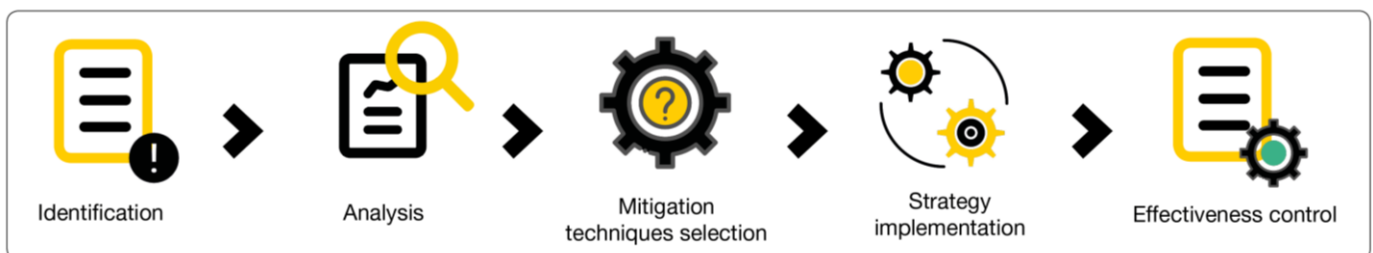
Effectively anticipating and building resilience against challenges requires effective risk management.

WHAT IS RISK MANAGEMENT?

The Federation of European Risk Management Associations (FERMA) defines risk management as “*managing the threats and opportunities to organisations within acceptable limits*”⁶.

According to Hollman and Mohammad-Zadeh (1984)⁷, risk management consists of five overarching steps: identifying risks, analysing risks, selecting techniques for risk mitigation, implementing the selected strategy and controlling its effectiveness regularly.

Figure 1: 5 steps of risk management



Risk management is not about avoiding all risks: it is about taking the appropriate risk for the appropriate return. To do this, all risks must be assessed and strategies put in place to manage them.

Traditionally, this has been the responsibility of the SME owner-managers themselves, sometimes with the help of a small management team. Successful entrepreneurs are by nature very good at managing risk for their areas of expertise. However, it is stressful for entrepreneurs to do this on their own and is not an efficient way of dealing with new emerging risks in an increasingly interconnected economy. One cannot manage what they do not know.

³ Risk Management is a recognised business discipline and profession based on a methodology (ERM), standards and norms (ISO 31000 and COSO) and a certification. It is performed by qualified professional risk practitioners, either within corporates or as external consultants or insurance brokers.

⁴ https://ec.europa.eu/eurostat/statistics-explained/index.php/Business_demography_statistics#Enterprise_survival_rate

⁵ Le Clair, J., speech before the US House of Representatives Committee on Small Business [as delivered], 22 April 2015, see <https://docs.house.gov/meetings/SM/SM00/20150422/103276/HHRG-114-SM00-20150422-SD003-U4.pdf>

⁶ <https://www.ferma.eu/about-ferma/>

⁷ Hollman, K. W. and Mohammad-Zadeh, S. (1984), *Risk Management in Small Business*, Journal of Small Business Management, Vol. 22 No. 1, pp. 7-55

WHY SMES SHOULD MANAGE THEIR RISKS?

Falkner and Hiebl (2015)⁸ argue that:

“misjudging or failing to recognize risks can – in the worst case – have disastrous consequences, ranging from customer loss to damaging liability, environmental damage and possibly even bankruptcy”⁹.

Risk management helps SMEs to identify in a timely manner such significant risks that could undermine the success or existence of their business.

Risk management is often thought to be solely for larger and more complex businesses. However, it is increasingly relevant for smaller companies too, because risk management can help to:

- **DEAL WITH NEW EMERGING RISKS**

As the global economy becomes more inter-linked and interdependent, SMEs are more exposed than ever to new forms of risks – on top of more ‘conventional’ risks that SME owner-managers already need to keep in mind. Risk management can help SMEs to have a more comprehensive picture of the risks and challenges that they are facing – including, crucially, the unknown-unknowns¹⁰. This will enable even better business planning and future-proof, long-term resilience.

- **FOSTER SUCCESS**

Based on a survey of 311 Austrian SMEs, Brustbauer (2014)¹¹ argues that risk management can help mitigate SME owners’ aversion to growth risks. The survey shows that SMEs that have *“a proactive (rather than passive) approach to risk management show higher propensity to expand to new markets and invest in new production and process technologies.”*¹²

- **DEAL WITH SUPPLY CHAIN REQUIREMENTS**

In the near future, SME risk management might not be a question of choice. SMEs that are part of larger supply chains will inevitably be affected by the adoption of risk management practices by the larger companies in the chain. The leading entities of supply chains would then require their smaller suppliers to conduct additional analysis, checks, risk mitigation measures and reporting in order to protect the supply chain as a whole.

- **IMPROVE ACCESS TO INSURANCE**

We are seeing developments in insurance products where new risks, such as cyber risks, are being ‘unbundled’ from general business risk insurance products, to only be available as standalone products. To obtain insurance for such risks, it is increasingly likely that the business will have to demonstrate that it has taken steps to minimise the risk in the first place.

⁸ Falkner, M.F., and Hiebl, M. R.W., (2015) *Risk management in SMEs: a systematic review of available evidence*[online] available at: https://www.researchgate.net/publication/271444609_Risk_management_in_SMEs_a_systematic_review_of_available_evidence

⁹ Ibid.

¹⁰ ‘Unknown unknowns’ commonly refers to unexpected or unforeseeable conditions, which may give rise to risks.

¹¹ Brustbauer, J., (2014) *Enterprise risk management in SMEs: Towards a structural model* [online] available at <https://journals.sagepub.com/doi/abs/10.1177/0266242614542853?journalCode=isbb>

¹² Ibid.

WHAT DOES RISK MANAGEMENT CONSIST OF?

IDENTIFY, ANALYSE, PLAN

Identifying and reporting risks cannot be done by the owner-managers alone. It requires the input from all staff in key positions to discuss where risks could arise, both within each business function and from externalities. This process is the first step to risk transparency and then risk management.

The identified potential risks must then be analysed in terms of potential consequences (both positive and negative, their importance to the business, the time scale of the risks and what can be done to manage those risks). Many SMEs lack the resources to put risk management procedures in place for all risks so what they need is a simplified and layered approach – working down from the most critical risks.

Each risk must then be looked at to determine what tailored actions can be taken.

EXAMPLES

Taking on a new client could be very lucrative but will divert resources from long-standing clients. Should the new client prove problematic or fail, the business faces the risk of financial loss through non-payment of debt and lose income from existing clients. This risk could be managed, for example, by researching the financials of the new client, investigating their treatment of existing suppliers and taking insurance to cover non-payment of debt. It may also be decided that the risk of taking such a dominant new client is not worth the potential return.

In other cases, we could be looking at loss management – i.e. the management of events that cause a fall in the value of the business' assets, revenues and services. Loss management will often involve a mix of internal procedures to identify and prevent loss, combined with risk transfer – i.e. external insurance.

FIND THE RIGHT EXPERTS

Solid risk management requires a broad range of skills and expertise. Different skills will also be needed to implement the appropriate preventive and mitigating measures, such as internal controls and effective procedures that do not hinder the day-do-day business.

So what can SMEs do to acquire the required risk management expertise? Hiring the right skills in-house is costly and difficult¹³. Using external experts could be a cost-effective solution, but only if the right experts are employed for the correct purposes.

In a comprehensive 'risk management ecosystem' for SMEs, different professions (such as accountants, certified risk managers, IT professionals, lawyers and insurance brokers) have a complimentary and mutually supportive roles.

Accountants have a particular role to play as a facilitator to encourage SMEs to start considering their risk environment. This is because they are often the first point of contact for business advice for many SMEs. Business advice should always include an assessment of the current and future risks that the SME faces. Consequently, accountants have an important role in assisting the SME in identifying and assessing its key risks. Depending on the specific risk area and its complexity, SME accountants can also help introduce certain 'first-line of defence' measures - such as advising and training on internal controls and emphasising the need for insurance.

In businesses facing more complex or very specific challenges, comprehensive risk management would require a qualified professional. In such situations, SME accountants can, if they have no sufficient experience in-house, at least develop relationships with their local risk managers as part of the risk management eco-system, to

¹³ European Committee of the Regions, (2019); *EU policy frameworks on SMEs: state of play and challenges* [online], available at: <https://publications.europa.eu/en/publication-detail/-/publication/2d8932f4-b273-11e9-9d01-01aa75ed71a1/language-en>

provide such services in cooperation with those experts or to help put their clients in touch with certified risk management experts.¹⁴

CREATE A ROBUST RISK MANAGEMENT CULTURE

Creating such a ‘risk hygiene’ culture within SMEs is pivotal because risk awareness should be one of the key considerations in business planning. It is also vital that all employees of an SME are onboard and aware of their role in the business’ risk management process.

This process may require dealing with staff that are protective of their particular area. It will also require dealing with the common bias that because something has never happened before it never will – or that because something has worked in the past it always will. Proper implementation, monitoring and refinement of the management process will not be effective without this culture shift.

ACCOUNTANTS CAN HELP SMES MANAGE RISKS

Accountants could play a greater role in building risk resilience in SMEs, and depending on local regulations and auditor independence rules where appropriate, because:

- most SMEs in Europe rely on the services of a professional accountant by default, meet with their accountants regularly and the accountants challenge and test the assumptions of the owner-managers
- accountants’ range of services for SMEs (financial and cashflow management, business planning, tax and other compliance risk management, bookkeeping, financial advice, etc.) already entail a risk management dimension

Through their work with their SME clients, accountants get an understanding of the fundamentals of the businesses they serve. They could thus provide tailored, business-specific risk assessment and management services at least in four broad areas:

- use their understanding of the underlying business to identify, assess and warn the owner-manager about these risks
- use their insight in legal compliance and internal control procedures to propose certain cost-effective and tailored basic measures to help mitigate the risks
- if the accountant’s core skills and knowledge do not enable them to directly address a business’ particular risk, they can still flag the threat and connect the SME owner-manager to other relevant expertise within the wider risk management ecosystem – for example, a certified risk manager, an IT expert or an insurance specialist
- act as a liaison between the SME and the authorities, or between the SME and other businesses in a supply chain.

Ultimately, SME owner-managers are the first and most important risk managers and SME accountants can support them in creating a strong risk management culture within their businesses

Some SME owners may feel that talking about their business risks is an admission of failure. However, discussing risks is not a failure or a mistake. The only mistake is the failure to deal with the risks. Hearing these facts from a third party – such as a trusted accountant – does make a difference.

*“ Discussing risks is not a failure or a mistake.
The only mistake is the failure to deal with the risks.*

For further information on this publication, contact [Paul Gisby](#) or [Johan Barros](#).

¹⁴ Should an SME, or their accountant, wish to provide more comprehensive and systematic risk management services on their own, they should consider acquiring this knowledge by for example getting the Rimap European risk management certification or embed a professional Risk Management support in their service. See more at: <https://www.ferma-forum.eu/on-the-programme/rimap-exam/>



Avenue d'Auderghem 22-28, 1040 Brussels



+32(0)2 893 33 60



www.accountancyeurope.eu



@AccountancyEU



Accountancy Europe

ABOUT ACCOUNTANCY EUROPE

Accountancy Europe unites 51 professional organisations from 35 countries that represent close to **1 million** professional accountants, auditors and advisors. They make numbers work for people. Accountancy Europe translates their daily experience to inform the public policy debate in Europe and beyond.

Accountancy Europe is in the EU Transparency Register (No 4713568401-18).