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IMPROVING RISK-BASED AUDITING IN COMMERCIAL BANKS

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A R T I C L E I N F O.

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Abstract

This in the article commerce in banks to risks based on advantages of the audit (Risk-Based Auditing - RBA). and development prospects analysis will be done. To risks based on audit of banks main risks identify them manage through financial stability to provide directed. The RBA method in the article traditional to the audit relatively efficiency, commerce banks for importance and his bank in the activity risks in minimization place will be lit. That's it additional, international experience based on the RBA 's main directions and his modern technologies using development prospects discussion will be done. From this except, in the article this audit method local in banks efficient app reach for recommendations given, including risks fast assessment, digital from platforms use and of the bank internal control system improvement like directions recommendation will be done. Article results commerce in banks to risks based on the audit in development scientific and practical manual being service to do can.

Introduction

face new tasks related to the management of financial and operational risks. One of the main tools that banks can use to reduce uncertainty and strengthen financial stability is risk-based auditing. Modern conditions require banks not only to respond to external changes, but also to anticipate possible risks, minimizing the negative impact on their business processes. A risk-based audit is different from traditional audits, which focus on retrospective review of processes It is aimed at planning and managing the most important risks, which makes it an indispensable tool in the internal control of banks.

Risk-based auditing has become an important part of internal control and management in commercial banks. Risk-based auditing helps identify and mitigate risks by minimizing potential losses and ensuring the sustainable development of financial institutions. Effective use of risk-based auditing requires a deep understanding of the risks faced by the bank and the implementation of advanced methods of their analysis. This thesis discusses modern trends and approaches to improving Risk-based auditing, and also offers directions for its optimization in the dynamic financial market.

In particular, at the same time as international standards are introduced in the field of reforms and risk management, risk-based audit is becoming more and more relevant for the banking sector of the Republic of Uzbekistan. This approach allows not only to increase the quality of internal control, but also contributes to the stable development of banks and the entire financial system of the country.

Literature review

Risk-based auditing (RBA) in commercial banks offers significant advantages and promising development prospects. This approach shifts the focus from traditional compliance-based audits to a more strategic evaluation of risks, thereby enhancing the effectiveness of risk management and compliance with regulations. RBA allows banks to identify high-risk areas and prioritize audits accordingly, which leads to improved operational efficiency and effectiveness. The development of RBA is supported by advances in technology and a growing emphasis on proactive risk management. Below are the key advantages and development prospects of RBA in commercial banks.

Advantages of Risk-Based Auditing

1. Operational Efficiency and Effectiveness: RBA focuses on high-risk areas, which helps banks allocate resources more efficiently and improve operational effectiveness. By concentrating on areas with the highest risk, banks can streamline their audit processes and reduce unnecessary interventions (Dharmawati et al., 2024) (Nakenov, 2010).
2. Proactive Risk Management: RBA enables banks to identify and manage risks proactively, thereby strengthening financial and operational stability. This approach allows banks to anticipate potential risks and implement mitigation strategies before issues arise (Dharmawati et al., 2024) (Mohammadi et al., 2014).
3. Regulatory Compliance: By ensuring that audits are aligned with regulatory requirements, RBA helps banks maintain compliance with industry standards, reducing the risk of sanctions and fines. This compliance is crucial in the context of evolving regulatory landscapes (Dharmawati et al., 2024) (Dănescu et al., 2010).
4. Enhanced Risk Management Culture: The implementation of RBA fosters a strong risk management culture within banks. It encourages the use of information technology to support risk management processes, which is essential for maintaining a competitive edge in the banking sector (Dharmawati et al., 2024) (Görener, 2017).
5. Improved Audit Planning: RBA allows for more effective audit planning by evaluating each area according to specified risk criteria. This ensures that resources are directed towards the most critical areas, allowing banks to respond quickly to changes in the internal and external environment (Dmyshko, 2024) (Hoque, 2005).

Development Prospects

- Integration with Technology: The development of big data and cloud computing technologies presents new opportunities for RBA. These technologies enable more comprehensive data analysis, allowing for more accurate risk assessments and audit planning (Yang, 2018).
- Adoption of Modern Tools: The use of advanced tools like the Azilon Risk Auditor system facilitates risk identification and prioritization, enhancing the overall audit process. Such tools help banks anticipate potential risks and allocate audit resources effectively (Nakenov, 2010).
- Global Adoption and Standardization: As banks worldwide recognize the benefits of RBA, there is a growing trend towards its adoption. This global shift is supported by international regulatory frameworks and corporate governance standards that emphasize risk management (Griffiths, 2005).
- Continuous Improvement and Adaptation: RBA is continuously evolving to address new challenges in the banking sector. This includes adapting to changes in market conditions, regulatory requirements, and technological advances, ensuring that banks remain resilient and competitive (Kurniawati, 2017).

While RBA offers numerous advantages, it is important to consider potential challenges and limitations. For instance, the successful implementation of RBA requires a significant investment in technology and training, which may be a barrier for some banks. Additionally, the dynamic nature of risks means that RBA processes must be continuously updated and refined to remain effective. Despite these challenges, the benefits of RBA in enhancing risk management and operational efficiency make it a valuable approach for commercial banks.

Analysis and results

Risk-based audit concept and features

Risk-based auditing is an evaluation and control system aimed at managing the main risks that may affect the financial position and reputation of a bank. This approach differs from a traditional audit because it is based on the analysis of risk probabilities and focuses on working with areas where they are most important.

risk-based audit, experts analyze the bank's internal and external environment, assess potential risks and propose measures to reduce them. This approach allows banks to allocate resources to examine the most vulnerable areas, thereby increasing the overall effectiveness of management.

Key aspects of risk-based auditing.

A risk-based audit focuses on areas of greatest risk. It is based on a comprehensive approach aimed at assessing the bank's activity and forecasting and minimizing possible threats. This approach includes the following main steps:

1. Identification of risks - identification of the main risks faced by the bank. At this stage, it is important to understand which processes and departments are most vulnerable and may suffer financial, operational or reputational losses.
2. Risk analysis and assessment - auditors assess the probability of occurrence of each risk and its possible consequences. Based on this analysis, measures are determined to reduce risks and integrate them into the general strategy of bank management.
3. Monitoring and control - Monitoring is an important element of the bank, which allows timely response to changes in the level of risk. Continuous monitoring ensures readiness to detect deviations from established standards and their prompt elimination.
4. Documentation and reporting – creating reports describing identified risks and proposed solutions. This enables bank management to make informed decisions on risk management.

3 main principles of risk-based auditing.

1. Risk assessment The basis of a risk-based audit is a comprehensive risk assessment. It involves identifying, analyzing and evaluating risks that may affect banks. Risks are categorized based on their likelihood and potential impact, allowing auditors to focus on areas of higher risk.
2. The extent and possible impact of materiality risks on the overall operations is assessed by auditors. They can then decide how much testing is required and what level of assurance is reasonable.
3. Customization Unlike one-size-fits-all audit plans, risk-based auditing tailors its approach to each organization's unique risk profile. This alignment ensures that resources are allocated where they are most needed and optimizes the effectiveness of the audit function.

While the benefits of a risk-based audit are great, it's important to recognize and address the issues.

Objectives and objectives of risk-based audit

The main purpose of the risk-based audit is to minimize and control the risks that can significantly affect the financial stability and reputation of the bank. In contrast to the classical approach of an audit, a risk-based audit not only identifies deficiencies and errors in already completed operations, but also helps the bank to strategically manage its weakest areas.

1. Risk assessment and management

Risk-based auditing e ng aims to identify and manage risks of high importance. This allows the b iz to focus primarily on the operations and processes that need to be monitored and improved. In this way, banks can detect and prevent potential losses in advance.

2. Improving risk management processes

A risk-based audit contributes to the continuous improvement of internal processes and controls, including the development and updating of risk management policies, procedures and tools. This allows the bank to adapt to changing conditions and increases its ability to quickly respond to emerging threats.

3. Compliance with international standards and regulatory requirements

Risk-based auditing helps banks comply with the requirements of national regulators and international standards (such as Basel III standards). This contributes to the creation of a unified control system and ensures transparency of financial transactions, which in turn strengthens the trust of customers and partners.

Risk-based auditing The main types of risk in the activity are as follows:

- Credit risk: related to borrowers' solvency and the deterioration of the quality of the loan portfolio.
- Operational risk: Covers disruptions in internal processes, fraud, data loss and other factors affecting the stability of business processes.
- Market risk: includes changes in currency and stock markets that may negatively affect the bank's financial results.

Risk-based audit of bank operations is risky allows to identify aspects, which makes it a decisive tool for reducing potential losses and strengthening the bank's stability.

Risk-based audit tools and techniques

Modern risk-based audit tools include various methodologies and analytical solutions that help banks effectively manage risks and make quick decisions. Some of these methods include:

- Probability analysis.

Using statistical methods, banks can calculate the probability of occurrence of various risks and determine which of them requires more attention. This allows you to take into account possible financial losses in advance and minimize them.

- Organization of stress tests.

This method allows banks to simulate various scenarios (for example, economic crisis, sudden changes in exchange rates) and assess their impact on financial stability. Stress testing helps prepare for unexpected situations and develop risk mitigation measures.

- Use of artificial intelligence systems.

how to use this method and modern technologies, including big data analysis, allow banks to plan more accurately and identify potential risks better. The use of this system helps to automate the processes of risk management, increases the speed and accuracy of the analysis.

Development of criteria for assessing the importance of a risk factor.

After identifying a number of risk factors, a set of criteria is usually developed for determining the points and the need to audit each audit object in the scope of the audit. Developing criteria can be relatively simple or quite complex. But many factors require personal judgment, so it is easy to determine only the lowest and highest scores, leaving the rest to judgement. Table 1 provides potential criteria for four key risk factors, three of which require specific assessment considerations (general control/resilience policy, exposure, and issues of management concern).

To obtain a risk index, it is necessary to consider the need to add a coefficient measure to each risk factor.

Not all risk factors will be equally important. For this reason, many internal audit departments use the risk factor measurement process to assign higher scores to factors deemed most important (eg, materiality or matters of management concern). After adding weighting factors that may be developed in consultation with management, the risk factor scores and weighted scores should be multiplied to obtain the risk index number. The risk index is then used to identify the audit object with a very high, high, medium and low priority level. Table 2 shows how it is used for the risk factor.

Table 1 Determination of risk factor scores

Each risk factor is assigned a score from 1 to 5, corresponding to the comments below.		
Element	Description	Ball
A. Importance	The share of the system is less than 1% of the annual budget	0
	The share of the system corresponds to 5-10% of the annual budget	2
	The share of the system corresponds to 25-50% of the annual budget	3
	The share of the system is not less than 75% of the annual budget	5
B. General Control/Responsibility Policy	Well controlled system with low risk of fraud and error	0
	A much better controlled system with some risk of fraud and error	3
	Initially a system with weak controls and a high risk of fraud and error	5
C. Effectiveness	Minimum interest (interest) of the team in the system	0
	If the system is ineffective, the possibility of an unfavorable situation with the team	3
	If the system is ineffective, serious problems with the team or legal problems may arise or	5
D. Issues of management concern	A system that does not play a significant role in the bank and does not have a significant impact on the achievement of the bank's goals	0
	A system that plays a significant role in a bank's burnout past and attracts management's concern about recurring disruptions in banking	5

Source: Developed by the author based on the study of international experience

By definition, all risk assessment systems provide an exact number. This may introduce a false degree of precision into the evaluation process. It is important to recognize that many risk factors are determined using subjective assessments and are not based on absolute measurements. The main exception is the importance factor, which is usually given a large loading. (Note: There are several ways to determine materiality, but the simplest models use percentages from total revenue and expenses).

Make sure the risk index scores and priorities make sense. (a) theoretically aim for the maximum before prioritizing the indices (b) be prepared to change the prioritization of the index if the results are not realistic (eg if every auditor receives a high priority).

Table 2 An example for determining the severity of a risk factor

<table>
<tr><td colspan="3">Step 1. A certain weight (weight) is given to them based on the assessment of the importance of the risk factor.</td></tr>
<tr><td rowspan="5"></td><td>Element</td><td>Weight</td></tr>
<tr><td>A. Significance</td><td>3</td></tr>
<tr><td>B. General control policy/discipline</td><td>2</td></tr>
<tr><td>C. Responsiveness</td><td>2</td></tr>
<tr><td>D. Issues of management concern</td><td>4</td></tr>
<tr><td colspan="3">Step 2. The score and each factor weight are then entered into a formula to calculate the risk index.
Risk index = (A *3)+(B *2)+(C *2)+(D *4)</td></tr>
<tr><td colspan="3">Step 3. Then, based on the risk index score, each audit object is divided into "high", "medium" and "low" risk categories.</td></tr>
<tr><td rowspan="5"></td><td>Risk index score</td><td>Risk/priority</td></tr>
<tr><td>Above 45</td><td>Very high</td></tr>
<tr><td>40-45</td><td>High</td></tr>
<tr><td>30-40</td><td>Medium</td></tr>
<tr><td>Below 30</td><td>Low</td></tr>
<tr><td colspan="3">It is relatively easy to modify this system for a wider range of risk factors. To determine the risk index, a greater or lesser number of factors is needed for the types of high, medium and low risk levels.</td></tr>
</table>

Source: Developed by the author based on the study of international experience

Impact of Regulatory Requirements

Risk-based audit in commercial banks is developed mainly under the influence of regulatory requirements set by national authorities and international standards. In recent years, due to financial crises and increased transparency in the financial sector, risk management and internal control requirements have become particularly stringent.

The main regulatory standards affecting risk-based auditing are:

1. Basel III

The Basel Committee on Banking Supervision has developed standards that define the basic principles of risk management and require banks to maintain adequate levels of capital to cover potential losses. Basel III obliges banks to strictly monitor liquidity and credit risks, making risk-based auditing an integral part of internal procedures. These standards help improve risk management and reduce the likelihood of bank failure.

2. Requirements of the Central Bank of Uzbekistan

The central bank plays an important role in overseeing the activities of commercial banks by establishing rules governing risk management and internal control processes. For example, the regulator may require continuous reporting of key risks in order to rapidly monitor the financial stability of banks and take corrective action when necessary.

3. International standards on internal audit

In addition to risk management requirements, International Standards on Internal Auditing also define the main principles of Regional Auditing Standards. These standards help banks to introduce uniform approaches that take into account the specificity of financial risks in the audit process and increase the effectiveness of audit work.

Advantages of risk audit for commercial banks

introduction of risk-based auditing brings several important advantages to commercial banks. These include the ability to improve operational efficiency, optimize risk management and improve the quality of internal controls.

1. Increasing resistance to external changes

Risk-based auditing allows banks to quickly adapt to market changes such as economic crises, interest rate and exchange rate fluctuations. The ability to predict risks allows banks to create a sustainable strategy and protect their assets.

2. Improving the quality of the loan portfolio

B helps banks minimize credit risk by enabling detailed analysis of borrowers and loan portfolios. This improves asset quality and reduces the likelihood of non-performing loans.

3. Optimization of operational processes a risk-based audit, banks can identify weaknesses in their operational processes, such as gaps in data management or inefficiencies in individual departments. This allows to improve the participation of employees and improve the quality of services provided.

Problems in the implementation of risk-based auditing

Despite the great advantages, the introduction of risk-based auditing in state-owned banks faces a number of challenges. The transition to risk-based auditing requires significant efforts by management and internal control professionals. Social difficulties include:

1. Lack of qualified personnel.

A successful risk-based audit requires highly skilled professionals in risk analysis, auditing and management. However, the training of such specialists requires time and large financial resources, which makes it difficult to carry out a risk-based audit, especially in small banks.

2. High costs for the introduction of modern technologies

In order to effectively use risk-based audit, banks need modern information systems and analytical tools that automate the process of identifying and evaluating risks.

However, the introduction of such technologies requires large investments, and not all banks can cover such costs.

3. The need to constantly update auditing standards

The financial market is changing rapidly, and banks must constantly adapt their internal control methods and procedures to meet new challenges. This requires flexibility and a willingness to change, which is not always easy to implement in practice.

4. The complexity of integrating risk- based audit into existing processes

The transition to risk-based auditing involves changing the bank's internal structure and processes. This requires reorganizing the work of different departments, which can lead to employee resistance and increase the time spent on performing a risk-based audit.

Prospects for the development of risk-based audit in Uzbekistan

In the context of the active development of the financial sector and the integration of Uzbekistan into the world economy, the improvement of risk-based audit is becoming one of the priority tasks for the country's commercial banks. At the state level, measures are being taken to improve risk management standards and strengthen regulation in the banking sector, which opens up new perspectives for the development of risk-based auditing.

1. Digitization and use of advanced technologies

of risk-based audit is the introduction of modern technologies such as artificial intelligence, machine learning and big data. These tools enable banks to effectively manage risk by automating many processes and providing more accurate forecasts.

2. Growing requirements for risk management by regulators

The Central Bank of the Republic of Uzbekistan is actively working on improving the legal framework, which will create an additional incentive for conducting risk-based audits in commercial banks. Clarity of reporting and transparency requirements helps to develop more effective internal control processes and improve risk management.

3. Development of professional skills of specialists

Risk-based auditing cannot be done without qualified experts. Training and professional development programs are actively being developed in Uzbekistan, which helps to train personnel capable of effective risk-based auditing and implementation of best management practices.

4. Emphasis on preventive measures. Instead of identifying risks when they occur, the focus should be on anticipating and preventing potential risks.

Conclusion

Improving risk-based auditing in commercial banks requires a comprehensive approach and strategic planning. This approach helps banks to minimize risks, strengthen financial stability and increase the level of trust of customers and partners. In the conditions of the increasing integration of Uzbekistan into the world economy, the republican system is becoming a necessary element to ensure the stability of the banking sector and the financial system. Risk-based internal audit is expected to help manage ongoing risks in banks by providing necessary checks and balances in the system. However, since risk-based internal auditing is a relatively new approach for most banks, its implementation will require a step-by-step but effective approach. Improving risk-based auditing in commercial banks is a necessity in the context of increasing complexity of financial transactions and regulatory requirements. Introduction of new technologies, development of employees' competences will allow banks to manage risks more effectively, reduce operational costs and increase customer confidence. By focusing audits on high-risk areas, banks can allocate resources more efficiently. This reduces the waste of resources in less important areas and allows more to be done. Proactive risk identification and mitigation in risk-based auditing helps banks proactively identify and manage risks. With comprehensive risk analysis techniques, banks can recognize potential risks in advance. This enables banks to implement timely mitigation measures, which in turn improves financial and operational stability. Risk-based audits ensure increased compliance with regulations and standards, and banks are more compliant with regulations and industry standards. Greater focus on high-level regulated areas will help banks comply with all legal requirements and avoid the risk of sanctions and fines. Building a strong risk management culture in performing a risk-based audit encourages and builds a strong risk management culture in the organization. The use of technology and data analytics in risk-based auditing promotes the use of information technology and supports the risk management process. In general, the Risk-Based Internal Audit System is important for banks in strengthening their management structures and improving their internal control systems.

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