



Economia Aziendale Online

Economia Aziendale Online

**Business and Management Sciences
International Quarterly Review**

**SPECIAL ISSUE
THE MULTIDIMENSIONAL CONTENT OF
ECONOMIA AZIENDALE**

**Exploring Theories and Applications
of Business Economics and Management
[1 of 3]**

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Pavia, Aprile 2019
Vol. 10 - N. 1/2019

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Poor Integration between Operational Risk Management activities and Internal Control System in the Municipalities: An analysis of the Italian legislative framework

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Cite as:

Riso V., Castellini M. (2019).
Poor Integration between
Operational Risk
Management activities and
Internal Control System in
the Municipalities: An
analysis of the Italian
legislative framework.
Economia Aziendale Online,
Special Issue, 10(1), 149-158.

Section: *Refereed*

Received: 19 November
2018

Published: 30 April 2019

ABSTRACT¹

Negli ultimi anni la Pubblica Amministrazione ha introdotto nelle proprie strategie logiche di Performance Management per accrescere i servizi offerti ai cittadini e la corretta gestione del Bene Pubblico. La salvaguardia del raggiungimento degli obiettivi prefissati passa dalle pratiche di gestione del rischio ed attraverso la capacità del singolo Comune di misurare i propri rischi. Questo lavoro ha lo scopo di offrire una visione d'insieme sulle pratiche di Risk Management, con particolare riguardo ai Rischi Operativi, previste dalle normative italiana nel sistema di controllo interno dei Comuni. Obiettivo del paper è sostenere il dibattito sull'introduzione delle logiche di gestione del rischio nel sistema di controllo interno pubblico al fine di assicurare il raggiungimento degli obiettivi prefissati ed il corretto utilizzo delle risorse pubbliche.

In the last years, the Public Administration introduced in its strategies logics of Performance Management to increase the services offered to the citizens and the correct treatment of the public goods. The safeguard of the objectives' achievement also passes for the risk management practices and through the ability of the Municipality to assess their risk and treat these in order to remove or reduce the impact of serious negative events (called also "operational risks"). This work aims to suggest an overall vision on the Risk Management practices, with particular regard of the Operational Risks, provided by the Internal Control System of the municipalities in the Italian legislative framework. The paper aims at sustaining the debate about the introduction of risk logics within the Public Internal Control System to ensure the goal's achievement and a correct used of the Public resources.

Keywords: Risk Management, Operational Risk, Public Administration, New Public Management, Control System

¹ Although the article is the result of the joint work of the authors, it is possible to attribute the paragraphs 1 and 2 to Monia Castellini and the paragraphs 3, 4 and 5 to Vincenzo Riso

1 – Introduction

In the last years the Public Administration, and more specifically, the Public Entities like municipalities, associations of these, provinces and regions evolved their organizations under different perspectives, focusing to produce services and good more useful for the citizens (Bracci et al, 2016).

A wide literature on the evolution Public Governance systems in which is stressed the passage from the “Old” Public Administration System to the “New” Public Management (Hood, 2000, Hood, 2005; Guthrie, 2005; Osborne et al, 2013; Robinson, 2015), the Performance Management and the creation of the Management Control Systems in the public organizations (Beni et al, 2002).

Through the New Public Management, in fact, were embedded, in the Public Administration the Control Systems instruments of management and control typically used in the economical private world.

However, Mussari (2001) explains how the use within the Public Administration of these management instruments do not implies to waive the public criteria of equal and sociality.

In this sense, though in managerial logics, the choices undertaken by the Public Administration aim to satisfy the Public good and every citizen in line with the resources available, like explained in the article 97 of the Italian Constitution.

According to this aim and to the achievement of the objectives in efficacy and efficient way provided in the Italian PA management control system, the Operational Risks Management practices represent a way to manage and prevent the achievement of these.

Indeed, Keban (2017) explains that the risk management represents a “vital instrument” in the Public Administration, discussing how it’s neglected.

More specifically, it is offered a wide definition of risk management activities where the awareness of risks has a strong role.

In according of this, Hatvanti explains: “*The entire risk management process is conditional to organisational goals being known, and the relevant risk being established with reference to those goals*” (Hatvanti, 2015).

To increase the awareness of these risks and to invite the Public Administration to put into practices the risk management provisions, the International Organisation of Supreme Audit Institutions (INTOSAI) provides guidelines to implement a recommended framework for applying the principles of entity risk management in the Public sector: for last, the INTOSAI GOV 9130.

There is a poor integration between the Operational Risk Management activities and Internal Control System in the Municipalities?

Analysing the Italian case is possible to observe that the legislative framework contemplates in abstract instruments to ensure the function of the Internal Control System but which does not appear informed to the risk logic (Peta, 2016, p.24).

Whereby, in the first paragraph is conducted a brief analysis on the evolution of the control systems in the Public Administration and, the second, how it would be desirable an integration between the internal control system and the risk management practices, with particular regard to the operational risks.

Finally, in the third paragraph, through a qualitative content analysis of the Italian legislative framework is shown how there is a poor integration between the Operational Risk Management activities and Internal Control System in the Municipalities.

In particular is conducted a manual content analysis with a translation of the INTOSAI GOV guidelines keywords to the Public sector in the principal laws provided and referred to the Italian Municipalities’.

This analysis contributes to sustain the debate about the introduction risk logics within the Public Internal Control System to ensure the goal’s achievement and a correct used of the Public resources.

2 - Internal Control System in the Public Administration

Words like the “management control” and the “performance management”, typically used in the economical private’s world, come ever more in the ordinary vocabulary of the Public Administration.

In the scientific literature, in fact, there are more studies in which are explained how the theories applied in the private sector are converted similarly in the public sector (Kickert, 2001).

In this sense, since 2000s in the Italian Public Administration were provided a series of reforms driven by the new public management aims with the scope to endow the public organisations of the management instruments and to give, through the management control, the instruments to achieve in planned manner the objectives programmed (Maran et al, 2018).

In the light of these observations, Ruffini (2010) offers a joint view about the control system provided in the Public Administration by the reforms processes in the “Matrix of the Public Controls” (Fig. 1) where the risk management perspective go cross in transversal way the control system, in the internal and external perspective (Chapman, 2001).

	Internal	External
	Control of accounting administrative regularity	Control of Court of Auditors
	Internal Audit Strategical Control Economical Management Control	External Revision and Audit Quality Assurance Certification

Figure 1 - The Matrix of the Public Control – Elaboration of Ruffini, R. (2010, p.13)

Indeed, as evidenced, in the Public Control System are present two principal approaches: the bureaucratic and the managerial.

These approaches, in fact, are the most widespread in the Italian’s public organizations culture and presented differences under different aspects, first the accounting methodologies (Iacovino et al, 2017).

Actually, the passage of bureaucratic approach to the managerial one doesn't happen in a net way but, probably in the Public Entities and specifically in the small and medium municipalities, this change of approach is still in progress (Mussari and Sorrentino, 2017).

The reasons of this phenomenon are various and of different nature but, as Hood (2000) explains in the New Public Management theme, "that one of its central themes is to stress the importance of public managers' discretionary space or freedom to manage".

The passage, in fact, consist to pass from a culture based on the respect of law as primary aim of the management to a culture where the legitimacy is one, but not the first, objective of the management.

In this sense, it is important understand how the Performance Management go within the organizations and how is important observe a multidimensional performance of the public organizations and not only the financial KPIs.

In according of this, Ricci and Civitillo (2018) explain that "financial performance should not be the ultimate objective of public management but instead an instrument to evaluate the financial comparability of various priorities to purse (public value, social, environmental, etc.)". Furthermore, to analyse the process of reforms since the 1990s is offered in Table 1 an excursus of the principal laws and provision the changes in the last years the Public Administration and, in particular, the municipalities.

Year	Provision	Principal Contents
1990	L. 142	Possibility to implement in the Public Administration the internal control system
1993	L.D. 29	Creation of the "evaluation core"
1995	L.D. 77	Implementation of the "executive management plan"
1997	L.D. 279	Introduction of the analytical accounting
1999	L.D. 286	Introduction of the "managerial logical" in the control system
2009	L.D. 150	General management of the performance
2012	L. 190	Prevention and repression of corruption risk
2013	L.D. 33	Obligations of public disclosure, transparency and divulgation of information
2015	L. 124	Reorganization of public administrations

Table 1 - Provisions evolution in the Public Administration – Our elaboration

The first observation is that in the last 10 years of the century (1990-2000) the legislative aims driven by the New Public Management influences are to introduce the managerial approach in the public organizations.

So, in the managerial approach the internal control system contemplates the presence in the public organizations of the internal auditors, of the management control system and the strategic control (Ruffini, 2010).

The management control system is the keystone where rests the risk management culture and where the controllers (or management in general) cross out the boundaries of the "typical" management control system reaching the way to assess and management the

organizations risks and to preserve the achievement of the organization's objectives (Kapuscinska and Matejun, p. 132).

Furthermore, in according to Aven and Vinnem (2000), this vision of the relationship between the management control system and the risk management practices express on one hand with the aim to counteract potential threats and, on the other hand, to avoid accidents, disaster and losses in general.

3 - Risk Management, Operational Risks and Internal Control System

Though the risk management practices, in particular management of the operational risks, are a vital instruments in the management control system in the Public Administration these are very neglected (Keban, 2017).

In the Italian Public Sector, specifically, there are not more scientific contributions that analyse and describe operational risk management practices: "Though Risk Management (RM) entered the public sector, the way RM is introduced within organizations is not empirically explored" Hinna et al (2018).

Hinna et al (2018) analyse the case study of the ISTAT and show how after the implementation of the risk management practices within the organization, now these are integrate in the activities, processes and in the culture and behaviour of the single components of the structure, confirming the opportunity to increase performance and learning.

Therefore, the INTOSAI put light on the necessity to create awareness of the organizations risk in the public sector.

In light of this, indeed, the implementation of the risk management practices in the wide management control system connotes the "maturity" of the management and control system of the public organization: "The entity risk management framework encompasses internal control, but in addition, forms a more robust conceptualisation of how an entity's business decisions should fall out of its core mission and associated objectives and provides a tool for management to help them to determine what the correct response to a particular event should be" (INTOSAI GOV 9130, p. 15).

Components of PIFC Model: Risk Management		Italian Regulation
Risk Assessment	Risk identification	No
	Risk evaluation	No
	Risk appetite assessment	No
	Responses to risks	No
Control activities	Authorization and approval procedures	Yes
	Reconciliations	Yes
	Reviews of operating performance	Yes
	Review of operations processes and activities	Yes
	Specific Information technology control activities	Yes

Table 2 - Extract of the Reginato et al. results', 2012, p. 395

In the Italian Public Administration and in the Municipalities there isn't integration between these two activities (Reginato et al, 2012).

In the Table 2 is reported a part of the results' Reginato et al. (2012) with a comparison between a Pif C//INTOSAI components of internal control in the public sector and Italian regulation.

As evidenced in Table 2, the Risk assessments (a component of the risk management process) aren't contemplate in the Italian legislation: there is an unsatisfactory level of permeation in the Italian Public organisation system due for the lack in the legislative framework and for the lack of faith by the policy makers on the utility and benefits related to an efficient control system (Peta, 2016).

On the lack on the risk management logics in the Public Administration, Peta affirms: "If on one hand, the Italian legislative framework contemplates in abstract formal instruments necessary to ensure the function of the internal control system (like the four types of control, the empowerment of the directors, supporting the management control with the analytical accounting), on the other, the action of this last don't appear informed to the risk logic" (Peta, 2016, p. 24).

4 - Methodology and results of observation

This work recurs to the qualitative Content Analysis (afterwards CA) to respond to the research question and to investigate if in the Italian legislative frameworks there is contents and provision about the operational risk management. Above all, the literature underlines the wide application of different methods of CA to analyse the text data in a flexible way (Cavanagh, 1997), choosing that in line with the theoretical interest of the research and the problem studied (Weber, 1990).

The analysis is carried out with two steps:

- the first to investigate the words present in the documents strictly;
- the second to analyse the sense of the key words through their meaning.

Starting from the INTOSAI GOV 9130 "Guidelines for Internal Control Standards for the Public Sector" are selected the keywords for the CA.

These are individuated in:

1. risk (rischio);
2. operational risk (rischio operativo);
3. management (gestione);
4. control (controllo).

In the Table 3 is reported the results of the CA (in the last column is evidenced the major disclosure of particular information).

To show a joint vision the result is reported in Figure 2 a sum of the frequency per word:

The word with most frequency is "control" with 283, follows "management" with 266 and, finally, "risk" with 16 and "operational risk" with 0.

Provision	Nouns researched	Frequency	Added Information
L. 142/1990	Risk [rischio]	1	Environmental risk
	Operational Risk [rischio operativo]	0	-
	Management [gestione]	24	-
	Control [controllo]	78	-
L.D. 29/1993	Risk [rischio]	0	-
	Operational Risk [rischio operativo]	0	-
	Management [gestione]	39	-
	Control [controllo]	24	-
Provision	Nouns researched	Frequency	Added Information
L.D. 77/1995	Risk [rischio]	0	-
	Operational Risk [rischio operativo]	0	-
	Management [gestione]	124	-
	Control [controllo]	74	-
L.D. 279/1997	Risk [rischio]	0	-
	Operational Risk [rischio operativo]	0	-
	Management [gestione]	22	-
	Control [controllo]	5	-
L.D. 286/1999	Risk [rischio]	1	Risk of serious negative result and evaluation process
	Operational Risk [rischio operativo]	0	-
	Management [gestione]	19	-
	Control [controllo]	44	-
L. 190/2012	Risk [rischio]	10	Corruption Risk
	Operational Risk [rischio operativo]	0	-
	Management [gestione]	6	-
	Control [controllo]	12	-
L.D. 33/2013	Risk [rischio]	2	Corruption Risk
	Operational Risk [rischio operativo]	0	-
	Management [gestione]	8	-
	Control [controllo]	17	-
L. 124/2015	Risk [rischio]	2	Risk and performance;
	Operational Risk [rischio operativo]	0	Corruption risk
	Management [gestione]	24	-
	Control [controllo]	29	-

Table 3 - Content Analysis of the legislative framework

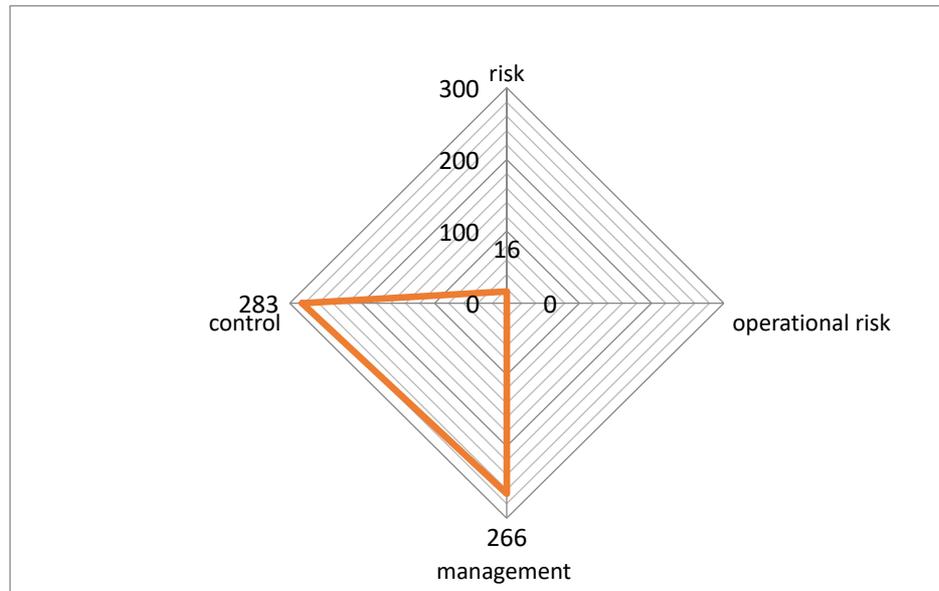


Figure 2 - Results of the content analysis on the Italian legislative framework – our elaboration

5 - Conclusions

The analysis conducted shows how in the Italian legislative framework there is poor integration among the operational risk management activities and the management control system and internal control.

Indeed, in accordance with Peta (2016), the laws and provisions in the last twenty years developed with the aim to introduce in the Public organizations logics not imprinted the “risk management”.

The results highlight how the “management” and “control”, in accordance with the post New Public Management, are the main issues treated in the legislative framework and how the policy makers are concentrated on it rather than also on risk management practices.

The reasons of this lack are probably various but not discussed in this work, remanding to the future research.

Observing the Content Analysis developed in Table 3 it is possible to observe that the word “risk” started to have a relevant frequency in the year 2012 when in Italy was introduced a systematic law on the corruption risk.

Therefore, this risk isn’t an operational risk in strict sense where the objectives to the Public Administration are “executing orderly, ethical, economical, efficient and effective operations; and safeguarding resources against loss, misuse and damage” (INTOSAI GOV 9130, 2007, p. 10).

The major limitation of this study is that there isn’t an empirical evidence about the poor integration between the operational risk management and management control system rather than a “conceptual” analysis conducted through a literature review in the field and the Content Analysis of the laws and norms that provide around the Public Administration and, in particular, the Municipalities.

Furthermore, art. 196 of the L.D. 267/2000 (Unique Text of the Public Local Entities) provides that every public local entity implement a management control system to ensure the:

- 1) achievement of the planned objectives;
- 2) economical management of the public resource;
- 3) good performance of the Public Administration.

The risks analysis and risk management operations are activities planned with the goal to assure an effective risk response and not compromise the achievement of its objectives.

In the future research would be desirable find empirical evidences of the assumption presented in this work.

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