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The prose of action: The micro dynamics of reporting on emerging risks in operational risk management

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Summary In this paper we study how risk management systems are applied to make organizational actors interested in responding to emerging risks. The empirical domain of the paper is the Defense Procurement Unit in a Scandinavian country. The paper is based on detailed data from monthly risk update meetings, interviews with both military and civilian managers, and 1 year's worth of monthly risk reports. Our study illustrates how Frontline Managers — to make General Management at the Procurement Unit interested in responding to emerging risks — use the content of the risk reports. The translation of emerging risks changes over time in response to a lack of action on reported risks. In these processes Frontline Managers take on new responsibilities to make General Managers take action on reported risk. The reporting practice changes from the mere identification of risk to risk assessment and, finally, to incorporating the possible response into the risk report. These findings add to extant literature by illustrating that actions do not automatically flow from the identification of risk. Rather, risk and action are dynamically interrelated in the sense that the prose in the risk report is a variable input to generate action and that a lack of action encourages managers to change their approach to reporting.

Introduction

Organizations face risks in multiple situations and from various domains (Andersen, 2010). Dealing with suppliers induces transaction risk (Dekker, Sakaguchi, & Kawai, 2013; Ding, Dekker, & Groot, 2013; Jordan, Jørgensen, & Mitterhofer, 2013), supplying credit generates risk (Arena, Arnaboldi, & Azzone, 2010), and innovation produces risk (Miller, Kurunmäki, & O'Leary, 2008). Risks are therefore dispersed in different parts of the organization and on different levels of the organizational hierarchy (Tekathen & Dechow, 2013).

Therefore, information about risk needs to be transferred between different levels and parts of the organization, if the

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organization is to make informed decisions about how to deal with emerging risk. This transfer of information is organized through processes where data from operations are reported to represent what risk there is (identification), what might happen (assessment), and what might be done about it (response) (COSO, 2004; Mikes, 2011, p. 243). The risk management system is the key vehicle for transferring information from the operational level to higher echelons by the use of various risk management templates (COSO, 2004; Drew & Kendrick, 2005).

The risk management process has been studied from functionalist, critical and institutional, and practice based perspectives. In the functionalist perspective, the key problem is to design the adequate risk management systems to control risks effectively (Kleffner, Lee, & McGannon, 2003; Manab, Kassim, & Hussin, 2010; Wu & Olson, 2009). The COSO framework constitutes a primary source of inspiration for such design efforts (COSO, 2004). In the COSO inspired ERM framework organizations should measure risk and relate it to organizational objectives (Ibid). The implementation of the framework is extensive and risk management has to be integrated with the mission, strategies, culture and operations in order to evaluate and coordinate the aggregated level of risk (COSO, 2004). Furthermore, it is assumed that organizational action linearly follows from the risk reporting system. With this approach risk management may be implemented in various organizational structures based on various contingencies (Woods, 2009), such as the level of integration (Miller & Waller, 2003; Young, 2011), and it should be implemented on a companywide level (Kleffner et al., 2003; Rao, 2009). However, this may "create inverse information hierarchies pushing complex, unresolved and abstract information to the top of the organization" (Tekathen & Dechow, 2013, p. 118).

Critical and institutional perspectives focus on companywide risk management issues (Arena et al., 2010; Noy & Ellis, 2003; Power, Schyett, Soin, & Sahlin, 2009; Rocher, 2011) or on the macro effects of risk management (Holzer & Millo, 2005; Rothstein, Huber, & Gaskell, 2006). Huber and Scheytt (2013) argue that risk management is a discursive resource that "reproduces larger societal values and determines organizational responses to the rise of risk management" and that "shapes organizational (im) balances of power" (Huber & Scheytt, 2013, p. 96). Maguire and Hardy (2013) argue that objects become risky by following certain organizing and discursive processes that either normalize the object or problematize the emerging risk. Power argues that quantitative ERM systems do not acknowledge inter-connectedness and therefore become "the costly risk management of nothing" (Power, 2009; 853). Arena et al. (2010) study how rationalities, technologies and experts evolve through circular interactions. These studies increase our understanding of the issues involved in designing ERM systems and the potential side effects of using ERM systems. Additionally these studies have informed us about the wider aspects of ERM systems, such as how risk management relates to macro institutions (Holzer & Millo, 2005) and discourses (Power et al., 2009). Yet little is known about the micro contexts within which managers make decisions about what to do about identified risk. An emerging line of inquiry within a practice-based perspective on risk management delves more into these micro aspects of risk management.

In the practice-based perspective, culture and managerial technologies are key concepts for understanding risk management processes (Boholm & Corvellec, 2012; Corvellec, 2009; Kaltoff, 2005; Mikes, 2009; Millo & McKenzie, 2009). Mikes (2009) focuses on the day-to-day practices of risk management and studies how a *calculative culture* affects the relevance of the risk reporting. Kaltoff (2005) analyzes how technologies intermediate risk-reporting processes and Millo and McKenzie (2009) argue that usefulness is potentially more important than accuracy in risk management processes.

The three perspectives point to different relevant aspects of risk management processes. Risk management systems should identify, assess and define responses to risk. This process is on a companywide level subject to discourses and relates to power and institutions. Finally, culture may affect reporting and the risk management system should strike a balance between usefulness and accuracy.

However there is a scarcity of practice-based papers looking into the micro dynamics of managing risk. For this reason, there have been several calls for research focusing on the organizational impact of risk management (Bhimani, 2009; Miller, 2009), the interrelation between risk, risk management and management accounting and control (Soin, 2013) and on first order risk categorization (Mikes, 2011). Extant literature does not make clear how action follows from reporting and albeit the practice-based approach points to usefulness and culture as important elements in making risk management relevant to organizational decision-making, it is not altogether clear how usefulness, culture and relevance are established in the risk-reporting process.

These deliberations motivate the paper and the choice to focus on first order risk categorization and on the relationship between acting and reporting using a practice-based approach. We have formulated the following research question: *When are risk reports able to attract managerial attention and generate action?* We are particularly interested in how different elements of the risk report, e.g. prose, is used to explain various risk categories and quantified risks are related to organizational action and how they dynamically interrelate on a day-to-day basis. We here define actions as the moment or the episode when managers actively do new things triggered by the risk report (e.g. agrees on additional funding, make a decision on an option or address issues with suppliers). Following Mikes (2009), we define prose as the non-quantified text sections of the risk reports that are used to explain identified risk, risk categorization and quantified risks.

The research question is analyzed by drawing on actor-network-theory (Callon, 1986) and following the Frontline Managers' reporting on risk in two embedded cases of investment within a Defense Procurement Unit. The Frontline Managers are managers at the very end of the "business line" working at the Defense Procurement Unit and reporting on risks to General Management of the Procurement Unit on a monthly basis. The "Mares case" follows the investment and procurement of several ships. The "Aeris case" follows the investment of a maintenance program for a series of airplanes. Each case is based on risk reports, interviews and observations from meetings where the risk reports were updated. All empirical material was collected in 2012.

Based on our empirical analysis we suggest that Frontline Mangers develop the contents of risk reports to interest