

Kateryna Yuriyivna SOKOLOVA

PhD Student,
Department of Tax and Customs,
National State Tax Service University of Ukraine
E-mail address: s_katya@ukr.net

THE MODEL OF THE INTEGRATED SYSTEM OF FINANCIAL MONITORING OF TAX RISKS IN THE SUPERVISORY AND REVIEW ACTIVITIES OF THE STATE FISCAL SERVICE BODIES OF UKRAINE

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Abstracts

Introduction. *The research considers the integrated system of financial monitoring of tax risks in the supervisory and reviews activities of the State Fiscal Service bodies of Ukraine.*

The purpose of the scientific research is to provide reasoning and the main focus areas for the integration of the system of financial monitoring of tax risks in the supervisory and review activities of the State Fiscal Service bodies of Ukraine. The main advantages of the integrated system of financial monitoring of tax risks are to be defined and their general description is to be compiled.

Methods (methodology). *The following general scientific and specific methods have been applied in the process of the scientific research: analysis and synthesis – to study the object and the subject of the research; generalization and scientific abstraction – to study the foundations of the work of the tax system, to establish the relationship and the subordination of the strategy, objectives and tactics of the fiscal services activities; systems analysis – to analyse the process of monitoring of tax risks and to determine the sequence of conducting the supervisory and review activities aimed at the taxpayers; a graphical method – to provide a visual demonstration of the studied phenomena and processes; economic and mathematical modelling – to develop the efficiency model of the integrated system of financial monitoring of tax risks in the supervisory and review activities of the State Fiscal Service bodies of Ukraine.*

Results. *The structure chart featuring the stages of the integrated system of financial monitoring of tax risks has been developed on the basis of these findings, their detailed description has been provided and the model of the integrated system of financial monitoring of tax risks in the supervisory and review activities of the State Fiscal Service bodies of Ukraine has been presented. The suggested model of the integrated system includes the analysis of the environment in which the financial monitoring of tax risks is carried out, the influence upon the taxpayers' behaviour, identification, risk analysis, assessment and taking a risk decision. The principles of developing the evaluation criteria for tax decision options with due regard for the risk have been established. The measures aimed at risk avoidance that can be implemented on the legislative and methodological levels have been indicated.*

Keywords: *tax risks; financial monitoring; risk identification; risk analysis; risk assessment; State Fiscal Service of Ukraine.*

МОДЕЛЬ ІНТЕГРОВАНОЇ СИСТЕМИ ФІНАНСОВОГО МОНІТОРИНГУ ПОДАТКОВИХ РИЗИКІВ У КОНТРОЛЬНО-ПЕРЕВІРОЧНІЙ РОБОТІ ОРГАНІВ ДФС УКРАЇНИ

Анотація

Вступ. Досліджується інтегрована система фінансового моніторингу податкових ризиків у контрольно-перевірочній роботі органів Державної фіскальної служби України.

Мета. Навести аргументи та основні напрямки інтеграції системи фінансового моніторингу податкових ризиків в контрольно-перевірочній роботі органів ДФС України. Визначити основні переваги саме інтегрованої системи фінансового моніторингу податкових ризиків та здійснити їх загальну характеристику.

Метод (методологія). У процесі наукового дослідження застосовувалися загальнонаукові та специфічні методи: аналізу і синтезу – для вивчення об'єкта та предмета дослідження; метод узагальнення і наукової абстракції – при вивченні основ функціонування податкової системи, встановленні взаємозв'язку і субординації стратегії, цілей і тактики діяльності фіскальної служби; системний аналіз – для аналізу процесу моніторингу податкових ризиків та визначення послідовності здійснення контрольно-перевірочних заходів платників податків; графічний – для наочного ілюстрування досліджуваних явищ і процесів; економіко-математичне моделювання – при розробленні моделі ефективності інтегрованої системи фінансового моніторингу податкових ризиків у контрольно-перевірочній роботі органів Державної фіскальної служби України.

Результати. На основі цього складена структурна схема етапів інтегрованої системи фінансового моніторингу податкових ризиків, наведена їх детальна характеристика та запропонована модель інтегрованої системи фінансового моніторингу податкових ризиків у контрольно-перевірочній роботі органів фіскальної служби України, що включає в себе аналіз середовища здійснення фінансового моніторингу податкових ризиків, впливу на поведінку платників податків, ідентифікацію, ризик-аналіз, оцінку та прийняття ризикового рішення. Сформовано принципи формування критерію оцінки варіантів податкових рішень з урахуванням ризику. Наведено заходи, спрямовані на уникнення ризику, які можуть бути впроваджені на законодавчому та методологічному рівнях.

Ключові слова: податкові ризики; фінансовий моніторинг; ідентифікація ризиків; ризик-аналіз; оцінка ризиків; Державна фіскальна служба України.

JEL classification: G28, G32, H30

Introduction

The fiscal area reflects complex economic relations which emerge in the course of monitoring the payments of taxes, fees and other mandatory payments and which, in the process of their redistribution, are followed by the ambiguity and risks, contradictions and conflicts as well as the multiplicity of objectives of certain business entities. The effective structure of the tax system of the country and managing its processes, and high-quality supervisory and review activities in particular, are to balance these interests in order to implement its purpose, aimed at resource mobilization and allocation in the country as well as promoting socio-economic development and improving the welfare of the society.

Nowadays finding the ways to increase the level of voluntary compliance has become a pressing issue. Tax revenues should be the main source of budget replenishment, and monitoring this process should be the main function of the fiscal service bodies.

Tax risks as a structural element of the tax policy and as an integral component of supervisory and review activities of the State Fiscal Service bodies of Ukraine attract more and more attention of both practitioners and academics. Ukrainian and foreign scientists have made a significant contribution into the knowledge of the risks by exploring the issue of risks, their intrinsic features and peculiarities. These issues are examined in the works by V. Andrushchenko, I. Balabanov, V. Vitlinskiy, N. Vnukova, N. Hnatyshyna, V. Hranaturov, O. Desiatniuk, M. Klapkiv, S. Nakonechnyi, S. Osadets, A. Skrypyuk, O. Tymchenko, D. Shtefanych, A. Yastremskyi and others.

Despite the significant achievements in this area, the issue of tax risks in terms of supervisory and review activities of the Fiscal Service bodies has not been studied well enough. First of all, this issue concerns the study of the peculiarities of their formation and their manifestations in the current environment, since the sources of

their origin and the factors that influence tax risks are constantly changing. Therefore, the outlined issues are relevant.

Tasks and objectives of article

The tension in the fiscal area largely determines the inefficiency of the tax policy of the country and simultaneously generates a “field” for risky activities performed by business entities. Therefore, studying tax risks in the context of uncertainty is of particular importance. The aim of the research is to develop methodological and theoretical-organizational foundations of the integrated system of financial monitoring of tax risks in the supervisory and review activities of the State Fiscal Service bodies of Ukraine.

The outline of the basic research data

The integrated system of financial monitoring of tax risks in the supervisory and review activities of the fiscal service bodies provides the establishment of necessary culture and the infrastructure of the state fiscal service bodies in order to:

- identify the causes and the main factors of risk emergence;
- identify, analyse and assess the risks;
- take decisions on the basis of the assessment that has been conducted;
- develop basic anti-crisis measures;
- reduce the risk for it to reach an admissible level;
- arrange the fulfilment of the planned program;
- control over the process of carrying out planned actions;
- analyse and evaluate the results of the risk decisions, etc.

Risk monitoring and risk management are connected with both negative and favourable outcomes. The essence of risk monitoring and risk management is to identify potential deviations from target results and manage these deviations in order to improve the prospects, reduce budget losses and improve the validity of decisions taken. To manage risks means to determine prospects and identify opportunities to improve the supervisory and review activities of state fiscal service bodies and to prevent or reduce the probability of the undesirable course of events.

Tax risks monitoring should be integrated into the daily routine of the fiscal service bodies (Chart 1).

Financial monitoring of tax risks requires thinking ahead. It is rather a process of determining what may happen and, at the same time, ensuring the state of preparedness for this through an integrated system and not through the “reaction” management of the activities of the state fiscal service bodies. In its turn, a formalized system of tax risk monitoring allows to create a system of managing the service that works to prevent possible problems. Based on the parallels drawn between tax risk monitoring and the process of risk management we can say that the process of risk management is one of the important components of a model of an integrated system of financial monitoring of tax risks in the supervisory and review activities of the state fiscal service bodies of Ukraine, as it is discussed further in the scientific research.

Monitoring of tax risks in the supervisory and review activities of the state fiscal service bodies and the risk management system require a distinct allocation of responsibility and authority which are necessary for managerial decision making. Senior management bears “general” responsibility for risk management within the organization, and the fiscal service in particular. The distribution of responsibility and authority among the corresponding employees is the exclusive prerogative of the senior management. Decisions which are taken in the process of monitoring and risk management should correspond to terms of the legal requirements and meet the objectives of tax and customs policy of the state. Thus, it is of vital importance to determine the optimal balance between the responsibility for the risk and the ability to manage this risk.

Here we present the main advantages of the integrated system of financial monitoring of tax risks (Table 1).

For the purposes of the integrated system of financial monitoring of tax risks, the latter act as a ratio between the probability of emergence of risky situations and their possible consequences. Risk occurrence results in the deviation of actual results of conducting supervisory and review activities from the planned ones.

The quantitative value of the risk level is often defined as a function of the indicators of the effects of the risky situation and the probability of its occurrence.

In addition, the process of implementing the integrated system of financial monitoring makes a considerable emphasis on implementing practical actions in risk management into the activities of the state fiscal service bodies as well as on the management of the potential benefits – additional tax revenues gained from conducting supervisory and review activities, and potential losses – probable budget loss acquired from identified and untreated risks of non-payment of taxes.

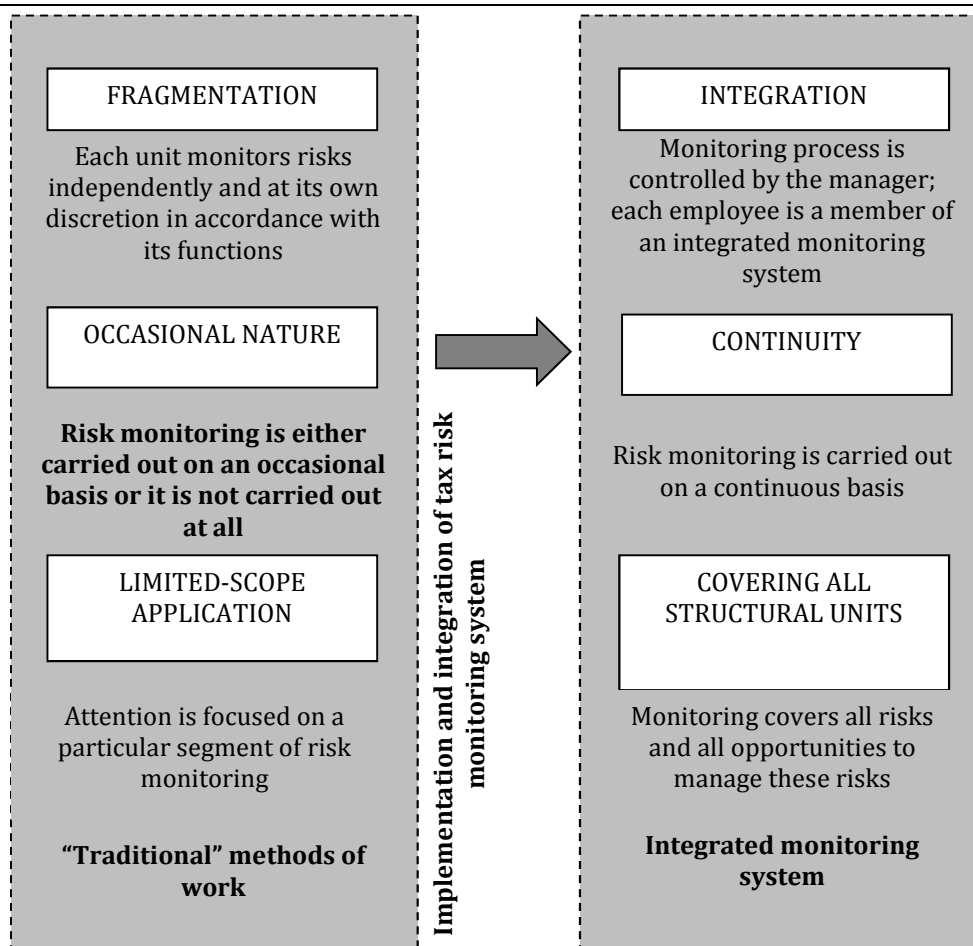


Chart 1. The main areas of integration of the tax risk monitoring system into the supervisory and review activities of the State Fiscal Service bodies of Ukraine

Implementing the integrated system of financial monitoring of tax risks in the supervisory and review activities of the State Fiscal Service bodies of Ukraine will provide the fiscal service bodies with guidance in:

- creating a solid foundation for taking risk decisions and planning;
- identifying prospects and hazards;
- benefiting from the uncertainty of the business environment;
- establishing a management system focused on preventing potential problems rather than rectifying consequences after their occurrence;
- efficient resource allocation and resource management;
- improving anti-crisis management and reducing losses and costs of risks;
- strengthening stakeholder confidence;
- compliance with the regulations of the existing legislation;
- improving management
- promoting the supervisory and review activities to a fundamentally higher level in accordance with the current requirements and world standards, etc.

Modelling the process of financial monitoring of tax risks in the supervisory and review activities of the State Fiscal Service bodies of Ukraine and the structure chart of the model are represented in Chart 2.

Table 1. The main advantages of the integrated system of financial monitoring

Advantages	Description
Reducing the uncertainty factor in the process of conducting the supervisory and review activities	The monitoring of adverse events is accompanied by particular actions aimed at reducing the probability of their occurrence and diminishing their influence. Even in case a compelling event occurs, the service can achieve the necessary degree of stability due to proper planning and preparedness.
The use of promising opportunities for improvement	The probability of a favourable outcome occurrence in a risky situation is estimated in the course of application of the integrated system of financial monitoring. Searching for the prospects becomes more effective if the staff is aware of the risks and has the skills necessary to manage them.
Improved planning and raising the performance efficiency	The availability of unbiased data concerning the business strategy of the service, its performance targets, operations and prospects allows to arrange a more deliberate and effective planning. This, in its turn, increases the organization's ability to use favourable prospects, reduce adverse effects and to achieve improvements in its activities.
Saving time resources in the course of conducting supervisory and review activities	Priority is given to treating the identified risks in the process of conducting the supervisory and review activities and additional charges of extra funds to the state budget of the country. The issue of economic feasibility of certain supervisory and review activities disappears per se. This approach allows us not only to avoid "expensive" errors and budget loss, but also to achieve higher level of voluntary compliance.
Improving the relationships with the stakeholders	The process of monitoring and risk management makes the employees of the state fiscal service bodies reveal their internal and external stakeholders and develop a bilateral dialogue between them and their managers. This communication channel provides the service with the information on how the stakeholders will respond to the changes in its activities.
Improving the quality of information for decision making	The process of applying the integrated system of financial monitoring of tax risks enhances the accuracy of the information and the analysis which are required for making strategic decisions at different levels of management in the course of conducting supervisory and review activities with taxpayers.
Promoting "good standing"	Setting up an open dialogue with the taxpayers concerning the payment of their tax liabilities and warning them against the use of tax avoidance schemes to minimize such liabilities by having a detailed database of potential risks and demonstrating the availability of controlled conditions under which the enterprises operate.

The integrated system model of financial monitoring of tax risks in the supervisory and review activities of the State Fiscal Service bodies of Ukraine includes the following units and structural elements:

A. The environment in which financial monitoring of tax risks and managing these risks are conducted:

1. 1. Context;
1. 2. Objectives;
1. 3. Strategy.

B. Influence upon the taxpayer behaviour:

2. 1. Tax behaviour as a general feature of a business entity.
2. 2. Cooperation and consulting.

C. Financial monitoring of tax risks:

3. 1. Risk identification;
3. 2. Risk analysis;
3. 3. Risk assessment;
3. 4. Taking and implementing a risk decision;
3. 5. Monitoring and control over the risk treatment.

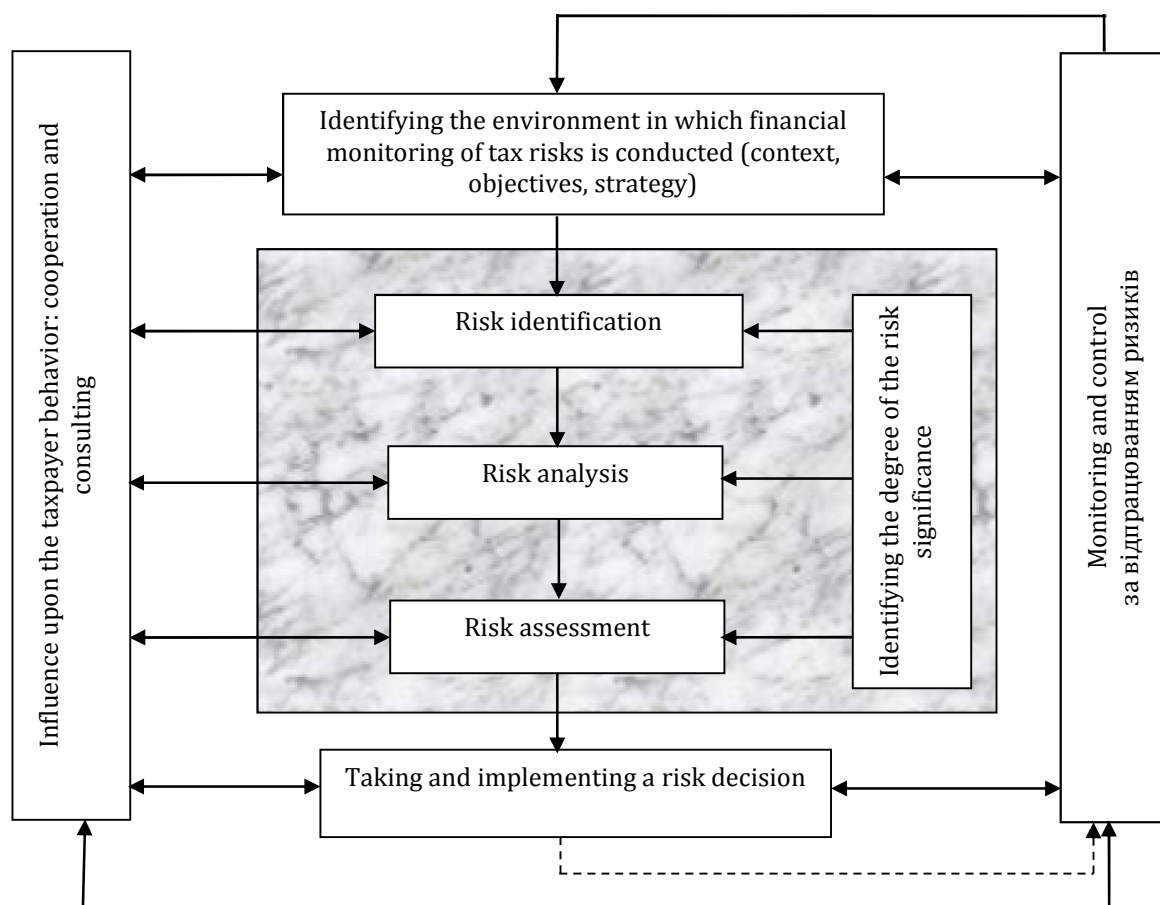


Chart 2. The structure chart of the integrated system of financial monitoring of tax risks

Hereafter we discuss the basic structural elements of the integrated system of financial monitoring of tax risks and provide their description.

1. *Identifying the environment in which financial monitoring of tax risks is conducted, its context, objectives, and strategy.* It is necessary to define the external features of the business environment, the internal parameters of the state fiscal service bodies as well as the parameters of financial monitoring and risk management, in which the process will be implemented. The context of financial monitoring of tax risks in the supervisory and review activities of the State Fiscal Service bodies of Ukraine is seen as a set of internal and external factors (conditions), in terms of which identification, analysis, assessment and risk management take place. Establishing the context of financial monitoring of tax risks in the supervisory and review activities of the State Fiscal Service bodies of Ukraine allows to set the basic parameters (boundaries), in terms of which the structural units of the fiscal service are to operate and risk management is to be conducted. The context also includes the internal and external environment of the organization and the objective of the model of financial monitoring of tax risks and risk management process in the supervisory and review activities of the State Fiscal Service bodies of Ukraine [1]. The main objective of this stage is conducting initial assessment of all risk factors that may affect the ability of the fiscal service bodies to achieve the target objectives. It is of particular importance for the process to have distinct boundaries (scope, objectives and tasks, input and output parameters, resources and managers), which will ensure that the model of financial monitoring of tax risks and risk management process function within managed conditions [1; 2].

Identifying the context can be divided into two basic stages.

The first stage in context identification is to identify objectives, tasks and internal parameters of supervisory and review activities, as well as external features of the business environment.

The second stage is to determine the scope of the process of financial monitoring of tax risks and risk management, key issues and challenges that the service is to face and the relationship between the strategy of the service and target effects that the supervisory and review measures are to have.

It should also be noted that financial monitoring process will not be comprehensive and complete, unless the key elements of supervisory and review measures are determined in the course of which risk management and

their strategy are conducted. The strategy is the approach used to achieve objectives. The objective describes what must be achieved and the strategy describes how it can be done. The strategy fills the gap between objectives and activities.

Financial monitoring of tax risks is a process that supports the establishment (development) and evaluation of strategies of supervisory and review activities, but it does not create a strategy itself. Supervisory and review activities should begin with the development of a strategy. A strategy can be a set of methods or principles describing how to act. However, the strategy also incorporates principles for ways of thinking. Also, it is important for strategies to be based on knowledge (information or data). Knowledge (information or data) is an absolutely necessary part of the process of financial monitoring of tax risks, regardless of the model, structure or definitions of risk.

2. *Cooperation and consulting, influence upon the taxpayer behaviour.* It is important to cooperate and hold consultations with both external and internal members of this process at each stage of an integrated system of financial monitoring of tax risks and risk management process. In addition, the tax behaviour is a general feature of business entities that is established on the basis of the facts discovered by revisions that state their degree of compliance with tax and currency legislation and the factors that indicate the presence of tax risks that need to be treated [3]. Financial monitoring of tax risks is not just a technical process consisting of operations conducted in accordance with formalized algorithms that allows taking an unambiguous and deterministic risky decision; it requires teamwork, which is carried out primarily in the communicative context. Cooperation and consulting between the participants of financial monitoring of tax risk is an inherent part of this process and should always be held in an open form.

The main objectives of cooperation and consulting in the implementation of the model of financial monitoring tax risk and risk management process are:

- understanding the causes and factors of risk;
- taking into consideration different points of view when taking risk decisions;
- involving employees of other structural units in the process of monitoring of tax risks;
- introducing the participants of the process to their functions, tasks and responsibilities, etc.

3. *Risk identification.* It is necessary to determine where, when, why and how risky situations may hinder, weaken, delay or contribute to achieving the target results (objectives) in the process of conducting supervisory and review activities by the State Fiscal Service bodies of Ukraine.

The purpose of risk identification is compiling a complete list of risks that may affect achieving the objectives of supervisory and review measures within the integrated system of financial monitoring of tax risks and their risk management. This list should be as an ultimate complete list since unidentified risks could constitute a significant danger for achieving the set objectives (additional tax charges) and result in losing promising opportunities (receiving additional tax revenues, reserves).

Cause and effect relationship between the basic components of risk identification is presented in chart 3.

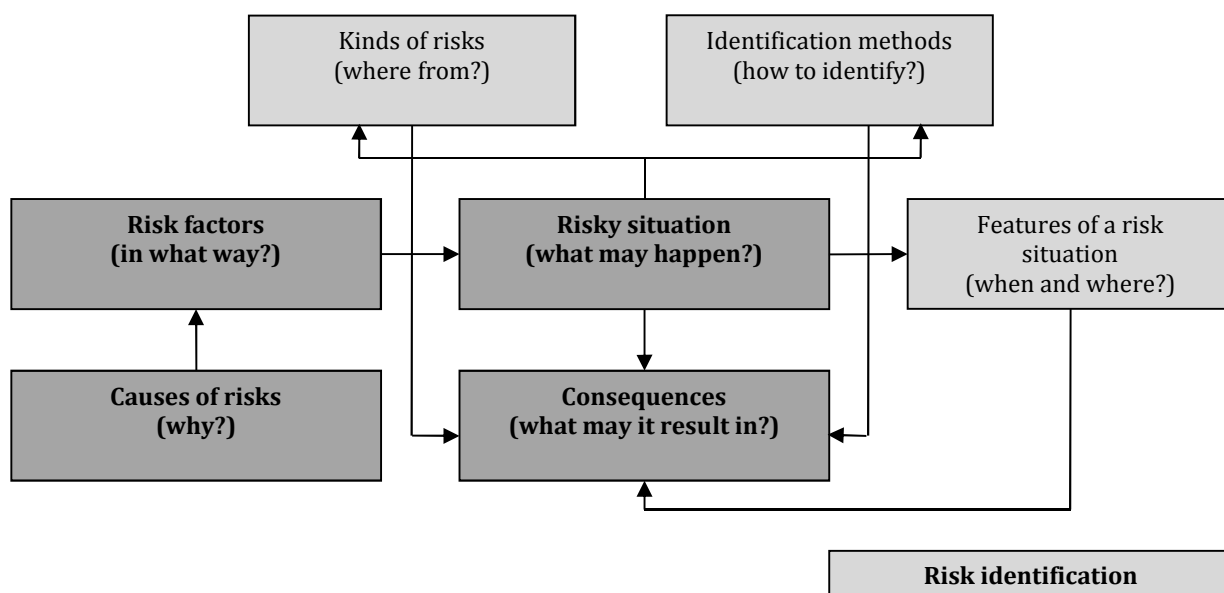


Chart. 3. Determining the relationship between the components of risk identification [4].

4. *Risk analysis.* Risk analysis is the methodology by which the uncertainty that is characteristic of economic indicators is analysed and considered in the context of future periods in order to evaluate the impact of risk on

the corresponding outcomes. [5].

Comprehensive risk analysis provides:

- qualitative risk analysis, that is detecting risk factors, risk areas, identification of all possible risks;
- establishing the system of quantitative indicators of a risk level;
- quantitative risk analysis, that is the numerical determination of the level of particular risks and the risk of budget loss in total;
- risk modelling and forecasting the risk;
- risk management aimed at reducing the influence of the risk.

Consequently, risk analysis provides a systematic approach that is based on the need to study all phenomena and processes in their interdependence, taking into consideration their influence upon each other and the feedback [5].

Such analysis should take into account the scope of potential impacts and possible origins of their occurrence. While conducting the process of risk analysis, it is also necessary to identify and evaluate available tools (models and methods) or risk management and their proper treatment in the course of supervisory and review activities of the State Fiscal Service bodies of Ukraine.

5. *Risk assessment.* The purpose of this stage is the establishment of quantitative risk indicators upon which the next stages of the process of risk analysis that refer to management decisions will be based. This is the very stage when the average quantitative measure of the risk is calculated applying the formula (1) [5].

$$R = \sum_{i=1}^n \sum_{j=1}^m g_{ij}(V) P_j P_i(j, z_j) X_i, \quad (1)$$

in which P_i – is the probability of acquiring the amount of loss due to the occurrence of i-type adverse event;

P_j – is the probability of the occurrence of a j-type adverse event;

X_i – is the amount of loss (usually stated in terms of costs);

R – is the quantitative measure of the risk (stated by applying the same indicators as of the loss);

n – is the number of possible variants of loss upon the occurrence of any adverse event (including the loss that equals zero);

$g_{ij}(V)$ – the probability of selecting a situation bearing the probability of the occurrence of adverse event as an object P_j and the law of loss distribution $P_i(j, z_j)$, that depend on the protective measures taken Z_i .

In practice, in order to conduct further necessary protective measures it is not the indicator of the amount of loss obtained in the process of calculation that is taken as a basis, but the ultimate admissible amount of loss and the ultimate admissible probability of its occurrence. Such an approach is justified in the process of arranging the supervisory and review activities in the fiscal service units since the forecasts concerning the deterioration of the economic environment and possible further loss are of indicative nature, and often the cost of measures taken to reduce such risks or budget losses are much higher than the anticipated probable loss. The balance between the potential benefits and negative consequences is determined. This allows to decide on the scope and the nature of a risk decision that manages the risk as well as to set the priority areas for activities connected with risk management.

6. *Taking and implementing a risk decision.* We can define three basic ways of taking a risk decision that can be applied and several options within these forms of the decision:

1. Risk transfer – passing the risk to other parties;
2. Risk reduction – using methods to minimise the frequency and/or the extent of the risk in a coming period;
3. Risk covering – carrying out activities to neutralise the impact of an occurred risk.

The most effective way, that is risk transfer, can be applied only in certain specific areas. Therefore, risk reduction and risk covering remain to be the most important strategies for taking a risk decision concerning the identified risks. Again, context, strategy and objectives will play their role in this. The enforcement of the law must meet all the requirements of equity but, for reasons of effective and efficient performance of their responsibilities, the fiscal service must make choices with respect to the degree of examination (conducting supervisory and review activities) of risks. The aim of this stage is to increase the potential benefits and reduce the potential loss that arise as the effects of risk situations.

In order to evaluate the options of tax decisions according to their risk component, in terms of methodology the analytical work should be arranged in the form of the following stages:

Stage 1 – defining the conditions of comparison: purposes of tax decision and the objectives that its evaluation is to complete; the temporary interval (point) of evaluation; requirements for tax and non-tax information applied and the possibility of meeting these requirements;

Stage 2 – establishing the indicator – the comparison should be performed by following certain principles, in

order to implement each of the latter it is necessary to give a distinct answer to the questions indicated in Table 2.

Table 2. The principles of establishing the evaluation criterion for tax decision options taken with regard to the risk

The principles of establishing the criterion	Questions that require a distinct answer in establishing the evaluation criterion
The compliance of the economic matter of the indicator with the evaluation objectives	The content and the place of the criterion within the system of the indicators of the financial analysis
The compliance of the initial information with the requirements	The determining factors and the analytic expression of the indicator
The accuracy of establishing the indicator and the suggested values	The possibility to calculate the criterion in terms of the comparable options

Stage 3 – calculating the value of the criterion in terms of all comparable options, their evaluation and their analytical interpretation in order to take the most reasonable decision.

The selection of one of the criteria mentioned above (*probability indicators of the change of taxation parameters*) or their combination depends on the selected strategy for tax risk management, the same is applied to defining their optimal value.

7. Monitoring and control. Having defined the appropriate contexts and having performed the necessary analysis and risk assessment, the next and final stage in modelling the process of financial monitoring of tax risks, in terms legal compliance, is monitoring and control over the risk treatment, by means of applying the proper risk decision, at the proper time and in a proper way. In order to evaluate the effectiveness of monitoring and control over risk treatment, the quality and efficiency of such treatment, here we suggest a system of analytical indicators of tax risk treatment:

- The degree of risk treatment – this indicator is the ratio of expressing the additional tax charges based on the results of the supervisory and review activity to the extent of the declared (identified and detected) tax risks and it is calculated in the following way:

The degree of risk treatment = the amount of additional assented tax liabilities / the amount of risks based on which the given business entities were included into the schedule of desk audits (estimated budget losses for risks) * 100;

- The degree of levy of additional tax charges – this indicator is the ratio of expressing the payment of additional tax charges based on the results of the supervisory and review activity to the general extent of additional assented tax liabilities and it is calculated in the following way:

The degree of levy of additional tax charges = the amount of revenues that were submitted according to the formal notes of desk audits / The amount of additional assented tax liabilities *100;

This indicator is used nowadays by the State Fiscal Service bodies in their statements to present the quality of supervisory and review activities. However, in our view, it needs adjustment and it will be more accurate once it incorporates the additional revenues gained from the identified tax risks, including:

- *The degree of levy of additional tax charges taking into account the additional revenues gained from the treated risks* = (the amount of revenues that were submitted according to the formal notes of desk audits + the amount of the additional revenues gained from the treated risks) / the amount of additional assented tax liabilities *100;

Thus, an important step of the stage of monitoring and control over the risk treatment is reducing the risk level – which is the reduction of the probability and the extent of loss.

Conclusions and recommendations for further research

The results and the efficiency of financial monitoring of tax risks. The implementation of the integrated system of financial monitoring of tax risks in the supervisory and review activities of the State Fiscal Service bodies of Ukraine and the systematization of working on the tax risks provides the opportunity to plan the supervisory and review activities as follows:

- to categorize the taxpayers in accordance with their fiscal significance and to categorize the tax risks in accordance with their importance;
- to carry out a proficient selection of taxpayers for conducting audits;
- to determine the most highly effective kind of tax audit;
- to minimize the number of inefficient audits;
- reduce the amount of work time spent on conducting tax audit, to make the forecast for budget loss;
- to prevent the emergence of various tax evasion schemes.

Therefore, the information on monitoring of tax risks allows to conduct a detailed analysis of tax violations, to

systematize them, to focus the efforts of the fiscal service on the priority issues and violations of tax legislation that cause significant budget loss.

The model of the integrated system of financial monitoring of tax risks and risk management can be applied at various levels of the organization: strategic, tactical (middle-level management) and operational. It can be used in certain projects, in finding the necessary solutions and in managing particular areas of risk. In our case it is the supervisory and review activities of the State Fiscal Service bodies of Ukraine.

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