The A, B, C's of Risk Management

Title Page

Risk management is a fundamental purpose of government. Among a local government's core obligations are health and safety, public welfare and security, emergency response, and the safeguarding of public assets—all of which can be classified as risk management responsibilities. In that sense, all local governments practise risk management whether or not they are aware of it.

More formally, risk management is defined as the process by which a local government assesses and addresses its risks. Historically, the role of risk management has been associated with insurance-buying, occupational safety and health, and legal liability management. In recent years governmental managers have begun to recognise that organisational risks are pervasive, that these risks are extraordinarily diverse and complex, and that these risks are not just confined to 'insurable' or accident-related situations. They may include risks arising from actions of the national or EU legislature, investment management practices, climatological phenomena, and even changing voter preferences.

This report describes the formal risk management process, but in doing so will suggest ways in which traditional risk management is being applied to new areas of local government risk. In developing this description readers will learn about the overall goals and objectives of risk management, the challenge of identifying and analysing risks, the tools and treatment options available, and the means by which risk management efforts are effectively implemented.

The A, B, C's of Risk Management

The Goals and Purposes of Risk Management

Risk management is the formal process by which an organisation establishes its risk management goals and objectives, identifies and analyses its risks, and selects and implements measures to address its risks in an organised and co-ordinated fashion.

Risk imposes two types of costs on local governments; the <u>cost of losses</u> that occur (fires, vehicular accidents, worker injuries), and the <u>cost of uncertainty</u>. Uncertainty affects a local government in numerous ways. It not only leads to fear and worry among employees and citizens, but it also leads to misallocations of limited resources. Both costs of risk impact negatively on budgets. Therefore, a primary goal of risk management is the maintenance of budget stability through control of the costs of risk.

Recently risk managers have begun to look at risks where 'up-side' potential exists; financial investment practices, training and development of employees, management of intergovernmental

relations. In each of these instances, and in many others, risk managers have discovered that they can make a positive contribution to local government 'risk-taking' decisions; a realisation that has contributed to a dramatic expansion in the scope of risk management. In such contexts the goal of 'budget stability' does not seem to relate adequately to the challenge of risk-taking decisions. Consequently, while a core objective of risk management is to minimise the negative impact of risk on budgets and on the human psyche, it also seeks to support sound analysis of risk-taking opportunities—opportunities that can enhance the capabilities of the local government.

Risk Identification and Analysis

The objective of risk assessment (that is, risk identification and analysis) is the development of a comprehensive understanding of local government risks. Effective risk assessment involves a systematic and ongoing process for identifying and examining risks—and, of course, deciding which risks are important.

In assessing risks three questions need to be addressed: 1) from where do risks arise? 2) what is a local government's exposure to risk?, and 3) how do local governments systematically gather information about risks?

From where do risks arise? Local governments are subject to risks arising from seven environmental sources of risk:

1. the physical environment (snow and ice, earthquakes)

2. the economic environment (monetary policy, state of the economy)

3. the political environment (legislative activity, pending elections)

4. the social environment (social attitudes and preferences)

5. the legal environment (court decisions, administrative/regulatory rules)

6. the operational environment (the day to day activities and actions within the local government)

7.   the cognitive environment (absence of information, the influence of attitudes toward risk on decision making)

These environments contain <u>hazards</u>, which are characterised as features within an environment that elevate the probability of loss or its potential severity. An example of a hazard would be a winter storm arising from the physical environment. Hazards, in and of themselves, do not produce losses. It is the <u>perils</u> (a 'peril' is a cause of loss) created by the hazardous conditions that lead to loss. For example, a winter storm may generate poor visibility and icy roadways, and these perils can cause accidents.

The same basic approach can be applied to 'up-side' risks. The economic environment produces <u>risk factors</u> (rather than hazards) that can create <u>opportunities</u> (rather than perils). A city treasurer may perceive the booming stock market as a risk factor that produces investment opportunities that can favorably impact the city's ability to finance major projects.

What is a local government's exposure to risk? Risk only matters in the assessment process where a local government has exposures. Broadly speaking, there are two types of exposure – asset and liability – of which asset exposures have three categories and liability exposures have two.

<u>Asset Exposures</u> The three general assets that local governments control are 1) physical assets, 2) financial assets, and 3) human assets.

Physical assets are vehicles, school buildings, computers, roads, waste treatment facilities and other tangible assets. It should be noted that the impact of a physical asset loss is not just that it must be replaced but that its loss of use for some period of time may amplify the economic impact of its loss.

Financial assets include stocks, bonds, derivatives, letters of credit, government paper, and other such instruments. Local governments have two primary bases of exposure; holding financial assets (say, investing in stocks), and issuing financial assets (a bond issuance). Each instance creates an exposure to financial risks (interest rate, price, currency exchange, default risk, among others).

Human assets are the managers, employees, elected members, and other relevant stakeholders in a local government. They are subject to physical and economic harm in numerous ways; premature death, injury, unemployment, and old age for example.

While a primary risk management concern will be safeguarding assets from harm, risk management decisions may also affect directly the 'productivity' of those assets. So, for instance, training employees to lift heavy items properly reduces the likelihood of injury, but may also directly contribute to enhanced worker productivity. Likewise, a sound diversification investment strategy can minimise downside risk while directly supporting the attainment of positive investment objectives.

<u>Liability Exposures</u> The two liability exposure areas are 1) legal liability, and 2) moral responsibility.

As a general proposition, a typical local government's exposure to legal liability will tend to sort into the following categories; 1) premises liability (slips and falls), 2) contractor liability (private or nonprofit contractors performing services for the government), 3) product or service liability, 4) environmental impairment liability, 5) employment liability, 6) workers' compensation, 7) motor vehicle liability, 8) professional liability, 9) errors and omissions (public officials liability), 10) police liability. Many other exposure areas may be relevant in specific types of local governments.

Moral responsibility may seem to be a risk management matter of peripheral concern, but this is not the case. Local government officials and managers are entrusted to manage the entity in the best interest of its citizens, and this obligation is—basically—a moral one. Public sector managers have a general responsibility to citizens that is not defined only by the law. Risk management also is concerned with the impact of risk on moral choices.

How do local governments systematically gather information about their risks? Local governments should develop a formal process whereby risks are systematically identified, analysed and measured. Numerous sources of information are available to assist in the assessment process. They include:

- **Checklists**, which help keep track of a local government's properties, services and exposures to risk. Checklists are available from risk management experts, insurance companies and brokers, and professional associations. Although most standardised checklists are limited to insurable risks, they do serve as a sound starting point for organising a more expansive search for organisational risks. Over time, a local government can customise such a list to meet its ongoing needs.

- **Interviews** with supervisors, managers, employees, outside professionals and other stakeholders are an essential source of information. No one has as sound an appreciation of risks as those who face those risks every day. Additionally, asking employees for their input provides for a level of involvement that can enhance support when risk management programmes are implemented.

- **Onsite inspections** often uncover risks not found through any other method. Improper maintenance practices, wear and tear, and deterioration-based risks are illustrative of risks that are detected only through personal observation.

- **Incident records and reports**, where available, can provide an important insight into 'hot' exposure areas (for example, locations where criminal activity is high, or stairwells that frequently produce slip and fall accidents). **Complaint forms** sometimes can serve a similar information gathering purpose.

- **Budget documents and other financial reports** listing programmes, services, financial values, and capital plans are excellent sources of information for identifying existing and new risks.

- **Council and committee minutes** can help managers anticipate new risks or impending risk management issues. Of course, council/committee actions in and of themselves may be a source of risk (for example, the council may have improperly rendered a zoning decision that could lead to a liability suit).

- **Real estate records** owned or used by the government often reveal loss exposures that may be overlooked—leases and easements being obvious illustrations of such exposures.

- **Permits** should be evaluated as they can sometimes create liability problems. For example, a restaurant may pass a health inspection, which means that a customer suffering food poisoning may have a basis to sue the authority for negligence.

- **Contracts** such as construction and purchase agreements outline the liabilities of each party. Some contracts allow external risks to 'pass through' the contract to the local government. For example, engaging professional engineers under contract, may expose the local government to professional liability matters that otherwise would not be a concern.

- **Public Fora** where citizens voice their opinions, desires and concerns to local officials. Risks of various types (and, certainly, attitudes toward risks) are often identified through this method.

Once an organisation has developed something of a comprehensive listing of risks at least two other assessment tasks must occur. First, the risks should be sorted, ranked, or otherwise separated to reflect the level of seriousness they represent. For example, risks could be sorted into four categories:

- **Category One** would contain risks that are 'low frequency/low severity' risks. These are risks that produce losses only rarely and when they do occur, they are of minor importance.

- **Category Two** risks would be characterised as 'low frequency/high severity,' meaning they rarely produce losses, but when losses do occur they are significant. Category Two risks tend to be classified as 'catastrophic risks,' though the definition of catastrophe is relative and may have quite different meanings from organisation to organisation.

- **Category Three** risks would be characterised as 'high frequency/low severity', meaning they frequently produce losses, but each loss tends to be relatively modest. Category Three risks sometimes are referred to as 'operational risks' reflecting the fact that they tend to be known, and in some instances can be anticipated.

- **Category Four** risks would be those rare risks that are 'high frequency/high severity,' meaning that losses occur frequently and they all are serious. Risk assessments rarely turn up such risks as their properties would have made them known long before the assessment was undertaken. However, assessments of new ventures or possible acquisitions sometimes yield evidence of such risks.

As a general proposition, a local government will focus most of its attention on Category Two and Three risks. Risk managers broadly seek to control (that is, prevent, reduce, avoid, or otherwise manage) Category Three risks, while Category Two risks would be candidates for

transferring (through insurance) or distributing (through a pool, for instance) to another party or parties.

The second, and remaining, assessment task is to analyse the risks in an effort to understand how risky conditions produce losses. For example, workplace accidents might be studied to better understand exactly what actions or circumstances lead to back injuries. Presumably, the results of such an analysis might also suggest possible remedies.

From a risk management perspective, exposures to risk have two bases of valuation. First, assets might be valued based upon the cost to replace those assets - indeed, insurance contracts base their claims payments on variations of this idea. 'Replacement cost' insurance provides policy proceeds based upon the cost of replacing an asset with a new and similar asset. 'Actual Cash Value' insurance bases payment on replacement cost less some recognition of the physical depreciation and obsolescence of the replaced asset. Even liability exposures can be valued based upon the replacement cost notion—that is, the liable party is replacing the loss of another. However, a second valuation consideration looms behind the replacement cost notion—the 'contributory' value of an asset. Contributory value reflects an asset's value to the local government as a whole. There may be assets that have some replacement value (old computers stored in astoreroom), but which are not contributing anything of value to the local government. Conversely, there may be assets with a very low replacement value that contribute significantly to local government's productivity. A municipality may own storage facilities that generate significant rental income for the city, but which have very little value in a replacement context.

While the cost of replacing an asset is a common risk measurement device; it can sometimes be a misleading way of thinking how an asset relates to a local government's other assets and its overall productivity.

Risk Management Tools and Treatment Options

Local governments have two broad categories of risk treatment methods at their disposal: <u>risk control</u> tools and techniques and <u>risk financing</u> measures. Risk control includes efforts to avoid, prevent, reduce, or otherwise manage risk and its impact on an organisation. Risk financing involves measures taken to anticipate and pay for losses that could occur.

Although risk control and financing are two discrete categories of action, it is worth noting that they are also highly interrelated. If measures are not taken to manage and control risks, they are more likely to produce losses—which then must be financed.   Thus, in a general sense local governments face a central dilemma; 'do we spend our money preventing losses, or risk spending considerably more of our money paying for losses?' If the return-on-expenditure for each choice was found to be identical, a manager might be wholly indifferent to the process of risk management. Research and practice, however, have shown that prevention tends to be vastly less expensive than does financing losses.

Risk Control

There are five basic techniques involved in controlling loss exposures: risk avoidance, loss prevention, loss reduction, uncertainty reduction, and risk transfer.

<u>Risk Avoidance</u> Some activities and services carry risks so great that the best way to handle them is to avoid the activity altogether. In the strictest sense, risk avoidance is an 'airtight' solution as it eliminates the chance of loss.

Risk avoidance can be achieved by deciding not to undertake an activity that creates a new risk or by discontinuing an existing activity. For example, a town may decide not to build a skateboard park because it prefers to avoid the liability exposures and safety risks involved.

Often, however, avoiding one risk creates others—or transfers the risk to another context. If the aforementioned town does not build the skateboard park, children may ride their skateboards on public streets, endangering themselves and others.

Risk avoidance may be the most complete technique to manage certain risks but it is not always feasible for public agencies since the provision of certain services is a statutory requirement, regardless of the risks. The inability to avoid many key risks most distinguishes public sector risk management from its private sector counterpart.

Risk avoidance may be determined by considering whether the benefits of the activity outweigh the cost, not only financially but also in social value. The skateboard facility provides social benefits by giving children a safe place to ride and by keeping them off the streets. Sometimes a subjective decision must be made, but in other cases weighing the tangible costs and benefits will indicate whether avoidance is the best route.

Loss prevention Loss prevention measures seek to prevent, or at least reduce the likelihood of, losses. Certain natural phenomena like earthquakes, hurricanes, and winter storms are not preventable, but most risks encountered by local governments do present opportunities for intervention. Proper training of public works employees can reduce the chance of injury; rigorous maintenance schedules can keep police patrol cars in a condition that reduces the likelihood of accidents; proper supervisory procedures can minimize the likelihood of management errors.

A decision to undertake a loss prevention measure should be based upon some type of cost-benefit consideration. It is easy to say that a local government should 'spare no expense' in introducing safety measures, but the fact is that governments have limited resources. Therefore, while a local government may hope to manage its risks in such a way that losses never occur, most managers find that the cost of preventing one additional loss ultimately climbs to a point where it is neither economically nor politically feasible to justify the expense. Having said that, for a broad band of local government risks, the cost of preventing losses is justifiable economically when compared with the probable costs of loss.

Loss reduction Loss reduction methods do not prevent losses from occurring, but rather minimise the impact of losses that do occur. Smoke detectors, hard hats, firewalls, and emergency response procedures will not prevent losses from occurring, but they can directly influence the severity of a loss and limit potential liability.

<u>Uncertainty reduction</u> 'Uncertainty' is the doubt we have about our ability to know what is going to happen. Often, an organisation cannot measurably control a risk but can improve its ability to function by better understanding the risk. Information management is a primary tool here as a better understanding of a given situation will—at least—allow managers and officials to make decisions that align with overall organizational objectives.

Focus on uncertainty reduction has led to an interest in matters related to human attitudes toward risk—what is called the psychology of risk. Uncertainty may be due to a lack of information, but people's attitudes toward risk are governed by many things; upbringing, cultural values, economic considerations, and even genetic influences. Since democratic institutions require consensus in decision making, the challenge of helping managers and officials clarify attitudes toward risk and reach consensus on how risks should be treated is an assignment that increasingly is falling into the hands of risk managers.

<u>Risk transfer</u> A local government can transfer some risks to private or nonprofit organisations by contracting for services and products, thus making the other parties responsible for the risks. Contractual risk transfer often is confused with risk avoidance, which totally eliminates the risk. Using the skateboard park example, if a town decides not to build the facility, it eliminates all associated risks. If the town contracts with a private company to build and maintain the park, liability risks exist, but they are assumed by the company and not the town.

Contractual risk transfer is often a useful option for many governments. Most services and activities carry loss exposures that put the government at great risk, yet the services must be

provided. Transferring the risk ensures that services will be provided while protecting the jurisdiction.

Since contracts are essential in transferring risks, standard procedures for preparing, reviewing, and filing all contracts should be established. No contract should be finalised without a risk review by the government's legal advisers and by someone with risk management responsibilities. Part of the review should include an examination of regulations regarding contracts.

Also, while a contractual transfer of risk may be appropriate - the counterparty to a contract may prove to be incapable of bearing the transferred risk or whilst the local government may transfer the <u>functional delivery</u> of certain services (food service at a county hospital, refuse collection in a town), <u>responsibility</u> for the provision of the service ultimately resides with the local government.

Risk Financing

Losses will inevitably occur which need to be paid for. All risk financing techniques are either <u>risk retention</u>, in which a jurisdiction assumes all or part of a loss, or <u>risk transfer</u>, in which one organisation agrees to pay for the losses of another organisation in exchange for a premium. Many municipalities often use a combination of financing alternatives. The most common risk financing mechanisms:

Insurance The local government pays premiums, and—should a loss arise—the insurance company adjusts the claim, and provides other services such as legal defence. Additionally, the insurer may provide some risk management services on an ongoing basis. At the end of the policy period, usually a year, coverage is updated and a new premium is calculated. Usually, the cost to the local government is the premium and a deductible (if one is present and a loss occurs).

Risk retention There are two forms of retention; passive or unplanned retention, and planned retention—which is referred to as 'self-insurance.' All organisations do some form of passive retention inasmuch as the risk assessment process may fail to identify a risk that later produces a loss.

Some governments self-insure by choice because they would rather pay for their losses than pay premiums to an insurance company. However, some local governments self-insure because they cannot find commercial insurance due to commercial insurance market conditions or other economic factors.

Very few local governments, except those with large budgets, can self-insure all their exposures, but most can find benefits in retaining some risks. The use of deductibles is a form of self-insurance, and to the extent that a local government can internally manage and finance small-to-moderate losses, it probably is in its best interest to do so.

In recent years, insurance companies—and, increasingly, reinsurance companies—have begun offering excess loss and catastrophe-level insurance coverages, which allow large local

governments to retain a much greater level of risk than traditional deductibles would permit, but which protect the entity from the risk of abnormally large losses. The amount that a government chooses to retain in such an arrangement is known as that government's self-insured retention (SIR).

Intergovernmental pools Some local governments pool their resources with other local governments to fund a portion of their losses. The primary purpose of pools is not to lower costs (although pool contributions may be lower than commercial insurance premiums) but to provide consistent coverage.

Pools come in various forms. Risk transfer pools are much like insurance companies; an indemnity agreement transfers the risk from the member entity to the pool. Although such pools require that premiums (or 'contributions') be paid, most also possess the ability to assess members additional amounts if the pool's losses far exceed expectations. The bases for determining each member's premium differ across pools. Some pools charge a flat rate, while others develop rates that are based specifically on a member's own past loss experience.

Alternatively, pools may be group insurance buying arrangements. That is, they are not risk bearing operations per se, but rather pool the purchasing power of members to buy commercial insurance. Interestingly, many pools are risk transfer pools at certain levels of loss exposure but then purchase excess loss/catastrophe level coverage to protect the pool from very large losses.

Other types of pools exist. A banking pool is one in which each member contributes to the pool to pay administrative expenses and to establish reserve funds for extraordinary losses. But, otherwise, each member has a separate account out of which its losses are paid. A risk management pool is one in which the pool serves as the risk manager for its entities. Interestingly, most successful pools (that began as risk financing pools) are evolving into a version of the risk management pool.

Other risk financing tools There are numerous other options that may be employed. They include such things as risk retention groups (private sector analogues to pools), captive insurance companies (an insurance company that insure only one client—its parent organisation), banking arrangements (such as lines and letters of credit, and other lending programmes), and occasionally, other public agencies. In regard to this last example, some local or regional authorities occasionally will extend their risk management and financing services to other entities within their region of service. This could be a significant trend over the next several decades.

Risk Management Programme Implementation

How do risk managers implement successfully a risk management programme?

1) Deciding What To Do

Cost/benefit analyses are a means to judge the merit of a particular risk management initiative because of the fundamental economic nature of many (if not most) risk management decisions. However, risk management projects pose many special challenges that test the effectiveness of conventional cost/benefit analyses. These challenges include:

1. Extended time horizons, which are an evident characteristic of most risk management projects. For example, safety programs may take many years before it is clear how the program is affecting persistent loss incidence. Employee health programs may not demonstrate meaningful results for 10-15 years. Cost/benefit analyses commonly discount future costs and benefits and the longer the time horizon, the more difficult it becomes to measure results accurately.

2. Externalities, which are spillover effects of a risk that are not easily measurable. Pollution has a broad community effect, and the costs and benefits are not easily assignable to responsible or relevant parties.

3. Data Credibility, which means that statistical data often are hard to come by and—more frequently than not—are of suspect quality.

4. Interdependencies, which are phenomena where the nature of one risk is strongly related to another risk. For example, storing all police vehicles in a single location exposes each asset to a common risk—say, a fire. Interdependency confounds the measurement of costs and benefits of a particular risk management measure.

5. <u>Uncertainty,</u> which is a concept that suggests a manager's doubt about his or her ability to know the objective reality of a particular risk. Rarely do managers have sufficient information to understand clearly a risk. Uncertainty clouds judgment.

6. <u>Measurement of Costs and Benefits,</u> which, paradoxically, is the most difficult problem. While costs of some risk management measures (the insurance premium, the cost of some safety feature on a motor vehicle) are easily ascertainable, benefits often are not. Effective risk management often means that nothing happens—no accidents occur, no people are injured, no liability suits are filed. Establishing the relationship between expenditures and 'things not happening' can be quite difficult.

The recent Y2K computer phenomenon illustrates a number of these problems. Billions of dollars were spent to prevent losses, and the absence of disaster has led many to wonder whether 1) the risk prevention measures actually prevented losses, 2) the possibility of loss was non-existent or dramatically overinflated, or 3) the probability of loss was present but we were just lucky. 'Nothing happened', and the debate goes on as to who deserves credit.

Each of these problems is serious and worthy of consideration, but a listing of these challenges does not mean that cost/benefit analysis should not be used. However, these challenges do suggest that risk management decisions require managers to think critically about their risk management problems and realise that answers will not be found by relying solely on a traditional cost/benefit approach.

2) Programme Management

The success of a risk management programme hinges on the involvement and support of the local government's top officials, both elected and appointed. This support is not won easily, for while most public officials are aware of the potential impact of a major claim, short term budget pressures mean current premium savings tend to be valued more highly than long term cost of risk reduction.

The elements common to successful risk management programmes are:

Risk Management Policy Matters

Mission Statement. A mission statement outlining the goals of the risk management program should be created and circulated to everyone whose support is needed to make efforts successful. The statement should outline the position of public leaders and supervisors regarding risk management. It should outline goals and objectives and describe the roles of supervisors and employees in meeting the goals. It should clearly establish who is responsible for ensuring that the mission statement is followed.

Risk Management Practices and Procedures

Risk Management Staff One person should be assigned to coordinate the risk management activities, regardless of organisation design.

In a sense, all local government staff are risk managers within the scope of their positions, so many risk management responsibilities extend beyond the 'risk management staff.'

All employees and public officials should be familiar with risk management and safety policies. New policies pose a special challenge. Because risk management efforts undoubtedly will introduce changes in standard operating procedures, the support of all employees is crucial. Officials and employees must do new things they have not done before and shed certain past policies. All supervisors and staff members should know their general loss control responsibilities as well as the specific details of their jobs. In general, supervisors should be responsible for ensuring that all staff members know and follow safety rules. Supervisors train and retrain employees and hold regular safety meetings. They also inspect facilities, vehicles, and workspaces. The risk manager cannot do it alone; it requires a team approach.

Risk Management Committee Managers and key staff members representing various departments can be valuable resources. The following tasks need to be performed:

- writing and distributing risk management policies and rules
- writing a risk management policy statement
- establishing inspection procedures to identify and monitor key risks in each department
- reviewing all major purchases, designs for buildings, and proposals for services to identify risks

- developing safety training programs for new employees

- establishing procedures for reporting and investigating all claims, incidents, and safety violations

- promoting risk management to employees through publicity and awards programs and other methods

- developing disciplinary standards for employees who violate safety rules

- reviewing and suggesting new risk management and safety measures

Almost every local government has operational policies and procedures dictating the ways that certain tasks should be performed. The risk management committee should review existing operational policies and procedures periodically to ensure that they are effective from the standpoint of risk management. For tasks with special risks, the committee should establish standard procedures, including safety rules, maintenance schedules, guidelines for property security, emergency action plans, procedures for reporting accidents and safety-related incidents, and hiring and firing practices.

Loss Control Committee Depending on the size of the community and the annual number of accidents and claims, it may be advantageous to create a safety and loss control committee separate from the risk management committee. The duties of the committee include

- creating a safety policy and safety rules

- developing an inspection programme

- designing a safety orientation programme for new employees

- developing disciplinary procedures

- creating an accident and claims investigation programme

- establishing a review board to investigate fatalities, serious injuries, and other major accidents or losses

- reporting safety measures that require major funding.

Risk Management Communications Matters

Risk Management Policy Statement Before implementing any risk management measures, a local government should draw up a policy statement and have it approved by the governing board. A policy statement emphasising the importance of risk management and committing the government to managing risks should be drawn up and be approved by the elected members or senior management team. Benefits are:

1) it is easier to maintain that support when new officials take office

2) it strengthens the authority of the person or committee assigned risk management responsibilities

3) it shows insurance companies that the government is committed to managing risks

4) it can be useful in litigation to show that the local government had a formal policy dictating certain procedures.

A policy statement does not describe specific actions, but presents guidelines for making decisions about controlling and financing risks. In general, a policy statement should include

1) an overview of the government's risk management objectives

2) a description of the authority and responsibilities of the person/committee overseeing the risk management effort

3) a description of the responsibilities of supervisors, managers, and other employees.

Risk Management Manual A risk management manual that outlines and describes the policies that a department or local government should follow should be developed and circulated to all risk management staff members and the chief executive. A summary document may also need to be sent to all managers and employees to convey key information. A risk management manual should include:

- criteria for making insurance decisions, such as types of risks and maximum amounts that may be assumed by the entity and risks that should be self-insured, and how funds are to be generated and invested

- guidance on whether to join a pool or a risk retention group

- types of risks to be insured through traditional commercial carriers

- how to select insurers, agents and brokers

- use of co-insurance and deductibles

- establishment and operation of a claims reserve fund

- guidelines for deciding whether to use insurance or risk management consultants under various circumstances

- description of procedures such as accident reporting and investigation

- records and statistics of assets that should be kept

- guidelines for risk transfer, with requirements that contractors carry liability insurance

- description of insurance cost allocation among various departments

- types of decisions that must be approved by the insurance committee or other specified officials

- training and employee orientation processes

- policy on the role of citizens in risk management

A short safety manual can provide guidance for employees. The manual does not need to be a hard-bound publication; a few pages of safety tips can sometimes be more effective.

Annual Reports An annual report to the members will keep them up-to-date on risk management efforts and results, and it can be a good marketing tool for risk management. The annual report can include comparisons with previous years in terms of the number of accidents, claims, insurance premiums, new programs, and other risk management efforts and results.

Training Programmes. The most common way to ensure that new employees know about loss control policies is to train them when they are first hired. Employees cannot perform their tasks safely and efficiently if they have not been taught the proper methods. Current employees should receive comprehensive training when a new policy or procedure is introduced.

In effective training programs, supervisors not only understand safety practices but they are able to communicate the consequences of not following the policies.

Staff Meetings. The risk management staff can meet with supervisors and other public officials

informally or formally to report on risk management efforts and to discuss areas that need work.

Supervisors should also hold periodic safety meetings within their departments. Some local

governments require departmental meetings after major incidents to examine how the event

occurred and what can be done to prevent future such occurrences. Staff participation in

decision-making is a key success factor. Employees are more committed to safety if they play a

role in identifying problems and devising solutions.

Public Forums and Community Safety Programs.   Community risk management efforts

aggressively seek to engage citizens, businesses and others in the active management of many

public risks. Creation of citizen advisory groups, the holding of public education and dialogue

forums, and other safety initiatives can serve multiple purposes—addressing the risks, to be sure,

but also developing means for developing community support for risk management efforts.

Publicity. Since safety and risk control are ongoing concerns, employees must be continually

reminded to follow the correct procedures. Training programs, employee manuals, and staff

meetings introduce employees to the concept of loss control and the local government's

commitment to it. The risk management team has to be creative to maintain employee interest,

however.

Signs and rules at work sites are common reminders of safe and correct procedures, and safety awards, safety dinners, financial incentives, and other rewards, have been used successfully to motivate employees.

Periodic newsletters can update employees about new safety tips or remind them of procedures they should follow. They can report success stories such as a decrease in the number of work-site injuries or lost work days to encourage workers and to show top officials that risk management is working. A one-page newsletter, stuffed into pay envelopes—for example—is a simple yet extremely effective way to promote safety.

Loss Reporting. Accurate and thorough record keeping is crucial to the success of loss control efforts. It is important that employees report all accidents and incidents, no matter how minor. Many minor accidents or near misses (which seldom result in claims or lawsuits) are never reported or recorded. Unfortunately, one near miss that hits the target can be disastrous for a local government.

A good record keeping system should include:

- reports of accidents and accident investigations

- safety violations

- complaints of hazardous conditions

- records of claims and subsequent actions

- reports of inspections and follow-up inspections

- recommended corrective actions following an accident or inspection

- safety equipment (cost, location, maintenance)

- safety training sessions, dates, content, attendees

- maintenance schedules of all vehicles and other types of equipment

Accurate records serve several purposes.

- analysis of the data relating to accidents can indicate patterns and the need for corrective actions, and data on the costs of accidents can be used to make an argument for corrective measures

- for filing insurance claims

- for documenting safety efforts and results also can help reduce insurance premiums

- documentation of all preventive actions and actions taken after a claim can be valuable for defence in the case of litigation

A word of warning though – memos have been used by claimant's lawyers to prove negligence. If documentation shows that a local government was aware of a hazardous condition but did not take measures to correct it, it may be caught with a 'smoking gun'.

Risk Management Audit and Review Matters

Inspections. Frequent inspections of all public facilities and work areas can minimise risks by identifying potential exposures. Site visits can ensure that buildings, roads, and other public properties are maintained properly and that work practices follow safety regulations.

Many inspections can be done by public employees, such as the director of safety or public works. Local fire marshals can conduct comprehensive fire safety inspections of all public buildings. Inspections can be conducted by outside parties and can be good opportunities to train public employees to conduct inspections in the future.

After inspections are completed, reports should be reviewed by the governing board, department supervisors, and the risk management or safety committee to decide what actions need to be taken. Their decisions must be conveyed to the person or department designated to carry them out. The person responsible for risk management should check after a specified period to make sure that changes have been made.

Accident Investigation. After an accident is reported, someone should conduct a thorough investigation, no matter how minor the accident. Loss control efforts must emphasise that all accidents or incidents are critical. Minor accidents that keep recurring could point out the need for changes. Also, many small accidents could add up to substantial losses or a single—seemingly innocuous—event could evolve into a costly and litigious nightmare.

Accident investigators should receive training. Training can be as simple as a review of a sample claim report or informal instruction from another supervisor. The supervisor or employee must learn who conducts accident investigation and what types of accidents are to be investigated. They must understand how facts are gathered, how final reports should be filed, and how to notify the appropriate persons to take corrective action.

After an investigation, a report should be given to the risk management committee or the person who oversees risk management. A standard form for all types of claims ensures that all reports are consistent; a space for diagrams or photographs will help ensure that all reports are complete. The report at least should contain:

- names of supervisors and other public officials who should receive the report

- details of the accident or loss, including time, date, and location

- descriptions of public vehicles, equipment, or property involved in the loss

- names of injured persons

- names and addresses of witnesses

- description of the loss or damage with estimated cost and how the amount of loss was determined

- recommendations for preventing recurrences

- additional information that may be required by insurers or other agencies

The investigations must not focus only on how the accident happened and who was at fault but also why the accident occurred and how it can be prevented in the future.

Claims Handling. Prompt reporting of claims, even if claims are not administered in-house, can expedite claims handling, help injured workers return to work quickly, and save money by allowing the local government to settle justifiable claims quickly. Sometimes losses can be

substantially reduced if action is taken quickly after an accident and information about the accident is collected and reported promptly.

As part of a training programme, before accidents occur, a local government should make sure that employees know not to admit fault at the time of the accident. Outline actions that need to be taken or avoided before the claim is settled, and describe in detail the contacts and discussions that employees can have with insurance companies, attorneys, or others regarding the claim. After an accident occurs, find as many witnesses as possible who can provide information about the accident and the events leading up to it. Be sure to respond to workplace injuries promptly to reassure employees that they will receive the care they need and all efforts will be made to help them return to work as soon as possible.

Enforcement Policies. Risk management rules must have clout. Some violations may necessitate punishment; a letter of reprimand in the employee's personnel file; suspension from work without pay; salary deductions to pay for damages, or termination for extreme cases or repeat offenders.

Programme Evaluation. Once risk management procedures are put into place, the risk management staff must maintain some control by establishing performance standards, determining whether actual practices meet those standards, and taking corrective action whenever necessary. There are two types of standards; results standards and activity standards.

Results can be measured in monetary values, percentages, ratios, or numbers of losses or claims. For example, if the local government's total cost of risk is 1.0 percent of its operating budget, a standard of 0.9 percent could be set for next year. Or a reduction in the total number of public vehicle accidents to a fraction of past levels could be used as a standard.

Activity standards measure efforts to achieve desired goals. For example, each supervisor may be required to make at least four safety inspections each year.

If performance falls below the standard, measures may need to be taken to meet the standard. Certain programs may need to be discontinued, new procedures may need to be instituted, or current procedures may need to be changed. If problems persist, standards may need to be reexamined. Sometimes adjusting an unrealistic standard can motivate employees to work harder to meet new standards.

If performance meets the standard, it may be that no action is necessary, or it may be that the standard needs to be raised. If performance exceeds the standard, the standard may simply be too low. However, it could be an indication of diligent effort on the part of managers and employees, and such efforts should be recognized and rewarded.

As loss exposures change, the methods used to manage risk should change as well--a consistent monitoring process will ensure that risk-handling efforts are current.

Concluding Thoughts

Risk management has grown rapidly over the past 20 years from a narrow, relatively technical insurance-buying and safety function into a broader managerial and policy-oriented form. More than ever, risk management is being defined as the management of <u>all</u> organization risks, which is putting increasing pressure on top managers and elected officials to become more engaged in setting risk policy and overseeing the creation of a risk management culture within the public entity. The expansion of the definition of risk management also means that while risk managers are increasingly important, managers across the public sector spectrum are experiencing growing pressure to better manage the risks that fall within the scope of their duties.

Developing and implementing an effective risk management program in a local government entails a lot of hard work and patience. But once it is in place and employees and supervisors are committed to making it work the benefits for citizens and government employees are well worth the effort. Risk management is 'good management.'