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RISK MANAGEMENT: A COMPREHENSIVE APPROACH

It could be said that risk management is a fundamental purpose of government. For instance, 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. All local governments practice risk management whether or not they are aware of it.

Risk management is the process by which a local government assesses and addresses its risks. Historically, risk management has been associated with insurance-buying, occupational safety and health, and legal liability management. In recent years governmental managers have begun to recognize that organizational risks are pervasive, that these risks are extraordinarily diverse and complex, and that they are not confined to "insurable" or accident-related situations. They may arise from actions of the state legislature, investment management practices, climatological phenomena, and even changing voter preferences.

This report describes the formal risk management process and shows how traditional risk management is being applied to new areas of local government risk. Readers will learn about the overall goals and objectives of risk management, the challenge of identifying and analyzing risks, the tools available, and the means by which risk management efforts are effectively implemented.



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Risk Management: A Comprehensive Approach

This report has been prepared for ICMA by the Public Risk Management Association (PRIMA). PRIMA is a non-profit education and training organization serving the needs of state and local government risk management practitioners across North America. PRIMA's membership includes roughly 1,900 states, cities, counties, school districts, special districts, and pools. The report's author is Dr. Peter C. Young, who is the E. W. Blanch, Sr. Chair in Insurance at the University of St. Thomas' Graduate School of Business in Minneapolis, Minnesota.

THE GOALS AND PURPOSES OF RISK MANAGEMENT

Risk management is the formal process by which an organization establishes its risk management goals and objectives, identifies and analyzes its risks, and selects and implements measures to address its risks in an organized and coordinated fashion.

Risk imposes two types of costs on local governments; the *cost of losses* that occur (fires, vehicular accidents, worker injuries), and the *cost of uncertainty*. Uncertainty affects a local government in numerous ways. Of course, uncertainty leads to fear and worry among employees and citizens, but it also can lead to misallocations of limited resources. Both costs of risk are of concern to local governments since they impact negatively on budgets. Therefore, a primary goal of risk management would seem to be the maintenance of budget stability through control of the costs of risk.

Recently, risk managers have begun to look not only at risks of loss but also at the potential for cost savings, service improvements, or revenue enhancements that exists in various areas of local government management: financial investment, training and development of employees, intergovernmental relations. This potential might be called the "upside" of risk management. In each of these instances, and in many others, risk managers have discovered that they can make a positive contribution to local government decisions that involve risk, a realization that dramatically expands the scope of risk management. In this new context, the goal of achieving budget stability does not seem adequate to guide risk management decisions. Consequently, risk managers today emphasize that while a core objective of risk management is to minimize the negative impact of risk on budgets and on the human psyche, they hasten to add that risk management also supports sound analysis of risk-taking opportunities—opportunities that can enhance the capabilities of the local govern-

ment. See the sample mission statement and objectives in Appendix A.

RISK IDENTIFICATION AND ANALYSIS

Risk assessment means identifying and analyzing risks. The objective 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.

It is impossible for an organization to identify all its risks. The world is too dynamic and a local government's environment is subject to constant and sometimes bewildering change. Thus, while total risk identification may be the objective, risk managers approach the challenge with humility and caution, recognizing that this ultimate goal is forever beyond their grasp.

How, then, do we organize our approach to assessing risks? The answer can be structured around three questions: 1) 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?

Where Do Risks Arise?

Local governments are subject to risks arising from seven sources:

- The physical environment (snow and ice, earthquakes)
- The economic environment (monetary policy, state of the economy)
- The political environment (legislative activity, pending elections)
- The social environment (social attitudes and preferences)

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- The legal environment (court decisions, administrative/regulatory rules)
- The operational environment (the day-to-day activities and actions within the local government)
- The cognitive environment (absence of information, the influence of attitudes toward risk on decision making).

In the parlance of risk management, we say that these environments contain *hazards*, which are characterized as features within an environment that elevate the probability of loss or its potential severity. An example of a hazard in the physical environment would be a winter storm. Hazards, in and of themselves, do not produce losses. It is the *perils* (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 “upside” risks. For example, we might say that the economic environment produces *risk factors* (rather than hazards) that can create *opportunities* (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 Our Exposure to Risk?

None of the preceding discussion of risk matters if the local government is not exposed to the risk. If a government does not have any of its vehicles out on the icy highways, the risk may exist in an abstract sense, but the government has no exposure. Exposure to risk is the principal motivation to practice risk management.

From a managerial perspective, it is useful to sort exposures according to type. There are, broadly, two types of exposures—asset and liability—of which asset exposures have three categories and liability exposures have two.

Asset exposures. The three general assets that local governments control are 1) physical assets, 2) financial assets, and 3) human assets.

Risk management decisions may also affect directly the “productivity” of those assets.

Physical assets are police vehicles, school buildings, computers, roads, waste treatment facilities, and other tangible assets. The impact of the loss of a physical asset is not just that it must be replaced but that it can’t be used for some period of time. The loss

of its use may amplify the economic impact of losing the asset itself.

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, and default risk, among others).

Human assets are the managers, employees, elected officials, 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 soundly diversified investment strategy can minimize downside risk while directly supporting the attainment of positive investment objectives.

Liability exposures. The two liability exposure areas are 1) legal liability, and 2) moral responsibility.

Exposure to legal liability is a major preoccupation of most risk managers. Despite the fact that many states extend tort caps or statutory immunities to local governments, these limitations do not minimize the frequency with which governments are subjected to lawsuits. Further, the visibility of a local government’s activities means that it is an easy target for lawsuits.

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. We often hear the phrase “we didn’t break any laws!” but as often as we hear it, it still rings hollow. Public sector managers have a general responsibility to citizens that is not defined only by the law. Risk management is concerned with the impact of local government decisions and actions within the context of its moral obligations.

How Do We Gather Information about Risks?

Local governments should develop a formal process whereby risks are systematically identified, analyzed, and measured.

Identifying risks. The preliminary risk identification questionnaire presented in Appendix B can serve as a starting point for identifying risks. Numerous sources of information are available to assist in the identification and assessment process. They include:

Checklists. Checklists 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 standardized checklists are limited to insurable risks, they do serve as a sound starting point for organizing a more expansive search for organizational risks. Over time, a local government can customize such a list to meet its ongoing needs.

Interviews. 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 enhances support when risk management programs are implemented.

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

Incident records and reports. When available, records and reports of incidents can provide an important insight into serious 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. Financial documents listing programs, services, financial values, and capital plans are excellent sources of information for identifying existing and new risks.

Council and committee minutes. Council and committee minutes can help managers anticipate new risks or impending risk management issues. Of course, council and 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. Records of real estate owned or used by the government often reveal loss exposures

that may be overlooked—leases and easements being obvious illustrations of such exposures.

Permits. Permits should be evaluated as they can sometimes create liability problems. For example, if a restaurant passes a county health inspection, a customer suffering food poisoning may have a basis to sue the county for negligence.

Contracts. Construction and purchase agreements outline the liabilities of each party. Further, 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 forums. Public forums allow citizens to voice their opinions, desires, and concerns to local officials. Risks of various types (and, certainly, attitudes toward risks) are often identified through this method.

Categorizing risks. Once an organization has developed a comprehensive listing of risks, it must take at least two other assessment steps. 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. Risks that are “low frequency/low severity” produce losses only rarely and when they do occur, they are of minor importance.

Category two. Risks characterized as “low frequency/high severity” 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 organization to organization.

Category three. Risks characterized as “high frequency/low severity” 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. For those rare risks that are “high frequency/high severity,” losses occur frequently and they all are serious. Not surprisingly, 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.

Analyzing risks. The remaining assessment task is to analyze the risks to understand how risky condi-

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tions 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.

As a general proposition, a local government will focus most of its attention on category two and three risks. Managers broadly seek to control (that is, prevent, reduce, avoid, or otherwise manage) category three risks, while category two risks are candidates for transferring (through insurance) or distributing (through a pool, for instance) to another party or parties.

Evaluating risks. A final word is necessary about the valuation of risks. From a risk management perspective, exposures to risk have two bases of valuation. First, assets might be valued on the basis of the cost to replace those assets. Not surprisingly, 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 on the basis of 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—a consideration that might be characterized as 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 a closet), 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 mightily to a local government’s productivity. A city may own storage facilities that generate significant rental income for the city, but which have very little value in a replacement context.

The point is that while the cost of replacing an asset is a common risk measurement device, it sometimes can be a misleading way of thinking about 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: *risk control* tools and techniques and *risk financing* measures. Risk control includes efforts to avoid, prevent, reduce, or otherwise manage risk and its impact on an organization. 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 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 money paying for losses? Were the return-on-expenditure for each choice found to be identical, a government manager might be wholly indifferent to the process of risk management. However, research and practice have shown that preventing losses tends to be vastly less expensive than financing loss, giving life to that age-old maxim, “an ounce of prevention is worth a pound of cure.”

Risk Control

Examining all risk control options is essential. Unfortunately, many local governments restrict themselves to traditional insurance or safety programs without even considering other alternatives, or they implement the first risk handling technique that comes to mind, even though it may not be the best option.

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

Risk avoidance. 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 because it eliminates the chance of loss.

Often, avoiding one risk creates others—or transfers the risk to another context.

Some governments can avoid risks 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 certain services must be provided regardless of the risks. It is, in fact, the inability to avoid many key risks that most distinguishes public sector risk management from its private sector counterpart.

One way to decide whether to avoid a risk is to

determine whether the benefits of the activity outweigh the cost, not only in dollars 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, such as 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.

Like risk avoidance, 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 no losses ever 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 minimize the impact of losses that do occur. 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.

In recent years a great deal of attention has been paid to the role of catastrophe or contingency planning in local government. Such plans are intended to provide a blueprint for a response to a catastrophic-level emergency. Catastrophe plans are loss reduction measures on a grand scale and are an important part (often a mandated part) of a local government's responsibilities. However, it is worth noting that catastrophe plans should be part of an overall risk management program. Catastrophe management requires technical knowledge and support within the local government. If a risk management culture is not in place, it is very difficult for a local government to see a catastrophe program through the planning phase and—should the situation ever arise—implement it.

Uncertainty reduction. Uncertainty is the doubt we have about our ability to know what is going

to happen. In recent years uncertainty management has been gaining more attention in the risk management world. Often, an organization cannot measurably control a risk but can improve its ability to function by better understanding the risk. Information management is a primary tool here because a better understanding of a given situation will—at the very 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.

Risk transfer. A local government can transfer some risks to private or nonprofit organizations 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 state and local governments. Many 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, a local government should establish standard procedures for preparing, reviewing, and filing all contracts. No contract should be finalized without a risk review by the government's attorney and by someone with risk management responsibilities. Part of the review should include an examination of state and local regulations regarding contracts. Some states require that all contracts exceeding certain amounts must be submitted for competitive bids. Some states exempt contracts for such transactions as professional services and land purchases.

Also, while a contractual transfer of risk may be appropriate, it is worth noting that reality may intrude in at least two different ways. First, the counterparty to a contract may prove incapable of bearing the transferred risk. A computer-servicing vendor may declare bankruptcy, leaving a local government high and dry. This is why certificates of in-

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insurance and other financial assurances of an ability to bear risk often are required as part of a contractual transfer of risk.

Second, while a local government may transfer the *functional delivery* of certain services (food service at a county hospital, refuse collection in a town), *responsibility* for the provision of the service ultimately resides with the local government. Though this matter is as much moral and political as it is economic or legal, a local government should consider the difficulties in transferring responsibility when using contractual transfers.

Risk Financing

No matter how successful the risk control efforts, local governments inevitably will suffer losses that need to be paid. All risk financing techniques can be classified as either *risk retention*, in which a jurisdiction assumes all or part of a loss, or *risk transfer*, in which one organization agrees to pay for the losses of another organization in exchange for a premium. Public agencies often use a combination of financing alternatives. The following are the most common risk financing mechanisms:

Insurance. The traditional way that local governments protect themselves is to purchase an insurance policy from a commercial insurance company. The local government pays premiums, and—should a loss arise—the insurance company adjusts the claim, and provides other services such as legal defense. 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 the policy includes a deductible 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. Since the risk assessment process can't identify all risks that later produce a loss, all organizations do some amount of passive retention.

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 because of 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 benefit 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 should 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, or SIR.

Intergovernmental pools. Some local governments pool their resources with other local governments to fund a portion of their losses. Pools currently exist in all states, and it is estimated that 35 to 40 percent of all local governments in the United States participate in one or more pools (there are over 425 pools in operation).

Most successful risk financing pools are evolving into a version of the risk management pool.

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. Most pools were formed in response to the periodic unavailability and unaffordability of commercial insurance in the 1970s and 1980s. In many states, pools are considered a form of self-insurance. In other states, special enabling legislation permits pools to operate as a kind of special-purpose mutual organization. This status allows most pools to escape the regulatory and tax treatment to which most insurance companies are subjected. To date, hardly any pools are seriously operating in a multi-state environment, though some discussions have occurred that might lead to regional pools.

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.

Some pools are 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. 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. Most successful risk financing pools are evolving into a version of the risk management pool.

Other risk financing tools. Numerous other options may be employed. They include such things as risk retention groups (private sector analogs to pools), captive insurance companies (an insurance company that insures only one client—its parent organization), banking arrangements (such as lines and letters of credit, and other lending programs), and occasionally, other public agencies. In regard to this last example, some local or regional authorities 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.

CHALLENGES TO RISK MANAGEMENT

How do risk managers decide which measures to undertake, and—upon deciding—what issues do they need to address to ensure that their local government can successfully implement the risk management program? The answers to these questions serve as the basis for the final section of this report.

At several points in this report, the idea of cost/benefit analysis has been suggested as a means to judge the merit of a particular risk management initiative. Many (if not most) risk management decisions are fundamentally economic in nature. A decision to buy insurance, to self-insure, to introduce a loss control measure, or to introduce a new process or procedure places a demand on financial resources—resources that are finite and that must be allocated among all the local government's functions. Because this is so, top managers and elected officials justifiably expect a demonstrable return on any investment they authorize.

Local government managers should note, however, that risk management projects pose many special challenges that test the effectiveness of conventional cost/benefit analyses. These challenges include:

- **Extended time horizons.** Extended time horizons are characteristic of most risk management projects. For example, it may take many years for a safety program's effect on persistent loss to become clear. Employee health programs may not demonstrate meaningful results for 10 or 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.

- **Externalities.** The spillover effects of a risk are not easily measurable. Pollution has a broad community effect, for example, and the costs and benefits of reducing pollution are not easily assignable to responsible or relevant parties.
- **Data credibility.** Credible statistical data often are hard to come by.
- **Interdependencies.** The nature of one risk is strongly related to other risks. 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.
- **Uncertainty.** Managers are used to making decisions based on information, but in risk management, they do not always have as much information as they need to make a decision with confidence. Uncertainty can lead to tentative or ineffective decision making.
- **Measurement of benefits.** Paradoxically, measuring benefits of risk management is the most difficult problem. While the costs of some risk management measures (the insurance premium, the cost of a 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 realize that answers will not be found by relying solely on a traditional cost/benefit approach. See the simplified risk management decision process in Appendix C.

RISK MANAGEMENT PROGRAM IMPLEMENTATION

The success of a risk management program hinges on the involvement and support of the local government's

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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 savings because of risk reduction.

The following discussion identifies several elements common to successful risk management programs. Although some of the elements may not be necessary in all organizations, all are commonly employed to engender support from top officials and ensure the success of risk management programs.

Risk Management Policy

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. This statement will guide the development of explicit policies and procedures.

Risk Management Practices and Procedures

Risk management staff. Some jurisdictions have a centralized, full-time risk manager and a staff of professionals to oversee loss control, claims, and other functions. Others may have one part-time staff member who is responsible for purchasing insurance. Obviously, the size of the risk management staff depends on the size of the local government and the scope of services it provides. Nonetheless, one person should be assigned to coordinate the risk management activities, regardless of organization design. Historically, someone with a safety or finance background has been the best candidate to handle risk management—whether on a full- or part-time basis. In recent years, the broadening definition of risk management has shifted the emphasis somewhat from safety and finance and drawn attorneys, policy analysts, deputies, and individuals with other backgrounds into the risk management field.

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 ensure 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.

Risk management committee. Managers and key staff members representing various departments can be valuable resources. In a local government that does not have a full-time risk manager—and even in some that do—the following tasks can be performed by an interdepartmental committee:

- 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 how 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 loss control committee is made up of supervisors and key staff members who are not managers. Including non-managers on the committee shows all employees that their knowledge of the workplace and input about safety are important.

Some of the duties of the committee include creating a safety policy and safety rules, developing an inspection program, designing a safety orientation program for new employees, and developing disciplinary procedures. The committee also should create an accident and claims investigation program and establish a review board to investigate fatalities, serious injuries, and other major accidents or losses. Finally, the committee reports safety measures that require major funding.

Risk Management Communications

Risk management policy statement. Before implementing any risk management measures, a local government should draw up a policy statement based on the mission statement and have it approved by the governing board. A policy statement emphasizes the importance of risk management and commits the government to managing risks. If top-level support is expressed in a written document, it is easier to maintain that support when new officials take office. This support strengthens the authority of the person or committee assigned risk management responsibilities.

A policy statement shows insurance companies that the government is committed to managing risks. In addition, 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 an overview of the government's risk management objectives; a description of the authority and responsibilities of the person or committee overseeing the risk management effort; and a description of the responsibilities of supervisors, managers, and other employees.

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

- Criteria for making insurance decisions, such as what types of risks and maximum amounts may be assumed by the entity, what risks 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 hardbound publication; a few pages of safety tips can sometimes be more effective. See sample manual outline in Appendix D.

Annual reports. An annual report to the governing board will keep board members 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 programs. 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 understand safety practices and 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 incidents. 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. Citizen advisory groups, public education and dialog forums, and other safety initiatives can serve multiple purposes—addressing the risks, to be sure, but also developing community support for risk management efforts.

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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 workdays 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 keep-

ing is crucial to the success of loss control efforts. Unfortunately, this process often is neglected, especially in smaller jurisdictions that do not have formal risk management procedures and see few, if any, major claims. It is important that employees report all accidents and incidents, no matter how minor. Many minor accidents and near misses (which seldom result in claims or lawsuits) are never reported or recorded. Unfortunately, one incident 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

Promoting workplace safety

The Workzone Safety Campaign in **Midland, Michigan** (38,053), was designed to encourage drivers approaching work zones to proceed with caution and to think about the people working there. The city wanted the public to see highway workers as real people with lives beyond their jobs and with loved ones to go home to. To get the message out to the general public, the city told its drivers "Our Safety Is in Your Hands" and aired a series of public service announcements (PSAs) on the local public access channel showing employees at work and at home. The program cost the city \$4,569, which included the PSAs and a series of safety roundtables.

Since 1983, when it implemented a 15-point safety action plan for municipal employees, **Anaheim, California** (266,000), has enjoyed a 79 percent decline in its disabling injury rate (a statistic that takes into account hours worked). Or to put it another way, thanks to the city's attention to its employees' safety, the equivalent of 20 full-time municipal workers (out of a workforce with 2,100 full-time and 1,500 part-time employees) are uninjured and on the job every day as compared with the 1983 level. To keep employees focused on safety, every city department has at least one safety coordinator and one safety manager (departments handling more risky activities, such as utilities and public safety, have more), who hold regular safety meetings and pass on information. The city also includes safety tips, many of which apply outside the workplace as well, in its quarterly newsletter. As a result of these efforts, Anaheim has the lowest workers'

compensation claim costs of any government entity in California with a population of 50,000 or more.

An employee safety incentive award program in **Manassas, Virginia** (28,000), recognizes city employees who have earned exemplary safety records by avoiding accidents, injury to themselves and the public, and damage to property through the cautious conduct of their assigned duties. The award program includes workers in the city's public works and utilities and public safety departments, who face the greatest risk of injury. Recognition is awarded on the basis of a point system and is conferred in two categories: a quarterly safe employee award (to an individual) and an annual safe department award (to a group). To win an award, city employees must earn at least 150 points by the end of a quarter and meet three safety performance criteria: they must 1) have no reportable on-the-job injury, preventable motor vehicle accident, or damage to city property; 2) incur no safety violation of any kind; and 3) attend and participate in all departmental safety meetings. An additional 50 points may be earned if an employee submits a safety suggestion that is implemented or identifies an existing or potential safety hazard. To win the annual safe department award, each participating group must hold all required safety meetings, conduct monthly safety inspections, have no preventable accidents, or demonstrate a 50 percent decrease in the number of accidents over the previous calendar year. Of the 211 employees eligible to participate in the program during its first quarter, 181 employees received safety recognition awards.

- 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 action. Data on the costs of accidents can be used to make an argument for corrective measures. Of course, accident records are useful for filing insurance claims, but documenting safety efforts and results can help reduce insurance premiums. Moreover, documentation of all preventive actions and actions taken after a claim can be valuable for defense in the case of litigation. However, records and even interoffice memos have also been used by plaintiff's attorneys to prove negligence. Documentation that shows that a local government was aware of a hazardous condition but did not take measures to correct it may be a "smoking gun."

Risk Management Audit and Review

Inspections. Frequent inspections of all public facilities and work areas can minimize 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—for instance, the director of safety or public works. Local fire marshals can conduct comprehensive fire safety inspections of all public buildings. In addition, insurance agents, state municipal leagues and county associations, intergovernmental pools, and private risk management and safety consultants can all provide assistance in conducting inspections. Inspections by outside parties can be good opportunities to train public employees to conduct inspections in the future.

After an inspection is completed, the report 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. Unfortunately, it sometimes takes a serious accident to convince officials that action is needed. Loss control efforts must emphasize that all accidents or incidents are critical. Minor accidents that keep recurring can indicate a need for changes. Also, many small accidents can add up to substantial losses, and a single—seemingly innocuous—event can evolve into a costly legal nightmare.

All supervisors and other employees who conduct accident investigations 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 investigations 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.

One of the most important functions of an accident investigation is to determine why an accident occurred. Too often, investigations focus only on how the accident happened and who was at fault, without delving into 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 program, 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 lead-

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ing 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.

Program 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. Broadly speaking, there are two types of standards: results standards and activity standards.

Results can be measured in dollars, 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 goals. For example, each supervisor may be required to make at least four safety inspections each year.

If performance falls below the standard, the manager may have to take measures to meet the standard. The local government may need to discontinue certain programs, institute new procedures, or change current procedures. If problems persist, the standards may need to be reexamined. Sometimes adjusting an unrealistic standard can motivate employees to work harder to meet the new standard.

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, effort that 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 *all* organization risks. This broader mission puts 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.

APPENDIX A SAMPLE MISSION STATEMENT AND OBJECTIVES—CHICAGO, ILLINOIS

Mission Statement

The Risk Management Section is responsible for effectively managing the City of Chicago’s exposures to accidental losses in ways which protect the City’s assets and assure continuity of its operations.

Objectives

- To protect the City against the financial consequences of accidental losses of a catastrophic nature.
- To preserve the City’s assets and service capabilities from loss, destruction, or depletion.
- To minimize the long-term cost of City activities by the identification, prevention, and control of accidental losses and their consequences.
- To apply risk management techniques to minimize the adverse effects of losses and to serve as a cost reduction center.

Functions

In order to achieve its objectives, risk management assumes responsibility for, but is not limited to, the following functions:

- Planning, organizing, directing, and managing a comprehensive risk management program to protect the City against catastrophic losses.
- Formulating and implementing administrative policies and procedures necessary for carrying out City insurance activities.
- Developing programs to deal with risk through insurance, self-insurance, non-insurance, contractual risk transfer, reduction, prevention (safety), and protection.
- Developing, writing, and implementing uniform and consistent terminology for City contracts, leases, permits, and any associated agreements in order to minimize risk to the City.
- Developing, coordinating, and implementing safety programs and safety education.

Courtesy of Caroline Cogtella, Risk Manager, City of Chicago.

APPENDIX B PRELIMINARY RISK IDENTIFICATION QUESTIONNAIRE

Yes	No	General
<input type="checkbox"/>	<input type="checkbox"/>	Does the agency have any significant or unusual circumstances involving risk, insurance, or losses?
<input type="checkbox"/>	<input type="checkbox"/>	Is there a documented risk management policy or program currently in place?
<input type="checkbox"/>	<input type="checkbox"/>	Is there a risk management committee or agency risk manager?
<input type="checkbox"/>	<input type="checkbox"/>	Does the agency produce periodic loss reports or itemized statements of losses?
<input type="checkbox"/>	<input type="checkbox"/>	Is there a documented “Disaster/ Emergency Plan” for the agency?
<input type="checkbox"/>	<input type="checkbox"/>	Are there written “Administrative Procedures/Directives” for the agency (standard operating procedures)?
Human Resources		
<input type="checkbox"/>	<input type="checkbox"/>	Do any agency employees work outside the state?
<input type="checkbox"/>	<input type="checkbox"/>	Is temporary/seasonal help or are volunteers ever hired?
<input type="checkbox"/>	<input type="checkbox"/>	Are specific employees’ recreational facilities or activities sponsored?
<input type="checkbox"/>	<input type="checkbox"/>	Does the agency have a personnel policies manual or handbook?
<input type="checkbox"/>	<input type="checkbox"/>	Do any agency employees regularly work from their homes or on other employers’ premises?
Safety		
<input type="checkbox"/>	<input type="checkbox"/>	Have the appropriate elements described in the state’s attorney general’s safety and health program document been implemented?
<input type="checkbox"/>	<input type="checkbox"/>	Are pre-employment physical examinations/screens given or required for any job classifications?
<input type="checkbox"/>	<input type="checkbox"/>	Are programs established to detect/ correct occupational illness hazards?
<input type="checkbox"/>	<input type="checkbox"/>	Is there a full-time agency safety manager?
<input type="checkbox"/>	<input type="checkbox"/>	Are there any named additional duty safety managers/ officers?
<input type="checkbox"/>	<input type="checkbox"/>	Is there an agency-wide safety committee?
<input type="checkbox"/>	<input type="checkbox"/>	Are safety committee meetings held regularly and are documented minutes kept?
<input type="checkbox"/>	<input type="checkbox"/>	Are there regularly scheduled divisional/section/unit safety meetings?

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Yes	No	Safety	Yes	No	Liability
<input type="checkbox"/>	<input type="checkbox"/>	Does the agency have an existing safety manual or written rules (other than the state's attorney general's official safety manual)?			equipment, exhibit space, permit for wires, overpass, pipe line/right of way across private or public property, electricity, steam, water, purchase orders or advertising?
		Automobiles/Heavy Equipment			
<input type="checkbox"/>	<input type="checkbox"/>	Are any hired/leased vehicles used regularly by agency?	<input type="checkbox"/>	<input type="checkbox"/>	Does the agency own or operate any locations with any exposure to liquor liability: ownership of premises or sponsored events?
<input type="checkbox"/>	<input type="checkbox"/>	Are certificates of insurance obtained from owners of hired/leased vehicles?	<input type="checkbox"/>	<input type="checkbox"/>	Does the agency have any water damage, sprinkler leakage, or fire legal liability exposure?
<input type="checkbox"/>	<input type="checkbox"/>	Are nonowned trailers hauled by agency-owned trucks?	<input type="checkbox"/>	<input type="checkbox"/>	Does the agency own or operate any underground storage tanks?
<input type="checkbox"/>	<input type="checkbox"/>	Do nonowned tractors haul agency-owned trailers?	<input type="checkbox"/>	<input type="checkbox"/>	Does the agency own or operate any hospital or infirmary?
<input type="checkbox"/>	<input type="checkbox"/>	Do employees drive personal cars on agency business?	<input type="checkbox"/>	<input type="checkbox"/>	Does the agency have medical doctors on payroll?
<input type="checkbox"/>	<input type="checkbox"/>	Does the agency have a policy with respect to personal use of agency vehicles?	<input type="checkbox"/>	<input type="checkbox"/>	Does the agency have medical doctors under contract?
<input type="checkbox"/>	<input type="checkbox"/>	Are any parking facilities operated by the agency?	<input type="checkbox"/>	<input type="checkbox"/>	Does the agency have nurses on payroll?
<input type="checkbox"/>	<input type="checkbox"/>	Are any garage facilities operated by the agency?	<input type="checkbox"/>	<input type="checkbox"/>	Does the agency have nurses under contract?
<input type="checkbox"/>	<input type="checkbox"/>	Are any repair/maintenance facilities operated by the agency?	<input type="checkbox"/>	<input type="checkbox"/>	Does the agency own any boats/watercraft?
<input type="checkbox"/>	<input type="checkbox"/>	Are employees transported by agency-owned trucks or vans?	<input type="checkbox"/>	<input type="checkbox"/>	Does the agency have any boats/watercraft leased or chartered?
<input type="checkbox"/>	<input type="checkbox"/>	Are agency employees transported by nonowned trucks or vans?	<input type="checkbox"/>	<input type="checkbox"/>	Does the agency provide any services regularly performed in foreign countries?
		Holdings/Contents	<input type="checkbox"/>	<input type="checkbox"/>	Does the agency have any professional liability or errors and omissions exposures for the following activities: accounting services, actuaries/pension consultants, adjusting services, advertising agency, ambulance service, appraisal of real estate, architects/engineers/testing laboratories, beauty parlors/barber equipment leasing, escrow agents, hospital/clinic/nursery, insurance agents/brokers, insurance consultants, land surveyors, lawyers, mortgage lending, real property/chattels, premium financing, publishers/graphic arts, real estate, telephone answering services, title abstractors, travel agency, or trust department?
<input type="checkbox"/>	<input type="checkbox"/>	Does the agency conduct an annual inventory (schedule) of agency-owned buildings and property including: purchase date, cost, new or used, location, current/replacement value, etc.?			Does the agency conduct any publishing activities?
<input type="checkbox"/>	<input type="checkbox"/>	Does the agency produce an annual inventory (schedule) of building contents?			Does the agency conduct operations that might adversely impact the environment: air, water, and land?
<input type="checkbox"/>	<input type="checkbox"/>	Does the agency contract for significant rental contents?			Does the agency have any explosion, collapse, or underground exposures?
		Liability			Does the agency have any hazardous waste exposures?
<input type="checkbox"/>	<input type="checkbox"/>	Does the agency conduct any operations involving the following: operation of industrial operations, industrial railroad, ponds, dams, parks or recreational facilities, swimming pools, bathing beaches, grandstands, gymnasiums, bowling alleys, or sale or co-generation of electricity, steam, water?	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	Does the agency assume any contractual liability for the following: lease or rental agreements for real estate, signs, EDP equipment, machinery, telephone	<input type="checkbox"/>	<input type="checkbox"/>	

- | Yes | No | Liability |
|--------------------------|--------------------------|--|
| <input type="checkbox"/> | <input type="checkbox"/> | Does the agency have any chemical waste exposures? |
| <input type="checkbox"/> | <input type="checkbox"/> | Does the agency have any asbestos exposures? |
| <input type="checkbox"/> | <input type="checkbox"/> | Does the agency have any nuclear exposures? |

Aircraft

- | | | |
|--------------------------|--------------------------|---|
| <input type="checkbox"/> | <input type="checkbox"/> | Does the agency own or lease any aircraft? |
| <input type="checkbox"/> | <input type="checkbox"/> | Are there any aircraft chartered for special purposes? |
| <input type="checkbox"/> | <input type="checkbox"/> | Does the agency have any known nonownership exposures: directors, officers or employees who fly their own aircraft on agency/department business? |
| <input type="checkbox"/> | <input type="checkbox"/> | Has the agency any known past aircraft losses? |

Fiduciary Liability/Crime Exposures

- | | | |
|--------------------------|--------------------------|---|
| <input type="checkbox"/> | <input type="checkbox"/> | Are any amounts of cash, securities, or checks on agency premises at regular intervals (other than petty cash)? |
| <input type="checkbox"/> | <input type="checkbox"/> | Are any unusual cash amounts on hand seasonally or occasionally? |
| <input type="checkbox"/> | <input type="checkbox"/> | Does the agency own/lease any safes or vaults? |
| <input type="checkbox"/> | <input type="checkbox"/> | Does the agency utilize any messengers to banks? |
| <input type="checkbox"/> | <input type="checkbox"/> | Are there any authorized night deposits? |
| <input type="checkbox"/> | <input type="checkbox"/> | Does the agency use any safe deposit boxes? |
| <input type="checkbox"/> | <input type="checkbox"/> | Is an annual physical inventory made of stock and supplies? |
| <input type="checkbox"/> | <input type="checkbox"/> | Have there been any known past exposures to extortion, threats, or attempt to kidnap? |
| <input type="checkbox"/> | <input type="checkbox"/> | Are there any temporary help, employees of others, or contracted services, which might present a dishonesty exposure directly or in collusion with others: custodians, agents, collectors, EDP service, etc.? |
| <input type="checkbox"/> | <input type="checkbox"/> | Are agency credit cards issued to directors, officers, or employees? |
| <input type="checkbox"/> | <input type="checkbox"/> | Have there been any crime losses during the past five years? |
| <input type="checkbox"/> | <input type="checkbox"/> | Are petty cash funds audited regularly? |

Boiler and Machinery: Agency-Owned

- | | | |
|--------------------------|--------------------------|--|
| <input type="checkbox"/> | <input type="checkbox"/> | Are there any heating or power boilers located on agency premises? |
|--------------------------|--------------------------|--|

Boiler and Machinery: Agency-Owned

- | | | |
|--------------------------|--------------------------|--|
| <input type="checkbox"/> | <input type="checkbox"/> | Are any other boiler and machinery objects used: refrigeration, pressure vessels, large motors? |
| <input type="checkbox"/> | <input type="checkbox"/> | Would any of the above items cause substantial business interruption if damaged? |
| <input type="checkbox"/> | <input type="checkbox"/> | Are there any alternate sources of power (or electricity) utilized? |
| <input type="checkbox"/> | <input type="checkbox"/> | Does the physical plant include generation of energy? |
| <input type="checkbox"/> | <input type="checkbox"/> | Are there any cold storage or controlled temperature rooms? |
| <input type="checkbox"/> | <input type="checkbox"/> | Has there been a recent study done on excess capacity or availability of replacement for critical objects, emergency generators, substitute equipment? |

Business Interruption

- | | | |
|--------------------------|--------------------------|--|
| <input type="checkbox"/> | <input type="checkbox"/> | In the event of an agency or major facility shutdown by fire or other catastrophe, is it essential that operations be resumed immediately, regardless of expenses? |
| <input type="checkbox"/> | <input type="checkbox"/> | If so, have plans been made for use of substitute facilities or equipment? |
| <input type="checkbox"/> | <input type="checkbox"/> | Are major materials, machines, or equipment difficult or impossible to replace "in kind"? |
| <input type="checkbox"/> | <input type="checkbox"/> | Are agency operations seasonal or otherwise subject to fluctuation? |
| <input type="checkbox"/> | <input type="checkbox"/> | Are there identified potential EDP replacement sources for equipment leasing or employee leasing, etc.? |
| <input type="checkbox"/> | <input type="checkbox"/> | Are duplicate EDP tapes, discs, cards, etc., maintained? |
| <input type="checkbox"/> | <input type="checkbox"/> | Are duplicates kept at different physical locations and updated regularly? |

Transportation

- | | | |
|--------------------------|--------------------------|--|
| <input type="checkbox"/> | <input type="checkbox"/> | Do any major exposures exist where goods are regularly shipped to the agency and possible delays or accumulation may occur? |
| <input type="checkbox"/> | <input type="checkbox"/> | Is there any potential need for major transit business interruption protection? |
| <input type="checkbox"/> | <input type="checkbox"/> | Are there any agency-controlled bridges, tunnels, roads, docks, ferries, warehouse facilities, etc., essential to the continuation of operation? |

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APPENDIX C SIMPLE RISK MANAGEMENT DECISION PROCESS

Undoubtedly, for very small local governments, the capacity to undertake . . . a systematized method to organize data for the purpose of making decisions about risk management projects is limited, and the capacity to subject all decisions to such an analysis is virtually impossible. Thus this section introduces a simple, nonquantitative method for evaluating individual projects and for looking at a risk management program as a whole. For purposes of introduction, this method is called the insurance method. The insurance method involves four basic steps, which are:

1. Risk identification
2. Insurance coverage identification
3. Risk and insurance coverage prioritization
4. Consideration of alternatives and supplements

Risk Identification

The first step is to undertake a risk identification process. You might imagine that the small local authority has obtained a risk checklist from its agent or broker and has identified its risks by completing the checklist.

Insurance Coverage Identification

After risks have been identified, the second step is to identify insurance coverages that correspond with the risks. For example, identification of the risk of fire to buildings would be matched against a standard property policy. The identification of errors and omissions risks would be matched against a public officials liability policy. Risks to boilers, heating and air conditioning equipment, and other machinery would be matched with a boiler and machinery policy.

Risk and Insurance Coverage Prioritization

The product of step 2 would be a side-by-side list of risks and coverages. Some risks will not have corresponding coverages, but this is not a bad thing necessarily. Such a finding simply points out areas where risks exist but insurance coverage does not.

The third step is to prioritize the risks and corresponding coverages. The categories would be:

- *Mandatory*: coverages/risks for which treatment is required

- *Important*: coverages or risks that correspond with serious or catastrophic outcomes
- *Useful*: coverages or risks that correspond with moderate or noncatastrophic outcomes
- *Unimportant*: coverages or risks that are neither important or useful.

Consideration of Alternatives and Supplements

The fourth step involves evaluation of alternative methods and techniques that might be employed. For example, a manager might consider whether a loss control program should be introduced in conjunction with important coverages. Or the manager might ponder whether a useful coverage might include a large deductible so the local government is paying for many of its small losses out of pocket (and thus reducing the premium dramatically). Or, in the case of risks where no insurance is available, the manager might consider whether an alternative financing mechanism might work best.

The result of the fourth step is a listing of the control and financing solutions that will be used by the local government.

Readers will realize that this process is highly flawed—at least from a theoretical perspective. It is heavily biased toward a decision to buy insurance. It does not contain decision rules (on what basis are deductible levels decided, or what is important). It also does not help sort out “how much”; that is, there is no guidance on how the programs relate to the overall purposes of the local government.

And yet, the insurance method does accomplish a number of things not ordinarily seen in organization management. First, it forces managers to systematically identify and think about risks. Second, it forces them to understand where coverages exist and where they do not. Third, it compels them to consider which are key problem areas, which are of moderate importance, and which are unimportant. And fourth, it motivates managers to consider what other measures might be undertaken to help the risk management effort succeed. So, while the method is neither scientific nor theoretically rigorous, it does impose a systematic process of thinking about risk management—which is a significant improvement on most small local government risk management practices.

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APPENDIX D SUGGESTED OUTLINE FOR A RISK MANAGEMENT MANUAL

A critical step for the development of a risk management function is the creation of a document that provides guidance and structure to the organizational practices that constitute risk management. This statement is true regardless of whether risk management assumes a traditional form or the broader “organization risk management” (ORM) form. For a traditional risk manager, a risk management manual is the principal means of communicating the purposes and practices of function. For an ORM-oriented program, a manual is a communication device, but it assumes the additional role of supporting the individualized risk management efforts that are being carried out throughout the organization.

Regardless of the context, one possible blueprint for a risk management manual would be:

- I. Risk management policies and procedures
 - A. Risk management policy statement
 - B. Statement of policy affirmation by top elected officials and appointed managers
 - C. Organizational policies affecting risk management
 - D. Risk management administration policy and practice
 1. Organization
 2. Reporting requirements
 3. Relationships
 4. Cost allocation procedures
- II. Risk assessment policy and practice
 - A. Assessment procedures, policies, documents
 - B. Physical asset exposures
 - C. Financial asset exposures
 - D. Human asset exposures
 - E. Legal liability exposures
 - F. Moral responsibility statement
 - G. Risk, claims, loss information
- III. Risk control policy and practice
 - A. Loss-prevention program statement
 - B. Claim-reporting procedures, policies, and documents
 - C. Physical asset loss-control programs
 - D. Financial asset loss-control programs
 - E. Human asset loss-control programs
 - F. Legal liability loss-control program
 - G. Statement on management of moral and ethical concerns
- IV. Risk financing policy and practice
 - A. Policy on risk retention
 - B. Policy on risk assumption
 - C. Statement on use of deductibles, retention limits
 - D. Self-insurance pool documentation
 - E. Insurance contract catalog
 - F. Leases, contracts, and noninsurance transfers
 - G. Financial risk management contracts and documentation
 - H. Financial structure of risk management function (including relationship of overall financial structure to cost allocation system)
- V. Statement on risk management program audit and review programs and procedures
- VI. Appendices
 - A. Insurance schedules
 - B. Exposure inspection checklists and support documentation
 - C. Return-to-work program guidelines
 - D. Catastrophe management plan policies and procedures
 - E. Frequently asked questions

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