

## **Conducting a Risk Management Needs Assessment**

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Conducting a comprehensive risk management needs assessment is an important activity for any organization. Besides the typical reasons, a comprehensive risk management assessment is a useful tool to uncover and identify lapses in insurable risks, unique unknown exposures, limited supply and distribution channels, to name only a few. Unfortunately, the variety of issues needed to be assessed are typically handled by various departments and personnel and often there is no one person with the knowledge, skill set, or authority to handle the entire subject properly.

When you conduct a risk management needs assessment, you must start with identifying a number of goals for the organization, and more importantly yourself, which can include:

1. Expand your thoughts to areas of the organization where you have not previously been involved.
2. Do not attempt to do the assessment by yourself.
3. Be a champion for effective communication throughout the organization.
4. Be prepared to market your function.
5. Be diligent in monitoring current programs and procedures.
6. Be open to new and developing exposures/issues, and designing, implementing, and following up on corrective action plans as needed.
7. Be prepared to fully explain the function and goal of the assessment to open previously closed doors.

### **Define the Risks to be Considered**

The cost of risk can be defined in a number of ways. You must define what you will be dealing with in the scope of your assessment. If this is not well defined, your efforts could be seen as incomplete or you could end up giving management a false sense of security that their risk issues have been identified, when you did not include them in your scope.

Risk can involve various aspects of the company's overall operations and can be identified into four main quadrants of risk to include: Hazard, Operational, Financial, and Strategic. Each area stands alone, but they are interdependent, and each aspect should be considered to effectively evaluate the total cost of risk.

1. **Hazard risk** – Hazard risk comprises, primarily, the traditionally insurable risks. These include fire, products liability, and a wide range of other sources of loss.
2. **Operational risk** – Operational risk arise out of daily operations (supply chain, quality control, cost overruns, faulty workmanship, product tampering and product recall, compliance with various regulatory agencies, etc.).
3. **Financial risk** – Financial risk concerns money. Included in this category are credit risk, cash-flow management, the cost/benefit ratio of research and development, economic instability, the cost of commodities or raw materials, and tax minimization.
4. **Strategic risk** – Strategic risk concerns business decisions. This includes anything that impacts your clients and/or customers' loyalty, patent infringement, the viability of partners with which your form joint ventures, the professional development of your organization's staff, the success or failure of any mergers and acquisitions, and risk management itself. (Marsh 2-4)

## The Risk Management Process

The Associate in Risk Management (ARM) program has a definition for the risk management process. For insurance professionals, the most common risk management definitions are taken from the Insurance Institute of America (IIA) Associate in Risk Management (ARM) series (IIA 4-5). There is a definition for risk management as a managerial or administrative process and another for risk management as a decision-making process.

1. "Risk management as a managerial or an administrative process is defined as a process that includes the four functions of planning, organizing, leading, and controlling the organization's activities to minimize the adverse effects of accidental and business losses on that organization at reasonable cost."
2. "Risk management as a decision-making process is a sequence of the following five steps:
  - 1) Identifying and analyzing exposures to accidental and business losses that might interfere with an organization's basic objectives;
  - 2) Examining feasible alternative risk management techniques for dealing with those exposures;
  - 3) Selecting the apparently best risk management techniques;
  - 4) Implementing the chosen risk management techniques; and
  - 5) Monitoring the results of the chosen techniques to ensure that the risk management program remains effective."

The traditional risk management model is reactive. To conduct a truly effective risk management needs assessment, you need to go beyond traditional risk management. The article "*Beyond Traditional Risk Management*", from the ASSE Risk Management/Insurance Practice Specialty Spring 2004 newsletter, provides additional discussion on this subject. This article points out that there is considerable opportunity for risk management professionals to expand their influence into

business risks (market risk, credit risk, operational risk, strategic risk, liquidity risk, etc.) – areas where risk management professionals have often been excluded. Senior management perceptions will influence how much involvement the risk management professional will have, and some organizations will be more receptive than others. Many of these business risk areas are not addressed in this article.

One needs to truly look into one's organization and develop an assessment and evaluation of not only the known and traditional sources of risk, but also to look deep into those other potential sources of risk to evaluate what may happen and how is it currently protected to prevent an adverse condition. To fully perform a risk management needs assessment, an organization has to not only look into the reactive, traditional causes of risk, but also needs to evaluate the unique and seldom performed operation or process to get a full grasp of the risks involved.

## Involve Others

Depending on your organizational structure, there will be different people who need to be involved in the assessment. This can be problematic if you do not have adequate authority to evaluate someone's programs and identify issues. The person responsible for managing a given function is not always the right person to be conducting the assessment. After all, if corrective actions or changes are needed, it might put the manager into an awkward position of explaining why the improvements were not made earlier.

Some of the parties to be involved in the process include, but are not limited to:

1. Human resources - loss information, hiring practices, disciplinary program, EEO, ADA, etc.
2. Occupational health – types of programs and exposures, evaluate MSDS for anomalies, etc.
3. Psychological services – post-crisis counseling psychological screening, employee assistance program, etc.
4. Risk management operations – current programs for risk, alternative markets and programs, industry trends, etc.
5. Loss control/safety – current programs, issues and alternatives, source of losses, regulatory requirements, etc.
6. Legal – union issues, regulatory changes, product liability, source of large claims, current trends, etc.
7. Design – what's planned, why configured in a certain way, how the process works, etc.
8. Operations – how things are done “actually”, workable solutions, problem identification
9. Claims personnel – cost of losses, regulatory issues, past history, etc.
10. Executive level – potential changes in operations, future ventures, exposures unknown at lower levels, etc.

## Components to Address

There are a wide range of issues that should be considered in a needs assessment. The list of issues can become longer and longer depending on how large of a scope is allowed. Some areas to be considered include:

1. **Understanding the business operations** – A full, detailed understanding of the functions and goals of each department, area, division, and location of the company is required. Without complete understanding of the functions and goals, the assessment will not include all relevant risk management concerns. This understanding will assist in evaluating the company culture in

various areas, barriers to change, areas of cooperation, and identify how the process can best fit into the overall company goals.

2. **Hiring practices** – There are many items to be evaluated with respect to hiring practices. This can include the application process, reference checks/background checks, interviews, Americans with Disabilities Act (ADA) ramifications, EEO issues, skill assessment and needs, language barriers, and many other items. This is an area given the label as “a necessity but not crucial” in many organizations. Remember, all companies hire their employment problems; if an organization has high turnover rates, is this an acceptable cost of risk? Are these employees the same ones that are driving the workers’ compensation costs, poor production, low quality, missing inventories?
3. **Medical, drug and functional capacity testing** – Medical, drug and functional capacity testing are important issues to consider. Initial and periodic screening methods must be established to adequately screen at-risk applicants. This can be a tricky issue given the variety of regulations that apply to this situation. Periodic medical evaluations should be completed according to what is required by regulations; additional medical evaluations might be appropriate. Drug testing is important when you consider that “More than 10% of full-time workers. . . were characterized with abuse of or dependence on alcohol or drugs in 2003.” (National Safety Council 12) Functional capacity testing is a developing area where the capacity of the individual can be evaluated with respect to his/her ability to do the given job. The evaluation must relate to the specific job in question. What one employee does can affect other employees, production, and critical timelines.
4. **Orientation procedures** – Relevant subjects must be covered in a timely manner. Orientation procedures must be standardized. You must track that each employee received new employee orientation and each specialized subject that is relevant to the employee’s position. A person must also be orientated to his/her work area; proper set up of their desk/cubical should be included for those working in an office. Without the proper orientation procedures the costs of risk increases, not only for the traditional workers’ compensation area, but also for other types of loss.
5. **On-going training and evaluations** – The need for on-going training and evaluations can not be underestimated. Employees of many organizations fall into habits, allowed by supervision, that are not consistent with initial training that was provided. A complete risk management evaluation will determine if methods of on-going training and evaluations are adequate to determine if proper procedures are actually being followed.
6. **Site evaluations** – Evaluating conditions in the field is essential to a proper assessment. How it is performed is crucial. Most traditional site evaluations are focused on the physical controls of hazards. These site evaluations analyze the programs and normally what the person can see during the time of the visit. However, as well as programs might be written, and as well as documentation may appear, you never know how programs and procedures are implemented without actually evaluating them in the field. There are limits in most organizations on the time allowed to conduct site evaluations. You must identify, in advance, those items that must be evaluated and investigated. These items can include: employee interviews, challenging who is operating machinery, knowledge of the programs, demonstration of the program elements, observing behaviors and actions, to identify a few. Site evaluations are often limited to a specific

duration. Therefore, priorities must be established to accomplish the main goals of the evaluations given the time constraints.

7. **Program evaluations and audits** – All company programs should be reviewed and consistently audited as it applies to each area or location. For programs that require regular auditing, you must determine how often, and by whom, evaluations and audits are conducted. Audit results must be adequately reviewed by personnel who understand the function. A significant issue to be addressed is the tracking method for identified issues. If you do not track your recommendations and how they are addressed, your evaluation/audit program will fail. All of these items need to be evaluated to have a full understanding of the risks involved in the organization. If an organization has all of the “right” programs but does not have the continued implementation, then what risks are the company accepting?
8. **Communication channels** – Evaluation of the communication channels is an often overlooked item when evaluating risk. Communication channels not only include employee supervisor but also across supervisor lines and across area/department/location/division lines. Communication needs to be both vertically and horizontally. What one area of the company is performing can adversely or positively effect another division or location. Sources of problems and solutions need to be able to be communicated throughout the organization so that other area can learn and prevent similar issues. Controlling risk can not be accomplished if this communication channel is not operating properly. If a plant manager learns of a problem at another location but thinks that is will not happen at this location, and therefore does not tell his/her staff, they may be taking on unnecessary risk.
9. **Management commitment** – This area is always talked about but rarely evaluated and commented upon. All organizations understand the value of management commitment, but few know how to measure it or properly implement it. To perform a risk management needs assessment, an evaluation of the management commitment is needed. This includes resource allocation, support, demonstrated leadership, and continuous emphasis. Areas where there are barriers or hindrance to the overall program have to be identified and alternatives identified.
10. **Disciplinary procedures** – You must address whether there is a disciplinary program in place, whether policies/procedures are consistently enforced, and how the whole issue is reviewed. One significant area of liability is inconsistent application of existing policies and procedures. Mixed enforcement at any level opens a Pandora’s Box of issues and risks that should be addressed and corrective action plans implemented.
11. **Loss analysis** – The most important issue is that you have adequate access to relevant data. This data must be credible and you must understand data. Data credibility issues are often complicated by improper cause or nature coding, or coding at an insufficient level. An “other” cause code is not relevant to determining the true cause of loss. If the “other” category is too high (for example, more than 5% -- this is determined by each entity), your data, and any analysis of it, is not relevant. You must understand the data. Without proper understanding of the data, you might miss a prime opportunity to explain the significance of the data. You must understand the difference between amounts paid, incurred, reserved, and fully developed and how the different categories affect the company and its risk.
12. **Citation/regulatory review** – Organizations are subject to a variety of regulations. You must determine which regulations apply, and what citations have been issued. This information must

be shared across company lines. One key issue is whether required correction action is still being followed. Another issue to consider is the exposure to repeated offenses. Repeated offenses are often subject to multiples of the initial fines.

13. **Workers' compensation claim procedures** – Workers' compensation claim procedures must be evaluated. Carrier and/or third party administrator (TPA) procedures must be monitored and reviewed. Claim reviews must be conducted for a representative sample of claims to determine if best practices are being applied to the given claims. Relevant metrics must be determined and tracked to judge carrier or TPA performance. There must be specific effort directed at workers' compensation fraud activities. Medical management organizations exist to review medical treatment relative to established guidelines and to monitor billing relative to established fee schedules.
14. **Liability claim procedures** – Liability claim reviews should occur with all of the relevant parties. There should be a roundtable process early in the process to gather relevant information. Other issues to be considered include monitoring of the carrier/TPA, the use of attorneys (inside counsel or contract counsel), and claim settlement authority levels.
15. **Employment practices** – The broad subject of employment practices must be evaluated. This includes sexual harassment, wrongful termination, racial harassment, and other issues. Establishing requirements for mediation before litigation can be helpful.
16. **Corrective action plan process** – The assessment should include an evaluation of whether a corrective action plan process exists. The process should address a procedure for elevating specific issues to higher levels of management. Formal plans should be required for large dollar/exposure cases. The plans must address loss causes and establish corrective action plans, and there must be an audit process to insure effective implementation of the plans.

## Communication

Regular communication between affected parties can not be underestimated. Reports need to be developed and distributed to the appropriate levels of management on the appropriate frequency. Marketing is needed to obtain and maintain management support. Information must be summarized for management into a language and format that is meaningful for them.

The creation of an annual risk management report is one method of marketing the results of an assessment. Such a report should include:

1. An executive summary;
2. A summary of the main focus and goals of the assessments;
3. A detailed description of any changes or operations that have impacted the organizations risk both positively and negatively;
4. A description of activities and results generated by each functional group of the risk management department;
5. A description of risk and how that risk is managed;
6. Loss trending and an analysis of why the results are improving or deteriorating;
7. Benchmarking against other similar entities;
8. Planned actions to improve the risk management of the organization;
9. Status of previous action plans and recommendations; and
10. Clearly defined responsibilities for action plan items and completion dates.

These reports must be generated on a meaningful timeline. An annual report should be published within a quarter of the end of the calendar/fiscal year.

## **Conclusion**

Conducting a comprehensive risk management needs assessment is a very important activity for any organization. Doing it right can greatly enhance the effectiveness of your risk management program. Doing it wrong can subject you to a significant risk that you had not considered and are not prepared to respond to. Just completing an assessment will increase awareness and understanding, and identify areas for further review and improvements. No matter how the risk management assessment is completed, unless it is shared with the organization and action plans are fully developed and followed up upon, the goals set out in the beginning of the assessment will not be met.

## **Bibliography**

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