THE PRACTICAL APPROACH TO RISK PREVENTION AND MANAGEMENT OF INSURABLE RISKS

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It is not possible in a short talk like this to cover any subject in great detail. However, I would like to run through a range of issues.

My aim, as those of you who know me, will appreciate, will be to stimulate debate and questions. Not only because that will be more interesting for the audience but also because I believe that those two words sum up my approach to risk management namely debate and questions.

DEBATE

No one knows everything. In fact Confucius defined knowledge as knowing what you do not know.

Therefore excluding certain parties, individuals or organisations from the risk management debate means that there will be inadequate and incomplete analysis.

By documenting the debate process, areas of further analysis are captured and made subject to further specific debate.

I believe that when looking at the issue of risk everyone should have the opportunity to give their views.

Not only senior managers but also staff and not only internal individuals but also suppliers, customers and advisors. In effect a 360º risk observation process.

Some of you may know that I am a very keen yachtsman and last year I sailed my boat across the Atlantic. If I had only maintained observation say through 250º I would have always run the risk of collision and accident from failing to complete the full rotation.

Inviting such participation should not be seen as a sign of weakness but as a sign of confident strength in wanting to protect your business.

I use the word debate in its fullest to include:

- Discussion at meetings.
- Responses to questionnaires.
- E-mails and similar written communications
- Electronic forums such as chat groups.

Debate should take place within the business with:

- Customers
- Suppliers

As well as what can be termed “protection” suppliers and advisors such as banks, insurers, brokers, loss adjusters, risk consultants, accountants.

And also with:

- Competitors

I believe that the competitor element is one that is often overlooked. However, often when dealing with a business interruption claim it is the most crucial aspect. Some competitors will move in very quickly and take over your market share and you will never get it back. Others recognise that to some extent your organisation is their insurance policy and vice versa. I dealt with one major explosion in Scandinavia several years ago where there were only two producers of a chemical in the world. Despite being serious competitors and without breaching any anti-trust regulations the competitor was willing to do two things.

Firstly, in the early days it sold some of its own stock to our insured so that crucial clients could be retained.

Secondly and this perhaps is the most important issue, the competitor requested a technical meeting to discuss the cause of the explosion. The competitor was very concerned that a similar loss could occur to them and without infringing patents and other such confidential details the two organisations met to benchmark on safety.

QUESTIONS

Some professionals take the view that you should never ask the question unless you know the answer. Barristers in particular are very fond of this phrase.

There is the tale of a Barrister prosecuting an individual in Court for theft. The Accused had been caught with a significant roll of large denomination notes in his possession. The Barrister said to him “Well, I suppose you always walk around with a large sum of money in your back pocket, do you"? At which the Accused said "Yes Guv" and proceeded to pull a roll of some £1,000 in £20 notes from his back pocket.

At this, once the jury had stopped laughing, it became clear that the prosecuting barrister had made an error and had in fact helped the Defence. The prosecuting barrister had asked a question that he did not know the answer to and you can understand why the Legal profession are so nervous of this practice.

However, such nervousness should not extend to the risk management and insurance community. Some people say that the most important personal attribute to be part of the Risk Management and Insurance Community is an "Enquiring Mind". I agree that some people take this to ridiculous extremes and become like the Spanish Inquisition and some are seen as very "Nosey Parkers". However, the important point is that questions should be seen in a positive light leading to clarification of uncertainty.

CLASSIFICATION OF RISKS

Over the past 25 years or so as a practising Chartered Loss Adjuster I have met individuals at times of major stress in their lives and in the life of their organisation.

Their businesses have suffered a serious loss and people may have died or been injured, remaining staff have concerns about their future wages, suppliers are concerned about their future sales and customers often find that they have extra cost to incur in order to cope with the interruption of product supply.

As I said earlier, this paper does not seek to rely on existing academic work relating to Risk Management Theory and Practice. It is my "soap box". From my soap box, I feel that a useful categorisation of risk is into visible and invisible.

<u>Visible.</u>

Visible Risk includes fire damage, explosion, flood, storm etc. Generally it causes physical damage as well as financial loss although not always. An example would be a fire at a suppliers premises causing financial loss to one of its customers who are dependant on a product which is to be incorporated in their product for resale. The customer has not suffered physical loss but has been exposed to financial loss as a result of the visible damage that has occurred at their suppliers.

How often do Risk Managers sit with their production colleagues and examine the sourcing of parts and the extent to which the suppliers are dealing with their visible risks.

Invisible

Here I would include topical invisible risks such as fraud, financial mis-statement, professional negligence, extortion and so on.

Later on I will seek to draw the distinction in both these categories of the location of the risk as between internal and external.

However continuing along with the experiences I have had visiting organisations, some had prepared themselves for the disaster that had occurred.

That preparation had included analysis, planning, and a significant amount of debate and conferring with their insurance brokers and insurers. At the time of the loss therefore, not only were the insured organisation aware of the recovery tactics that could be employed but also these had been reviewed and agreed with the broker and the insurer who were therefore able to assist more readily the organisation's recovery. However, that has not always been my experience and many organisations that I have visited had abdicated their responsibility to their brokers and insurers. This in my view is a crucial difference.

While all organisations had transferred the insurable risks to their insurer via their broker, those that had not conferred and agreed contingency plans had in effect **abdicated** responsibility to their broker and insurer. They had not only transferred the risk but also the responsibility.

I have found that organisations in the "abdication" camp have always had a much harder time coping with the recovery. Some even failed to convince key staff, significant suppliers and customers that they could depend on the recovery actually being accomplished.

So when I counsel debate and questions as a practical Risk Management approach I would say that from my experience great value is obtained by including the broker and the insurer in that process.

STAKEHOLDERS

The Risk Management process should be of interest to all of the stakeholders in an organisation.

The stakeholders will include: -

- Shareholders
- Directors
- Senior Management
- Staff

- Suppliers
- Customers
- Brokers
- Insurers
- Loss Adjusters
- Banks
- Auditors
- Economy

I have probably missed some other interested parties but again that is the whole point of having questions and debate as the central features of a Risk Management exercise.

While all these stakeholders do have an interest in an efficient Risk Management process I believe that the responsibility for such a process should unquestionably be with the board of directors. If the Chairman and the Directors do not have a copy of your business recovery plan at home in their bedside cabinet, and if they have not reviewed debated and questioned its content then the organisation has not fully embraced the important concept of Risk Management and is exposed.

RISK MANAGEMENT MATRIX

Each organisation is different but a standard approach to identifying risk is helpful. Again I stress that this is not an academic paper on Risk Management and I know that there are numerous frameworks, protocols, questionnaires, risk based computer programmes etc available.

However, whichever framework you choose the important point from my perspective is that you do choose one and then you work hard to follow it.

From my perspective the matrix formed by comparing invisible and visible risks with internal and external causes is a simple and useful starting point

	Invisible	Visible
Internal		
External		

Matrix 1

Through the process of debate and questions with all the stakeholders that I have mentioned, it should be possible to place in the matrix each and every risk that is thought of.

For example, in the invisible internal square, you may have risks such as fraud, loss of reputation caused by behaviour of senior personnel, critical illness of key employee, breach of corporate governance.

In the external invisible square might appear issues such as audit failure, product tamper followed by extortion demand is also an invisible external.

Internal visible could include arson by or sabotage by employees, breakdown or accidents caused by a cut back on the maintenance budgets leading to inadequate inspections and maintenance.

An external-visible could be the act of terrorist, vandals. It could include defects in products that have been purchased that malfunction and cause a fire. And it most certainly includes weather related risks.

These are just examples and of course each of you will have your own thoughts on how this framework will apply to your organisation.

Identifying the risks is one thing but how to deal with them is clearly the next step.

I have found that organisations that treat the handling of risk as a problem for the entire organisation tend to recover the best from a problem. Having therefore identified the risks using the framework it is necessary to establish the probability and consequences of each one. This is an area where common sense is normally the best approach although I recognise that obtaining assistance from experts such as brokers, insurers and risk consultants makes sense.

You will then decide which risks you will retain and those which you will pass on to your insurers. As I mentioned earlier, whilst you can transfer the risk it is vital that you do not transfer the responsibility.

Therefore a detailed business recovery plan should not just say against fire for example "insured problem with the insurers" etc. It should clearly specify how your business will recover from a fire. Usually bringing the key internal personnel together is a useful way to start off a brainstorming session to run through a lot of questions of a "what if" nature. Brokers, Insurers and Loss Adjusters have considerable experience in this area and normally have a series of checklists which would deal with 80% of most issues.

In considering the approach to dealing with the risks identified in the matrix mentioned earlier, I would like to suggest another matix.

Consequences of Risk

Reaction to Risk	Physical	Financial
Protections		
Recovery Plan		

Matrix 2

When looking at the consequences it may be helpful to consider whether they are physical and/or financial. By physical I mean actual damage to property and by financial I have in mind the cost that the organisation will suffer or be liable for. Clearly a physical loss would also be a financial cost although a financial loss may not necessarily involve any physical loss. So one axis of my matrix relates to the consequences of the risk the other axis relates to your reaction to that risk. Although you could probably come up with numerous reactions for the purposes of having a 2 x 2 matrix I have chosen two reactions that is protection and recovery plan. Again these are not mutually exclusive, as you will undoubtedly want to protect against fire by various measures such as good security, proper fire extinguishing appliances and staff training and a good insurance policy for the correct values. At the same time you will want a recovery plan to enable your organisation to respond as part of the business recovery operation after the event.

Having identified the various risks you are exposed to these can be analysed in terms of protections and the way in which you would want to respond in your Business Recovery Plan. This is clearly a lot of hard work and I have been into organisations where they couldn't be bothered to do the whole job and that led to inadequate recovery or a very slow recovery back to the position the business was in before the loss.

There are of course numerous books articles, courses, Risk Management products available and these should all be considered as well as the advice and input from your Brokers, Insurers and Loss Adjusters as well as some of the other stakeholders that I mentioned earlier.

An organisation without a Business Recovery Plan is driving dangerously and I hope that my small talk will be of help in encouraging debate to increase the levels of Risk Management in your economy.

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11th July 2002