THE NATIONAL ALLIANCE
for Insurance Education & Research

Elements of Risk Management

Welcome

Insurance and risk professionals today need learning choices from many sources. As time and economic pressures bear down on everyone, The National Alliance continues to push forward with excellent online programs, carefully designed to fulfill your professional development needs.

In the pages that follow, be sure to read and understand the requirements for completing your course. If you have any questions, you may contact us via the link on the bottom navigation bar.

I hope you enjoy your journey into online learning. Thank you for choosing a National Alliance online course!

William T. Hold, Ph.D., CIC, CPCU, CLU
President

Our promise of a distinctive learning experience.

You may wish to become proficient in analyzing insurance policies, or simply wish to keep up with important information about the National Flood Insurance Program.

Throughout your career you can count on The National Alliance Online Courses to provide you with practical, high-quality education programs.

Internet Browser Warning

This course is designed to work with Microsoft Internet Explorer 6.0 or above, with JavaScript enabled. Students using Firefox or Google Chrome will have difficulties with interactive pages and self quizzes.

If you need technical help with your browser, please contact the Online Help Desk.

Did you print your student instructions when you registered?

Before you get started, be sure you have your student instructions for this course. The student instructions for each of our programs are always available at our website:
www.scic.com/online_courses/general/student_instructions

CISR

Log On ... It's all about you!

Your online Document of Certification and other important National Alliance professional education information is in one convenient place on MyPage, including:

- Contact information
- CE certificates (download online)
- Course history
- Exam results
- When your next update is due
- Membership dues status (you can pay dues online)
- New program offerings

View your MyPage on our website, www.TheNationalAlliance.com/MyPage.

Elements of Risk Management

Insurance professionals need training in the risk management process for two reasons. First, insurance is an integral part of their client's overall risk management program. Second, services provided by carriers, agencies and brokerages are often significant items in the organization's cost of risk.

Our course will cover each of the five powerful steps in this process, which protects not only the organization's assets, but also its mission and its brand.

Why is the Risk Management Process Important?

The risk manager's primary responsibility is to protect the organization's assets and financial wellbeing. The risk management process provides the methods by which this can be accomplished. An effective risk management program allows an organization to preplan for losses with tolerable uncertainty and to have a plan in place to manage and control losses after they occur.

Risk management is also important to the insurance professional.

- If you help clients identify their potential exposures to loss, you are engaging in Step 1 Risk Identification.
- If you suggest to a client that they implement a safety committee, repair a broken handrail, put a lock on a fence or not engage in an activity, you are applying Step 3 Risk Control.
- When you recommend insurance protection to cover a loss, you are applying Step 4 Risk Financing.

Insurance professionals taking this course can study the information while noticing new ways to relate to the risk managers that they serve.

By offering solutions for your customer's overall risk management program you can:

1. Establish credibility and create a professional image;
2. Improve customer retention;
3. Increase number of customer referrals;
4. Reducing Errors & Omissions exposures; and
5. Increasing income possibilities when risk management is provided to clients on a fee basis.

A Solid Foundation of Insurance Research

The Risk Management Essentials book, published by The National Alliance Research Academy, was used as a source for developing this course. Risk Management Essentials is practical and extremely thorough, with nearly 500 pages. This guide allows readers to learn the basic principles, terms, and concepts for the various risk management activities: identification, analysis, control, finance, and administration. This study focuses on the key areas of financial statements, loss data, claims management, information technology, and enterprise risk management. A Q&A CD study guide is included to enhance the learning process. The book may be ordered from The Academy bookstore at www.TheNationalAlliance.com.

How to Receive Credit

You may use this course to earn CISR or CSRM designation update credit or continuing education credits/hours (CE) towards your state insurance license renewal.

Note: The requirements for receiving CISR or CSRM update credit are not the same as the requirements for receiving state CE credit.

If you are updating your CISR or CSRM designation only:

Complete each of the self quizzes and the review test with a score of 70% or higher for each.

- Multiple attempts are allowed for the review test.
- A proctor/monitor is not required when completing the review test.
- An affidavit of exam is not required after passing the review test.

If you also plan to request credit/hours for state insurance license renewal:

Complete each of the self quizzes and the review test with a score of 70% or higher. Then, complete the proctored final exam with a score of 70% or higher.

- Three attempts are allowed for the final exam.
- A proctor/monitor is required when completing the final exam.
- An affidavit of exam is required in order to receive credit for passing the final exam.

THE NATIONAL ALLIANCE
for Insurance Education & Research

Taking the Review Test for Designation Update Credit

The review test is a randomized test with 20 questions, designed to let you know how well you have understood the course material. Multiple attempts are allowed for the self quizzes and review test.

- You must pass all self quizzes and the review test before taking the final exam.
- You may navigate to the **Review Test and Final Exam area** by clicking on the Course Status link above. The link to the review test will become available when all self quizzes show a score of 70 or above.
- When you have passed the review test, your CISR or CSRM record will reflect 8 hours of credit towards your annual designation update.
- The review test alone does not earn continuing education credit for state license renewal.

Final Exam For State Continuing Education Credit

The final exam for state continuing education credit is a randomized test comprised of 50 multiple choice questions worth 2 points each. It is designed to test your ability to apply what you have learned in the course. Three attempts are allowed for the final exam for this course.

Affidavit of Exam and Continuing Education Request Form

The final exam lasts one hour, and must be completed in the presence of a disinterested third-party proctor/monitor. Three attempts at the final exam are allowed, and a passing score is 70% or higher. You and/or your proctor are responsible for submitting the Affidavit of Exam and Continuing Education Request Form to The National Alliance. (In New York, the state approved monitor is required to fax/mail the Affidavit of Exam and Continuing Education Request Form.)

Fax the Affidavit of Exam and Continuing Education Request Form to the fax number printed on the cover sheet.

Please send the original affidavit by mail (address also printed on the affidavit cover sheet.) We strongly recommend that you keep a copy for your records.

Some students will have no need to request Continuing Education credits for an insurance license, and wish only to earn update hours for the designation. Please send the CE Request Form even if you are not requesting CE hours/credits for insurance license renewal. Check off the "No CE" box at the bottom of the form.

Note: You will receive an email reminding you to send in the affidavit if you pass your exam with a score of 70 or above. Do not submit an affidavit for an unsuccessful exam.

THE NATIONAL ALLIANCE
for Insurance Education & Research

Curriculum Support

Faculty members from The National Alliance for Insurance Education & Research are assigned to take emails from students participating in the online courses.

Our faculty are experienced practitioners and teachers in the industry. We ask them to respond to each email within 24 hours, or before the end of the next business day.

The course mentor will be happy to clarify any portion of the curriculum for you if you need help.

Make sure you have carefully reviewed the course curriculum and clearly note the page or self quiz question number when you contact a course mentor.

Help Desk

The mentors will refer any computer issues you have to the Online Help desk.

National Alliance staff are available by phone or email for technical support issues.

online@scic.com.

To phone the Online Help Desk call: 800-633-2165 and select option 2.

Monday through Friday
8:30 am to 5:00 pm
Central Time

Course Study and Exam Preparation

Have you ever thought about how you learn? The study aids listed below will help you determine your progress and test your understanding of concepts and examples presented in the course.

- **Learning Objectives**: Learning objectives are designed for managing your own learning. The learning objectives for the course are listed at the beginning of each topic. The learning objectives are indicated throughout the course pages as well. At the end of the course, you will have the opportunity to read the learning objectives again, and see how confident you feel about each one.

- **Self Quizzes:** Self Quizzes are another learning management tool. You are required to pass each self quiz with a score of 70 or above before moving forward in the course, and you can launch a self quiz as many times as needed. To print the score page of your self quiz, click on Assessment Results, then right click on the page. The Assessment Results page makes an excellent study aid.

- **Glossary terms and definitions:** Glossary terms and definitions are critical to insurance and risk management professionals, and a key study aid for your online course. To define a term, click on the Glossary link above. Definitions of newly introduced terms will also be included on the course pages.

- **Knowledge Checks:** Knowledge checks are application level questions. By attempting to apply the concepts of the course, you will better prepare yourself for the final exam. Make sure you attempt each knowledge check in the course.

- **Course Mentor:** And don't forget to email the Course Mentor with your questions about the curriculum. Our faculty members are distinguished producers and risk managers who currently work in the insurance industry. The mentors are happy to explain and clarify the concepts in the course. They will return your email on or before the next business day.

Frequently Asked Questions (FAQs): Please see the following guides for more information.

General Question FAQs: http://magma.magma.scic.com/Elearning/Intro/GeneralQuestionFAQs.html

Computer/Technical FAQs: http://magma.magma.scic.com/Elearning/Intro/ComputerFAQs.html

Final Exam FAQs:
http://magma.magma.scic.com/Elearning/Intro/FinalExamFAQs.html

Continuing Education FAQs:
http://magma.magma.scic.com/Elearning/Intro/CEFAQs.html

FLORIDA RESIDENTS ONLY

An entity that is required to be licensed or registered with the Florida Office of Insurance Regulation but is operating without the proper authorization is identified as an unauthorized insurer. All persons have the responsibility of conducting reasonable research to ensure they are not writing policies or placing business with an unauthorized insurer. Any person who, directly or indirectly, aid or represent an unauthorized insurer can lose their licenses or face other disciplinary sanctions. Please see section 626.901, Florida Statutes, to read the laws. Lack of careful screening can result in significant financial loss to Florida consumers due to unpaid claims and/or theft of premiums. Under Florida law, a person can be charged with a third-degree felony and also held liable for any unpaid claims and refund of premiums when representing an unauthorized insurer. It is the person's responsibility to give fair and accurate information regarding the companies they represent.

THE NATIONAL ALLIANCE
for Insurance Education & Research

Lesson 1 - The Risk Management Process

Lesson 1 Intro p1 (ELR)

In this section, we define the risk management process and then we define each step in the risk management process.

We will also preview the concepts that will provide the foundation of each section of the course. You can use this section later as a review tool.

Note that we take time to define Cost of Risk (TCOR) early in the course. TCOR is a critical metric for risk managers and the organizations they serve.

Lesson 1 Intro p2 (ELR)

Lesson 1 – Learning Objectives

After completing this lesson, you will be able to:

1. Define risk, the types of risk and risk management.
2. Discuss the terminology used by risk managers.
3. Identify the five steps of the risk management process.
4. Describe the components of Total Cost of Risk and how Total Cost of Risk is used by risk managers.

Lesson 1 Topic A - Definition of Risk Management

Lesson 1 Topic A Definition of Risk Management p1 (ELR)

Risk management has many definitions. For the purpose of this course, the definition of risk management is as follows:

"The process of managing uncertainty of exposures that affect an organization's assets and financial statements using five steps: identification, analysis, control, financing, and administration."

Lesson 1 Topic A Definition of Risk Management p2 (ELR)

Definition of Risk Management continued

Learning Objective: Define risk, types of risk and risk management.

"If you fail to plan, you plan to fail." As risk managers, we focus on two primary responsibilities:

1. Protect the assets of the organization, and
2. Protect the financial statements of the organization; thereby, protecting its solvency and viability (its bottom line)

Lesson 1 Topic A Definition of Risk Management p3 (ELR)

Benefits of an Effective Risk Management Program

Learning Objective: Define risk, types of risk and risk management.

As you go through the course, you will begin to see that a comprehensive risk management program is designed to help management increase the value of the organization, and to support the achievement of the organization's goals.

Identify the organization's exposures and the risks associated with those exposures

An effective risk management program identifies not only the assets the organization has exposed to loss but also the events that could reduce the value of those assets. With this information, the organization can implement risk control techniques to reduce the frequency or severity of losses.

Determining the Organization's "Appetite" for Risk

Risk appetite is the amount of risk exposure the organization is willing to accept or retain. It refers to an organization's willingness to retain all or part of an exposure to loss.

Reduce and mitigate losses and associated costs

Reducing both the frequency and severity of losses will positively impact the profitability of an organization. Money not spent on losses is money available for the organization to use elsewhere. Fewer losses and smaller losses can lower insurance rates as well as the cost of other methods of risk financing.

Allocate costs associated with its risk and losses

Cost of Risk is a concept to which you will soon be introduced. An organization may choose to allocate, "charge back" the cost of managing risk to the various departments or divisions based on their losses.

Improve the organization's ability to budget and plan

An organization that has analyzed its data to project its expected losses can budget for those expenses and plan accordingly.

Integrates risk control and safety

Here is an example: Any aspect of the firm's safety program can be rationalized and evaluated according to the risk control technique that it employs. The installation and maintenance of a sprinkler system for example, is a control technique which (hopefully) reduces the expected severity of fire damage and protects life. Fire drills are intended to reduce the severity of an accident by protecting life.

Adds value

The cost of risk and the cost of surviving unplanned risks obviously directly affects a company's bottom line. The risk management program should keep ordinary losses to the minimum and allow the business to plan for expected losses. In the long term, this should add value by protecting the rate of increase in the company's assets.

Please refer to Lesson 1 Topic A Definition of Risk Management p4 (ELR) to complete the Knowledge Check at this time.

Lesson 1 Topic A Definition of Risk Management p5 (ELR)

The Risk Management Process continued

Learning Objective: Identify the five steps of the risk management process.

We've stated previously that there are five steps to the risk management process. We will study each step in detail. Click on each of the five steps below for a description.

Identification

The process of identifying and examining exposures of an organization.

Example: A loss control specialist conducts a physical inspection at a job site.

Analysis

The assessment of the potential impact of various exposures to an organization.

Example: A risk manager reviews loss data from slip-and-fall claims in order to predict future losses.

Control

Any conscious action or inaction to minimize, at the optimal cost, the probability, frequency, severity, or unpredictability of loss.

Example: Management institutes new machine safety training for all employees.

Finance

The acquisition of internal and external funds to pay losses at the most favorable cost.

Example: The company CFO budgets $250,000 for retained losses.

Administration

The implementation of the desired actions and risk management plans and monitoring, examining and evaluating the results.

Example: The risk manager monitors the effectiveness of new safety equipment on injury claims.

THE NATIONAL ALLIANCE
for Insurance Education & Research

Lesson 1 Topic B - Risk Identification Concepts

Lesson 1 Topic B Risk Management Concepts p1 (ELR)

Learning Objective: Identify the five steps of the risk management process.

Step 1: Risk Identification

The process of identifying and examining exposures of an organization.

Risk identification is the most important step of the risk management process. An exposure to loss cannot be analyzed, controlled or financed unless its existence is first known.

Lesson 1 Topic B Risk Management Concepts p2 (ELR)

Risk Identification Continued

Learning Objective: Identify the five steps of the risk management process.

An organization's exposures to loss come from sources both internal and external to the organization. In addition to identifying the exposures internal to the organization, it is important to identify those exposures created by external sources such as suppliers and distributors, customers, regulatory authorities and competitors.

Internal Exposures

- Employees
- Products or Services
- Property and Other Assets
- Activities

External Exposures

- Suppliers and
- Distributors
- Customers
- Regulatory
- Authorities
- Competitors

Lesson 1 Topic B Risk Management Concepts p3 (ELR)

Risk Identification Continued
Learning Objective: Identify the five steps of the risk management process.

We'll study these concepts in Lesson 3 Risk Identification.

General Classes of Risk

Six general classes of risk affect all organizations, regardless of the economic activity of the organization.

General classes include:

Economic
Legal
Political
Social
Physical
Juridical risk

Logical Classifications

Exposures to loss are divided into four categories of logical classifications. The four logical classifications of risk we will study are:

Property
Liability
Human Resources
Net Income

Identifying Risk

Ten methods for identifying risk that will be studied in this course are:

Checklists/surveys/questionnaires
Flowcharts
Insurance policy reviews
Physical inspections
Compliance reviews
Procedures/policies reviews
Contract reviews
Experts
Financial statement analysis
Loss data analysis

Lesson 1 Topic B Risk Management Concepts p4 (ELR)

Step 2: Risk Analysis

Learning Objective: Identify the five steps of the risk management process.

The assessment of the potential impact of various exposures to an organization.

In the Risk Identification step, risk exposures are identified.

In Risk Analysis, data is collected and analyzed using both qualitative and quantitative analyses. This information is used by risk managers to make the appropriate and most effective risk control, risk financing and risk administration decisions for their organizations.

For example, data about slip and fall claims, would be systematically collected and tracked. Analysis would be used to quantify the need for further action to reduce these losses and to estimate their future costs.

Lesson 1 Topic B Risk Management Concepts p5 (ELR)

Risk Analysis Continued

Learning Objective: Identify the five steps of the risk management process.

We'll study these concepts in Lesson 4 Risk Analysis.

Collecting and Analyzing Data

The collection and analysis of loss data:

- helps an organization identify and understand the potential impact of losses,
- helps the organization address product/service development and pricing,
- helps the risk manager in working with the organization's insurance programs, and
- provides the foundation on which the organization calculates its cost of risk.

Qualitative vs. Quantitative Analysis

Qualitative analysis can be thought of as the "what" analysis process, in other words, the identification and evaluation of loss exposures that cannot be easily measured by traditional statistical or financial methods.

Quantitative analysis is the "how much" analysis, which attempts to accurately measure risks by using acceptable, traditional methodologies to calculate relative numeric values.

Loss Data Types

The types of data collected and analyzed from each of the logical classifications of risk are important to the effectiveness of the loss data analysis.

Examples of the loss data types under human resources classification would be cause of injury, type of injury, body part injured, location of injury etc.

Loss Data Credibility

The components of loss data quality include:

Completeness - statistical analysis is valid if the data set is complete.
Consistency - comparisons are valid if the same items (apples to apples) are used.
Integrity - data with good integrity is reliable, accurate and current to the time period being measured.
Relevance - the data must yield information on matters of concern to the organization.

Benchmarking

Benchmarking is a systematic way of continuously comparing an organization's performance against others at a given time or against itself over a given time period.

Risk managers may elect to:

- Compare the organization to "best in industry" or competitors.
- Compare the organization's performance to "best in class" or those recognized as performing certain functions at a high level.
- Compare the organization's current performance to its own performance in other time periods.

Lesson 1 Topic B Risk Management Concepts p6 (ELR)

Step 3: Risk Control

Learning Objective: Identify the five steps of the risk management process.

Any conscious action or inaction to minimize, at the optimal cost, the probability, frequency, severity, or unpredictability of loss.

Risk control is the “action step” of risk management. You apply the information you identified and analyzed in the first two steps of the Risk Management Process and take actions that minimize the frequency and/or severity of the losses.

Redundancies in computer networks prevent costly loss of service and data. This is an example of the segregation/separation/duplication risk control technique.

Lesson 1 Topic B Risk Management Concepts p7 (ELR)

Learning Objective: Identify the five steps of the risk management process.

We'll study these concepts in Lesson 5 Risk Control.

Risk Control Methods

Techniques of minimizing the frequency and/or severity of losses with training, safety and security measures.

Claims Management

The prompt resolution of an organization's losses subject to insurance or an active retention (self insurance) program, including claims by other persons or entities to which it may be legally or ethically bound.

Lesson 1 Topic B Risk Management Concepts p8 (ELR)

Step 4: Risk Financing

Learning Objective: Identify the five steps of the risk management process.

The acquisition of internal and external funds to pay losses at the most favorable cost.

Your organization decides to self-insure (retain) the first $1M for fire losses and to purchase insurance for any loss amounts between $10M and $100M. Internal reserves are designated and reserved to pay any losses between $0 and $1M.

Did the organization select the correct retention level? Is the limit of insurance adequate?

Whatever risks your organization faces, addressing funding before losses occur keeps expenditures in check and assists with budgeting and planning. The alternative can be extremely costly - both financially and socially.

Lesson 1 Topic B Risk Management Concepts p9 (ELR)

Risk Financing Continued

Learning Objective: Identify the five steps of the risk management process.

Risk-taking Appetite & Ability

Organizations use internal funds and/or external funds to pay for losses. An organization may choose to retain losses, either in whole or part (internal funding) or transfer the financing of losses using insurance (external funding).

The decision as to which finance method is best is based, in part, on how much the organization is able and willing to retain.

Transfer Options & Criteria for Comparison

The risk manager may have several financing options to consider. Each option has characteristics that should be evaluated and compared by the risk managers when they are determining which is the most appropriate for their organization.

Simple Transfer Options

Simple transfer options are not loss sensitive to any large degree. An example of a simple transfer option will be a Guaranteed Cost plan. In this plan, the organization (the insured) pays the premium to the insurance carrier who in turn makes claim payments to the claimant. There is no deductible or self-insured retention.

Loss Sensitive Transfer Options

Simple Transfer Options are not loss sensitive to any large degree. We'll study a truly loss sensitive option - the Large Deductible Plan. For purposes of this course, a large deductible is $100,000 and higher.

Lesson 1 Topic B Risk Management Concepts p10 (ELR)

Step 5: Risk Administration

Learning Objective: Identify the five steps of the risk management process.

Risk administration is the process of planning, implementing, and monitoring the risk management program.

In this final step of the Risk Management Process, risk managers work with their team to plan, implement and monitor the risk management program - in other words, to continuously improve and move it forward.

Implementation includes commitment and participation, communication, design and structure, training and accountability. Monitoring includes indicators and measures, continuous tracking, regular evaluation, adjustments, upgrades, and feedback.

Risk Administration encompasses the planning and risk management policy development for the organization.

Members of the Risk Management Team

- Risk Management Department
- Risk Management Consultants
- Legal Counsel
- Insurance Professionals
- Organization's Management
- Others

Lesson 1 Topic G Risk Administration Concepts p11 (ELR)

Risk Administration Continued

Learning Objective: Identify the five steps of the risk management process.

The Risk Management Team

The Risk Manager cannot complete every function alone. Members of the risk management team are formal and informal, internal and external.

Internal - Those within the organization, such as the risk management team, human resources, legal, accounting department and operation management. Internal support is often overlooked or underutilized due to expertise, political and/or jurisdictional issues.

External - Those outside the organization, such as insurance providers, brokers, agents, risk management consultants, captive managers, financial consultants, legal consultants, safety consultants, and private investigators. The range of outside service providers is broad depending upon the issues requiring support and outside expertise.

Risk Management Information System

A RMIS is an information system that supports the user or risk manager and the organization, or the risk consultant an multiple client organizations in identifying, measuring, and managing risk.

A RMIS is also more than an information database; it is a way to deploy risk management tools and often a customer relationship module as well.

Lesson 1 Topic B Risk Management Concepts p12 (ELR))

Risk Management Process – Summary
Learning Objective: Identify the five steps of the risk management process.

The risk manager has completed the five steps in the risk management process. The organization's risks have been identified and analyzed. Risk control techniques have been implemented to reduce the frequency and/or severity of losses, and financing has been arranged.

However, the risk management process is never complete. It begins anew with each new exposure that arises as the organization continues its operations.

What if the organization acquires additional assets, engages in new activities, or signs new contracts? These are just a few examples of situations that require the risk manager to identify, analyze, control and finance new exposures to loss the organization may have.

Lesson 1 Topic C - Total Cost of Risk (TCOR)

Lesson 1 Topic C Total Cost of Risk p1 (ELR)

Learning Objective: Describe the components of Total Cost of Risk and how Cost of Risk is used by risk managers.

The risk management program need not be viewed as simply another cost center. Careful management of TCOR improves profit margins. The seasoned risk manager is able to communicate this to stakeholders and key people in the firm. What is Cost of Risk?

Total Cost of Risk (TCOR) is defined as the sum of all costs and expenses associated with the risk management function of an organization. It is the cost of managing risk!

Lesson 1 Topic C Total Cost of Risk p2 (ELR)

Four Components of the Total Cost of Risk

Learning Objective: Describe the components of Total Cost of Risk and how Cost of Risk is used by risk managers.

Four components of the TCOR formula are measurable:

Insurance Costs: Note that insurance is simply one component of an organization's Total Cost of Risk.

Retained losses and allocated loss adjustment expenses: Predictable losses that the organization can plan and pay for with internal funds are an example of retained losses

Risk management departmental costs: Salaries, training and travel expenses, risk management information system, management overhead, etc.

Outside Services Fees: Risk management consultants, third party administrators, loss control, legal, fee-for-service insurance agent/brokers, etc.

Lesson 1 Topic C Total Cost of Risk p3 (ELR)

Indirect Costs

Learning Objective: Describe the components of Total Cost of Risk and how Cost of Risk is used by risk managers.

In addition to these measurable components, indirect costs are also included in Total Cost of Risk calculations.

Indirect costs to an organization after a loss include:

- Disruption in production or sales
- Management time spent on loss-related activities
- Overtime costs
- Hiring and training replacement
- Opportunity costs
- Loss of goodwill
- Social costs due to public image, reputation, etc.

Indirect costs may be difficult to quantify. The various methods used by organizations to do so is beyond the scope of this course.

An employee at Rincon Public Utilities (RPU) had an accident while driving a company truck. Even though the employee was not hurt, he and his supervisor spent most of the day completing the required loss reports, meeting with the risk management department, etc.

As a result, RPU experienced a disruption in production and management time spent on loss-related activities. These are examples of indirect costs.

Lesson 1 Topic C Total Cost of Risk p4 (ELR)

Total Cost of Risk Formula

Learning Objective: Describe the components of Total Cost of Risk and how Cost of Risk is used by risk managers.

The total cost of risk formula is the sum of all quantified costs and expenses associated with the risk management function of an organization.

Insurance costs
+ Retained losses and allocated loss adjustment expense (ALAE)
+ Risk management departmental costs
+ Outside service fees
+ Indirect costs
Total Cost of Risk

Lesson 1 Topic C Total Cost of Risk p5 (ELR)

An Example of XYZ Corporation's Cost of Risk

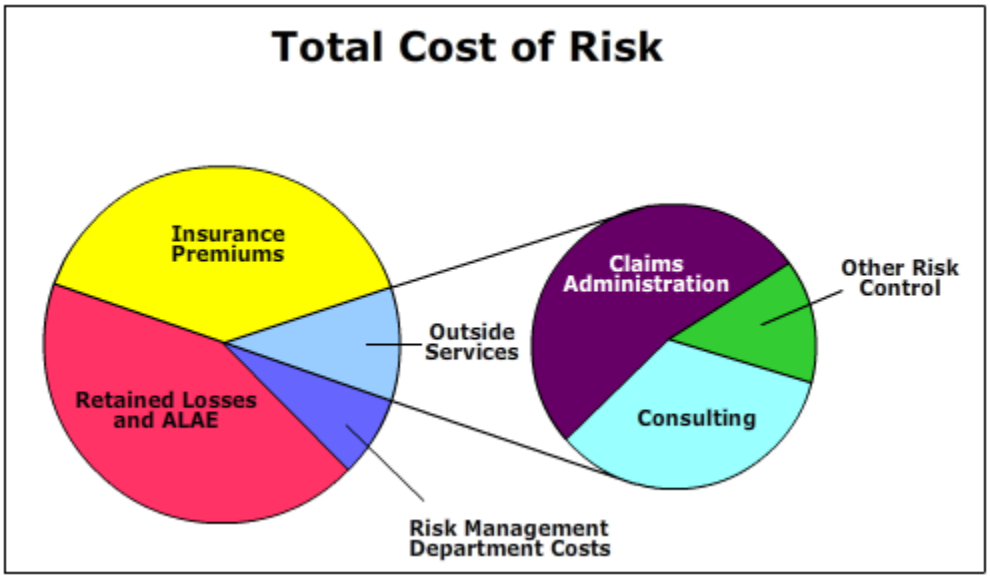
Learning Objective: Describe the components of Total Cost of Risk and how Total Cost of Risk is used by risk managers.

Risk Management-Internal (Administration) $100,000
Insurance Costs (net of placement, other fees) $800,000
Retained losses and ALAE $850,000

Outside Services:

Consulting, Brokerage Services $50,000
Claims Administration $85,000
Other Risk Control $25,000

Total $1,910,000



Lesson 1 Topic C Total Cost of Risk p6 (ELR)

How Total Cost of Risk is used

Learning Objective: Describe the components of Total Cost of Risk and how Cost of Risk is used by risk managers.

How Total Cost of Risk is Used in the Organization Once known, Total Cost of Risk is a key risk management tool. The risk manager can use

TCOR to:

1. Assist with making effective risk management decisions
2. Measure progress towards risk management objectives
3. Focus and promote safety and loss control
4. Assist with accurate pricing of products and services
5. Assist with effective management of financial budgets

Benchmarking

Risk managers can also compare their firm's TCOR to similar organizations or use it as a benchmark to measure and monitor improvement.

One typical objective of a risk manager is to minimize TCOR by identifying those factors from each component that can be more effectively controlled.

TCOR is often "allocated".

Total Cost of Risk must also be determined if expenses associated with the organization's risk management program are allocated or "charged back" to various divisions or departments to promote accountability.

Please refer to the end of Lesson 1 to complete Self Quiz 1 at this time.

THE NATIONAL ALLIANCE
for Insurance Education & Research

Lesson 2 - Risk Terms

Lesson 2 Intro p1 (ELR)

In this section we will study the terms that we will use in the course.

Lesson 2 Intro p2 (ELR)

Lesson 2 – Learning Objectives

After completing this lesson, you will be able to:

1. Understand the terminology used by risk managers.

Lesson 2 Topic A - Defining Risk

Lesson 2 Topic A Defining Risk p1 (ELR)

Learning Objective: Discuss the terminology used by risk managers.

Risk is a term widely used in the risk management and insurance worlds. What does risk really mean? Does it mean the same thing to a risk manager as it does to an insurance professional? The term “risk” has different meanings depending upon the perspective of the user.

In the insurance world, risk may be used by the insurance company underwriter to refer to the person or entity being insured. To an agent or broker, risk may be the insured or the exposure such as a building or a vehicle. To others, risk may be the peril such as wind or fire or the hazard such as poor housekeeping.

Lesson 2 Topic A Defining Risk p2 (ELR)

Defining Risk Continued

Learning Objective: Discuss the terminology used by risk managers.

Four broad definitions of risk are commonly recognized, related to risk management, as follows:

Difference Between Expected Losses and Actual Losses

The risk manager gathered the organization's last 5 years of loss data, completed a statistical analysis and projected the organization's losses for the upcoming year to be S1.5 M. Financing was arranged to cover the Expected Losses. Actual losses amounted to S2.0 M. The difference between S1.5M and S2.M is "risk" to the organization.

Probability of a Variation of Outcomes From a Given Set of Circumstances

Two buildings are located within 10 feet of one another One is frame construction and the other is concrete block. Should a fire occur, the frame building is more likely to be destroyed than the concrete building. Should an earthquake occur, both are likely to be destroyed. The risk from fire is greater than the risk from an earthquake because of the possibility of a variation of outcomes. With an earthquake, both are likely to be destroyed so there is a lesser possibility of variation of outcomes.

Uncertainty Concerning a Loss

A youth organization is sponsoring its first annual week-long camp. The risk manager may use "risk" when referring to the fact that she does not know if losses will occur during the camp. "The potential risk to our organization created by the camp sponsorship is not fully known."

Chance or Probability of Loss
Employment-related exposures have been a topic of conversation in the risk management department. The risk manager may use "risk" when referring to the chance that an employee might make a claim for wrongful discharge or harassment. What is the risk that an employment-related lawsuit would actually occur?

Lesson 2 Topic A Defining Risk p3 (ELR)

Defining Risk Continued

Learning Objective: Discuss the terminology used by risk managers.

For purposes of this course, the most useful definition of risk is:

“Uncertainty that may be either positive or negative arising out of a given set of circumstances.

Lesson 2 Topic A Defining Risk p4 (ELR)

What is Risk?

Learning Objective: Discuss the terminology used by risk managers.

There are two types of risk.

Pure Risk

Only a chance of loss or no loss (break-even) (For a risk manager, a break-even day is a good day)

Example: A building burning down or an employee being injured in an accident

Speculative

Chance of loss or gain, usually associated with business or financial risk

Example: The value of the company's stock may go up or it may go down; there may be a market for the organization's goods, or its product may have become obsolete.

Lesson 2 Topic A Defining Risk p5 (ELR)

"Pure Risk"

Learning Objective: Discuss the terminology used by risk managers.

From the traditional viewpoint, risk management and insurance have historically addressed only pure risk.

Sometimes a very fine line exists between pure and speculative risk, as the insured/insurer relationship illustrates. The recognition of this fine line has added to the interest in “enterprise risk management” - the concept that risk is risk and all risks can be managed.

Note: While Enterprise Risk Management is part of most risk management programs, any further discussion is outside the scope of this course.

Please refer to Lesson 2 Topic A Defining Risk p6 (ELR) to complete the Knowledge Check at this time.

THE NATIONAL ALLIANCE
for Insurance Education & Research

Lesson 2 Topic B - Identification Terms

Lesson 2 Topic B Identification Terms p1 (ELR)

The risk terms we've selected are used throughout the risk management process. However, we've associated them with each risk step to provide a context for their definitions. In the Risk Identification Step, you must understand the differences among exposure, hazard, and peril.

Lesson 2 Topic B Identification Terms p2 (ELR)

Exposure, Hazard and Peril

Learning Objective: Discuss the terminology used by risk managers.

Exposure: a situation, practice, or condition that may lead to an adverse financial consequence; an activity or asset.

Example: A building

Hazard: a condition that may give rise to a loss from a given peril; physical, moral, or morale characteristics that increases the likelihood of a loss.

Example:
A building could be damaged by a fire. The improper storage of flammable liquids (a hazard) increases the likelihood that a fire will occur.

Peril: the cause of loss, such as fire, wind, hail, slip and fall, etc.

Please refer to Lesson 2 Topic B Identification Terms p3 (ELR) to complete the Knowledge Check at this time.

THE NATIONAL ALLIANCE
for Insurance Education & Research

Lesson 2 Topic C - Analysis Terminology

Lesson 2 Topic C Analysis Terms p1 (ELR)

Learning Objective: Discuss the terminology used by risk managers.

Understanding frequency and severity is critical to the Control, Analysis, and Financing steps. The concepts first show up in the Analysis Step, when measuring the impact of losses from loss data. In the Control step, an analysis of frequency and/or severity is also used by risk managers when prioritizing their organization's exposures to select the most effective risk control and risk financing methods.

Lesson 2 Topic C Analysis Terms p2 (ELR)

Analysis Terminology continued

Learning Objective: Discuss the terminology used by risk managers.

Frequency

Frequency - the number of losses occurring in a given time period

Accidents are evaluated according to how often they might occur.

Severity

Severity - the dollar amount of a given loss or the aggregate dollar amount of all losses for a given period

Accidents are also evaluated according to how severe the ensuing injury or property damage may be.

Lesson 2 Topic C Analysis Terms p3 (ELR)

Analysis Terminology continued

Learning Objective: Discuss the terminology used by risk managers.

Loss Terminology

The terms we are about to review are commonly used to mean the same thing when, in fact, they do not. Those of you with an insurance background may use "loss" and "claim" interchangeably, but they are not the same. An effective risk management program must record "incidents", "accidents", as well as "occurrences."

Incident: an event that disrupts normal activities and may become a loss (also referred to as a near miss)
Example: Maintenance worker feels overheated and rests in the shade for an hour

Accident: an unplanned event definite as to time and place that results in injury or damage to a person or property

Example: Maintenance worker suffers from heat stroke and must go to the hospital, leading to a workers compensation claim.

Occurrence: an accident with the limitation of time removed (an "accident" that is extended over a period of time rather than a single observable happening)

Example: Mold found in the walls of a house

Loss: a reduction in the value of assets

Not all losses become claims. For example, an organization's vehicle may be damaged during a hailstorm, but a claim is not made as there is not outside financing (insurance) to cover a loss such as this. Or a client falls in the parking lot resulting in small abrasions, but chooses not to pursue compensation for her injuries.

Claim: a demand for payment or an obligation to pay as a result of a loss

Lesson 2 Topic C Analysis Terms p4 (ELR)

Analysis Terminology continued

Learning Objective: Discuss the terminology used by risk managers.

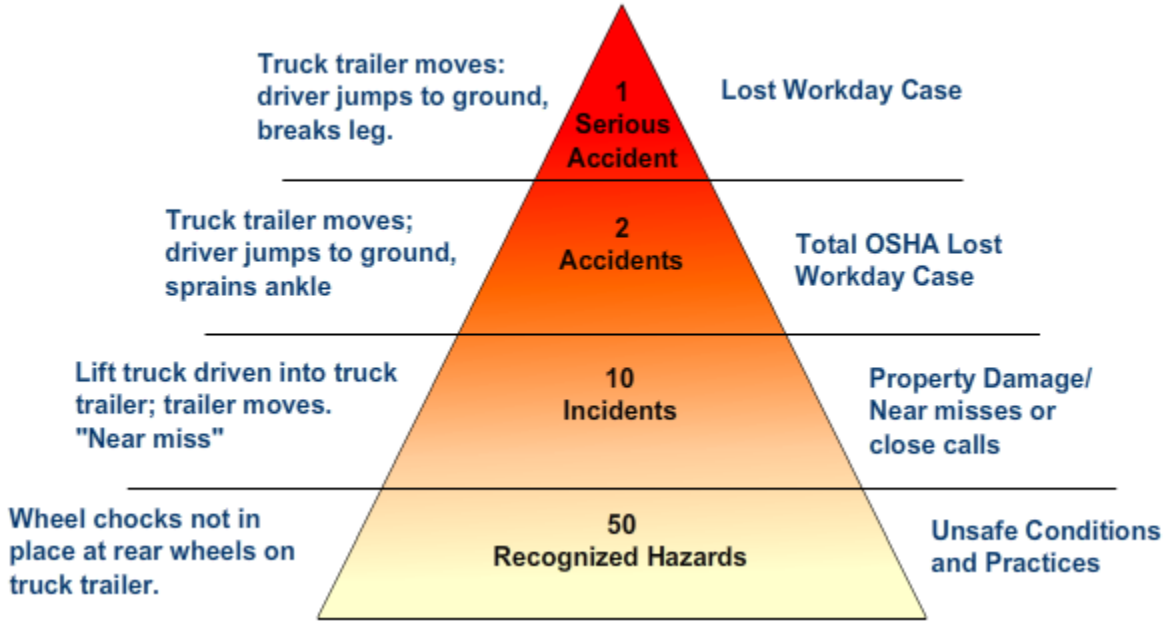
Incidents

Let's go back to "incidents" versus "accidents". What is the importance?

After all, "losses" matter; "incidents" don't really cost the organization anything, right? The truth is "incidents" can lead to "accidents". It is all about numbers.

In this example, 2 "accidents" occurred for every 10 "incidents". This is important information to capture and analyze.

The risk manager can apply risk control techniques that are more timely or proximate to the event that may help avoid or lessen future events of a similar nature.



Lesson 2 Topic C Analysis Terms p5 (ELR)

Analysis Terminology continued

Learning Objective: Discuss the terminology used by risk managers.

If the first goal of analysis is to understand frequency and severity, the second would be to analyze the financial impact of losses on the organization. The terms below are also important in Step 4 Financing of Risk. Note that some of the terms have to do with the development of claims over time.

Incurred But Not Reported (IBNR)

Losses that are not reported until sometimes years later. Some liability claims may be made long after the event that caused the injury to occur. Asbestos-related diseases, for example, do not show up until decades after the exposure. IBNR also refers to estimates made about claims already reported but where the full extent of the injury is not yet known, such as a workers compensation claim where the degree to which work-related injuries prevents a worker from earning what he or she earned before the injury unfolds over time. Reserves for such claims are adjusted as new information becomes available.

Loss Trending

Adjusting historical losses to account for inflationary trends so that the ultimate value is more current or meaningful. Loss trend factors are multiplied by actual historical losses to trend losses.

You are evaluating the past five years of losses to project expected losses for next year. Losses from five years ago would automatically cost more if they occurred today simply due to inflation. Loss trending is the application of a Loss Trend Factor to account for the inflationary trends needed to bring past losses to today's dollars.

Loss Development

Difference between the value of a loss as originally reported and its subsequent evaluation at a later date or at the time of its final disposition.

Workers compensation and bodily injury losses take longer to settle than property damage losses. When a risk manager is analyzing loss data to project ultimate payout, it may be incorrect to use the initial $25,000 reserve for a bodily injury claim that is certain to increase. Loss Development Factors are applied to the current valuation of losses to determine an estimate of ultimate incurred losses.

Loss Development Factor

Ratios that are applied to a current valuation of losses to determine an estimate of ultimate incurred losses. These factors are calculated by comparing the period-to-period changes in values of loss reserves, under the assumption that current losses will be paid according to the same pattern as prior losses at similar states of development. Loss development factors (LDF) are frequently calculated separately for incurred losses, paid losses, and claims counts. ^Calculation of the Loss Development Factor ratio, while important to the risk manager, will not be covered in this course.

Expected Losses

Loss projections ("loss pics" or "loss picks") based on probability distributions and statistics; frequently developed using actuarial techniques including trending and development.

Analysis Terminology continued

Learning Objective: Discuss the terminology used by risk managers.

Exposure Bases

If estimated injury losses have been developed for, say 1,000 full time employees, and the risk manager knows that 200 more full time employees are going to be taken on in the coming fiscal year, he or she would adjust the estimate to account for the increase in number of employees.

The metric, full time employees, is an exposure base. It is a method for indexing losses to a meaningful level of exposure. Other exposure bases might be building square footage, vehicle miles driven, hours of facility usage, etc.

Please refer to Lesson 2 Topic C Analysis Terms p7 (ELR) to complete the Knowledge Check at this time.

Lesson 2 Topic D - Risk Control Terminology

Lesson 2 Topic D Control Terms p1 (ELR)

Learning Objective: Discuss the terminology used by risk managers.

Our key terms under the Step 3 - Control are the five risk control methods. We'll study these in detail in Lesson 5. Some methods are designed to reduce severity, some are designed to reduce frequency, and some do both.

Lesson 2 Topic D Control Terms p2 (ELR)

Risk Control Terminology Continued

Learning Objective: Discuss the terminology used by risk managers.

1. Avoidance

Eliminate an activity or exposure which eliminates chance of loss.

Example: Your company decides to cease using a dangerous chemical in the manufacturing of one of your products.

2. Prevention

Breaks a sequence of events that leads to a loss or that makes the event less likely.

Example: Performing regular equipment checks

3. Reduction

Reducing the severity or financial impact from unpreventable losses.

Example: A fire sprinkler system is installed in the manufacturing plant.

4. Segregation/separation/duplication

Work primarily to reduce the severity of the loss

Example: A second arc welding unit is purchased as a backup to the primary unit

5. Transfer (Contractual, physical, or both)

Have another party be financially responsible for all or a partial amount of the loss.

Example: Purchasing insurance

Please refer to Lesson 2 Topic D Control Terms p3 (ELR) to complete the Knowledge Check

---

THE NATIONAL ALLIANCE
for Insurance Education & Research

Lesson 2 Topic E - Risk Finance Terms

Lesson 2 Topic E Financing Terms p1 (ELR)

Learning Objective: Discuss the terminology used by risk managers.

Understanding that the acquisition of funds to pay claims can be from either internal sources (retention) or external sources (transfer of financial responsibility) is important to the risk manager when making risk finance recommendations or decisions.

Examples of Retention

- Retained losses
- Deductibles
- Contractual agreements that assume financial liability

Examples of Transfer

- Insurance Program
- Contractual agreements that transfer financial responsibility to another

Funding Risk

Retention of Financial Responsibility
Transfer of Financial Responsibility

Lesson 2 Topic E Financing Terms p2 (ELR)

Retention
Learning Objective: Understand the terminology used by risk managers.

Retention is when the organization uses internal funds to pay for some or all of a loss that occurs. Retention can be either active or passive.

Active Retention

Active retention is planned financial responsibility for the loss. The organization knows in advance that it will be financially responsible should a loss occur. For example, the risk manager recently took collision coverage off the trucks over 10 years old that are insured on a commercial auto policy. In the event a truck is damaged in a collision, the organization will be financially responsible for the damages. In another example, the organization chose a $100,000 deductible on its property insurance. In the event of a fire, the organization will be financially responsible for the first $100,000 of the loss.

Passive Retention

Passive retention is not planned. It is an organization's unplanned financial responsibility for the loss. Passive retention can be the result of failure of the risk manager or insurance professional to identify the exposure, failure to act or forgetting to act. For example, the college's School of Science recently acquired equipment valued at $500,000. The risk manager became aware of this acquisition only after it was destroyed in a fire; therefore, external financing had not been arranged. The college now has the financial responsibility to pay for the damage to the equipment. Passive retention is not good!

Lesson 2 Topic E Financing Terms p3 (ELR)

Retention Level

Learning Objective: Discuss the terminology used by risk managers.

Retention level is the amount of loss that is self-insured. It is usually expressed on a per occurrence basis. It is sometimes referred to as the self-insured retention.

Lesson 2 Topic E Financing Terms p4 (ELR)

Transfer

Learning Objective: Discuss the terminology used by risk managers.

Transfer is one of the five control methods, but it is very much the subject of Step 4 Risk Financing. Recall that as a Step 3 Control method, transfer included physical transfer and contractual transfer.

In Step 4, Risk Financing, transfer refers to the use of external sources, such as an insurance program (or the "excess" insurance used in a self insurance program) to pay claims and other loss costs.

In Section 5 we will go over transfer options, (such as a guaranteed cost plan or a self insurance plan,) which are programs of insurance and/or self insurance that organizations use to finance risk.

Transfer

Contractual Transfer
Physical Transfer

Examples of Contractual Transfer

- Insurance program
- Contractual agreements that transfer financial responsibility to another

---

Lesson 2 Topic E Financing Terms p5 (ELR)

Loss sensitivity
Learning Objective: Discuss the terminology used by risk managers.

This term describes how quickly an organization's Total Cost of Risk (TCOR) responds to increases or decreases in loss costs.

For example, some insurance programs defer the impact of an increase or decrease in loss severity until it is time for the policy to renew. So TCOR would remain stable during the period of time when the losses were, say, increasing, and go up later by virtual of a premium increase at renewal (or a change in underwriting). These programs would be considered to have low loss sensitivity.

Lesson 2 Topic E Financing Terms p6 (ELR)

Risk-Taking Appetite

Learning Objective: Discuss the terminology used by risk managers.

Frequently used in the risk management community, risk-taking appetite is the amount of risk the organization is willing to accept or retain. Once the organization reaches this risk-appetite threshold, it implements risk management control and external financing to bring the exposure level back within the accepted range.

Risk managers and insurance professionals should fully understand the risk appetite of their clients/organizations. Risk appetite directly impacts retention levels and external financing of risk. Both internal and external factors affect an organization’s risk-taking appetite.

External Factors

- Market maturity
- Competition and the need to take business risk
- Public image
- Stakeholders' attitudes (owners, creditors, government, beneficiaries, etc.)

Internal Factors

- Company history of risk-taking
- Long-term organizational objectives
- Stage in organizational life cycle
- Financial stability (assets, income, and cash flows)
- Management's willingness to take risk versus the organization's financial ability to assume risk

---

Please refer to Lesson 2 Topic E Financing Terms p7 (ELR) to complete the Knowledge Check at this time.

Lesson 2 Topic F - Risk Administration Terms

Lesson 2 Topic F Administration Terms p1 (ELR)

Learning Objective: Discuss the terminology used by risk managers.

Step 5 Risk Administration activities can include a system for allocating TCOR.

A **cost of risk allocation system** is a process that identifies and attributes the cost of risk among the various sections of an organization or company.

Not all organizations choose to allocate their Cost of Risk. Among those who do, there any many philosophies behind, as well as methods to the actual allocation. While those philosophies and methods will not be covered in this course, it is important to understand that an allocation system can benefit the organization in the following ways:

- Understand true costs
- Create accountability
- Enhance loss control
- Stay competitive
- Change behavior

Lesson 2 Topic F Administration Terms p2 (ELR)

Example of Allocation Systems

Learning Objective: Discuss the terminology used by risk managers.

You are the risk manager for a chain of retail stores. One store has more workers compensation claims than all of the others combined. You have tried to work with the store manager to promote employee safety; however, the response is always, “Hey, why are you so worried about it. That’s why we have insurance!”

Meanwhile, because of this store’s loss experience, the worker compensation rates are increasing, the experience modifier is going through the roof, time is being spent taking claim reports and store morale is suffering overall.

Do you think it is possible that the store manager’s attitude might change if the store’s share of the TCOR was taken out of that store’s budget?

Lesson 2 Topic F Administration Terms p3 (ELR)

Risk Management Information System (RMIS)

Learning Objective: Discuss the terminology used by risk managers.
A RMIS is a database that supports the risk manager in each step of the risk management process. It can include applications such as claims administration, tracking and analysis, interfacing of claims data with insurance carriers and third-party administrators, and maintenance of insurance policy records.

Most RMIS have reporting tools that can generate an array of reports in both data and graphical formats.

Tip: For those in the insurance industry, a RMIS is similar to an agency management system.

Uses for an RMIS

Collect data to further control activities.
Track improvements (Benchmarking)
Create charts and diagrams
Create insurance program summary

Please refer to the end of Lesson 2 to complete Self Quiz 2 at this time.

Lesson 3 - Risk Identification

Lesson 3 Intro p1 (ELR)

Risk was defined in Lesson 2 as “uncertainty concerning a loss arising out of a given set of circumstances”. Risks to an organization, including both “pure” and “speculative”, fall within one of six classes. “General Classes of Risk” identify risks that affect all organizations, regardless of their economic activity.

Using property, liability, human resources and net income “Logical Classifications” along with one or more of the “Ten Methods of Identification” will equip the risk manager with the tools to be comprehensive and systematic during this first step of the risk management process.

Lesson 3 Intro p2 (ELR)

Lesson 3 – Learning Objectives

After completing this lesson, you will be able to:

1. Explain why risk identification is the most important step of the risk management process.
2. Identify and discuss the six general classes of risk.
3. Explain the purpose, method, strength and weaknesses of the ten risk identification methods.
4. Identify and describe each of the four logical classifications of exposures.

Lesson 3 Topic A - Risk Identification

Lesson 3 Topic A Identification p1 (ELR)

Learning Objective: Explain why risk identification is the most important step of the risk management process.

Exposures, perils, and hazards that may interfere with the achievement of an organization's objectives resulting in an adverse financial impact must first be identified if they are to be effectively managed and controlled.

Therefore, risk identification is the most important step of the risk management process because an exposure must be identified before it can be effectively analyzed, controlled, or financed.

Lesson 3 Topic A Identification p2 (ELR)

Why Identify Risks?

Learning Objective: Explain why risk identification is the most important step of the risk management process.

Exposures must first be identified if they are to be adequately managed and controlled.

To properly identify exposures, the risk manager must:

- use effective methods of exposure identification and
- classify exposures.

Classification:

- An analysis of exposures provides details for classifying and controlling.

Please refer to Lesson 3 Topic A Identification p3 (ELR) to complete the Knowledge Check at this time.

Lesson 3 Topic B - General Classes of Risk

Lesson 3 Topic B General Classes of Risk p1 (ELR)

Learning Objective: Identify and discuss the six general classes of risk.

After understanding the two types of risks, “pure” and “speculative”, we organize them in terms of risk class, roughly corresponding to each sphere of activity within society that produces the risk.

There are 6 general classes of risk:

1. Economic
2. Legal
3. Political
4. Social
5. Physical
6. Juridical

Lesson 3 Topic B General Classes of Risk p2 (ELR)

Classes of Risk Continued

Learning Objective: Identify and discuss the six general classes of risk.

We have already introduced you to these General Classes of Risk; however, there may be others that you might not have thought of previously. As each class is introduced and examples provided, you will see very quickly that speculative risks are abundant.

Lesson 3 Topic B General Classes of Risk p3 (ELR)

Classes of Risk Continued

Learning Objective: Identify and discuss the six general classes of risk.

Economic

Definition: The risk arising out of an organization's operational, marketplace, financial or entrepreneurial activities.

Examples

- Recession leads to reduced sales.
- A ski resort suffers financial loss when it is unable to open for the entire ski season due to inadequate snowfall

Legal

Definition: The risks inherent in compliance or arising from statutory liability.

Example

- EEOC begins administrative proceedings against a tire store for alleged discrimination against some of its employees.

Political

Definition: The risk associated with legal changes by the governmental interpretations (or reinterpretations) of rules and regulations.

Examples

- Due to political unrest in a foreign country, a company is forced to shut down a profitable operation located there and have all employees return to the United States
- Many conventions scheduled at your hotel and conference center have been cancelled due to a new law passed in your state

Social

Definition: The risks arising from public relations, loss of reputation, image or cultural problems.
Examples

- A major network news department broadcasts a segment on safety concerns for one of your company's products
- Video store revenues have dropped and stores are closing as their customers are choosing instead to rent movies and games online or from a kiosk at their grocery store

Physical

Definition: Risks arising from property, persons, or information

Examples

- Confidential client information is accessed by a computer hacker
- A building is destroyed by arson

Juridical

Definition: Risks arising from the decision of a judge or jury, or from court or jury attitudes.

Examples:
A jury renders a $1 million punitive damage judgment against your company
Juries in your state are known for awarding large judgments against large corporations in favor of the "little guy"

Lesson 3 Topic B General Classes of Risk p4 (ELR)

Classes of Risk Continued

Learning Objective: Identify and discuss the six general classes of risk.

Did you notice both the "pure" and "speculative" risks? Insurance professionals might not have considered the losses to an organization originating from something outside of the control of a client and not actually injuring someone or damaging property.

You may have also noticed the classes and examples within each class that may not be "insurable" in the traditional sense. For example, insurance isn't a solution for society changing its direction and as a result a company's product becomes obsolete. Enterprise risk management would address this, in the company's risk management program. Just because something isn't "insurable" doesn't mean it isn't important to identify.

Lesson 3 Topic B General Classes of Risk p5 (ELR)

Multiple Classes of Risk

Learning Objective: Identify and discuss the six general classes of risk.

Did you also notice the possibility of risks easily crossing lines and falling into multiple classes?

For example, if a food product is contaminated and the information is made public, it can become a legal risk, a social risk, an economic risk, and a physical risk.

Depending upon where litigation is filed, it could become a juridical risk. In some cases, food contamination has led to a political risk because of changes in legislation.

Please refer to Lesson 3 Topic B General Classes of Risk p6 (ELR) to complete the Knowledge Check at this time.

Lesson 3 Topic C - Logical Classifications

Lesson 3 Topic C Logical Classifications p1 (ELR)

Learning Objective: Identify and describe define each of the four logical classifications of exposures.

Think of logical classifications as the buckets by which risks are sorted. It's useful to classify risks that have similar implications and characteristics.

Logical classifications provide the risk manager with a starting point for analyzing exposures, perils, hazards and losses associated with Property, Human Resources, Liability and Net Income.

Lesson 3 Topic C Logical Classifications p2 (ELR)

Logical Classifications Continued

Learning Objective: Identify and describe define each of the four logical classifications of exposures.

First, consider how these "buckets" are defined. We will look more closely at each area of logical classification.

Property

This classification includes real property, personal property, intangible property, intellectual property and legal interest.

Example: fire damage to a company building

Human Resources

This classification is based on the relationship between the organization and its owners, board members, officers, employees, leased or temporary employees, volunteers, independent contractors, etc.

Liability

This classification is related to exposures such as activities on or away from the premises, personal injury, products or services provided, statutory, etc.

Examples might include a lawsuit filed by a customer alleging your product malfunctioned due to a safety violation.

Net Income

This classification includes exposures that can be either the organization's problem or someone else's problem, but in either case it becomes the organization's problem. Causes related to exposures such as loss of use of property, loss of productivity of human resources, reduction of income or assets, and speculative risk.

Please refer to Lesson 3 Topic C Logical Classifications p3 (ELR) to complete the Knowledge Check at this time

---

Please refer to Lesson 3 Topic C Logical Classifications p4 (ELR) to download the study aid for the logical classifications.

Lesson 3 Topic D - Logical Classification #1: Property

Lesson 3 Topic D Classification 1: Property p1 (ELR)

Learning Objective: Identify and describe define each of the four logical classifications of exposures.

Loss exposures associated with tangible or intangible property are very large for most organizations. On the next few pages we'll define what is included in this classification.

Property

Real Property
Personal Property
Intangible Property
Intellectual Property
Legal Interest

Lesson 3 Topic D Classification 1: Property p2 (ELR)

Types of Property

Property is further classified into four types.

Real

- Buildings
- Structures
- Land

Personal Property

- Cash and securities
- Records and documents
- Equipment, machinery, furnishings and supplies
- Mobile Equipment
- Computer Systems, hardware, software, databases

Intangible

- Branding
- Reputation
- Goodwill

Legal Interest
Can be for tangible or intangible property

- Ownership
- Control and use (rented or leased property)
- Bailment
- Secured Creditors

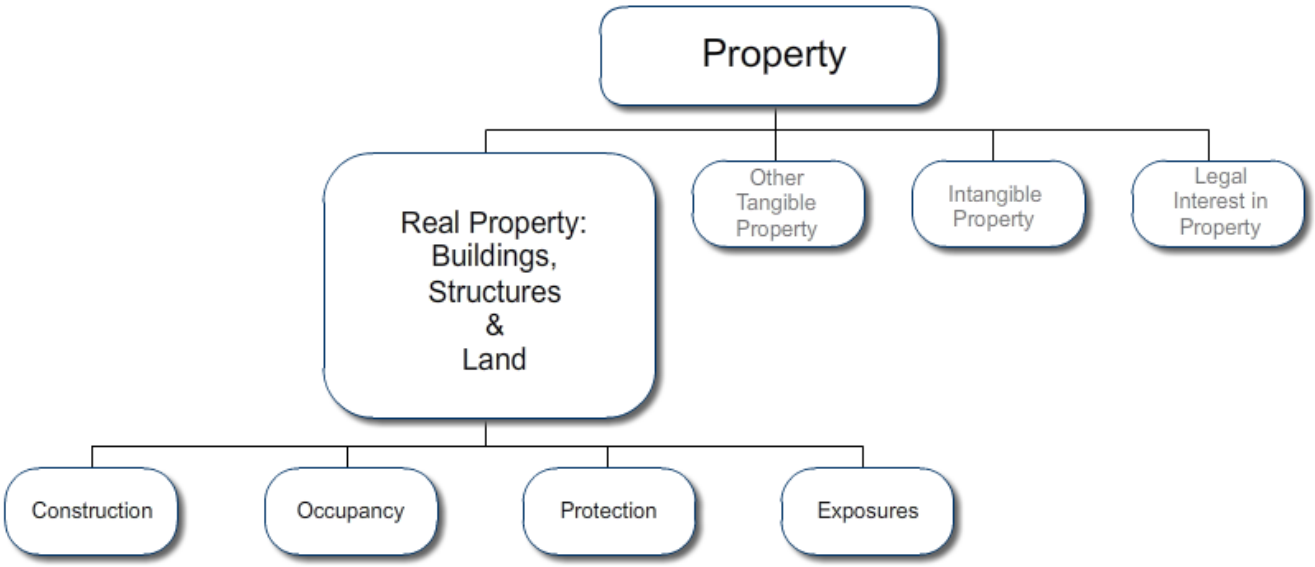
Intellectual Property

- Copyrights or patents, trademarks or trade names, trade secrets
- Trade secrets
- Licenses and franchises

Lesson 3 Topic D Classification 1: Property p3 (ELR)

Real Property

Learning Objective: Identify and describe define each of the four logical classifications of exposures.



Lesson 3 Topic D Classification 1: Property p4 (ELR)

Classification 1: Property Continued

Learning Objective: Identify and describe define each of the four logical classifications of exposures.

In order to have a property loss, there are three criteria:

1. A value exposed;

   Example: land, buildings, infrastructure, inventory, furniture, other contents

2. A peril which causes a loss;

   Example: fire

3. A financial consequence of the loss;

   Example: interruption of business; costs to repair or replace property; deductible expense, etc.

Lesson 3 Topic D Classification 1: Property p5 (ELR)

Learning Objective: Identify and describe define each of the four logical classifications of exposures.

A value exposed to loss and the financial consequences of the loss are closely related. The difference is essentially the pre-loss value and the value of the property post-loss; that is the property that is damaged or destroyed.

Pre Loss Value
- Post Loss Value
Financial Consequence of Loss

Please refer to Lesson 3 Topic D Classification 1: Property p6 (ELR) to complete the Knowledge Check at this time.

Lesson 3 Topic D Classification 1: Property p7 (ELR)

Basis for Property Valuation

Learning Objective: Identify and describe define each of the four logical classifications of exposures.

In order to identify financial consequences, an actual loss must occur. Property values are estimated before the loss and measured after the loss to determine the financial consequences of the loss. The values of exposed property are measured by using property valuation methods.

Property values must be measured using the same methodology both before and after the loss.

Lesson 3 Topic E - Logical Classification #2 Human Resources

Lesson 3 Topic E Classification 2: Human Resources p1 (ELR)

Learning Objective: Identify and describe define each of the four logical classifications of exposures.

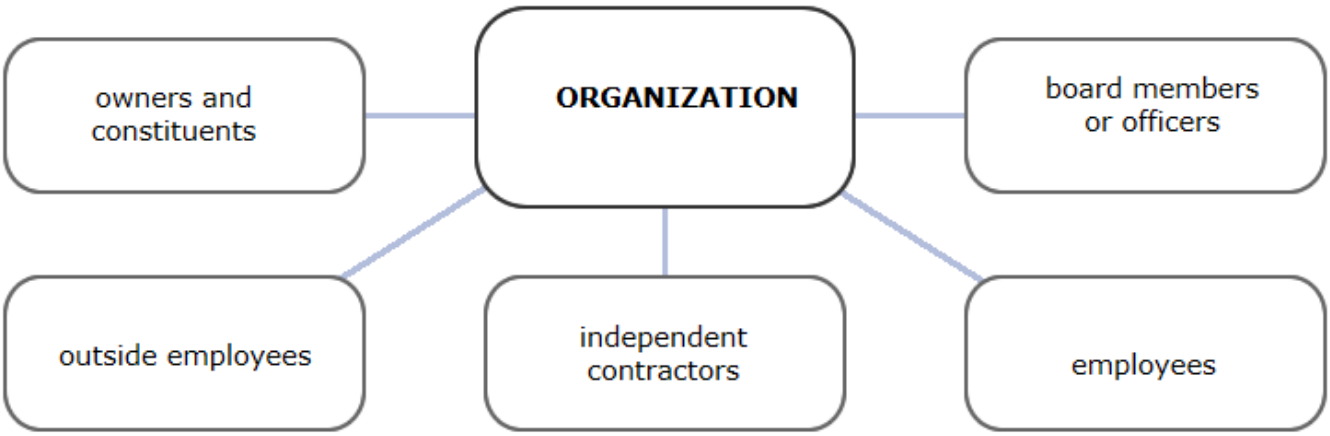
The greatest investment that most companies make is with their people. It is no wonder that Human Resources exposures are such an important concern. In the next few pages we'll study the issues involved in this classification of risk.

Lesson 3 Topic E Classification 2: Human Resources p2 (ELR)

Logical Classification #2 Human Resources continued

Learning Objective: Identify and describe define each of the four logical classifications of exposures.

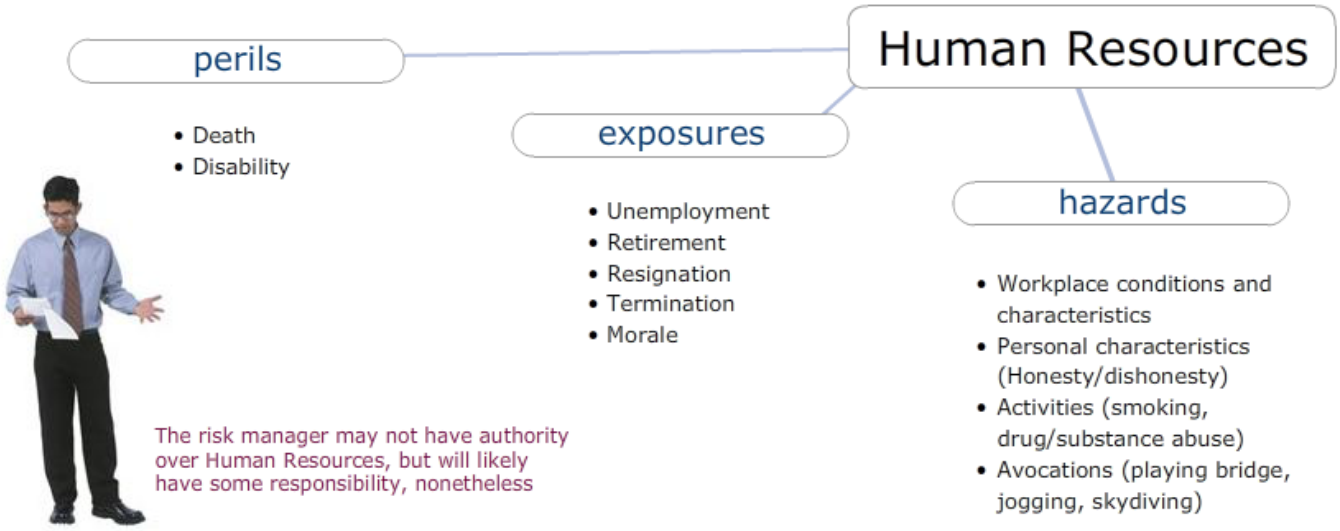
Human Resource exposures arise out of relationships:



Lesson 3 Topic E Classification 2: Human Resources p3 (ELR)

Logical Classification #2 Human Resources continued

Learning Objective: Identify and describe define each of the four logical classifications of exposures.



Lesson 3 Topic E Classification 2: Human Resources p4 (ELR)

Auxiliary Concerns

Learning Objective: Identify and describe define each of the four logical classifications of exposures.

- International employment - Conducting business in other countries creates exposures simply from differences in laws, business practices and cultures
- Benefits programs - The existence of an employee benefit program may require compliance with federal laws regulating such benefits.
- Employee contracts - If employee contracts exist, do they include a non-compete restrictive covenant or a non-disclosure requirement?
- Incentive programs - What incentive programs, such as wellness programs, volunteering in the community, safety, etc. exist and how are they managed?

THE NATIONAL ALLIANCE
for Insurance Education & Research

Lesson 3 Topic F - Logical Classification #3 Liability

Lesson 3 Topic F Classification 3: Liability p1 (ELR)

Learning Objective: Identify and describe define each of the four logical classifications of exposures.

Liability exposures are related to property, human resources, and activities (including activities conducted on the premises, away from the premises, and the products or services provided to customers and others).

The exposure is essentially one arising out of harm to society in general and to individuals and property. Liabilities stem from multiple sources from within and outside the company, including the board of directors, executive administration, middle management, employees, visitors, contractors, and the public.

Lesson 3 Topic F Classification 3: Liability p2 (ELR)

Liability

Learning Objective: Identify and describe define each of the four logical classifications of exposures.

There are many sources of liability exposures of which the risk manager should be aware. Sources of liability include:

- Premises
- Operations
- Personal Injury (libel, slander and defamation)
- Products
- Completed Operations
- Ownership, Maintenance or Use of Autos
- Ownership, Maintenance or Use of Other Conveyances
- Employing Workers (discussed in Human Resources classification)
- Liquor Manufacturing, Distribution or Sales
- Environmental Impairment
- Professional Activities
- Bailment
- Contractual liability
- Statutory liability

Lesson 3 Topic F Classification 3: Liability p3 (ELR)

Liability Continued

Learning Objective: Identify and describe define each of the four logical classifications of exposures.

Classification 3: Sources of Liability

Premises

Premises liability arises out of an injury and/or damage due to the ownership, maintenance, or use of that location. The exposure is usually confined to specific location(s).

Example: A customer slips and falls due to water on the floor.

Operations

Operations liability arises out of injury and/or damage caused by activities (construction, processing, repairing, loading/unloading, etc.), which are necessary and incidental for conducting business. The exposure can be at the premises or wherever the insured's business activity occurs.

Example: A tree trimming contractor causes damage to power lines by removing fallen limbs.

Personal Injury (Libel, slander and defamation)

Personal injury - physical or mental damage to a person as a result of coming into contact with your business
Libel - making of defamatory statements in a printed or fixed medium, such as a magazine or newspaper
Slander - making of defamatory statements, usually an oral (spoken) representation
Defamation - issuance of a false statement about another person, which causes that person to suffer harm
Examples: Wrongful eviction and invasion of privacy

Products

Products liability arises out of injury and/or damage caused by defects in product design, manufacture, or the failure to warn or explain. Exposure applies to the use of an insured's product. It begins after the sale and as soon as the product has left the premises.

Example: Packaged salad containing salmonella resulted in over 25 people being hospitalized.

Lesson 3 Topic F Classification 3: Liability p4 (ELR)

Liability Continued

Learning Objective: Identify and describe define each of the four logical classifications of exposures.

Classification 3: Liability

Completed Operations
Completed operations liability arises out of injury and/or damage caused by defective or improper workmanship.

The exposure applies to an insured's work and begins once the operations have been completed and the insured leaves the site.

Example: Three weeks after kitchen cupboards were installed for a customer, one of the cupboards fell off the wall and injured the homeowner.

Ownership, Maintenance or Use of Autos

This liability arises out of injury and/or damage due to the ownership, maintenance, or use of an auto, including entrustment and/or supervision. The exposure is normally triggered by negligence and subject to statute.

Example: An employee runs a red light while driving a company car and causes an automobile accident.

Ownership, Maintenance or Use of Other Conveyances

This exposure will vary from business to business.

Examples include the use of

1. "mobile equipment" (as defined in the policy),
2. watercraft,
3. aircraft,
4. recreational vehicles, which results in injury or damage.

Employing Workers

Exposure is subject to laws and regulations governing Workers Compensation, Employers Liability Coverage, and other employment related issues.

Liability arises from injury and/or disease to an employee and may cover various consequential injuries to others, caused by the employee's injury or disease
Examples:

1) An employee is injured during the scope of employment;
2} A defective product made by an employer injures his employee while on the job;
3) An employee suffers injury from sexual harassment

Liability Continued

Learning Objective: Identify and describe define each of the four logical classifications of exposures.

Classification 3: Liability

Liquor Manufacturing, Distribution or Sales

Exposure will vary and is subject to state statutes and case law.

Examples:

1. An individual becomes intoxicated at a company picnic, where the company provided alcoholic beverages;
2. An individual becomes intoxicated from purchasing and consuming alcoholic beverages at a bar

Environmental Impairment

Exposure may arise from direct or indirect involvement.

Examples:

Your negligent operation of a vehicle results in an accident, causing another's tank truck to overturn and spill hazardous chemicals; You purchase a site or building that contains leaking underground storage tanks or asbestos.

Professional Activities

Exposure will vary on the nature of the business and by state statute and case law.

Example:

A CPA gives the wrong advice, resulting in IRS penalties and/or fines.

Bailment

Arises out of insured's possession of other's property. The exposure will vary based on the nature of the business.

Example: A customer's electronic property is left for repair and is damaged while in your care, custody, or control.

Liability Continued

Learning Objective: Identify and describe define each of the four logical classifications of exposures.
Contractual Liability

A contract is an agreement between two or more parties, which creates an obligation to do or not to do a particular thing. Often in contracts, one party assumes the financial consequences of certain liabilities of another.

Contractual liability includes:

Assumption of liability
Breach of contract

Parties commonly involved:
Lessor-Lessee
Owner-Contractor
Contractor-Sub Contractor
Manufacturer-Distributor
A common example can be found in a lease. The firm may be required to agree to pay for any judgment assessed against its landlord because of activities at the firm's rented property.

Statutory Liability

Statutory liability holds that a person or company can be held responsible for a certain action or omission because of a related law that is not open to interpretation.

Companies often seek to indemnify themselves against penalties or fines resulting from unintentional or accidental violations of law.

Examples of statutory liability include Liquor Liability, American with Disabilities Acts, and various federal employment acts.

Example: An applicant for employment files a complaint with the Equal Opportunity Employment Commission (EEOC) on the basis he was discriminated against because of his race.

Please refer to Lesson 3 Topic F Classification 3: Liability p7 (ELR) to complete the Knowledge Check at this time.

THE NATIONAL ALLIANCE
for Insurance Education & Research

Lesson 3 Topic G - Logical Classification #4 Net Income

Lesson 3 Topic G Classification 4: Net Income p1 (ELR)

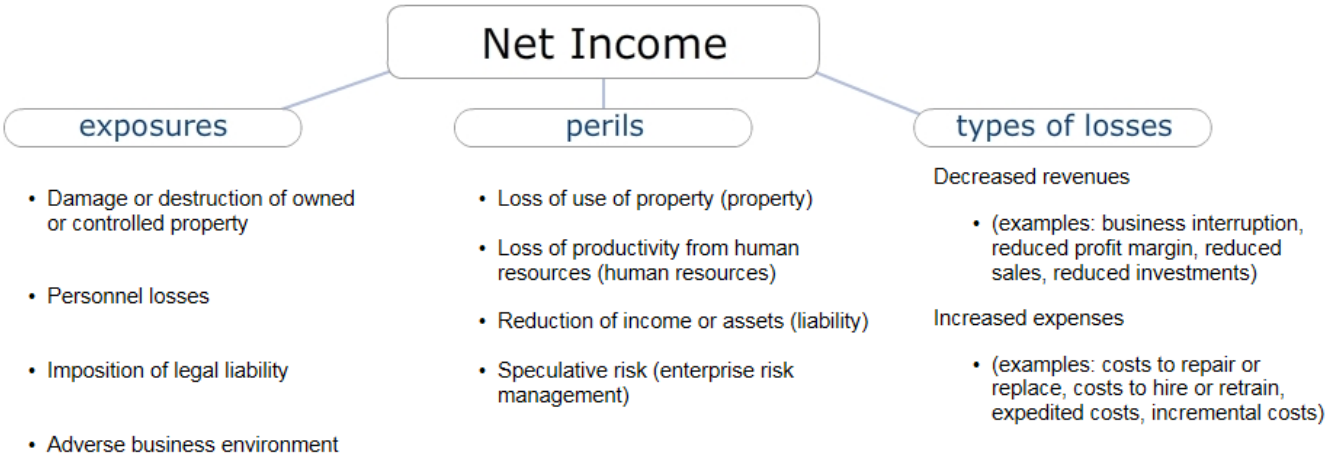
Learning Objective: Identify and describe define each of the four logical classifications of exposures.

Net income exposures arise from the other three logical classifications: property, liability, and human resources.

Lesson 3 Topic G Classification 4: Net Income p2 (ELR)

Net Income

Learning Objective: Identify and describe define each of the four logical classifications of exposures.



Lesson 3 Topic G Classification 4: Net Income p3 (ELR)

Summary of Classifications

The 6 General Classes of Risk that an organization faces and the 4 Logical Classifications serve as the starting point for risk managers identifying their organization's exposures to loss.

What tools and methods are used by risk managers to identify the organization's risks? We'll spend the rest of this section on the 10 Methods of Risk Identification.

Lesson 3 Topic H - Ten Identification Methods

Lesson 3 Topic H Identification Methods p1 (ELR)

Learning Objective: Explain the purpose, method, strengths and weaknesses for each of the 10 risk identification methods.

Risk managers and insurance professionals use various methods to identify loss exposures for their organization or client. The primary purpose for using one or more methods is to identify risks systematically and methodically.

Being able to review insurance policies, budgets, compliance issues and policies enables the risk manager to understand any limitations of the risk management program. Contract analysis, physical inspections and the use of experts can identify particular aspects of risks needed in the analysis and control steps.

Lesson 3 Topic H Identification Methods p2 (ELR)

Ten Identification Methods Continued

Learning Objective: Explain the purpose, method, strengths and weaknesses for each of the 10 risk identification methods.

We introduced Risk Identification Methods in Section 1. We'll now look at these 10 methods including the purpose, method, strengths and weaknesses of each.

The ten risk identification methods are:

1. 1.Checklist and survey
2. 2.Flowchart
3. 3.Insurance policy review
4. 4.Physical inspection
5. 5.Compliance review
6. 6.Procedures and policies review
7. 7.Contract review
8. 8.Experts
9. 9.Financial statement analysis
10. 10.Loss data analysis

Another option, while less organized and logical, is equally important: the risk manager must use common sense in seeking out loss exposures. The difference between a good risk manager and a great risk manager may lie in the subjective areas of instinct and intuition.

Lesson 3 Topic H Identification Methods p3 (ELR)

Learning Objective: Explain the purpose, method, strengths and weaknesses for each of the 10 risk identification methods.

You may be asking yourself, which one is best? The answer depends on the type of operation and the types of exposure the risk manager is trying to identify. And, rarely is only one method used.

We'll start with Method 1, Checklists, Surveys and Questionnaires.

Lesson 3 Topic H Identification Methods p4 (ELR)

Method 1: Checklists, Surveys and Questionnaires Method

Learning Objective: Explain the purpose, method, strengths and weaknesses for each of the 10 risk identification methods.

The Checklists, Surveys and Questionnaires Method uses information-gathering documents (lists and surveys) to search systematically for as many loss exposures as possible.

It is standardized, provides a history for the risk manager, is easily classified and tabulated, and, because very little training is required to use this method, can be utilized by non-risk management personnel.

Examples of checklists, surveys and questionnaires include:•List of Assets

- Activity or Situation List
- Perils Analysis
- Insurance Checklist
- Industry List

Refer to the online course to view a sample insurance checklist

---

Lesson 3 Topic H Identification Methods p5 (ELR)

Method 1 Continued

Learning Objective: Explain the purpose, method, strengths and weaknesses for each of the 10 risk identification methods.

Risk Identification Method

1. Purpose

To systematically search, using a list to identify as many exposures, perils, and hazards as possible

2. Method

Use of information gathering documents

3. Strengths
    - Standardized
    - Can be used by non-risk management personnel with minimal required training
    - Information can be easily classified and tabulated
    - Provides a history
4. Weaknesses
    - Cannot cover all areas or operations
    - Provides limited financial impact
    - Does not prioritize exposures
    - May not identify new exposures

Lesson 3 Topic H Identification Methods p6 (ELR)

Method 1 continued

Learning Objective: Explain the purpose, method, strengths and weaknesses for each of the 10 risk identification methods.

Each tool within the checklist/survey method has its own use, strengths and weakness.

Checklists, Surveys and Questionnaires

List of Assets

A checklist best suited for property and physical assets.
Strengths of this method are that it provides a list of all resources and capacities, stimulates staff to account for assets, and identifies assets that are often overlooked.

Weaknesses of this method are that it does not ordinarily address liability risks, must be updated regularly (especially when new assets are acquired), and provides varying cost estimates depending upon when the survey was completed.

Activity or Situation List

Checklist best suited for liability and human assets.

Strengths include instilling a thought process for loss prevention, evaluating equipment, personnel, and operations that function together, and identifying activities that are often overlooked.
Weaknesses include too much detail, it does not focus on the financial aspect of identification, and operations and activities may vary by locale.

Perils Analysis
Commonly used to identify the potential cause of loss from human, economic, and natural perils.
Strengths are that it provides a list of common or likely causes of loss, uses insurance terminology, and can assist in identifying perils that occur infrequently and might otherwise be missed.

Weaknesses are that new perils are created daily, old perils are forgotten or overlooked, and the analysis may become obsolete. Upper management may be skeptical of this method as well.

Insurance Checklist
Used to determine the feasibility of contractual transfer.
Strengths include that it is a definitive list of available coverage and exclusions, it evaluates exposures, and it requires limited work by the risk manager.

Weaknesses include that it is, by definition, geared to exposures that are currently insured or are conventionally insurable, and that swings in the insurance market can cause the scope of insurable exposures to expand and contract.

Industry List
Checklist specific to a certain operation or industry and is generally tailored to specific assets, activities, perils, and insurable exposures commonly found in that industry or operation.

Its strength is that it facilitates comparisons with peers.

Its weaknesses include that it can be too focused on the industry or it can be too generic. If the checklist is not created or at least edited by others outside the industry the users may continue to make the same mistakes other industry participants have made.

Lesson 3 Topic H Identification Methods p7 (ELR)

Method 2: Flowchart Method

Learning Objective: Explain the purpose, method, strengths and weaknesses for each of the 10 risk identification methods.

The Flowchart Method graphically and sequentially depicts the activities of a particular operation or process. It is process-driven and follows a logical flow. A flowchart is useful in isolating the points in a process where a quality check or the insertion of a quality assurance process might be beneficial.

Flowcharts are also effective in identifying a bottleneck in the operations as well as the existence of a concentration of values, both of which create an exposure to loss.

One flowchart for a financial institution illustrates where money travels within the institution and where it is kept. This would include the flow of money in and out of an ATM.

A flowchart for a manufacturer includes all steps in the manufacturing process which helps the risk manager identify work in progress, establish when value is added to the product, know where inventory is stored, etc.

Problem solving flowcharts display the problem to be solved, then shows branching to other criteria.

Please refer to Lesson 3 Topic H Identification Methods p8 (ELR) to view the Example Problem Solving Flow Chart at this time.

Lesson 3 Topic H Identification Methods p9 (ELR)

Flowcharts

Learning Objective: Explain the purpose, method, strengths and weaknesses for each of the 10 risk identification methods.

1. Purpose

To graphically and sequentially depict the activities of a particular operation or process to identify exposures, perils, and hazards.

2. Method
    - Product analysis
    - Dependency analysis
    - Site analysis
    - Decision analysis
    - Critical path analysis
3. Strengths
    - Can illustrate interdependency within an organization
    - Can easily pinpoint bottlenecks or chokepoints
    - Can determine critical path or critical points
4. Weaknesses
    - Does not indicate frequency or severity
    - Does not show minor processes with major loss potential
    - Limited applicability to liability exposures

- May be too process-oriented

Lesson 3 Topic H Identification Methods p10 (ELR)

Method 3: Insurance Policy Review Method

Learning Objective: Explain the purpose, method, strengths and weaknesses for each of the 10 risk identification methods.

Insurance Policy Review Method is used for reviewing an insurance contract or related documents to determine exposures and perils that are covered and those that are not covered, either because the insuring agreement does not extend to the asset or activity, or because terms, conditions, or exclusions are limiting.

Refer to the online course to view more about insurance policy review.

Lesson 3 Topic H Identification Methods p11 (ELR)

Insurance Policy Review

Learning Objective: Explain the purpose, method, strengths and weaknesses for each of the 10 risk identification methods.

1. Purpose

To determine exposures and perils covered and not covered

2. Internal Review
    - Internal Review
    - Outside Expert Review
3. Strengths
    - Many perils are given a precise definition
    - States what specifically is covered
    - States what specifically is not covered
4. Weaknesses
    - Policies are not standardized so each policy has to be reviewed individually
    - Case law may disregard what policy says
    - Addresses only exposures covered by the policy
    - May be difficult to analyze before a loss because there are so many variables that impact whether or not coverage exists

Lesson 3 Topic H Identification Methods p12 (ELR)

Method 4: Physical Inspections Method
Learning Objective: Explain the purpose, method, strengths and weaknesses for each of the 10 risk identification methods.

Physical Inspections are conducted by informational visits to critical sites, both inside and outside the organization, to determine exposures to risk.

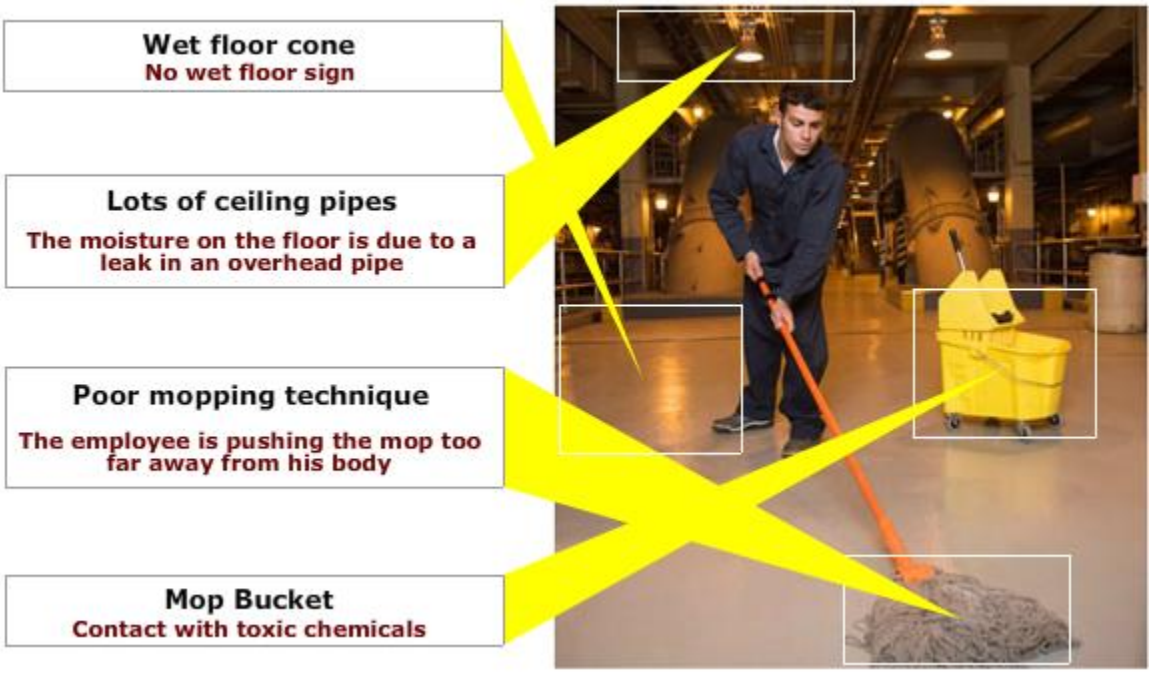
They allow the risk manager and the risk management team to personally view potential exposures. The benefits to the team's ability to conduct qualitative analyses as well as quantitative analyses are considerable.

Refer to the online course for a sample physical inspections method.

Lesson 3 Topic H Identification Methods p13 (ELR)

Performing a Physical Inspection

Learning Objective: Explain the purpose, method, strengths and weaknesses for each of the 10 risk identification methods.



On the next page, you'll match your findings to the categories listed on a checklist.

Refer to Lesson 3 Topic H Identification Methods p14 (ELR) to complete the Knowledge Check at this time.

Lesson 3 Topic H Identification Methods p15 (ELR)

Method 4 Continued

Learning Objective: Explain the purpose, method, strengths and weaknesses for each of the 10 risk identification methods.

Physical Inspections Method

1. Purpose

Informational visits to critical sites, within and outside the organization, to determine exposures, perils, and hazards

2. Method

Use internal staff, such as:

a. Risk management
b. Safety department
c. Operating personnel

External

In some cases it is appropriate to rely on physical inspections conducted by outside entities, such as:

a. Professional consultants (such as loss control experts)
b. Regulatory agencies (such as building and health department inspectors)
c. Community services (such as the fire department)
d. Insurance carrier services

3. Strengths
   - Places the examiner in the actual environment to review or critique exposures
   - Usually is personal
   - Provides visualization of processes, locations, etc.
   - May find unreported hazards and/or assets
4. Weaknesses
   - Time consuming and often expensive
   - Subject to steering by local personnel
   - Situations change often

Lesson 3 Topic H Identification Methods p16 (ELR)

Method 5: Compliance Review Method

Learning Objective: Explain the purpose, method, strengths and weaknesses for each of the 10 risk identification methods.

There are several types of compliance reviews. They can either be

- statutory (local, state, or federal) or
- professional (voluntary, involuntary, industry, or governmental insurance programs).

1. Purpose: To determine compliance with regulations and laws
2. Method:

The Compliance Review method uses a combination of internal and external sources to identify key regulations or laws and review operations to ascertain compliance.

3. Strengths

Most are free of charge and provide you with an outside opinion, whether you want it or not.

4. Most regulations and laws have their own problems and there may be little or no control over compliance evaluation. Compliance review may also focus unwanted attention on the organization and expose it to liability, fines, penalties, or injunctions.

Refer to the online course to view a sample form

Lesson 3 Topic H Identification Methods p17 (ELR)

Compliance Reviews Continued

Learning Objective: Explain the purpose, method, strengths and weaknesses for each of the 10 risk identification methods.

Examples of statutory compliance issues include local and city code enforcement, state or federal mandates imposed by either statute or regulation.

The organization itself may impose compliance with professional standards such as licensure, or membership in related associations, attainment of professional designations, and continuing education.

Compliance reviews are very important when participating in government insurance programs, such as workers compensation.

Lesson 3 Topic H Identification Methods p18 (ELR)

Method 6: Procedures and Policies Review Method

Learning Objective: Explain the purpose, method, strengths and weaknesses for each of the 10 risk identification methods.

Policy and procedures reviews are useful for maintaining up-to-date policies relating to the organization's legal responsibilities. They evaluate corporate by-laws, board minutes, mission statements, organizational charts, employee manuals, procedures manuals, and risk management policy manuals. This type of review can uncover exposures that others in the organization create, but organizational politics and realities may prevent any effective treatment of the exposures.

1. Purpose: To identify how an organization functions
2. Method
    a. Internal Review
    b. External Review
    c. Legal Review
3. Strengths: Identifies exposures within the organization
4. Weaknesses: Organizational politics may prevent effective treatment

---

Lesson 3 Topic H Identification Methods p19 (ELR)

Procedures and Policies Review Method Continued

Learning Objective: Explain the purpose, method, strengths and weaknesses for each of the 10 risk identification methods.

What kinds of items are reviewed?

- Charter and/or Articles of Incorporation
- Policies (legal and local)
- Minutes and public records of meetings
- Employee manuals-These should be department specific
- Procedures manuals-For best results these types of manuals should be process oriented

- Mission Statements-descriptive, concise, who and what we are
- Organizational charts-Review the Chain-of-Command from a risk perspective
- Risk Management policies-For example, are safety policies adequate?

Lesson 3 Topic H Identification Methods p20 (ELR)

Method 7: Contract Review Method

Learning Objective: Explain the purpose, method, strengths and weaknesses for each of the 10 risk identification methods.

Contracts come in many shapes and sizes, and businesses enter into them frequently. There are a wide variety of contracts involved. It is best to have the persons employed to enforce the contract complete the review. The reviews are completed by internal or external entities, as appropriate. Contract review helps the risk manager identify

1. gaps in the current risk management plan and
2. new "risk" created by contracts. In other words, what has the organization committed to? Does the contract contain a hold harmless or indemnity agreement? Is there a Waiver of Subrogation requirement in the lease?

1. Purpose: To identify obligations and compliance with contractual requirements
2. Method:

Contract Identification and Analysis reviews contracts, leases, hold-harmless or indemnification agreements, purchase orders and sales contracts, bills of lading, warranties, advertising materials, mergers and acquisitions, joint ventures and alliances, employment contracts, and service contracts. Reviews may be internal, external, or legal.

3. Strengths: May identify “holes” in risk management plan
4. Weaknesses: Involvement of second party may prevent control of exposures

Refer to the online course to view a sample contract review

Lesson 3 Topic H Identification Methods p21 (ELR)

Method 8: Experts Method

Learning Objective: Explain the purpose, method, strengths and weaknesses for each of the 10 risk identification methods.

Consulting with experts can help a risk manager expedite contracts, programs, and services. Expert reviews can either be internal or external. The company can usually save time and obtain more immediate benefits from the expert's experience. On the other hand, a qualified expert may be difficult to find and services can be expensive.

1. Purpose: Use of experts to identify exposures, perils and hazards
2. Method

Selection of the expert depends on the topic or product in question. Experts give professional advice, opinions and direction for resolving issues associated with a particular topic, and can either be internal (staff or operations) or external (industry or some specialty).

3. Strengths: Saves time and provides a level of experience to focus on exposure
4. Weaknesses: May be difficult to find qualified experts and external experts can be expensive

---

Lesson 3 Topic H Identification Methods p22 (ELR)

Experts Continued

Learning Objective: Explain the purpose, method, strengths and weaknesses for each of the 10 risk identification methods.

Don't forget that many experts are located within your organization:

- Staff with functional or managerial expertise: HR consultants, accountants, procurement officers, etc.
- Staff with craft skills from mechanical and operation departments: Vehicle, HVAC etc.

External experts are consultants with experience in your organization's line of business, or specialists who can focus on one function of your organization - such as loss control specialists, brokers, actuaries, etc.

Lesson 3 Topic H Identification Methods p23 (ELR)

Method 9: Financial Statement Analysis Method

Learning Objective: Explain the purpose, method, strengths and weaknesses for each of the 10 risk identification methods.

Financial Statement Analysis is used to identify values that are subject to loss, the event that could cause the loss, and the fiscal impact to the organization after the loss. The analysis can be the basis for initial insight in developing crisis contingency plans. These types of reports analyze both growth in expenses and reduction in revenues.

1. Purpose: Aid in exposure identification and valuation, financial capabilities, and financial –based decision making.

2. Method
- Evaluation of revenues
- Evaluation of expenses
- Review of Financial Statements
- Review of indebtedness and outstanding loans
- Financial ratio analysis
3. Strengths
- Assists in forecasting financial losses from a specific event
- Demonstrates financial impact from a loss on other areas within the organization
- Serves as the basis for the development of crisis contingency plans
4. Weaknesses
- Usually does not address business risks
- Unable to predict losses of sole or key suppliers, customers, or employees
- Can lead to manipulation of financial records

Note: The values shown for assets are not necessarily the amount actually at risk. The difference between "book value" and "replacement cost" must be taken into consideration when identifying risk using the financial statement analysis method.

Please refer to Lesson 3 Topic H Identification Methods p24 (ELR) to complete the Knowledge Check at this time.

Lesson 3 Topic H Identification Methods p25 (ELR)

Method 10: Loss Data Analysis Method

Learning Objective: Explain the purpose, method, strengths and weaknesses for each of the 10 risk identification methods.

Through collection, organization, and analysis, the loss data or loss history can reveal the effectiveness of the risk management program.

1. Purpose: To identify exposures and their valuation based on history
2. Method: A Loss Data Review can be performed on insurance carrier or TPA loss runs, internal loss runs, accident and incident reports, indexing loss information against exposure information, and trend analysis in losses and exposures.
3. Strengths: Can be used for benchmarking and determining if losses were caused by or the result of a risk not previously identified.
4. Weaknesses:

- Since data is historical or "after the fact," the method is reactive rather than proactive
- History does not always repeat itself
- Losses may not have occurred in the past
- Data credibility may be an issue

Please refer to Lesson 3 Topic H Identification Methods p26 (ELR) to complete the Knowledge check at this time.

THE NATIONAL ALLIANCE
for Insurance Education & Research

Lesson 4 - Risk Analysis

Lesson 4 Intro p1 (ELR)

Once an organization's exposures to loss have been identified during Step 1 Risk Identification, it is time to analyze those exposures for several reasons as follows.

During Step 2 Risk Analysis, the risk manager will collect data from a variety of sources and conduct both qualitative and quantitative analyses. These analyses enable the risk manager to project expected losses, also referred to as a "loss pick."

With this information, the risk manager is also able to determine which exposures to loss have greater potential to negatively impact the organization and then recommend or implement the appropriate risk control technique and arrange financing accordingly. The analysis can also be used to benchmark the organization's results against similar organizations or against itself to monitor the effectiveness of the organization's risk management program.

Lesson 4 Intro p2 (ELR)

Lesson 4 – Learning Objectives

After completing this lesson, you will be able to:

1. Discuss how collection and analysis of loss data aids an organization with decision making.
2. Discuss the ways in which the credibility of data is evaluated.
3. Distinguish between qualitative analysis and quantitative analysis and understand the purpose of each.
4. Discuss the use of benchmarking in risk management.

Lesson 4 Topic A - Collecting & Analyzing Loss Data

Lesson 4 Topic A Collecting and Analyzing Loss Data p1 (ELR)

Learning Objective: Discuss how collection and analysis of loss data aids an organization with decision making.

The collection and analysis of loss data helps an organization identify and understand the potential impact those losses may have on the organization's net income, risk management program and the total cost of risk. The risk manager then uses this information when making decisions or recommendations for the following:

1. Loss Control Programs
2. Products/Product Safety
3. Methods of Financing
4. Insurance
5. Cost of Risk Allocations
6. Performance Evaluation

Lesson 4 Topic A Collecting and Analyzing Loss Data p2 (ELR)

Loss Data Analysis and Loss Control Programs

Learning Objective: Discuss how collection and analysis of loss data aids an organization with decision making.

Loss Data Analysis and Loss Control Programs

Which exposures to loss need to be controlled? Before loss control decisions can be made, the risk manager needs to know:

- Causes of loss frequency and severity
- Trends in loss experience, e.g. increases in frequency or severity, trends showing decreases.

What will the risk manager do with this information?

Evaluate the effectiveness of the current loss control programs

Are they working? Is there a reduction in either frequency or severity since the loss control techniques were implemented? Example: Has the number of auto accidents decreased since the fleet safety program was implemented 2 years ago?

Evaluate potential costs and benefits of loss control alternatives to gain support

Example: The analysis shows a high frequency of employees with back injuries. What loss control methods could be implemented and what are the costs? What is the expected reduction in losses and costs for each method?

Evaluate the performance of outside service providers.

Example: Two years ago the organization contracted with a third-party administrator to manage the claims administration of its workers compensation program. How does the current loss severity compare to when the organization was managing its own claims?

Lesson 4 Topic A Collecting and Analyzing Loss Data p3 (ELR)

Loss Data Analysis and the Organization's Products or Services

Learning Objective: Discuss how collection and analysis of loss data aids an organization with decision making.

Analysis of loss data can help the organization address product/service development and pricing. What if during the analysis, the risk manager discovers that during the past couple of years a particular product or service is the leading cause of loss frequency or severity? Worse yet, the trend indicates both are on the rise.

As a result of this information, the organization may decide to:

- Include total cost of risk in its pricing of products and services
- Redesign the product or service to reduce the frequency and/or severity
- Terminate production of the product or service

Lesson 4 Topic A Collecting and Analyzing Loss Data p4 (ELR)

Loss Data Analysis and the Organization's Products or Services continued

Learning Objective: Discuss how collection and analysis of loss data aids an organization with decision making.

The analysis also provides the organization with the information it may need to respond to litigation or regulatory actions from:

- Litigation
- Occupational Safety and Health Administration's Survey of Occupational Injuries and Illnesses (SOII)
- Consumer Product Safety Commissions
- Environmental Protection Agency
- Federal Drug Administration

By gathering and analyzing loss data, the risk manager has the ability to respond in a meaningful way.

Lesson 4 Topic A Collecting and Analyzing Loss Data p5 (ELR)

Loss Data Analysis and the Organization's Method of Financing

Learning Objective: Discuss how collection and analysis of loss data aids an organization with decision making.

Risk managers will draw upon loss data analysis when determining the appropriate method to finance losses including the following:

- Determine risk appetite
- Assess retention levels
- Choose deductibles and limits
- Establish a basis for allocating premiums and/or loss costs
- Address cash flow and budgets

These areas will be discussed in Lesson 5 Risk Financing.

Lesson 4 Topic A Collecting and Analyzing Loss Data p6 (ELR)

Loss Data Analysis and the Organization's Insurance Programs

Learning Objective: Discuss how collection and analysis of loss data aids an organization with decision making.

Loss data analysis is also useful when insurance is selected to finance certain losses. Knowledge of the organization's past loss history is beneficial to the risk manager when:

- Negotiating premiums
- Determining coverage restrictions and exclusions
- Setting appropriate reserves for loss-sensitive programs
- Establishing collateral, e.g., letters of credit, surety bonds, etc.

For example, insurance professionals assisting the risk manager are interested in loss data analysis because it reveals the organization's loss experience. This has direct impact on the negotiation of rates and coverage with underwriters and determining annual premiums.

These areas will be discussed in Lesson 5 Risk Finance.

Lesson 4 Topic A Collecting and Analyzing Loss Data p7 (ELR)

Loss Data Collection and Analysis and the Cost of Risk

Learning Objective: Discuss how collection and analysis of loss data aids an organization with decision making.

Loss data collection and analysis helps build the foundation on which the risk manager calculates the organization's total cost of risk. Losses can impact all five components of cost of risk. Loss data analysis equips the risk manager to:

- Focus management's attention on the organization's cost of risk
- Evaluate potential costs and benefits of alternative methods for financing losses

- Reduce and control losses by allocating losses to the departmental level

---

Lesson 4 Topic A Collecting and Analyzing Loss Data p8 (ELR)

Loss Data Collection and Analysis and Performance Evaluation

Learning Objective: Discuss how collection and analysis of loss data aids an organization with decision making.

The risk manager may gather and analyze loss data to use as a basis for establishing and monitoring vendor performance agreements, such as;

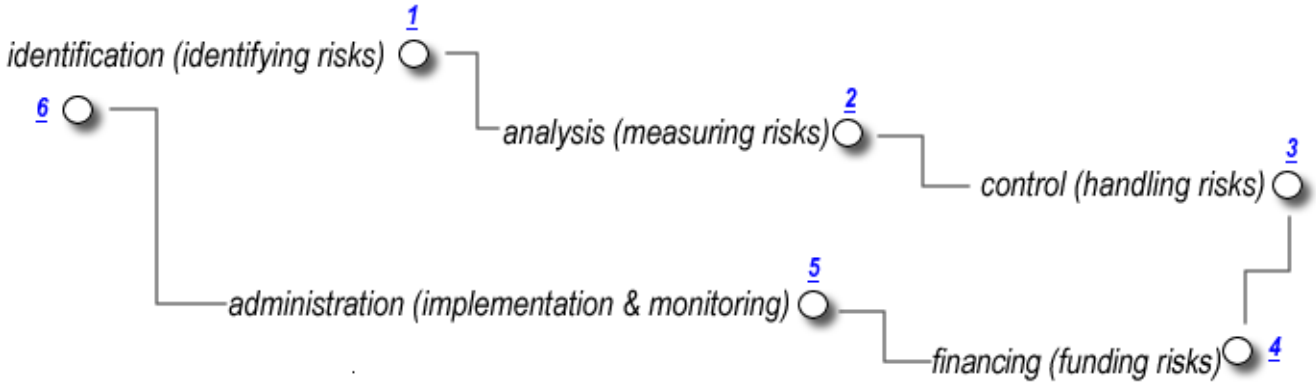
- Third-party administrators
- Loss control services

Please refer to Lesson 4 Topic A Collecting and Analyzing Loss Data p9 (ELR) to complete the Knowledge Check at this time.

Lesson 4 Topic A Collecting and Analyzing Loss Data p10 (ELR)

Loss Data Collection? Analysis and the Risk Management Process

The issue of gathering and analyzing loss data provides an opportunity to show how steps of the risk management process interact with one another.



1. Identification is the first and most important step.
2. Determining frequency/severity of risk helps determine the method(s) used to control the risk.
3. The degree to which a risk can be controlled plays an important role in selecting the method (or methods) to finance losses.
4. Determining whether to transfer or retain the risk is a key function of the risk financing step.

5. The cost of risk can be negatively impacted if the appropriate implementation and monitoring is not achieved.
6. Monitoring and implementation helps identify new risk issues to address.

Lesson 4 Topic A Collecting and Analyzing Loss Data p11 (ELR)

Benefits of Loss Data Collection & Analysis to Risk Control

Learning Objective: Discuss how collection and analysis of loss data aids an organization with decision making.

Consider 4 ways that loss gathering and analysis activities benefit the risk control program.

1. Allows Risk Professionals to Focus on the Organization's Loss Experience

The risk manager is enabled by an effective program of loss data gathering and analysis when he or she is looking for trends in the organization's loss experience.

2. Prioritizes Loss Control Issues

The most severe/frequent losses can controlled more quickly.

3. Allows Improved Cost/Benefit Analysis of Loss Control Efforts

A disciplined program of loss data gathering and analysis helps the risk manager to evaluate costs vs. benefits of the loss control methods in use. He or she is also in a better position to do cost/benefit analysis for new control methods under consideration.

4. Helps the Risk Manager Gain Support for Loss Control Efforts

Loss run analyses can be presented in graphic format when communicating about the Risk Management Program to stakeholders.

Lesson 4 Topic A Collecting and Analyzing Loss Data p12 (ELR)

Benefits of Loss Data Collection & Analysis to Risk Financing

Learning Objective: Discuss how collection and analysis of loss data aids an organization with decision making.

Consider 2 ways that loss gathering and analysis activities benefit the risk financing program.

1. Helps in Evaluating the Cost/Benefits of Risk Finance Efforts

Loss histories are useful when looking at new or alternative forms of risk finance.

How?

- Working with loss runs helps the risk manager decide what to insure and the level of retention.
- Property values and past claims history influence the selection of limits and deductibles.
- Loss analysis influences the selection of a loss sensitive plan or a plan with a cash flow advantage.

Lesson 4 Topic A Collecting and Analyzing Loss Data p13 (ELR)

Benefits of Loss Data Collection & Analysis to Risk Administration

Learning Objective: Discuss how collection and analysis of loss data aids an organization with decision making.

A comprehensive program of loss data gathering and loss data analysis is key to the Risk Administration function: monitoring effectiveness of the risk management program.

This information will be of interest to anyone associated with risk identification, risk control, risk finance and implementation of the program. Stakeholders who use loss data analysis include: managers, supervisors, employee safety program directors, insurance carriers, third party administrators, brokers, managed care administrators.

Please refer to Lesson 4 Topic A Collecting and Analyzing Loss Data p14 (ELR) to complete the Knowledge Check at this time.

THE NATIONAL ALLIANCE
for Insurance Education & Research

Lesson 4 Topic B - The Difference Between Qualitative and Quantitative Analysis

Lesson 4 Topic B Qualitative Analysis vs. Quantitative Analysis p1 (ELR)

Learning Objective: Distinguish between qualitative analysis and quantitative analysis and understand the purpose of each.

As introduced in Lesson 1, Qualitative and Quantitative are the two types of analyses performed by risk managers.

QuaLitative = Language
QuaNtitative = Numbers

Note: Loss Data Assessment is one type of Qualitative Risk Analysis.

Two other types of analyses, risk assessment and financial risk assessment, can be considered to be "qualitative" as well. We will focus only on Loss Data Assessment in this course.

Lesson 4 Topic B Qualitative Analysis vs. Quantitative Analysis p2 (ELR)

Qualitative Risk Analysis the "what" analysis process

Learning Objective: Distinguish between qualitative analysis and quantitative analysis and understand the purpose of each.

Loss Data Assessment

Identify, understand and apply various methods of assessing loss data and analyze the impact those losses may have on the organization's risk management policy and the ultimate cost of risk.

Risk Assessment

Identify and assess those loss exposures that cannot be easily measured by traditional statistical or financial methods and to understand their impact on the ultimate risks and performance.

Financial Risk Assessment

Identify and assess those broad loss exposures that have a financial impact on the organization but that may be difficult to quantify.

Lesson 4 Topic B Qualitative Analysis vs. Quantitative Analysis p3 (ELR)

Quantitative Analysis
Learning Objective: Distinguish between qualitative analysis and quantitative analysis and understand the purpose of each.

Quantitative Analysis is the "how much" analysis process; attempts to accurately measure risks by using acceptable traditional methodologies which calculate relative values.

- Loss projections or forecasts
- Cash discounting and net present value (NPV) calculations
- Cost-benefit analyses
- Total Cost of risk calculations and analyses

Please refer to Lesson 4 Topic B Qualitative Analysis vs. Quantitative Analysis p4 (ELR) to complete the Knowledge Check at this time.

Lesson 4 Topic C - Sources of Loss Data

Lesson 4 Topic C Sources of Loss Data p1 (ELR)

Learning Objective: Discuss how collection and analysis of loss data aids an organization with decision making.

Internal Sources

The organization's loss experience.

Examples:

- Accident or incident reports
- First aid logs
- OSHA logs
- Insurance carrier or TPA loss runs
- Litigation records
- Accounting entries on financial statements

External Sources

Other organization's loss experience

Examples:

- Industry associations
- Insurance company loss runs (company-wide, not insured-specific)
- Bureau of Labor Statistics incident rates (NAICS code)
- Bureau of Transportation Statistics
- National Safety Council (Accident Facts - Occupational and Non-Occupational)
- Risk and Insurance Management Society Cost of Risk Survey
- National Council on Compensation Insurance

While this loss data provides the experience of other organizations, the collective experience may be useful a several levels. First, it may indicate losses that others have experienced that have not yet affected the organization. Second, the accumulation of loss data may provide a degree of credibility that the organization's loss data is missing.

Lesson 4 Topic D - Specific Types of Loss Data that Should be Collected

Lesson 4 Topic D Types of Loss Data p1 (ELR)

Learning Objective: Discuss how collection and analysis of loss data aids an organization with decision making.

Now that you know the sources of data, what specific data should the risk manager collect? While the risk manager is interested in the number of losses (frequency) and the size of losses (severity), there is additional data that is also of importance to the risk manager.

We will look more closely at each type of data on the following pages.

1. Category of loss
2. Date and time of loss
3. Claimant
4. Location
5. Hazard
6. Cause
7. Type
8. Body part
9. Management

Lesson 4 Topic D Types of Loss Data p2 (ELR)

Examples of Loss Data

Learning Objective: Discuss how collection and analysis of loss data aids an organization with decision making.

1. Category of loss - property damage, auto accident, industrial injury, injury from product
2. Date and time of loss - year, date, day of week, shift, time of day
3. Claimant - name, date of hire, occupation, shift
4. Location - division, plant, department, operation point
5. Hazard - noise level, floor surface, lack of protection, weather
6. Cause - fall from height, repetitive motion, inhalation, lifting, twisting
7. Type - sprain/strain, laceration, disease, water damage, auto physical damage
8. Body Part - left wrist, lower back, eye, etc.
9. Management - supervisor, team leader

Lesson 4 Topic D Types of Loss Data p3 (ELR)

Types of Loss Data
Learning Objective: Discuss how collection and analysis of loss data aids an organization with decision making.

Collecting this data enables the risk manager to identify trends. For example, are most workers compensation losses occurring during one specific shift or during one day of the week? Are newer employees getting injured on the job more frequently than long-time employees or is it the other way around?

If newer employees are more likely to be injured on the job, the risk manager may implement more effective safety training at the time of hire. If the long-time employees are being injured more frequently, the risk manager may implement “refresher” safety training. If the data shows there are more back injuries caused when employees lift boxes in the warehouse, proper lifting techniques training may be required to reduce the frequency of losses.

Collecting this variety of loss data can be very useful to the risk manager in reducing the frequency and/or severity of losses.

Lesson 4 Topic E - Evaluating and Ensuring the Credibility of Loss Data

Lesson 4 Topic E Credibility of Loss Data p1 (ELR)

Learning Objective: Discuss the ways in which the credibility of data is evaluated.

It is one thing to collect loss data; it is another to collect quality loss data; that is, data that can be accurately and effectively analyzed by the risk manager and used to project the organization's expected losses (loss pick).

There are four methods of assessing the quality of loss data.

1. Completeness
2. Consistency
3. Integrity
4. Relevance

Lesson 4 Topic E Credibility of Loss Data p2 (ELR)

Components of Credible Loss Data

Learning Objective: Discuss the ways in which the credibility of data is evaluated.

Completeness

Statistical analysis is invalid if the data set used is incomplete. It is important to guard against using duplicate reports and incorrect location codes. Also, incurred but not reported claims (IBNR) must be included in the analysis.

The following items are components of complete data:

- All losses are included and reported, including losses not covered by insurance because of deductibles or exclusions or limits
- Enough loss data (frequency); a rule of thumb is at least 5 years of data, preferably 10+ years
- Adequate details about each data record (date of loss, cause of loss, person causing loss, person injured, type of loss, dollar value of loss, etc.)
- Complete description of paid and open reserve amounts

Lesson 4 Topic E Credibility of Loss Data p3 (ELR)

Components of Credible Loss Data continued

Learning Objective: Discuss the ways in which the credibility of data is evaluated.

Consistency

Comparisons are invalid if the same items (apples to apples) are not used.

Do not compare the number of back strains to the number of back sprains. Be sure to compare within the same policy years, deductible levels and valuation periods.

Analysis is invalid if the criteria and/or definitions regarding the data is inconsistent or misunderstood. Make sure that hazards, injury type, cause of loss, etc. are all consistently defined.

The following items are components of consistent data:

- Same types of data provided for each data record (type, cause, time, claimant name, length of employment, etc.)
- Same policy year, accident year, calendar year
- Same recording methodology (differences between carriers, TPA's)
- Same definitions of types of injuries, perils, hazards, etc.

Lesson 4 Topic E Credibility of Loss Data p4 (ELR)

Components of Credible Loss Data continued

Learning Objective: Discuss the ways in which the credibility of data is evaluated.

Data Integrity

The following items are components of data integrity:

- Reliability of data and accuracy of input (errors, omissions, duplications)
- Prompt reporting and current data
- Accuracy of loss reserves

Example:

The company has 10 years of data on slip and fall accidents. The reporting requirements and definition for this cause of injury have not changed during that time and accuracy of the data has been validated separately. The data is determined to have sufficient integrity for analysis and planning purposes.

Lesson 4 Topic E Credibility of Loss Data p5 (ELR)

Components of Credible Loss Data continued

Learning Objective: Discuss the ways in which the credibility of data is evaluated.

Relevance

Relevance is data that will yield information on matters of concern to the organization. The risk manager needs to be sure that the loss data under analysis is related to the risk he is seeking to mitigate. For example, he would have no use for slip and fall injury data while developing mitigation strategies to reduce vehicle accidents.
All of the following affect the relevance of loss data:

Discontinued operations:

Do not include data from operations or activities that are no longer part of the organization.

Acquiring operations:

Include the loss data from the portion of the acquired organization only. If the retail side of a business was acquired, but not the wholesale side, do not include loss information for the wholesale side.

Commingling of data:

Do not combine data from diverse operations when trying to analyze losses. For example, if losses associated with your organization's manufacturing plant are being analyzed, do not include losses related to your restaurant operations. Loss data from the manufacturing plant is not relevant to loss data from the restaurant and will cause inconsistency when analyzing the frequency, severity, types and causes of losses.

Irrelevant data:

Do not include unnecessary data.

Lesson 4 Topic E Credibility of Loss Data p6 (ELR)

Changes in Exposures

Learning Objective: Discuss the ways in which the credibility of data is evaluated.

What changes in exposures can you think of?

- the introduction of a new product or service
- new equipment, materials, or work processes
- acquisition, divestiture, merger, restructuring
- changes in legal and regulatory matters, including statutory benefits

- changes in the social and economic environment, including inflation
- labor and management issues
- the introduction (or retirement) of safety, incentive, or awards programs
- new deductible or retention levels
- changes in the insurance carrier or third-party administrator
- changes in insurance coverage (exclusions, extensions)
- changes in the demographic of the customer or constituent base

---

Please refer to Lesson 4 Topic E Credibility of Loss Data p7 (ELR) to complete the Knowledge Check at this time.

Lesson 4 Topic F - Purpose of Quantitative Analysis Tools

Lesson 4 Topic F Basics of Quantitative Analysis p1 (ELR)

Learning Objective: Distinguish between qualitative analysis and quantitative analysis and understand the purpose of each.

The analysis of loss and exposure data ultimately provides the information needed to allocate resources. Remember, the risk manager's objective is to protect the assets and financial well-being of the organization.

Lesson 4 Topic F Basics of Quantitative Analysis p2 (ELR)

Purpose of Quantitative Analysis Tools

Learning Objective: Distinguish between qualitative analysis and quantitative analysis and understand the purpose of each.

Determine loss picks and assist in forecasting losses for subsequent years.

Example: Loss Trends

Our risk manager, Roger, needs an accurate estimate of what the organizations should expect in workers compensation losses during the next year. To do so, Roger will need to "develop" losses to take into consideration losses that have not yet been reported as well as those loss revenues that may increase from now until the time the loss is settled and closed.

Determine retention, deductible, and transfer levels for decision making.

Example: Retention & Transfer Decisions After analyzing the organization's auto physical damage losses over the past five years, Roger purchased insurance with a $1,000 deductible. As a result, he was able to save the company money by selecting vehicle insurance coverage with a $1,000 deductible and a $50,000 aggregate stop loss.

Compare funding programs for cost effectiveness.

Example: Cost Effectiveness of Funding Programs After determining his organization's expected losses, Roger compared the total cost of a Large Deductible Plan against a Retrospective Rating Plan for his organization's workers compensation.

Determine which projects to fund

Example: Funding Choices The risk manager was given a choice to fund only one of three potential projects due to limited availability of funds. By conducting a cost-benefit analysis, Roger was able to determine that by

investing $70,000 in a sprinkler system at one location, the company would recover the installation costs within a five year period by realizing a reduction in retained losses during that time.

Determine appetite for risk.

Example: Appetite for Risk

The CFO has asked that Roger, the risk manager for the organization, take every possible action in order to assure that no company funds would be paid out in litigation settlements stemming from actions of the board.

Consequently, Roger decided to purchase a Director's and Officer's policy for the organization with several additional coverages and features at a higher premium than other available coverages.

Lesson 4 Topic F Basics of Quantitative Analysis p3 (ELR)

Common Tools Used in Quantitative Analysis

Learning Objective: Distinguish between qualitative analysis and quantitative analysis and understand the purpose of each.

In many cases, loss data is prepared by actuaries or insurance companies using statistical calculations on behalf of the organization to identify trends.

Such calculations are outside the scope of this course, however, we will provide you with an overview of the basic tools for risk analysis. Often, a combination of the following is more effective in displaying, discussing, and making decisions regarding the organization's mitigation efforts.

1. **Graphs** – used to establish and visualize trends and identify anomalies. (See graph on next page.)

2. **Measures of central tendency** – used to forecast losses and make decisions on retention/deductible levels; they should always be used in conjunction with other tools.

3. **Measures of dispersion and confidence intervals** – used to forecast a range of losses and make decisions on retention/deductible levels.
4. **Development factors, inflation index factors, and exposure bases** – used to estimate indexed ultimate total loss allowing for more accurate comparisons from year to year.

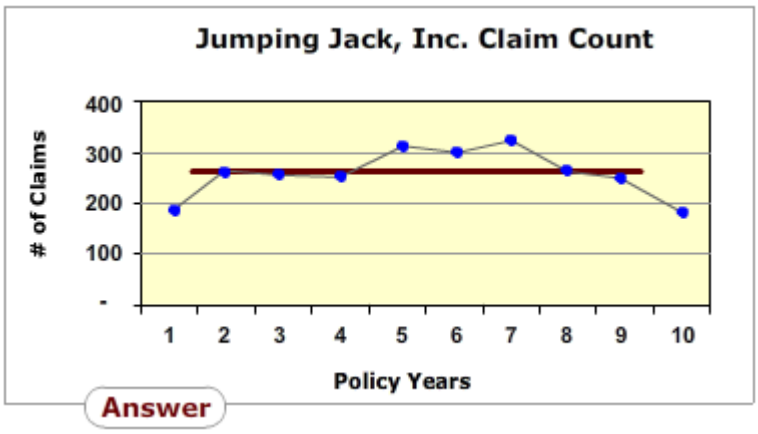
Lesson 4 Topic F Basics of Quantitative Analysis p4 (ELR)

Common Tools Used in Quantitative Analysis continued

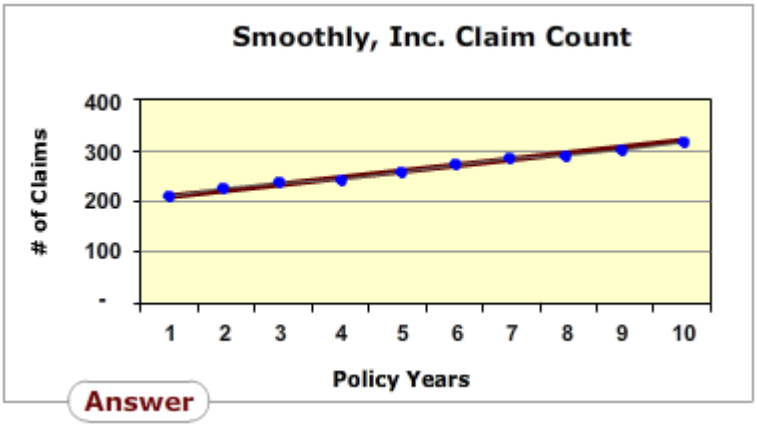
Learning Objective: Identify common tools for quantitative analysis.

Below are claims count graphs for two companies, Jumping Jack, Inc. and Smoothly, Inc.. When you look at the data, you can see how the companies got their names. For each graph, consider whether you would feel comfortable predicting the losses for year 11.

Do you feel that you can predict this by looking at these graphs? Click on each "Answer" below.



Jumping Jack, Inc. reveals the unpredictability of its claims when viewed over a 10 year period. There is no obvious trend, making a prediction of next years' losses (X11) highly speculative.



Smoothly, Inc. on the other hand, has had a predictable increasing number of claims over the 10 year period. The annual increase in claims has increased so steadily and predictably that the obvious trend could be used to predict next years' # claims (X11) with a fairly high degree of confidence.

Lesson 4 Topic G – Benchmarking

Lesson 4 Topic G Benchmarking p1 (ELR)

Learning Objective: Describe when to use benchmarking in risk management.

We will end our study of Risk Analysis with a discussion on Benchmarking.

Benchmarking is "continually comparing an organization's performance to itself or against that of the best in industry (competitors) or best in class (those recognized in performing certain functions) to determine what should be improved."

Lesson 4 Topic G Benchmarking p2 (ELR)

Benchmarking Continued

Learning Objective: Describe when to use benchmarking in risk management.

The benefits to benchmarking include tracking continued improvement, being able to enhance "out-of-the-box" thinking and creativity, and prioritizing areas that need improvement.

To recap, benchmarking can include:

1. Comparison to "best in industry" or competitors
2. Comparison to "best in class" or those recognized as performing certain functions at a high level
3. Comparison of "self" over time

Lesson 4 Topic G Benchmarking p3 (ELR)

Examples of Benchmarking

Learning Objective: Describe when to use benchmarking in risk management.

Example 1

The risk manager for a national beverage distributor is interested to see how his organization's workers compensation losses compare to other national beverage distributors. If the other distributor is experiencing fewer losses, the risk manager may conduct research to find out what steps they have taken to reduce losses.

Example 2

After several years of losses related to employee substance abuse, the risk manager finally got management support and funding to implement a Substance Abuse Program. The risk manager can now compare the current year's losses against losses in previous years to determine if the Substance Abuse Program is effective.

Lesson 4 Topic G Benchmarking p4 (ELR)

Objectives of Benchmarking

Learning Objective: Describe when to use benchmarking in risk management.

Benchmarking is also a measurement of the effectiveness of an organization's policies, products, programs, strategies, etc., as compared to standard measurements, or similar measurements of the best-in-class organizations. The objectives of benchmarking are

1. to determine what and where improvements are called for,
2. how other firms achieve their high performance levels, and
3. to use this information to improve performance.

Benchmarking should be used when a baseline program has been established, and internal trending and comparisons are needed and/or improvement opportunities are sought.

Lesson 4 Topic G Benchmarking p5 (ELR)

Pitfalls of Benchmarking

Learning Objective: Describe when to use benchmarking in risk management.

Common pitfalls of benchmarking:

- Belief that being lower (or higher) is better
- Implying more precision or accuracy than what really exists
- Inappropriate comparison groups - "apples to oranges" e.g., comparing a manufacturing operation to a sales office
- Inconsistent comparison data - comparing data that varies from group to group
- Insufficient comparison group population - not enough data
- Focus on one causation or factor - several factors usually contribute to unfavorable results
- One-time, point-in-time comparisons in a dynamic environment
- "Slightly" different comparison data can make the comparison
- "slightly" invalid
- Statistically invalid comparisons - work injuries to auto accidents
- Statistically massaged data

- Unknown data - data from a questionable source

Please refer to the end of Lesson 4 to begin Self Quiz 4 at this time.

THE NATIONAL ALLIANCE
for Insurance Education & Research

Lesson 5 - Risk Control

Lesson 5 Intro p1 (ELR)

After an organization's exposures to loss have been identified during Step 1 - Risk Identification and then analyzed during Step 2 – Risk Analysis, it is time to select and apply the appropriate risk control techniques necessary to reduce the frequency and/or severity of potential losses.

Successful risk control programs are based on careful risk identification and risk analysis.

Lesson 5 Intro p2 (ELR)

Lesson 5 – Learning Objectives

After completing this lesson, you will be able to:

1. Define risk control and discuss its role in the risk management process.
2. Discuss the key elements of the five types of risk control techniques.
3. Define claims management and explain its role in a risk control program.

Lesson 5 Topic A - Risk Control

Lesson 5 Topic A Control of Risk p1 (ELR)

Learning Objective: Define risk control and discuss its role in the risk management process.

The focus of risk control is to find solutions that will prevent or reduce losses to the organization.

Risk control is a people process – individuals throughout the organization must be involved in all aspects of an effective risk control program.

Definition of risk control: any conscious action or inaction to minimize, at the optimal cost, the probability, frequency, severity, or unpredictability of loss.

Lesson 5 Topic A Control of Risk p2 (ELR)

Three Important Impacts on the Risk Control Step

Learning Objective: Define risk control and discuss its role in the risk management process.

Activities from the Identification and Analysis Steps help shape the organization's Risk Control program.

Risk Identification Methods

Identification Methods

We discussed the ten methods in Section 3. Risk Control activities interact most frequently with the Identification and Analysis Steps.

Incident Analysis

Incident analysis involves tracking incidents without regard to subsequent accidents, losses, occurrences or claims. Reporting procedures, tracking and review may be specific to the organization. Incident analysis is more effectively managed by using a risk management information system (RMIS).

By tracking and analyzing incidents, risk control techniques can be applied:

- in a manner more timely to the event,
- as a preemptive act, avoiding or minimizing the chance of an incident,
- in a manner that reinforces risk control practices involving employees, or
- to demonstrate due diligence or reasonable investigation in defense of claims.

Cost Benefits Analysis

Cost-benefit analysis is a financial decision-making tool used to help management choose between risk control alternatives.

The risk manager can compare the present value costs (cash outflows) with present value benefits (reductions in losses and other cash inflows) over time to measure the best rate of return.

Losses, probabilities, interest rates, and cash flows require assumptions that may vary from expected.

The solution with the best rate of return may not be chosen unless it is compatible with the organization's management philosophy.

Lesson 5 Topic A Control of Risk p3 (ELR)

Frequency and Severity

Learning Objective: Define risk control and discuss its role in the risk management process.

Frequency

The number of times an incident, accident, or occurrence occurs

Through analysis of historical loss data, it is determined that the organization has had only 3 losses due to fire over the past 10 years

Severity

The monetary or financial impact of losses.

Although 2 of the tire losses resulted in only minor financial losses, the third fire cost the organization $3,000,000.

Lesson 5 Topic A Control of Risk p4 (ELR)

The Relationship Between Frequency, Severity, and Risk Control

Learning Objective: Define risk control and discuss its role in the risk management process.

Determining the frequency and severity of risks can help you identify the best methods for controlling them.

Frequency + Severity = Risk Control Method

Please refer to Lesson 5 Topic A Control of Risk p5 (ELR) to complete the Knowledge Check at this time.

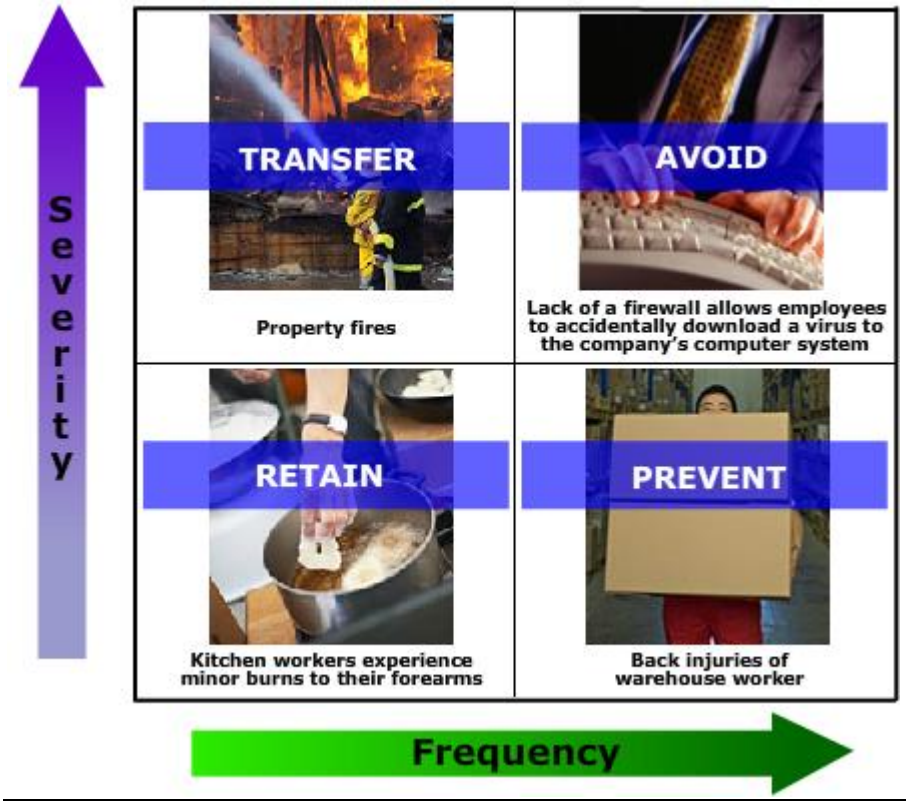
Please refer to Lesson 5 Topic A Control of Risk p6 (ELR) to complete the Frequency & Severity Chart at this time.

Please refer to Lesson 5 Topic A Control of Risk p7 (ELR) to complete the Knowledge Check at this time.

Lesson 5 Topic A Control of Risk p8 (ELR)

The Frequency Severity Chart – Summary

Because of this correlation, the risk manager can decide on a risk control method for a loss, given its frequency and severity data.



Lesson 5 Topic B - Risk Control Techniques

Lesson 5 Topic B Primary Risk Control Techniques p1 (ELR)

Learning Objective: Discuss five primary types of risk control techniques.

1. Avoidance

Eliminating an activity or exposure which eliminates chance of loss

2. Prevention

Breaks sequence of events that leads to a loss or that makes the event less likely

3. Reduction

Reducing the severity or financial impact from unpreventable losses

4. Segregation/separation/duplication

Work primarily to reduce the severity of the loss

5. Transfer (Contractual, physical, or both)

Have another party be financially responsible for all or a partial amount of the loss

---

Lesson 5 Topic B Primary Risk Control Techniques p2 (ELR)

Risk Control Technique #1 – Avoidance

True risk avoidance is totally eliminating an activity and/or exposure to an activity. Avoidance means choosing not to engage in an activity or owning the property in question to begin with OR eliminating the activity with which the organization is already engaged in or getting rid of property it owns.

Avoidance eliminates the chance of loss. It is a self-sufficient risk control technique, and no further action is required so long as the activity is fully eliminated.

Lesson 5 Topic B Primary Risk Control Techniques p3 (ELR)

Avoidance Continued

Learning Objective: Discuss five primary types of risk control techniques.

A college attracts a large number of students with its international programs. Chances are good that the college will not seriously consider a recommendation to close its campus in Europe, just because the risk manager is concerned about the frequency and severity of losses that have occurred in the past five years.

Avoidance is often not feasible.

As you can imagine, avoidance may be a difficult technique to "sell" to management for several reasons.

- Eliminating the activity or property may be in conflict with the goals and profit motives of the organization.
- The organization relying on the revenue from the activity or product you are recommending be avoided may not be in favor of the recommendation.
- The activity may be inherent to the overall corporate mission or identity.
- It is also a difficult technique to implement because the risk manager may lack the appropriate decision-making authority.

Lesson 5 Topic B Primary Risk Control Techniques p4 (ELR)

Avoidance continued

Learning Objective: Discuss five primary types of risk control techniques.

Example:

Gephardt, Inc. owns several large shopping malls in the Pacific Northwest. Under discussion is whether to provide valet parking services for shoppers.

After identifying and analyzing the potential loss exposures from a valet service, the risk manager has recommended to management that valet parking not be provided.

It is important to remember that when avoidance is applied and the activity is discontinued, it eliminates future losses; however, there may still be an exposure from the past activities.

Example:

A firm has decided to discontinue manufacturing a product that has been responsible for injuries to children. While the product is no longer being made available, previously sold products are still in the marketplace and subject to losses and claims.

Lesson 5 Topic B Primary Risk Control Techniques p5 (ELR)

Risk Control Technique #2 – Prevention

Learning Objective: Discuss five primary types of risk control techniques.

The goal of loss prevention is to reduce the frequency of types of claims from activities or property that cannot or will not be avoided. The term “prevention” implies an action taken to break the sequence of events that may lead to a loss, or at least to make it less likely; loss prevention interrupts the “domino” effect whereby one hazardous event leads to another, resulting in incidents or accidents. It also allows entities to conduct operations that might otherwise have to be avoided.

Loss prevention does not reduce severity; it reduces frequency.

Example: performing preventative maintenance on company vehicles.

Lesson 5 Topic B Primary Risk Control Techniques p6 (ELR)

Risk Control Technique #3 – Reduction

Learning Objective: Discuss five primary types of risk control techniques.

The goal of loss reduction is to reduce the severity or financial impact from losses that are not prevented. It presumes a loss will occur but attempts to reduce the size or extent of the loss. Loss reduction techniques can be applied both before and after a loss.

Pre-Loss

Loss reduction techniques can be applied before the loss.

Example: Fire suppression equipment is installed to reduce the severity of a fire loss.

Post-Loss

Even after a loss has occurred, loss reduction techniques can be effective.

Example: Two major management processes that can significantly reduce the severity of losses are the organization's claims management process, and its crisis management plan.

Lesson 5 Topic B Primary Risk Control Techniques p7 (ELR)

Risk Control Technique #4 - Segregation / Separation / Duplication

Learning Objective: Discuss five primary types of risk control techniques.
Segregation, separation or duplication is used to reduce the overall severity of losses.

Segregation - an isolation of an exposure from other exposures, perils, or hazards

Segregation Example

Security-controlled access and specialized fire suppression equipment in a computer room located within a building.

Separation - the spread of exposures or activities over several locations

Separation Example

Parking 25 company trucks at one location and 25 trucks at another location across town. Should a fire or vandalism loss occur, only 25 trucks are at risk at to loss any one time (barring a catastrophe affecting the area). The company could continue operations with 25 trucks if necessary.

Senior management flying on different airplanes to attend a meeting.

Duplication - the use of back-ups for critical systems or operations

Duplication Example

Duplication can be having spare parts for a critical piece of equipment and storing them off site.

Lesson 5 Topic B Primary Risk Control Techniques p8 (ELR)

Risk Control Technique #5 – Transfer

Learning Objective: Discuss five primary types of risk control techniques.

The goal of risk transfer is to reduce risk to the organization by transferring some or all of the risk to another party. Transfer is accomplished through either physical or contractual means.

Please refer to Lesson 5 Topic B Primary Risk Control Techniques p9 (ELR) to complete the Knowledge Check at this time.

Lesson 5 Topic B Primary Risk Control Techniques p10 (ELR)

Physical Transfer

Learning Objective: Discuss five primary types of risk control techniques.
Physical transfer shifts some or all of an operation function or exposure to an outside source.

Physical Transfer

Example 1

A school district contracts with a third party to provide food services for the district.

Example 2

A furniture store contracts with a third party for its deliveries.

Lesson 5 Topic B Primary Risk Control Techniques p11 (ELR)

Contractual Transfer

Learning Objective: Discuss five primary types of risk control techniques.

Contractual transfer shifts responsibility of certain liabilities to another party. There are four types of contractual transfer.

Hold harmless or indemnification agreement

Affirmative assumption of the financial consequences for liabilities of another through a contract

Note: Indemnitee - the one who is owed the obligation from another Indemnitor - the one who owes the obligation to another

*There are three types of hold harmless agreements - Limited, Immediate Form, and Broad Form. Discussion on these is outside the scope of this course.

Example:

Jenkins Auto Dealership has hired ABC Roofing to repair the roof on one of its buildings. The contract requires ABC Roofing to hold Jenkins Auto Dealership harmless from any loss while repairing the roof and to be financially responsible for any damages or injuries to a third party.

Exculpatory agreement or clause

Pre-event exoneration of the fault of one party that results in any loss or specified loss to another

Example:

MasterPark Airport Parking has language on each ticket stating it is not responsible for loss of contents or damage to the vehicle.

Waiver of subrogation

Pre-event relinquishment of the right of one or both parties' insurers to seek recovery from a culpable party for loss payments made to the insured.

Example:

The lease contains a waiver of subrogation in favor of the tenant. In the event the tenant is legally responsible for fire damage to the building, the building owner's insurance company cannot subrogate against the tenant.

Limit of liability or liquidated damages clause

Pre-event limitation of the amount, type, or method of calculation of damages available by one or both parties to an agreement.

Example:

A major shipping company limits the amount payable in the event of a damaged or lost package to $100.

Lesson 5 Topic B Primary Risk Control Techniques p12 (ELR)

Note: Contractual transfer is outside the scope of this course, however you can find a comparison of various types of contractual transfer agreements in our Forms Library.

Please refer to Lesson 5 Topic B Primary Risk Control Techniques p13 (ELR) to complete the Knowledge Check at this time.

Lesson 5 Topic C - Claims Management

Lesson 5 Topic C Claims Management p1 (ELR)

Learning Objective: Define claims management and describe the primary types of claims management plans.

Earlier we said there are post-loss activities that can reduce the severity of a loss. Claims management is an example of a post-loss activity.

Claims Management is defined as...

"The prompt resolution of an organization's losses subject to insurance or an active retention program, including claims by other persons or entities to which it may be legally or ethically bound."

Lesson 5 Topic C Claims Management p2 (ELR)

Claims Management Continued

Learning Objective: Define claims management and describe the primary types of claims management plans.

Prompt:

The primary goal of claims management is to resolve claims matters promptly and effectively.

Resolution:

A resolution includes a full or negotiated settlement, a denial of the claim, completion of litigation and/or alternative dispute resolution or subrogation.

Losses:

A reduction in the value of assets

Subject to insurance or an active retention program:

This refers to the fact that many types of organizational losses are not subject to state licensing limitations.

Claim:

A demand for payment or obligation to pay as a result of a loss; claims are made by either of the following:

- First party: The organization
- Second party: Employee(s) in course and scope of employment (contract implied-in-law - not so much a contract as a duty imposed by law)

- Third party: Any entity other than the organization itself or a second party

Ethically bound:

This refers to payments that are voluntary payments or compensation made without regard to legal fault or responsibility.

Lesson 5 Topic C Claims Management p3 (ELR)

Bundling versus Unbundling

Learning Objective: Define claims management and describe the primary types of claims management plans.

While detailed information about the three types of Claims Management Plans are outside the scope of this course, there is basic information about which you should be familiar. In order to understand the basic differences, you need to first understand the difference between “bundling” and “unbundling”.

Bundling

When an insurance policy is purchased, the insurance company includes services in the traditional/standard insurance contract such as:

- State filings
- Loss control
- Claims services
- Policy issuance
- Statistical filings

The insured is not responsible for any of these services and the cost for them is embedded in the insurance premium. These services are said to be "bundled" in the insurance policy. Therefore, in a bundled insurance contract, the insurance company is responsible for claims management.

Unbundling

When an insurance contract is placed on an "unbundled" basis, services such as loss control and claims administration are not automatically included. The insured selects and pays for services on an a la carte basis. If claims service is not included, the insured becomes responsible for claims management.

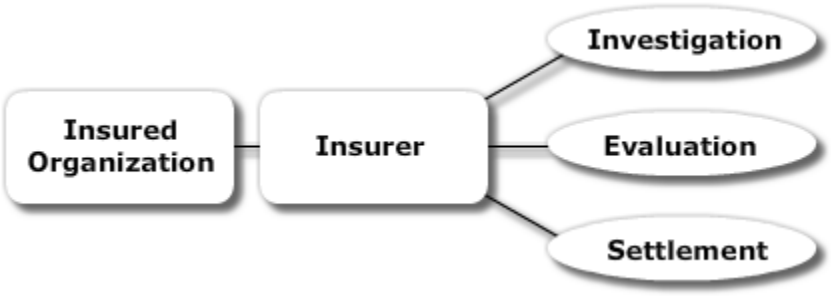
Lesson 5 Topic C Claims Management p4 (ELR)

Types of Claims Management Plans

Learning Objective: Describe features of three principal types of claims management plans.

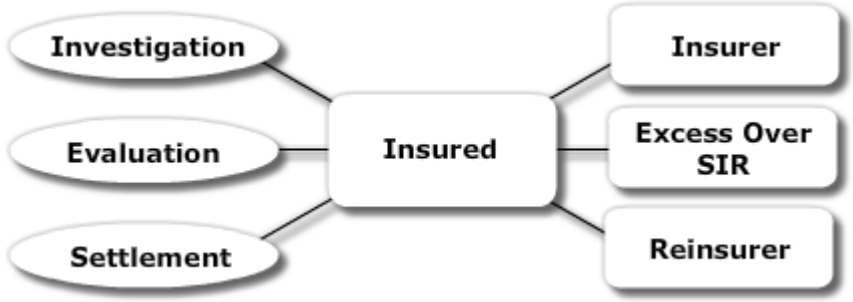
Insured Plan (bundled insurance program)

In the insured plan approach, the insurer provides both insurance and claims management services including investigation, evaluation and settlement.



Self-administered plan (unbundled insurance transaction)

A self-administered plan is also used in conjunction with unbundled insurance. Self-administered plans normally have a very large self-insured retention. Again, the insured, not the insurance company is responsible for claims management. The organization handles its own claims management including investigation, evaluation and settlement.



Third-party administered (TPA) plan (unbundled insurance transaction)

A third party administered plan is used in conjunction with an unbundled insurance contract. The insured, not the insurance company, is responsible for claims management. As the insured organization may not have staff or expertise to manage claims, the insured organization will contract with a Third Party Administrator to handle its claims management including investigation, evaluation and settlement.

Lesson 5 Topic C Claims Management p5 (ELR)

Note: While all other characteristics of these three plans are outside of the scope of this course, there is additional information provided for your reference.

Please refer to the online course to view the reference pdf.

Lesson 5 Topic C Claims Management p6 (ELR)

Claims Management Activities

Gathering data -incident/accident reports, contractual obligations, verification of loss/claim amounts, other aspects of "investigation".

Enforcing contractual obligations – insurance policy, hold harmless, additional insured

Mitigating damages after a loss event - actions taken to minimize severity

Promoting equitable compromise of claims - settling for lowest, reasonable dollar amount

Identifying and combating fraud - internal, external, and systemic fraud

Forecasting losses – setting accurate reserves, performing trend analysis (inflation and loss development)

Advising and consulting with insured and internal departments - legal, underwriting, operations, loss control, administering sales, product development

---

Please refer to Lesson 5 Topic C Claims Management p7 (ELR) to complete the Knowledge Check at this time.

Please refer to the end of Lesson 5 to complete Self Quiz 5 at this time.

THE NATIONAL ALLIANCE
for Insurance Education & Research

Lesson 6 - Risk Financing

Lesson 6 Intro p1 (ELR)

An organization's risks have been identified and analyzed. For those risks that cannot be avoided, risk control techniques have been implemented to either prevent reduce the frequency and/or severity of losses.

The next step in the risk management process is Step 4 – Financing of Risk. It is during this step that the risk manager determines the source (or sources) of funds to pay for expected losses.

Lesson 6 Intro p2 (ELR)

Lesson 6 - Learning Objectives

After completing this lesson, you will be able to:

1. Discuss retention and risk transfer.
2. Identify and describe simple transfer options.
3. Identify and describe loss sensitive transfer options.

Lesson 6 Topic A - Risk-Taking Appetite and Ability

Lesson 6 Topic A Risk-Taking Appetite and Ability p1 (ELR)

Organizations use internal funds and/or external funds to pay for losses. An organization may choose to retain losses, either in whole or part (internal funding) or transfer the financing of losses using insurance (external funding).

For those of you with an insurance background, there is a natural tendency to recommend insurance as the primary source of risk financing. For the risk manager, however, insurance is not the first choice. There are other finance methods that may be more effective and/or economical for the organization.

The decision as to which finance method is best is based, in part, on how much the organization is able and willing to retain.

Lesson 6 Topic A Risk-Taking Appetite and Ability p2 (ELR)

Risk Appetite and Ability Continued

It is important to remember that insurance is a method to finance a loss, not transfer risk.

It is also important to remember that the only losses financed by the insurance policy are those that are within the coverage provided and within the limit of insurance. Losses outside the scope of coverage or in excess of the limit of insurance are no longer financed externally.

Lesson 6 Topic A Risk-Taking Appetite and Ability p3 (ELR)

Risk Appetite and Ability Continued

Both quantitative and qualitative constraints should be considered by the risk manager when determining and recommending a retention level. It is possible that the organization has the financial ability for a large deductible plan; however, management is risk adverse and not willing to jeopardize the financial well-being of the organization.

Likewise, an organization could be willing to have a large deductible program, yet is not financially able to do so without jeopardizing the financial security of the organization.

Risk Taking Appetite and Ability

- Quantitative Constraints
- Qualitative Constraints

Lesson 6 Topic A Risk-Taking Appetite and Ability p5 (ELR)

Qualitative Constraints

Qualitative Constraints may include both internal and external factors. What is the organization's appetite for risk? Is it conservative with a low appetite for risk? If so, even though the Quantitative Analysis clearly indicated funds are available, management may be unwilling to use those funds to pay for retained losses. In this case, the firm has the Risk Taking Ability, but not the Risk Taking Appetite.

Internal Factors

- History of Risk-Taking
- Long-term Organizational Objectives
- Stages in Organization Life Cycle
- Financial Stability
- Management's Willingness to Assume Risk Versus Financial Ability to Assume Risk

External Factors

- Market Maturity
- Competition and Need to Take Business Risk
- Public Image
- Stockholder or Stakeholder Attitudes

Lesson 6 Topic B - Characteristics of Transfer Options

Lesson 6 Topic B Transfer Options and Criteria for Comparison p1 (ELR)

The risk manager may have several financing options to consider. Each option has characteristics that should be evaluated and compared by the risk managers when they are determining which is the most appropriate for their organization.

Lesson 6 Topic B Transfer Options and Criteria for Comparison p2 (ELR)

Accounting & Tax Impact

When are premiums, loss reserves and loss payments deductible to the organization?

Program Flexibility

Is there flexibility in the insurance contract language? Will the insurance company provide manuscript coverage not included in the policy if needed?

Service Options

What services, if any, will be provided by the insurance company versus provided by the organization's internal staff? Are services bundled or unbundled?

Degree of Retention

How much will be retained (internal financing) versus how much will be paid by an entity outside the organization (external financing)?

Premium Certainty
Are the rates guaranteed based on estimated exposures (subject to an audit) regardless of the amount or size of losses paid during the policy period?

Cash Flow Possibilities

When is the premium due? Is it due at policy inception or can it be paid throughout the policy period, allowing the organization to use the money elsewhere. If a Loss Sensitive Plan, when is it anticipated loss payments would be made?

Degree of Loss Sensitivity

Will the cost of the finance plan be impacted by losses, either per occurrence or on an aggregate basis? For example, a finance option containing a large deductible would be more sensitive to losses than one without a deductible.

Lesson 6 Topic B Transfer Options and Criteria for Comparison p3 (ELR)

Transfer Options

During the rest of this section, you will be introduced to various transfer options with a focus on Guaranteed Cost Plans, Small Deductible Plans and Large Deductible Plans. The other options are outside the scope of this course.

SIMPLE TRANSFER	LOSS SENSITIVE TRANSFER	ALTERNATIVE FINANCING OPTIONS
Guaranteed Cost of Fully Insured Plan	**Large Deductible Plan**	Pooling Arrangements
Small Deductible Plan	Retrospectively Rated Plan	Captives
Dividend Plan	Self Insurance Plan	Finite Risk Reinsurance Contracts

---

Lesson 6 Topic C - Simple Transfer Options

Lesson 6 Topic C Simple Transfer Options p1 (ELR)

Learning Objective: Understand the characteristics, advantages, and disadvantages of a guaranteed cost plan.

Guaranteed Cost (Fully Insured Plan)

The first simple transfer option we will look at is Guaranteed Cost.

With a Guaranteed Cost plan, the organization (the insured) pays the premium to the insurance carrier who in turn makes claim payments to the claimant.

Guaranteed Cost Plans are also called Fully Insured Plans. These plans offer 100% external financing of risk, subject to policy terms and conditions. The organization has complete certainty as to premium level and a very stable cost of risk under this type of plan. Tradeoffs include few or no cash flow advantages and no immediate loss sensitivity.

Insured > Insurance Carrier > Claimants

Lesson 6 Topic C Simple Transfer Options p2 (ELR)

What are the characteristics of a Guaranteed Cost Plan?

Learning Objective: Understand the characteristics, advantages, and disadvantages of a guaranteed cost plan.

Accounting & Tax Impact

Premiums are deductible when paid unless the organization is on an accrual basis. A tax accountant can provide advice related to deductibility.

Program Flexibility

This option has limited flexibility in both contract language and rating plan options.

Degree of Retention

With this option, there is 100% external financing of risk by the insurance company, subject to the policy terms and conditions, up to the policy limits. Losses not covered by the policy and losses in excess of the policy limits become the organization's responsibility (retention).

Premium Certainty

Rates are fixed or guaranteed and applied to estimated exposures. Modifiers (scheduled, discretionary and experience) are known in advance. The policy may be subject to audit. This component of Cost of Risk is very stable.

Cash Flow Possibilities

Cash flow is poor or non-existent. The premium is typically due at the beginning of the policy period.
Degree of Loss Sensitivity

There is no immediate sensitivity as the rates are guaranteed. The policy may be sensitive to loss frequency and severity at renewal as losses may result in an increase in premium or underwriting action.

Lesson 6 Topic C Simple Transfer Options p3 (ELR)

Learning Objective: Understand the characteristics, advantages, and disadvantages of a guaranteed cost plan.

Advantages of a Guaranteed Cost Plan

1. Plans provide high budget predictability or certainty (subject to audit of exposures known to insured)
2. Insured enjoys easy, one stop shopping; all services provided by the insurer
3. The agent/broker or the insurer provides the Certificates of Insurance
4. Coverage is standardized and predictable
5. Poor experience may go "unpunished" at renewal (deferred to later renewals)

Bob owns 10 fast food restaurants. There are several workers' compensation losses each year, and losses are projected to continue as Bob does not necessarily promote safety in the workplace. After all, Bob is not worried about the losses since his insurance pays for them. Bob's insurance may not be negatively impacted at renewal because workers compensation claims normally have long development tails and the ultimate incurred cost will not be known for several years when they close.

Lesson 6 Topic C Simple Transfer Options p4 (ELR)

Learning Objective: Understand the characteristics, advantages, and disadvantages of a guaranteed cost plan.

Disadvantages of a Guaranteed Cost Plan

1. Insurer's expenses and profit are passed along

If Bob's Insurer has been running a combined ratio less than 100% for his class of business, it will find that competitive pressures and capacity will keep premium levels depressed even though his particular account has a 100%-plus loss ratio. Alternately, if the Insurer files rate increases across the board for the state Bob's operations are located, he'll get hit with premium increases regardless of loss ratio.

2. Limited cash flow to deferral of premium over maximum of 12 months (generally)

Most premium payment plans are accelerated to have complete payment by 3rd quarter of the policy period. While there are no penalties or interest on an audit bill for Workers' Compensation, most other carriers offer payment plans that are front-loaded (25% up front and 9 equal payments) in order to capture the minimum earned.

3. Good experience may go unrewarded at renewal (deferred to later renewal)

Chet is concerned about the losses at the 10 restaurants he owns and operates. He recently implemented risk control techniques that are projected to reduce his losses by 50 percent. Since bodily Injury-type claims usually have longer
tails than property-type claims, the carrier will be hesitant to immediately apply credits until or unless developed losses are extinguished.

4. Services provided by the insurer may be inappropriate, inadequate, or not needed
5. Coverage and rating is often inflexible with few or no options
6. No short-term incentives to reduce losses are provided, so long term cost of risk may be affected

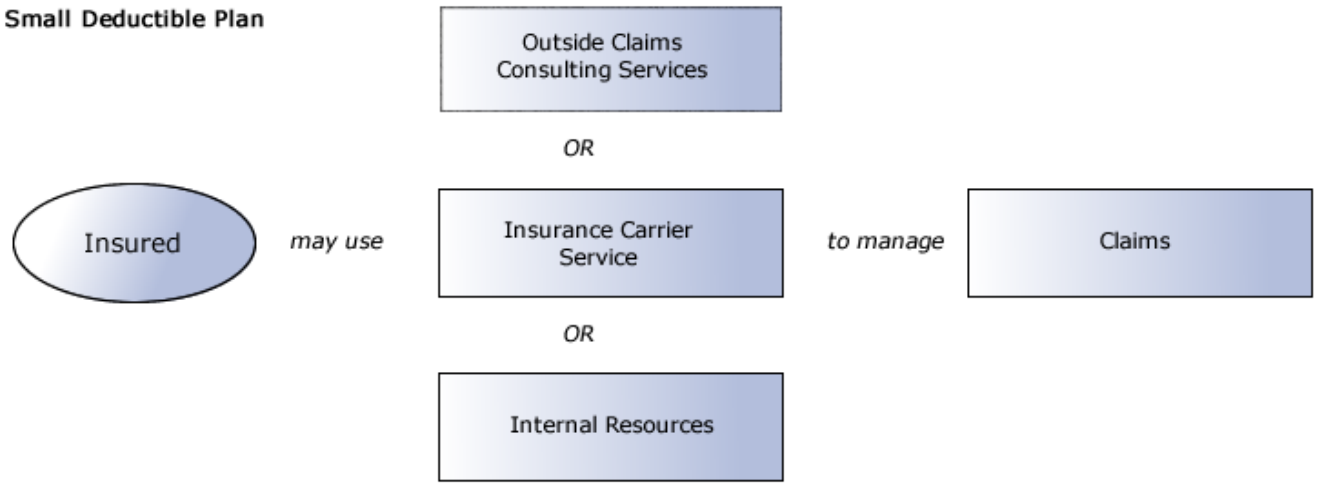
---

Lesson 6 Topic C Simple Transfer Options p5 (ELR)

Small Deductible Plans

Learning Objective: Understand the characteristics, advantages, and disadvantages of a small deductible plan.

Small Deductible Plans, for purposes of this course, are normally plans that have a deductible of $100,000 or less. The amount of risk that the organization retains can be very small to rather large, premiums are fixed and the plans can be somewhat sensitive to losses, depending upon the size of the deductible and loss frequency.



Lesson 6 Topic C Simple Transfer Options p6 (ELR)

What are the Characteristics of a Small Deductible Plan?

Learning Objective: Understand the characteristics, advantages, and disadvantages of a small deductible plan.

Accounting & Tax Impact

Premiums are deductible when paid unless the organization is on an accrual basis. A tax accountant can provide advice related to deductibility.

Program Flexibility

Premiums are deductible when paid. Losses are deductible as paid. A tax accountant can provide advice related to deductibility.

Service Options

Services are bundled; the insurance company provides claims services although there may be a claim consultant involved.

Degree of Retention

With this option, retention can range from very slight to rather substantial if the firm is frequency prone and there is no aggregate deductible. Losses not covered by the policy and losses in excess of the policy limits become the organization's responsibility (retention).

Premium Certainty

Rates are fixed or guaranteed and applied to estimated exposures. Modifiers (scheduled, discretionary and experience) are known in advance. The policy may be subject to audit. This component of Cost of Risk is very stable.

Cash Flow Possibilities

Cash flow can be advantageous. Installments may be available and there is a deductible credit resulting in a premium savings. The "lag time" between the loss and the deductible reimbursement can also provide cash flow opportunities.

Degree of Loss Sensitivity
This option can be quite sensitive to losses depending on claim frequency and the size of the deductible.

Lesson 6 Topic C Simple Transfer Options p7 (ELR)

Advantages of a Small Deductible Plan

Learning Objective: Understand the characteristics, advantages, and disadvantages of a small deductible plan.

1. These types of plans can be structured to produce reasonable budget certainty for the organization.
2. Depending upon the insurer, these plans are usually easy to implement, easy to understand, relatively easy to administer.
3.Insurance policy and certificates are standard; deductibles need NOT be shown on certificate.
4. Direct savings and cash flow savings can be substantial, particularly if frequency is low and credits are reasonable.

A good rule of thumb is 3:1 delta when negotiating credits - i.e., the reduction in premium should be equal to at least the deductible cost for 3 claims. A 1:1 delta, where the premium deductible is equal to 1 claim deductible is tantamount to exchanging dollars with the Insurer, giving the insured no advantage or incentive.

We'll see in the upcoming pages the opportunity for savings under a Small Deductible Plan.

5. These plans can provide a real incentive to reduce frequency of losses resulting in a direct savings in premiums and cash flow savings and any reduction in frequency lessens the likelihood of a severe loss.

Lesson 6 Topic C Simple Transfer Options p8 (ELR)
Disadvantages of Small Deductible Plan

Learning Objective: Understand the characteristics, advantages, and disadvantages of a small deductible plan.

1. Since these plans are based on standardized insurance policies that usually are class-rated or manually-rated, there is often little or no flexibility with respect to coverage and pricing.

2. The rating schedules frequently do not offer credits that are adequate to justify the additional expenses of paying losses within the deductibles.
3. Services may be inadequate or inappropriate for a particular insured.
4. While these plans create more interest in claims handling, the insured has little or no control over the claims payments since the carrier provides the claims services and will reserve according to their own interests.
5. Firm may be required to offer some form of security, often in the form of escrow, which reduces cash flow advantages.
6. Policy accounts may be held open for long periods of time before final cost is known for those claims with long development - depends on plan and insurer.

A delivery truck struck another vehicle in 2006 resulting in both Workers' Compensation benefits to the injured driver, as well as a bodily Injury claim from the occupant of the other vehicle. Because of the significant injuries, neither claim closed until 2011 because of the long tail development to close. The carrier was reluctant to release any deductible collateral as long as the claims were open, reducing cash-flow advantages in several ways.

Lesson 6 Topic C Simple Transfer Options p9 (ELR)

Comparing Simple Transfer Options

Learning Objective: Understand the characteristics, advantages, and disadvantages of a small deductible plan.

Let's make a few comparisons between a Guaranteed Cost Plan and Small Deductible Plan.

Criteria For Comparison	Guaranteed Cost Plan	Small Deductible Plan
Degree of Rentention	None	Low
Cash Flow Advantages	(Generally) No	Some
Loss Sensitivity	No	Some

Lesson 6 Topic C Simple Transfer Options p10 (ELR)

Example

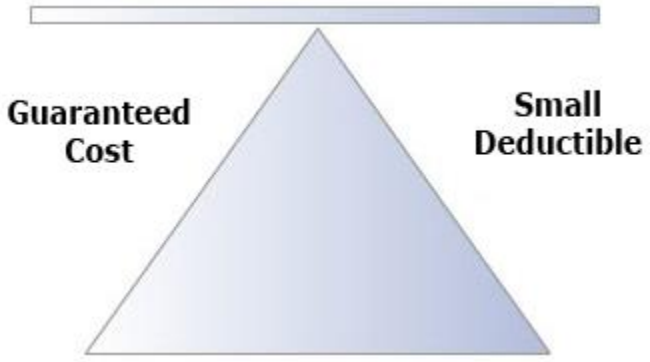
Learning Objective: Understand the characteristics, advantages, and disadvantages of a small deductible plan.

We'll say that $270,000 is the premium for a Guaranteed Cost Workers Compensation policy for a firm.

What would that look like as a Small Deductible Plan?

For purposes of comparison, we have calculated the premium for a Small Deductible Plan (with a $25,000 per claim deductible and expected losses at $110,000) at $240,946.

Note: The calculation of the "cost" for our Small Deductible Plan is beyond the scope of this course, however it includes not only the insurance premium, but also the retention created by the deductible.



Lesson 6 Topic C Simple Transfer Options p11 (ELR)

Sensitivity of Plan Costs to Losses

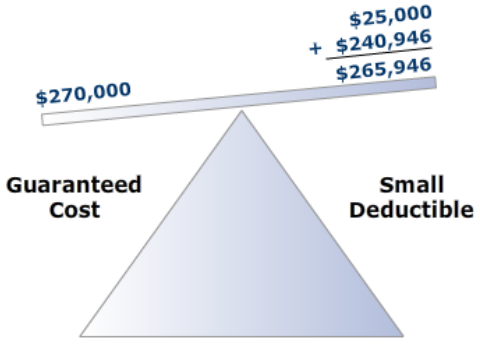
Learning Objective: Understand the characteristics, advantages, and disadvantages of a small deductible plan.

The Guaranteed Cost premium is $270,000.

The Small Deductible Plan offers an 11 percent savings IF projected losses are actually realized.

- Small Deductible Plans quickly become the more expensive option if loss frequency or severity is higher than projected.

- Small Deductible Plans offer additional savings if loss frequency or severity is lower than projected.



Please refer to Lesson 6 Topic C Simple Transfer Options p12 (ELR) to complete the Knowledge Check at this time.

Lesson 6 Topic C Simple Transfer Options p13 (ELR)

Dividend Plan

Learning Objective: Understand a dividend plan.

A Dividend Plan is also a Simple Transfer Option. It is a Guaranteed Cost Program with a Dividend Option. A Sliding Scale Dividend Option pays according to actual incurred losses. The lower the losses, the higher the dividend and the higher the losses, the lower the dividend.

Dividends cannot be guaranteed by the insurance company so there are no promises that dividends WILL be paid. The possibility of a dividend, however, creates an incentive to reduce losses. We will not cover the dividend calculation in this course.

Insured <> Insurance Carrier > Claimant

The insured pays premium to the insurance carrier but may receive a dividend based on actual incurred losses.

THE NATIONAL ALLIANCE
for Insurance Education & Research

Lesson 6 Topic D - Loss Sensitive Transfer

Lesson 6 Topic D Loss Sensitive Transfer Options p1 (ELR)

Recall the definition of Loss sensitivity

Loss sensitivity describes how quickly an organization's Cost of Risk (TCOR) responds to increases or decreases in loss costs.

Simple Transfer Options are not loss sensitive to any large degree. Now let's look at a finance option that is truly loss sensitive – the Large Deductible Plan. For purposes of this course a large deductible is $100,000 and higher.

Lesson 6 Topic D Loss Sensitive Transfer Options p2 (ELR)

Characteristics of a Large Deductible Plan

Learning Objective: Identify and describe loss sensitive transfer options.

Accounting & Tax Impact
Complex accounting and tax impact with regard to premiums, loss reserves and loss payments. A tax accountant can provide advice related to deductibility.

Program Flexibility
Program flexibility is high

Service Options
Services may be unbundled; services options are widely available such as loss control, claims service and actuarial assistance in loss projections.

Degree of Retention

With this option, retention can approach $100,000 and higher and range from very slight to rather substantial if the firm is frequency prone and there is no aggregate deductible. Losses not covered by the policy and losses in excess of the policy limits become the organization's responsibility (retention).

Premium Certainty
Premium certainty is high with fixed rates, subject to audit. The Cost of Risk varies based on actual retained losses.

Cash Flow Possibilities
Cash flow possibilities can be high depending upon the length of time to settle claims - "lag time".

Degree of Loss Sensitivity

This option is quite sensitive to losses depending on claim frequency and the size of the deductible.

Lesson 6 Topic D Loss Sensitive Transfer Options p3 (ELR)

The Attachment Point

Learning Objective: Identify and describe loss sensitive transfer options.

The attachment point is the level at which the insurance policy covers a loss.

Loss projections, loss stratification and loss sensitivity calculations help the insurer to establish the attachment point.

Insured Pays > Attachment Point > Carrier Pays

Lesson 6 Topic D Loss Sensitive Transfer Options p4 (ELR)

Advantages of a Large Deductible Plan

1. Positive cash flow potential
2. Return on loss control program investments can be realized.

Carl's organization spent $10,000 on a driver safety training program for its 50 company drivers. As a result, the frequency of the vehicle losses decreased by 40% over the previous year resulting in a savings of 20% on the vehicle liability insurance
premium of $250,000 or $50,000 savings.

3. Coverages may be customized.
4. Services may be customized.
5. Claims services with a large deductible can be unbundled or purchased outside the carrier. Therefore, claims can be better managed and controlled by the insured.
6. Policies and certificates are available from the insurance carrier.
7. Expense components can be negotiated with the insurance carriers.

The first year Bob purchased his $150,000 large deductible program, the carrier charged him 16% for the Loss Conversion Factors (LCF), which represents the direct costs incurred to close a claim (adjuster's time, legal counsel's time on that claim, etc.) However, if Bob renewed the program, the LCF could be negotiated to reduce every year for 4 years eventually bottoming out at 12%.

8. First step toward self -insurance or captive program.

Bob is reluctant to totally self-insure his fleet risk because of uncertainty in severity claim cash flow, but is willing to set aside funds sufficient to fund variable and fixed costs up to the $250,000 level. This gives him the experience in adjusting claims, controlling development and reserving practices and applying effective loss control measures. Then, after gaining a sufficient comfort level with loss projections and correlations to exposures, he might be prepared to consider the necessary capital investment for a captive, or rent-a-captive program.

The advantages and disadvantages take into consideration the risk of losses subject to the deductible and the financial incentive for the organization to reduce losses.

Lesson 6 Topic D Loss Sensitive Transfer Options p5 (ELR)

Disadvantages of a Large Deductible Plan

Click on the highlighted headings below.
1. Poor loss experience can cancel advantages.
2. Accurate attachment point determination is a must.

After several years of controlling claims below the $250,000 threshold, Bob had 3 successive claims over a span of 2 months that each exceeded the $250,000 stop loss. Even though he previously had concurrent claims, none of them had hit the reinsurance attachment point and these three claims caused severe cash flow issues. At renewal, Bob talked with his Agent about alternatives available to protect his balance sheet, including an aggregate contract but because of the recent prior claims history, the premiums for aggregate protection were more than he could afford.

3. Insurer may require expensive security or collateral with which the organization may not be willing or able to comply.
4. Aggregate protection may be cost prohibitive or may not be available.

The advantages and disadvantages take into consideration the risk of losses subject to the deductible and the financial incentive for the organization to reduce losses.

Lesson 6 Topic D Loss Sensitive Transfer Options p6 (ELR)

Transfer Options and Criteria for Comparison

Type of Plan	Degree of Retention	Cash Flow Advantages	Loss Sensitive
1. Guaranteed Cost, Full Insurance	None	Generally No	No
2. Dividends	None	No	Yes
3. Small Deductibles	Low	Some	Some
4. Large Deductibles	Moderate to High	Yes	Yes

Other Factors

- Characteristics of plans
- Fixed vs. variable costs
- Service (claims and loss control)
- sources and quality Plans flexibility (customization possible)
- Accounting and tax impact

Please refer to Lesson 6 Topic D Loss Sensitive Transfer Options p7 (ELR) to complete the Knowledge Check at this time.

THE NATIONAL ALLIANCE
for Insurance Education & Research

Lesson 7 - Risk Administration

Lesson 7 Intro p1 (ELR)

After an organization's exposures to loss have been identified during Step 1 - Risk Identification, analyzed during Step 2 – Risk Analysis, reduced or prevented during Step 3 – Risk Control, and the risk manager has selected the most appropriate financing technique during Step 4 – Risk Financing, it is time for the fifth and final step in the risk management process: Step 5 – Risk Administration.

Risk Administration is the implementation and monitoring of the risk management process. Risk managers do not do this alone; therefore, they must be effective managers and have strong teams. They rely on their risk management team, comprised of individuals both internal and external to the organization. A Risk Management Information System (RMIS) is an information system that supports the risk manager in identifying, measuring and managing risk in the organization.

Risk Managers also have responsibilities for (1) managing Executive Risk such as Directors and Officers and Fiduciary Exposures; (2) participating in the Due Diligence for a Merger or Acquisition; and (3) Enterprise Risk Management.*

*Note: these topics are outside of the scope of this course.

Lesson 7 Intro p2 (ELR)

Lesson 7 – Learning Objectives

After completing this lesson, you will be able to:

1. Define Risk Administration.
2. Understand the responsibilities, demands and attributes required of an effective risk manager.
3. Identify members of the internal and external risk management teams.
4. Describe a Risk Management Information System (RMIS) and how it is used.

Lesson 7 Topic A - The Risk Manager

Lesson 7 Topic A The Risk Manager p1 (ELR)

Typical responsibilities of a risk manager include the following:

1. Develop risk management policies and procedures.
2. Risk management staff and team management.
3. Select risk management information system (RMIS).
4. Calculate TCOR and allocations.
5. Contract and lease review.
6. Regulatory compliance, related training and loss control programs
7. Accident investigation
8. Claims and litigation management

Lesson 7 Topic A The Risk Manager p2 (ELR)

Risk Managers

Risk managers may be viewed as the “ultimate pessimist”; always focusing on the risk associated with the activity and bringing to the attention of others the possibilities of things going wrong.

Others may view the risk manager and the risk management department as a “cost center” rather than a “profit center”. After all, everything the risk management department does costs money, right? If the Cost of Risk is allocated to departments or divisions within the organization, that is money coming out of that department or division’s budget.

There are 4 Key Steps to Being an Effective Risk Manager that can help overcome these views of the risk manager and/or the risk management department.

Demonstrate impact of TCOR > Stay "plugged in" to the organizations activities > Communicate your results > Continue to innovate

---

Lesson 7 Topic A The Risk Manager p4 (ELR)

Demands on a Risk Manager

The risk manager wears many hats to meet the many different demands of the job:

Technical Demands

The risk manager uses technical expertise to:

1. Purchase insurance programs, evaluate and interpret coverage

2. Select agent/brokers/insurers
3. Negotiate bids
4. Identify exposures
5. Analyze losses, manage claim
6. Conduct cost benefit analyses

Managerial Demands

The risk manager uses the managerial skills of planning, leading, organizing, and controlling to accomplish risk management objectives through others. In addition, risk managers are typically "staff authority" and are considered to be advisors. Therefore, they must implement their programs and plans through other managers. For this reason, solid people skills, in addition to having strong senior management support, are essential to the risk manager's success.

Lesson 7 Topic A The Risk Manager p5 (ELR)

By definition, risk management is a managerial process.

Planning: The process a risk manager takes to predetermine a course of action.

- Establish risk management policy
- Publish loss control procedures
- Establish insurance program
- Forecast losses

Organizing: The actions of a risk manager takes to arrange and relate work to be done so that it can be performed most effectively by others.

- Hire risk management staff and build risk management team
- Organize committees
- Delegate tasks
- Develop organizational structure
- Coordinate activities of external and internal team members

Leading: The behaviors of a risk manager to cause people to take action.

- Produces clear direction and goals
- Effective decision making
- Fosters open communication
- Works within formal and informal networks to ensure the risk manager is "plugged in "

Controlling: The actions a risk manager takes to assess and regulate work-in-progress and completed work.

- Determine cost of risk and establish allocation system
- Submit reports to senior management

- Establish performance standards

Lesson 7 Topic A The Risk Manager p4 (ELR)

Demands on a Risk Manager

The risk manager wears many hats to meet the many different demands of the job:

Technical Demands

The risk manager uses technical expertise to:

1. Purchase insurance programs, evaluate and interpret coverage
2. Select agent/brokers/insurers
3. Negotiate bids
4. Identify exposures
5. Analyze losses, manage claims
6. Conduct cost benefit analyses

Managerial Demands

The risk manager uses the managerial skills of planning, leading, organizing, and controlling to accomplish risk management objectives through others. In addition, risk managers are typically "staff authority" and are considered to be advisors. Therefore, they must implement their programs and plans through other managers. For this reason, solid people skills, in addition to having strong senior management support, are essential to the risk manager's success.

Lesson 7 Topic A The Risk Manager p5 (ELR)

By definition, risk management is a managerial process.

Planning: The process a risk manager takes to predetermine a course of action.

- Establish risk management policy
- Publish loss control procedures
- Establish insurance program
- Forecast losses

Organizing: The actions of a risk manager takes to arrange and relate work to be done so that it can be performed most effectively by others.

- Hire risk management staff and build risk management team
- Organize committees

- Delegate tasks
- Develop organizational structure
- Coordinate activities of external and internal team members

Leading: The behaviors of a risk manager to cause people to take action.

- Produces clear direction and goals
- Effective decision making
- Fosters open communication
- Works within formal and informal networks to ensure the risk manager is "plugged in "

Controlling: The actions a risk manager takes to assess and regulate work-in-progress and completed work.

- Determine cost of risk and establish allocation system
- Submit reports to senior management
- Establish performance standards

Lesson 7 Topic A The Risk Manager p6 (ELR)

The Influence of the Risk Manager

To be effective, the risk manager has to have an influence on the activities of the organization. To do this, the risk manager should make sure all levels of management understand and accept risk management policies and procedures.

This means elevating the importance of risk management within the organization by getting senior management's proactive support of the risk management goals and policies.

It is the risk manager's job to show a direct tie-in between these benefits and risk management issues.

This can be done by demonstrating that effective risk management will accomplish the following:

- Enhancing profits by reducing costs or increasing revenues (in the form of reduced cost of risk and protecting assets and cash flow)
- Allowing management to plan and budget more accurately
- Reducing frequency and severity of losses
- Allowing more effective analysis of losses for projection of future losses
- Providing increased awareness of indirect losses
- Reducing exposures in new operations, mergers, and acquisitions
- Increasing productivity and morale in the work force
- Improving product quality, processes, and technology

Lesson 7 Topic A The Risk Manager p7 (ELR)

Characteristics of a Risk Manager

As you have seen throughout this course, the role of the risk manager is multi-faceted. It is not just being responsible for the consequences of his or her own decisions and actions, but also being responsible for the consequences of the decisions and actions of others both internal and external to the organization. The risk manager also relies on others to assist in the management of risk.

For these reasons, successful risk managers tend to possess the following characteristics:

Personal Attributes

- Is ethical and has integrity
- Ability to stay level-headed/objective in a crisis
- Detail oriented but capable of maintaining sight of the "big picture"
- Desire to get the job done; solution minded
- Creative risk taker; innovative, and inquisitive
- Proven people skills that will encourage support from all levels
- Change driven

Professional and Technical Skills

- Strong written and oral communications skills
- Risk identification and exposure analysis experience and training
- Experience with loss control programs
- Experience in managing claims and litigation
- Knowledge of commercial insurance coverage
- Financial analysis experience and training

Managerial Skills and Experience

- Knowledgeable about the industry and the company
- Knowledge of and experience in general management and project
- management (planning, leading, organizing, controlling)
- Experience in policy and strategy development and implementation
- Experience in negotiations and conflict resolution
- Successful leadership experience and training

Lesson 7 Topic B - Building Your Risk Management Team

Lesson 7 Topic B Building Your RM Team p1 (ELR)

Learning Objective: Identify members of the risk management team.

Internal versus External Team

Risk managers cannot perform every risk management function alone. They may need information/ expertise from others within the organization as well as expertise from outside the organization. They need a team. Team members can be either internal or external.

Internal – Those within the organization, for example, risk management team, human resources, accounting department, operations, and manufacturing. Internal support is often overlooked or underutilized due to political and jurisdictional issues.

External – Those outside the organization, for example, risk management consultants, captive managers, financial consultants, legal consultants, safety consultants, and private investigators. The range of outside service providers is broad depending upon the issues requiring support.

Lesson 7 Topic B Building Your RM Team p2 (ELR)

Internal vs External Team Continued

Learning Objective: Identify members of the risk management team.

Selecting the appropriate team members requires that the risk manager not only understand the firm's needs but also the capabilities of the provider and how to contract and manage the provider in order to obtain the desired risk management objective.

Lesson 7 Topic B Building Your RM Team p3 (ELR)

Who can be on the team? (either externally, internally, or both)

Learning Objective: Identify members of the risk management team.

Agents/Brokers: provide insurance expertise, loss control, international business advice, training and access to coverage.

Legal services, law firms: legal matters including statutory filings, lawsuits, claims litigation, litigation management

Claims administration, TPAs: third party claims, employee injuries, property claims

Safety and security, loss control, engineering, environmental: safety inspections, on site security, setting up safety committees, private investigators, skip tracers

Human resource professionals: payroll, benefits, hiring, terminations

Accountants, CPAs, financial consultants, auditors: tax filings, auditing company books, keeping company financial records

Actuarial services: audit insurance program, determine adequacy of reserves , calculate development factors

Medical providers: first aid, employee injury care, long term care, disability care

RMIS consultants or Providers: (covered in "Information Technology and Allocations for Risk Managers")

Lesson 7 Topic B Building Your RM Team p4 (ELR)

Learning Objective: Identify members of the risk management team.

Other team members

- Operations, department managers
- Captive managers
- Private investigators, tracers
- Risk management consultants (covered in “Risk Management Consulting”)
- Structured benefits/settlements consultants
- Providers of certificates of insurance and bonds
- Providers of MVRs, workers compensation history
- Other risk managers

Lesson 7 Topic B Building Your RM Team p5 (ELR)

Learning Objective: Identify members of the risk management team.

In addition to having members of the risk management team that are internal to the organization, external members play a valuable role. There may be areas where the risk manager is not be an expert and may need assistance from an outside service provider. It is often more effective and less time consuming to rely on another’s expertise. A risk manager uses external providers when:

A. Access to products and services – the provider has access to products or services that the company wishes to purchase
B. Internal talent unavailable – internal skill or talent is unavailable for a particular project
C. Outside viewpoint needed – an outside or objective viewpoint is required
D. Short project timeframe – the project must be done quickly and internal resources are not available
E. Cost effective use of experts – use of outside experts may be more cost effective
F. Outside validation needed – validation is needed that the ongoing risk management program is meeting the company's needs
G. Request for assistance made by executive management – management such as the CEO, CFO or CRO requests outside assistance

---

Lesson 7 Topic B Building Your RM Team p6 (ELR)

Reasons to Use Outside Service Providers

Learning Objective: Know when a risk manager might find it necessary to get assistance from outside service providers.

Regardless of the reason one is needed, it is important to select the Outside Service Provider that will not only provide the necessary services, but also work well with the risk manager and the organization.

Access to products and services

The provider has access to products or services that the company wishes to purchase.

The company is using insurance as a risk financing option and purchases insurance from an insurance company.

Access to expertise

There are areas in which the company risk manager is not an expert and an outside service provider can more efficiently and effectively augment the risk management team.

Elaine is the risk manager for the company. She needs to evaluate the current retention level for the company's workers compensation coverage.

Based on the company's losses the past few years, she will make a recommendation to management about whether the retention level should remain the same or if it should be increased.

Elaine needs to know the district's projected workers compensation losses for the next year. Since statistical analysis is not a major strength of hers, an actuarial firm is hired to analyze the data and consult on projected losses.

Internal talent unavailable

Internal skill or talent is unavailable for a particular project.

The company's general liability insurance policy has a $250,000 retention. The company does not currently have staff claims adjusters. The company has contracted with a third party administrator (TPA) for all aspects of general liability claims within the retention level.

Outside viewpoint needed

An outside or objective viewpoint is required.

The company has received three proposals for its property insurance. The company hired a risk management consultant to evaluate the proposals and make a recommendation as to which proposal best meets the needs of the company.

Short project timeframe

The project must be done quickly and internal resources are not available.

The company is required to provide anti-harassment and anti-discrimination training to all employees. The staff person who would normally provide the training is on medical disability leave. To meet the state mandated deadline for this training, the company hires a consulting firm to provide the required training.

Cost effective use of experts

Use of outside experts may be more cost effective.

The company hires a safety inspector on an as-needed basis rather than incur the expenses to have one on staff.

Outside verification needed

Verification is needed that the ongoing risk management program is meeting the company's needs.

The company hires an actuarial firm to audit the company's self-insured insurance program. The firm will audit paid losses, the company's loss reserving practices, and other areas of the program.

Request for assistance made by central office

Administration such as the superintendent or school board requests outside assistance.

After a large fire loss that was only partially covered by insurance, the school board has requested the district to hire an outside consultant to determine current insurance values for all district buildings.

Lesson 7 Topic B Building Your RM Team p7 (ELR)

Service Providers

Learning Objective: Know when a risk manager might find it necessary to get assistance from outside service providers.

What expectations should the risk manager have when dealing with service providers? What questions need to be asked?

Pre-Hire

- What specifically am I expecting from the service provider? What do I expect this consultant to provide?
- How often or long will I need these services? Only once or over a long period of time?
- What are my delivery expectations? When do I want the work to be completed?
- Will upper management agree to spend the money for an outside service provider? Or do they expect it to be done internally?
- Will the provider function as a member of the internal team or as an outside consultant?
- Will this be an RFP (request for proposal) or a direct hire? From how many providers will I need proposals? Does the RFP require a minority bid because of the type of organization I work for?

Interviewing

What do you want to find out?

- Provider's experience or skill in this specialty
- Last major project the provider worked on that was similar to what is needed for this one
- The most difficult project and/or client the provider had to deal with
- Get samples of provider's previous work
- Ask for specific references of past clients; follow up on references
- Find out if provider can meet the goals, expectations, budget and time frame
- Whether the provider has been involved in any recent litigation
- How the provider will approach the work; who will be assigned to the work?
- Whether the provider will sub-contract any work and to whom
- Determine if there is chemistry. Can you work with the people assigned? Are your communications styles compatible?
- What support will your company have to provide to the service provider?
- Ask for copies of certificates of insurance (WC, GL, AL, E&O, Professional Liability, etc.)

Contract

The contract should spell out:

- Work that is to be performed, how it will be performed, and how accomplishments or deadlines will be reported
- How change orders will be handled
- Time frame and length of the project
- Compensation, timing of payments, and payment method; incentive or disincentive clauses
- Performance expected including a failure to perform clause
- Confidentiality and disclosure clauses; statement of limitations, disclaimers
- Liability and indemnification clauses; certificates of insurance; additional insured status
- Cancellation and re-negotiation terms Dispute resolution including arbitration, mediation, lawsuits, jurisdiction

THE NATIONAL ALLIANCE for Insurance Education & Research

Lesson 7 Topic C - IT For Risk Managers

Lesson 7 Topic C IT for Risk Managers p1 (ELR)

Learning Objective: Know the various uses for a Risk Management Information System (RMIS).

Risk Management Information System

Information Database > Customer Satisfaction Module > Risk Management Tools

How can a risk manager use RMIS?

This course will briefly discuss the Information Database and the Risk Management Tools, but not the Customer Satisfaction Module (applies to risk management consultants) noted on this page.

A RMIS is a relational data base that supports the risk manager or risk management consultant in all steps of the risk management process.

Lesson 7 Topic C IT for Risk Managers p2 (ELR)

RMIS as a Risk Management Tool

Learning Objective: Know the various uses for a Risk Management Information System (RMIS).

While initially the RMIS was used only to track claims and claims data, it has been expanded to include many other functions relied upon by risk managers. Today RMIS is often a critical tool.

Basic uses of RMIS include:

Collecting Data to Further Risk Control Activities

- Use data to monitor, take action, and make improvements
    - Who got hurt and how much will it cost?
    - What was the cause of the accident?
    - How can this accident be prevented in the future?
- Data base of claims/losses necessary for trending and forecasting losses
- Keeping track of any exposure bases (revenues, vehicles, miles driven, units produced, payroll, number of employees, etc.) used for indexing losses to an exposure basis (e.g., automobile liability accidents per miles driven, employee injuries per unit produced, etc.)
- Any other data that the risk manager is responsible for keeping track of

Creating an Insurance Program Summary

Create lists of insurance policies identifying types of coverage, policy effective/expiration dates, deductibles/retentions, limits of liability, etc. It can also be used to monitor the issuance, receiving and organization of Certificates of Insurance and other proof of insurance documents.

Creating Charts and Diagrams

Risk managers frequently need to provide reports to management. It may be more effective to use charts and graphs to illustrate what would otherwise require numerous pages of data. The RMIS can be used to create charts and diagrams such as loss trending reports, litigation reports, OSHA log reports, etc.

Tracking Improvements – Benchmarking

Risk management decisions will be based on data collected and comparisons made with it. (Note that benchmarking was discussed previously in this course.)

Please refer to the end of Lesson 7 to complete Self Quiz 6 at this time.

THE NATIONAL ALLIANCE
for Insurance Education & Research

Course Summary of Elements of Risk Management

Course Summary p1 (ELR)

We suggest reviewing the Learning Objectives for this course to prepare for the final exam.

Lesson 1 Review

1. Define risk management.
2. Describe the five steps of the risk management process.
3. Describe the components of Total Cost of Risk and how Total Cost of Risk is used by risk managers.

Lesson 2 Review

1. Understand the terminology used by risk managers.

Lesson 3 Review

1. Explain why risk identification is the most important step of the risk management process.
2. Identify and discuss the six general classes of risk.
3. Explain the purpose, method, strength and weaknesses of the ten risk identification methods.
4. Identify and describe each of the four logical classifications of exposures.

Lesson 4 Review

1. Discuss how collection and analysis of loss data aids an organization with decision making.
2. Discuss the ways in which the credibility of data is evaluated.
3. Distinguish between qualitative analysis and quantitative analysis and understand the purpose of each.
4. Discuss the use of benchmarking in risk management.

Lesson 5 Review

1. Define risk control and discuss its role in the risk management process.
2. Discuss the five primary types of risk control techniques.
3. Define claims management and describe the primary types of claims management plans.

Lesson 6 Review

1. Discuss retention and risk transfer.
2. Identify and describe simple transfer options.
3. Identify and describe loss sensitive transfer options.

Lesson 7 Review

1. Define Risk Administration.
2. Understand the responsibilities, demands and attributes required of an effective risk manager.
3. Identify members of the internal and external risk management teams.
4. Describe a Risk Management Information System (RMIS) and how it is used.

Please login to your Online Course to complete the Evaluation and Final Exam at this time.
