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Not All Risks Are Alike/Equal/Isos*

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Introduction

This paper will explore the perceptions and realities of risk control based on the financial aspects from the carrier, client, and broker standpoint as well as the risk control purest perspective. Each aspect of the risk control process will be discussed to enhance the readers understanding. Several case studies will be used to illustrate the methods and perseverance needed to turn the questionable client in some consultant's mind to a highly desirable business risk.

What Do We Mean By Risk?

The term "risk" has been used by insurance professionals for many years to refer to clients or potential clients and is partially based on the nature of the operation. By definition "risk" is the possibility or potential for injury or loss. The risk control professional has typically focused on these insurable risks or pure risks that involve "controllable events". Examples include the exposures associated with workers' compensation, general liability, fleet and property related insurance coverages or policies. As we know the insurance policy is purchased by a business or entity to protect them from the financial consequences of damage or loss from a specific event. The insurance industry has used the term "risk" to represent the business or entity as a short hand way to discuss or refer to a business. We hear questions phrased in the context of "What does the risk do?", "Where is the risk located?", "How many people does the risk employ?". The term business or entity is probably more appropriate although risk has been the industry substitute. The ultimate goal of any business is to maximize resources, enhance profits, and continue operations in a safe and efficient manner. The goal of the risk control professional is to initially determine if the business operates in a safe manner or to partner with the management of the business to move in the direction of safe and efficient operations. We know this goal is easier said than done because not all risks are alike or equal as the title of this article states. The title also uses "isos" the Greek term for equal.

<u>Historical Perspective and Loss Control: What Is in a Name?</u>
The loss control profession has generally been associated with the insurance industry. The insurance companies were proactive in hiring "safety engineers' soon after the workers' compensation laws began to take effect in the US in the early part of the twentieth century. The

larger companies began to hire individuals to “inspect” both prospective and current insureds (another iteration of “risk”) to determine insurability and to assist in establishing various safety processes to minimize losses. The assistance aspect from insurance carriers has become know as “loss control service”. The insurability and service process continues today with most insurance companies along with many broker or agent personnel sometimes supplemented by contractors or vendors providing these capabilities.

The names or titles used for professional providing service to clients has changed and yet remained the same. The names have included the following:

- Safety Engineer
- Insurance Engineer or Inspector
- Loss Prevention
- Loss Control
- Risk Control

A few years ago a local newspaper advertised for a “Lost Control” professional. Most anyone reading this article can easily identify with the real meaning of this term.

Bird and Loftus provide two definitions that are still in vogue today. They framed the work of the loss control profession with these definitions in the 1970s.

1. Loss Control is any intentional management action directed at the prevention, reduction, or elimination of the pure (non speculative) risks of business.
2. Loss Control Management is the application of professional management techniques and skills through those program activities (directed at risk avoidance, loss prevention, and loss reduction) specifically intended to minimize losses resulting from the pure (non speculative) risks of business. Loss Control management involves the following:
    - The identification of risk exposures.
    - The measurement and analysis of the exposures.
    - The determination of exposures that will respond to treatment by existing or available loss control techniques or activities.
    - The selection of appropriate loss control actions based on effectiveness and economic feasibility.
    - The management of program implementation in the most effective manner subject to economic restraints.

It is important to note that the late Frank E. Bird Jr. was the Director of Engineering Services for the Insurance Company of North America (INA) prior to joining Lukens Steel as Supervisor of Safety. His many years in safety crossed over from insurance to private industry and ultimately to consulting as President and Chairman of the International Loss Control Institute. His work included both writing and lecturing on an international basis. Both Mr. Bird and Mr. Loftus heavily influenced the loss control profession in the 60s and 70s.

<u>Loss Control Versus Risk Control (A Risk Management Component)</u>

The terms risk and risk of business are prevalent in the above definitions. The title anyone uses may be considered somewhat semantical. In reality the title should describe the nature of the work that the professional is attempting to accomplish. Loss control might be self defeating in a sense. Literally the control of loss is difficult at best. Which loss is being controlled? What level of loss is being controlled? This title may be more appropriate for fire prevention. The use of sprinklers and safe storage and use practices will control loss. An activated sprinkler head will minimize loss as well. The risk control title may be better suited for the work done by most insurance company professionals devoted to identifying, measuring, analyzing, and assisting in the implementation of actions to minimize the losses resulting from the pure risks of business. Many businesses clearly have come to grips with the term “risk management” and risk control is a critical element of this process.

Risk management has become a management tool for US Air Force. The Air Force has adopted an approach to risk management as discussed in Pamphlet 90-902, Operational Risk Management (ORM) Guidelines and Tools. The following key concepts are useful to the risk control professional. In fact the risk management term could easily be replaced by risk control in the following sentences.

Key Concepts

Each level of any organization should be responsible for identifying both actual and potential risks and for identifying appropriate corrective actions to minimize risk to an acceptable level. Applying the actions to minimize risk should take place both on and off the job.

1. Risk management should be an essential element of any business. Risk is defined as the probability and severity of failures or loss from exposure to various hazards. Identifying the hazard, analyzing the hazard and controlling the hazard to an acceptable risk are critical for success in any operation.
2. Risk management is defined as the process of identifying hazards and controlling the risks associated with them.
3. Risk management is not a new business process. It must be a key element that is fully integrated into the all aspects of any business. If done effectively risk management will have a direct impact on the bottom line and the culture of the organization.

Business Culture and the Risk Control Professional

In his book titled “Organizational Culture and Leadership”, Edgar H. Schein defines culture as “a pattern of basic assumptions- invented, discovered, or developed by a given group as it learns to cope with its problems of external adaptation and internal integration- that has worked well enough to be considered valid and, therefore, to be taught to new members as the correct way to perceive, think, and feel in relation to those problems”. The risk control professional must become a team player in this culture development as it relates to the management of risk.

Traditional Risk Management

Risk management has also been defined as a process that uses physical and human resources to accomplish certain objectives concerning most pure loss exposures. There are both post loss and pre-loss objectives that must be considered. Post-loss objectives include: (1) survival, (2) continuity of operations, (3) earnings stability, (4) continued growth, and (5) good citizenship or social responsibility. Pre-loss objectives include: (1) economy, (2) reduction in anxiety, (3) meeting externally imposed obligations, and (4) good citizenship and social responsibility. The risk management process consists of four steps:

1. Identification and analyzing loss exposures.
2. Selecting the technique or combination of techniques to be used to handle each exposure.
3. Implementing the techniques chosen.
4. Monitoring the decisions made and implementing changes where appropriate. (Williams, et all 18).

The above model has been the foundation of risk management in many organizations for many years. Small to midsize companies have purchased insurance to meet the various economic/financial needs. Success in minimizing risk is largely a result of dedicated human capital and enlightened management. The risk control professional must be a leader in a successful process as it relates to risk management.

Who Is at Risk?

The events of the past eight to ten years has taught that we a re all at risk. The actions of terrorists, whether using weapons of mass destruction, airplanes, or chemicals has indeed sensitized everyone to the dangers of living in this world.

The answer in the context of the insurance triangle or three legged stool (insurance company, broker/agent, and client) is not an easy answer. The insurance carrier will pay claims based on the terms and conditions detailed in the insurance contract. An insurance broker/agent may be at risk if there are so called errors or omissions in the insurance program. The reputation of the broker/agent is at risk if the services provided are not in keeping with the expectations of the client. The client is at risk based on the type of insurance program or individual policy. The deductibles that are typically found in our own automobile or homeowners are also found in commercial insurance policies. These require the client to pay the first portion of the loss, therefore there is a secondary (the insurance premium is the primary) cost of risk.

The importance of risk control will vary based on the type of exposures, cost of insurance and where the most significant financial aspects apply within deductible or self insured retention programs.

Risk Control Service Today

What is the role of risk control in the context of the insurance triangle?
Insurance companies in some states are required to provide services to policyholders. In Pennsylvania the Bureau of Labor and Industry specifies that any carrier selling commercial insurance in the state must make services available. The Bureau does not provide details as to the extent of the services that the carrier must make available to their clients. Pennsylvania has been very proactive in the emphasis for safety committees. The carrier must provide a 5% discount for businesses that maintain certified committees. Carriers that provide risk control services will offer them based on size of premium, type of operation, or on a fee for service basis. Brokers/agents will provide service based on revenue/commission, type of risk or on a fee for service basis. From the client standpoint service may be important depending on in house resources or lack of resources. Smaller businesses can make good use of the training, hazard identification and similar resources made available as part of the insurance program.

Risk Control Metrics

As noted earlier in this article, the carrier risk control consultant has a two part job. The first is usually to assist in determining insurability and to provide service after the sale. The first impression is extremely important from the prospective carrier and the prospective client standpoint. The carrier risk control consultant must gather important information in the decision making process. The underwriter is a key component as is the broker/agent application in this step. If a robust submittal is presented to the carrier the job of the consultant is less complex. In addition to the submission, the information on the internet is extremely beneficial. Often times an internet site will provide a detailed overview of the operations of a prospective client. In addition, a search on the Occupational Safety and Health Administration's website can reveal any past visits and including citations and penalties. The more data made available to the risk consultant at this point makes the process less cumbersome for all parties. With this data in hand a research on the nature of the risk and types of exposures that may be encountered, the consultant is ready to visit the prospective client.

The risk control consultant may have good loss history from a complete submission including OSHA logs of Injury and Illness. The question is "How good or accurate is this data?" The data is only as good as the prospective client wants it to be. A roofing contractor admitted that the experience modifier is a key to the bidding process. He routinely did not report all claims to suppress the experience modifier. This business owner is not alone in this approach to incident reporting.

While incidence rates, experience modifiers, loss ratios and similar metrics are important they only tell half the story. An assessment of a prospective risk should include but not be limited to the following:

- The real or perceived management commitment.
- A careful analysis of current operations and/or processes.
- The willingness of management to make any needed changes and to install/implement necessary controls.
- The taking of appropriate corrective, adaptive, and preventative actions to prevent recurrence of unwanted conditions.

Wilson, Dell, and Anderson in there text book Root Cause Analysis indicate that the above four elements are often the difference between success and failure in quality control programs. The same could be said for a successful safety program.

The consultant will want to determine management's understanding of the cost of risk and that insurance and risk can be controlled with management actions and best practices.

The less than adequate prospective client will may have significant gaps in the basic understanding of risk control. It is the consultant role to determine where the gaps exist and find ways to fill the gaps.

Top Ten Ways to Identify a Less than Adequate Prospective Client

During the initial visit the following may be considered "red flags" regarding management's understanding of the importance of risk control:

1. Management knows the distance from Wausau to OSHA.
2. OSHA is a Thai restaurant in San Francisco
3. The lady who keeps the records is on vacation.
4. OSHA was in here and said everything was safe.
5. Loss ratio has something to do with NASCAR.
6. Are you here to inspect our fire extinguishers?
7. We think safety is a good idea.
8. We tried safety a few years ago but the doughnuts got expensive.
9. You are the 17th insurance inspector in the past three weeks.
10. The owner has to clean of a chair before you sit down.

If the risk control consultant determines that the above are inherent aspects of the prospective client, a call to underwriting is probably in order.

A Model for an Above-Average Client

Fred A. Manuel in his seminal work titled "Advanced Safety Management Focusing on Z10 and Serious Injury Prevention" he presents a systematic model related to Occupational Incidents. In the section of the model on Operations Management the author has provided an excellent checklist of process that need to be in place to minimize incidents these include the following:

- Hazard/risk assessments
- Work methods
- Personnel selection
- Supervision
- Personnel motivation
- Training
- Work scheduling
- Maintenance
- Investigations
- Inspections
- Personal protective equipment
- Management of Change

If the above are integrated into the EHS process any client/business/entity is on the right track to control risk in the workplace.

<u>Insurance and Skin in the Game</u>
Early in this article we briefly discussed insurance deductible programs that can impact risk control. The guaranteed cost insurance program rarely enhances risk control. If there is no out of packet expense beyond the insurance premium the client has little reason to “invest” or provide additional resources to minimize or control risk. The use of self insured retention (SIR) or dividend plans will provide an element of risk or “skin in the game’ to enhance risk control in many cases. The best example of skin in the game is the late actress and Pin Up Girl of the 1940’s. Betty Grable. She is quoted as saying “There are two reasons I’m in show business, and I ‘m standing on them.” Her legs were insured for one million dollars to protect her business investment. Business must participate in the risk control process, management must be engaged. Having skin in the game is a definite incentive.

Two Case Studies

The following case studies illustrate how risk control turned two less than adequate clients to better than average.

<u>Construction Company Success</u>
Client: The client is a privately held, regional general construction company that specializes in flat concrete construction. Current operations in Western Pennsylvania with plans to expand into the southeastern U.S.

Problem: Family owned and operated for over forty years. There was minimal emphasis on risk control and safety. Workers compensation carrier was not satisfied with progress on recommendation compliance in past three years and was asking that coverage be replaced. Experienced modifier was thirty percent higher than average at 1.317.

Solution: Recommended that a full time safety manager be appointed to correct problems with broker and new workers compensation carrier assistance. A safety coordinator working on a large wrap up project for the client was appointed to head the effort. He implemented a return to work program, OSHA compliance training for all key management personnel and implementation of a safety committee with the services of the broker and carrier risk control consultants. On –going job site visits were conducted to observe both safe and unsafe practices.

Results: In three years the experience modifier was improved to .854. The savings in premium and cash flow were substantial. The savings in the third year more than paid for the program and the salary and benefits for the safety manager.

Metal Goods Manufacturer Success
Client: A privately held manufacturer of metal moulds for the glass industry. Six plants in the insured program located in the Eastern and Midwestern US.

Problem: The Company was formed through acquisitions. There was no on going safety effort at any location. The guaranteed insurance program for workers' compensation was quoted to exceed $1.2 million in 2001.

Solution: The decision maker and the human resources/safety manager agreed that a self-retention program would be tried for at least one year. In addition, safety efforts would be enhanced at all locations with incident investigation training for all supervisors and managers, safety committees would be implemented at all locations and the safety manager and broker consultant would visit all plants at least twice annually to conduct detailed hazard analysis.

Results: In the current policy year the combined cost of the self-retention program and the loss costs are expected to be approximately $500,000. A savings of almost $700,000 was realized for the current year alone. Savings in the past three years has exceeded $1.1 million. The safety manager recently remarked, "Good pizza takes time". How true.

Conclusion

The above are two examples of success stories from risk control at work. It is important to remember that safety, health and environmental concerns are really about people. Mr. Riley P. Bechtel, Chair and CEO of Bechtel Group, Inc. in his remarks at the Executive Summit at the professional Development Conference for ASSE in June 2004 in Las Vegas noted that his company wants "passionate professionals" to lead the safety effort. The risk control consultant must be passionate about his/her vocation or consider finding another vocation. If we build value driven relationships with our clients with the safety of people as our major goal we can all be successful in making the world a safer, less risky place to live, work and play.

Endnote

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