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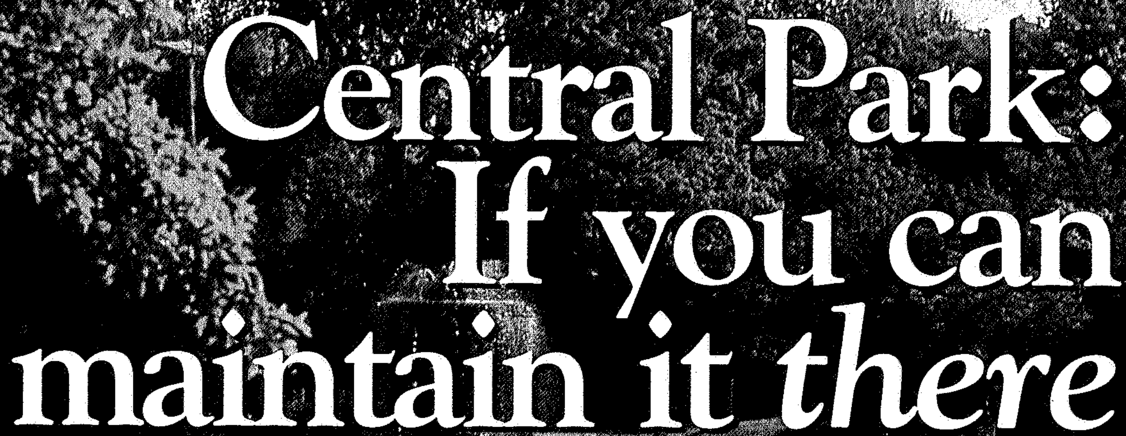
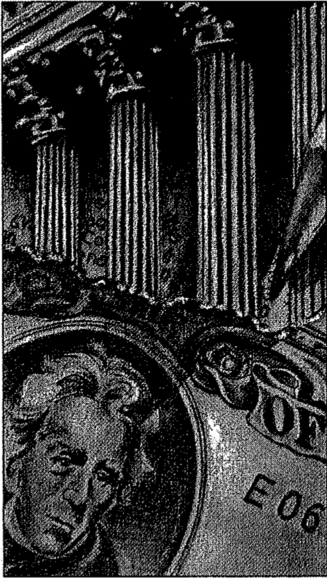


Central Park: If you can maintain it *there*

Snow and ice control: Warming up to technology

Building a GIS from the ground up

Saving dollars by managing risk



By Kevin Harper

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Aggressive risk-taking may be appropriate for Generation X snowboarders, but not for city and county managers, as Orange County, Calif., demonstrated in 1994. Unbeknownst to other county officials, the treasurer poured large sums of county money into risky investments that went bad, leaving the county in a severe fiscal bind.

While public sector risk management historically has focused on insurable risk, managers now are recognizing that the scope of risk extends beyond catastrophes and workers' compensation. In fact, risk is the threat that an event or action will hinder an organization's ability to achieve its objectives.

In government, investment risk, tax shortfalls, fraud and embezzlement, employee incompetence and bureaucratic red tape all constitute risks, many of which are not insurable. Moreover, privatizing, re-engineering and other cost-cutting practices can increase risk exposure.

Activities organizations perform to reduce risk or increase their ability to meet objectives represent controls. The equation "risk – control = exposure" defines the relationship between risk and exposure. In the Orange County fiasco, a systematic risk management program could have controlled risk by identifying the need to separate accounting and asset management.

Enterprise risk management is a systematic approach to identifying, assessing, prioritizing and controlling risks throughout an organization. It has five basic steps:

At every stage, managers should try to build consensus.

• Set objectives. Governments typically do an excellent job of that during the annual budgeting process, but often fall short with the follow-through;

• Identify key risks. Each department should collect input from all experts with knowledge of potential risks and risk impact. Soliciting input from employees yields answers, builds morale and can strengthen support for risk management initiatives;

• Assess the potential impact and likelihood of occurrence. Identified risks can be assessed and priorities set in a four-cell matrix: low impact/low probability; low impact/high probability; high impact/low probability and high impact/high probability. The matrix will determine which risks need to be attacked first, and it can help guide resource allocation during budgeting;

• Choose a course of action for each risk. Once risks are understood and priorities are set, managers either need to accept them, as would happen with low probability/low impact risks, or take action. The acronym "ACT" sums up the three basic action steps: avoid the risk (i.e., do not engage it); control it through internal procedures; or transfer it, either through contractual agreement or the purchase of insurance; and

• Continuously monitor the internal and external environments for changes in conditions and compliance with controls.

At every stage of the process, managers should try to build consensus. Although employee involvement is key, support from the top is critical to ensure that necessary resources are budgeted and that departments work together effectively.

Garnering that support could prove troublesome if the person at the top is an elected official as opposed to a full-time, appointed public administrator. While the former can be from all walks of life and possess varying degrees of interest in the matters at hand, the latter usually is closer to the action and has sufficient professional and academic training to be aware of risk management's benefits.

Many of the new duties resulting from devolution carry with them risks that are not fully understood. Enterprise risk management may not guarantee that correct decisions always will be made, but it at least ensures that those who are responsible have systematically reviewed and analyzed their risks. ☆