



Risk Management: The Risk Management Process

An Online Continuing Education Course for Engineers

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Risk Management: The Risk Management Process

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Introduction

This course is designed to provide the basic concepts of risk management. The application of risk management practices can lead to reduced risk exposures, improved project or business efficiencies, and the potential of increased profits from business enterprises through the reduction, control and elimination of exposures to financial loss during a project or within a business venture.

The concepts can assist with beginning to develop and implement a risk management program for your organization. This course will provide the necessary knowledge to begin or assist with the risk management process within the organization.

Like any other endeavor, there will need to be continued research and education to develop the skills required of a professional risk manager fully.

This course in itself is not intended to provide the depth of knowledge or education for becoming a licensed or certified risk management professional.

This course will provide a basic understanding of:

- the definitions used in risk management,
- risk management guiding principles,
- identification of the components of the risk management process,
- a review of each step of the risk management process,
- benefits and objectives of a risk management program,
- costs of a risk management program, and
- management of risk within the organization.

Upon completion of this course, the reader will be positioned to begin the efforts needed to develop, complete, and implement a risk management program or to begin to be an active member of the organization's risk management team or department.

Overview

The International Organization for Standardization, ISO, has developed ISO 31000, Risk Management, for guidelines that provide the principles, framework, and process for effectively managing risk by any organization or business enterprise.

The implementation of an ISO-based risk management program allows businesses to compare their risk management practices with an internationally recognized benchmark.

Upon completion of this course, it is recommended that the ISO 31000 standard be used to supplement any efforts to develop and implement a risk management program within your organization.

Dr. P. K. Gupta ¹, a recognized insurance and risk management professional, has said that "Risk management is an integrated process of delineating specific areas of risk, developing a comprehensive plan, integrating the plan, and conducting the ongoing evaluation."

No one can see the future, yet business decisions are made with certain assumptions, expectations, or forecasts about the future. This involves taking on risk.

Organizations need a methodology for effectively handling risks to the organization, and this is the function of the risk management program.

The risk management process involves a systematic process which includes the identification, analysis, assessment, control, and avoidance of unacceptable risks associated with projects or business operations.

The risk is typically defined as the chance of loss or an unfavorable outcome associated with an action. Uncertainty is the inability to know what will happen in the future. As

uncertainty increases, the risk will also increase. Risk management involves maximizing expected returns to the organization based on the various risks involved and the risk tolerance of management.

The risk management process must be implemented with adherence to a strict code of ethics by all involved. This will help to maintain full transparency and accountability for the risk management program's success.

It is also essential to know and remember that the classifications for exposures include property, human resources, liability, and net income. Using the classifications will assist with effectively implementing the risk management process.

Each of these classifications will need to be considered for their related exposures, perils, hazards, and losses.

Equally important is understanding the source of potential losses, the impact of the loss if it occurs, the actions needed when the loss occurs, and the potential financial or economic cost to the organization for loss mitigation efforts.

With these factors in mind, start with the components of the risk management process to begin the development of the organization's risk management plan.

The ultimate goal is to roll out a fully implemented risk management plan for the organization with the consent and support of top management.

Definitions Used in Risk Management

To understand and implement a risk management plan, it is essential to know the language of risk management. The definitions of terms used in risk management are the key to knowing and understanding the language.

The term "risk" is commonly used in risk management but may have a variety of meanings depending upon your point of view. For risk management, risk is

defined as an unknown or uncertainty that can result in a positive or negative outcome in a given situation.

Other definitions outside of risk management include the probability of a loss, the difference between an expected loss and an actual loss, loss uncertainty and outcome possibilities. These are all based on unique circumstances for each unique situation and are not the definitions used in risk management.

Exposure is defined as practices, conditions or situations that could result in an adverse financial impact to business operations, inventory, assets, or people.

Hazard is defined as any condition that could result in a loss from a specific peril. Hazards can result in a higher probability of a loss due to physical, moral or moral factors and implications.

The term "peril" is defined as the cause of loss.

An accident is defined as an unexpected event at a specific time and location that causes injury or damage to property or a person.

An incident is defined as any event that negatively impacts normal operations or activities and which may result in damages or injuries to persons or property.

An occurrence is defined as an accident with no time limitation. Generally, this is for an accident that exists over some time rather than a single point in time.

Loss is defined as the reduction in value of an asset.

Claim is defined as a loss that results in a specific liability or obligation to pay for damages or loss.

The expected loss is the projected frequency and severity of a loss. It is derived from a statistical analysis of historical losses and probabilities of the distribution of losses. The expected loss is commonly referred to as a loss pick.

Frequency is defined as the number of losses during a specific time frame. These are generally reviewed in annual periods or longer.

Severity is defined as the total dollar amount of specific loss or the total of the aggregate dollar loss of all losses during a given time.

Physical risk is a risk that impacts company property, workforce resources or information.

Legal risk impacts an organization or project based on compliance with codes and standards or liability imposed from statutory law such as products liability laws.

Economic risk takes into consideration the risk that is impacted by business operations, economic forces, financial market forces, or business expansion decisions.

Social risk can impact business organizations through loss of brand recognition or reputation, adverse social media, changes in social direction or climate, or public relations events that are not handled effectively.

Political risk can impact an organization when laws change, governmental entities change enforcement interpretations, or from a change in government policy at the Federal, State or local level.

A juridical risk is a risk that results from jury decisions, court adjudications or even the attitudes of a jury.

Risk Management is a systematic process for managing a company's or project's exposure to risk factors that can negatively impact the assets or financial status.

The risk management process has five necessary components. Depending on the business entity's attitude toward and need for a risk management program, a risk management program can follow a traditional format that is intended to focus on real risk or can take a more holistic approach with enterprise risk management which also considers speculative risk. Both of these approaches are designed to protect both the assets and financial condition of the company.

Insurance is a contractual arrangement of purchasing indemnification at a known cost and known retention, in the event of a loss.

This method can include traditional insurance markets, specialty lines insurance markets, and captive insurers.

It is important to understand that insurance is not a substitute for an emergency response plan. Insurance is only a financial process.

Captive Insurance (IRMI) as defined by the Insurance Management Institute (IMI) is a risk management organization owned and controlled by its insureds; it is not a traditional insurance company. Captive insurance is owned by its insureds, and its insureds benefit from the risk management services provided.

Six risk classifications are used to categorize risks. They include physical, legal, economic, social, political, and reputational. In the definitions listed previously. Each of these risk classifications is discussed throughout the risk management process.

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