DOCUMENT RESUME

ED 070 198 EA 004 749

AUTHOR	Brown, F. R.
TITLE	Risk Management and Retention.
PUB DATE	23 Oct 72
NOTE	4p.; Speech presented at Association of School Business Officials Annual Convention. (58th, Chicago, Illinois, October 23-25, 1972)
EDRS PRICE	MF-$0.65 HC-$3.29
DESCRIPTORS	*Administrative Personnel; *Administrative Principles; Costs; *Decision Making; *Insurance Programs; *Risk; Speeches
IDENTIFIERS	*Risk Management

ABSTRACT

The objective of risk management is the reduction of the adverse effects of risks at a minimum cost through their identification, measurement, and control. The combination of protection and cost chosen should be based on the best data available and designed for a school's unique need. Risk management involves (1) discovery or identification, (2) measuring possible losses, (3) choosing the best alternative solution to the problem, and (4) implementing the decision. Alternative solutions usually involve risk avoidance or risk retention. Risk of large losses may be insured. (Author/JF)

RISK MANAGEMENT AND RETENTION

F. K. Brown

Risk Management and Retention is an interesting and practical topic. It is one that all of us in school business management have found more time consuming in recent years.

A risk is commonly defined to mean the chance of loss, or the doubt that a person may have, concerning the future outcome of a given situation.

All Business Managers, whether from large or small districts, recognize the serious consequences that may result from unexpected losses. They must constantly be alert to ways of securing the assets of their district through sound economic decisions.

Risk management is a relatively new term and may be defined as the reduction of the adverse effects of risks, at a minimum cost, through their identification, measurement, and control. The approach of each district is unique because of, not only the size of the district, but because of a variety of other local factors.

The theories and practices of risk management are too extensive for our program today. I do think that it may be important, however, to mention some general guidelines in making decisions in this area.

1. Risk discovery or identification is the first and, perhaps, the most difficult decision of the administrator. Although most of you are aware of your exposure to risks, these are changing times and your insurance representative, who is a professional risk analyst, may be most helpful to you in the identification of new risks.

2. Measurement of the possible losses associated with the risks identified is the second step. Your measurement should include the possibility or chance that the losses will occur, the impact the losses would have on the financial affairs of your district should they occur, and an estimate of the portion of the possible losses that will actually occur during the budget period.

3. Once the risk is identified and measured, the various alternatives and solutions, or tools of risk management, should be considered and decisions made with respect to the best combinations of tools to be used in attacking the problem.

4. After deciding among the alternative methods of risk treatment, the Board and the Administration must establish means for effectively implementing the decision made.

One of the alternative methods of risk treatment that might be used in dealing with possible exposures would be first to simply avoid the risk altogether. This method obviously has severe limitations because a choice is seldom possible. However, avoiding the risk may be both possible and desirable. When the risk cannot be avoided, other methods of handling the risk are necessary. One of the most common methods is retention by the school district itself.

Retention may be either active or passive. Many districts may be passively retaining some property and liability risks, because they have either failed to recognize them, or have chosen to ignore them. When the decision is made to pay potential losses from district resources, the retention of risk is considered to be active.

This tool of risk management should be considered only when one or more of the following conditions exist: (1) It is impossible to transfer the risk or to prevent the loss from occurring.

(2) The maximum possible loss, or if conservatively valued, the maximum probable loss is so small that the district can safely absorb it in the current operating budget or from a small reserve. (3) The district controls so many separate, homogeneous exposure units that it can predict fairly well its losses. The Board and the Administration must be willing to accept the risk of some bad years if retention is their choice.

Of course, there are arguments both for and against retention. Some say that part of the cost of transferring the risk may be avoided if the risk is retained (i.e.: costs for selling, loss prevention services, general administration, estimates of losses and adjustments, taxes, profits and contingencies).

On the other hand, a district does not avoid all of these costs. Estimates of possible losses and loss adjustments, loss prevention and reduction activities, and others, must be undertaken by district personnel or through an independent agency by contract. In addition, it may be wise to protect the district against unusually large losses through the purchase of excess insurance, the cost of which could not be avoided. Basically, then, many of the possible savings may disappear on close examination.

If the district has better-than-average loss experience, retention may be feasible since insurers may often fail to recognize adequately your good loss experience. It is, however, true that large districts are eligible for various pricing methods, some of which may base the premium rate, at least in part, on the districts own loss experience.

A district that decides to retain some risk may plan to treat losses, if they occur, as current operating expenses; or there may be periodic payments to a special reserve out of which losses may be paid. In recent years, increased fluctuations in losses have created an unstable situation. The establishment of a special retention fund for larger losses may help to stabilize the costs from one fiscal year to the next

Finally, in conclusion, it is important to point out that the objective of risk management is to achieve the optimum combination of protection and cost. The combination you choose should be based on the best available data to you, and designed for your unique needs.

F. R. Brown RSBO

Presented at
Risk Management Discussion Group
58th Annual ASBO Meeting
Chicago, Illinois
October 23, 1972