

# Risk Management

## Risk:

Risk is any uncertainty about a future event that threatens your organization's ability to accomplish its mission.

## Cost of Risk Equals:

- Insurance premiums; plus
- retained losses; plus
- internal administrative costs; plus
- external administrative costs.

**Risk Management** is the systematic method of identifying, measuring and treating exposures to property and casualty loss. Risk management focuses on risks stemming from physical or legal causes (e.g. natural disasters or fires, accidents, death, and lawsuits).

**Purpose** – To develop pre-emptive strategies to prevent or reduce losses and loss effects; and to develop strategies to reduce the effects of a loss after it happens (Business Continuity Planning); reduce surprises after the loss. Risk Management is a discipline for dealing with the possibility that some future event will cause harm. It provides strategies, techniques, and an approach to recognizing and confronting most threats faced by an organization in fulfilling its mission. Risk management may be as uncomplicated as asking and answering three basic questions:

What can go wrong?

What will we do (both to prevent the harm from occurring and in the aftermath of an incident)?

If something happens, how will we pay for it?

**Importance** -To protect the assets and financial resources of your agency so that you can continue to service clients and the community. It will help ensure the survival of the agency after a severe loss.

## Essential Components of The Risk Management Plan:

- **Identify Sources of risk exposure**
- **Evaluate or analyze risk exposure** (measure the cost of the risk to the organization)
- **Treatment of risk exposure**
- **Monitor the plan**

## Sources of Risk Exposure:

- **Property:** Loss of real, personal, owned, leased, rented or owned by others; includes theft or embezzlement

- **Indirect:** Extra expense, loss of income, loss of valuable lease or location
- **Liability from:** Employees, clients, vendors, public, vendors, advertising, tenants
- **Services of key people**

## **Implementing the Plan:**

### **Who should be involved:**

- Point Person >Designated “Risk Manager” – Administrative or financial manager
- Human resource manager
- Key people from all departments
- Independent risk management consultant or knowledgeable insurance broker

### **Policy Statement**

- Signed by CEO
- Communicate to all employees
- Stating that it is the organization’s policy and goal to maintain a safe workplace for employees, to protect the safety of clients and to conserve the assets of the organization
- Identify the person responsible for managing the risk management policy; and
- Stating it is everyone’s responsibility to cooperate to achieve the goals of the risk management policy

### **Establish an Employee and Life Safety Committee and identify their responsibilities**

### **In many nonprofits the focus of the risk management effort is on:**

- Screening volunteers to protect clients from harm;
- Checking motor vehicle records for employees and volunteers driving on the nonprofit's behalf;
- Developing board orientation and training materials;
- Development and consistent use of employment practices;
- Purchasing property and liability insurance to address the organization's principal exposures;
- Addressing hazards associated with the organization's fundraising events; and
- Developing policies and procedures that insulate the organization from liability when it enters into relationships with other organizations.

### **Identification & Evaluation of Risk Exposure:**

- Risk management consultant or insurance broker with “Risk Manager” using a detailed Risk survey or questionnaire should:
- Conduct detailed fact finding inquiries and inspections
- Interview decision makers in all departments

- Determine exposures from the following types of losses:
  - Property (use professional replacement cost estimates for buildings; up to date inventory of contents)
  - Boiler and machinery
  - Loss of income; extra expense
  - Crime (employee dishonesty & theft by outsiders), including computer related theft
  - General liability (bodily injury & property damage liability)
  - Pollution liability (carbon monoxide, asbestos, mold etc.)
  - Personal Injury liability (false arrest, libel & slander etc.)
  - Auto liability (owned, non-owned & hired)
  - Professional liability(including sexual abuse & molestation of clients)
  - Workers compensation & Employers' liability
  - Employment practices liability (including sexual abuse & molestation of employees)
  - Directors & Officers liability
  - Fiduciary liability (from alleged mismanagement of benefit plans)
  - Epidemics or pandemics
  - Terrorism
  - Loss of key people

Other sources and tools to use:

- Financial Statements
- Brochures
- Contracts and leases; hold harmless agreements
- OSHA and ERISA records
- Insurance Claim Reports

**Treatment of Risk Exposure** – Once the exposures to loss have been identified and evaluated, you must then decide how to treat the loss by one or more of the following methods:

- **Elimination or avoidance** – eliminate or avoid the location or activity
- **Reduction or control** – mitigate the potential impact of the risk  
Written, formal safety programs, automatic sprinklers etc.
- **Self-assumption**  
Deductibles or other non-action measures
- **Self-insurance**  
Not the same as self-assumption – a more formal approach
- **Non-insurance transfer**  
Contracts, hold harmless agreements – many pitfalls
- **Insurance**
  - Only when other methods don't solve the problem
  - Don't risk a lot to save a little

- Don't spend a lot to insure a little

Ideally, a prioritization process is followed whereby the risks with the greatest severity and the greatest probability of occurring are handled first, and risks with lower probability of occurrence and lower loss potential are handled later.

### **Review and evaluation of the plan**

Initial risk management plans will never be perfect. Experience, and actual loss results, will necessitate changes in the plan.

Risk analysis results and management plans should be updated periodically. There are two primary reasons for this: 1.) to evaluate whether the previously selected controls are still applicable and effective; and 2.) to evaluate the possible risk level changes in the organization's environment.

Risk management is simply a practice of systematically selecting cost effective approaches for minimizing the effect of threat realization to the organization. All risks can never be fully avoided or mitigated simply because of financial and practical limitations of the real world. Therefore all organizations have to accept some level of residual risks which still may develop despite their efforts.

### **Business Continuity Planning – Have a Battle Plan**

It is especially important to have a plan in place to deal with disasters such as fire or storms with resources that will enable the organization to continue operations. The plan should identify who is responsible for executing the plan and identify what resources (such as a temporary location, temporary phones etc.) might be required. Evacuation plans should also be addressed.

### **Insurable Risks:**

For claims and lawsuits filed against the nonprofit and its staff, the following types of insurance coverage apply:

- commercial general liability
- directors' and officers' liability
- improper sexual conduct/sexual abuse
- automobile liability
- professional liability
- umbrella or excess insurance
- employment practices liability
- employee benefits liability
- water craft and aircraft (owned and no owned)

Claims for injuries to staff and volunteers:

- workers compensation and employers' liability (employees and sometimes volunteers)
- accident and injury coverage

Claims for property a nonprofit owns or is responsible for:

- general property coverage (including property of others)
- crime coverage (including employee dishonesty and money & securities)
- boiler and machinery (heating, air conditioning, and ventilating equipment)
- computer equipment and software
- property in transit and off premises

### **Non- insurance contractual transfer of risk:**

#### **1. Waivers**

A participant waiver is a type of hold harmless agreement that an organization creates to protect itself from the potential claims of participants in an activity it sponsors. The term refers to an express or written agreement, customarily. Liability waivers are valid only if the person enters into the agreement knowingly, voluntarily and the person waiving certain rights receives something in exchange. Few waivers satisfy these standards. Courts often find that arrangements are not voluntary when they are between an individual and an organization because of unequal bargaining power. Courts often invalidate waivers on the grounds that a participant did not fully appreciate the rights being waived or that the waiver did not specifically indicate that it covered liability for negligence.

#### **2. Hold Harmless Agreements**

A hold harmless agreement is a written contract between two parties that states that one party will assume the risk of legal liability for the other party. Rather than seeking to bar a lawsuit, a hold-harmless agreement obligates one party to pay any costs the other incurs as a result of a claim or lawsuit. A landlord will often include hold harmless language in a lease to protect himself from liability resulting from an event occurring on his property. Funders, including governmental agencies, may also insist that a grantee execute a hold harmless agreement so that a claim will not hold them responsible simply because they provide financial underwriting for an activity.

Many contracts increasingly include hold harmless agreements. For example, a landlord (public or private) might require such an agreement when the nonprofit is leasing space. To protect your nonprofit, carefully read the language in the agreement and make certain that you are not assuming a disproportionate share of the risk. If you must assume risk, assume it for those things over which you have control. If your agency rents space from a local government for a special event, it is unlikely that you will assume responsibility for the maintenance of the building. However, it is not uncommon for the facility contract to contain a hold harmless agreement transferring liability to your agency for injuries occurring during your event including the failure to perform routine maintenance.

A nonprofit can also use hold harmless agreements to its advantage, especially with vendors and contractors. In these documents, the vendor agrees to hold the nonprofit harmless in the event of an accident arising from the vendor's operations.

Because a hold harmless agreement does not foreclose a lawsuit, the ability of the executing party to pay expenses that do arise limits its practical value. A hold harmless

agreement from an entity with no assets and no insurance is nearly worthless. For this reason, most hold harmless agreements require proof of insurance coverage. The entity promising to pay must provide proof that it has insurance to cover any claims that may arise. For complete protection, the insurance policy must include coverage for liability assumed under contract. A certificate of insurance verifies that the entity carries insurance with the specified limit and offers possible assurance of payment.

### **3. Additional Insured Endorsements**

These endorsements modify the policy's coverage by including the named endorsement holder as an insured. A hold harmless agreement is a separate agreement between the parties, while an additional insured endorsement is a modification of an existing contract between the insurance company, or risk pool, and the insured person or organization. For example, the landlord of the building where you are holding a special event may require that he or she be added as an additional insured under your insurance policy. If the nonprofit causes an accident that results in a claim, the nonprofit's policy would respond for both the agency and the landlord.

### **4. Disclaimers**

A "disclaimer" is an express disavowal, repudiation, or limitation of liability by one party to a transaction. Disclaimers differ from waivers in that they are unilateral; the injured party does not explicitly agree to the liability limitation. As such, they are of limited legal value. Their principal functions are to refute assertions about extra duties that a program has taken upon itself and to apprise potential claimants of relevant program limitations.

### **5. Indemnification**

Many nonprofits seek to protect the personal assets of their volunteers, especially directors and officers, by agreeing to indemnify them. Through indemnification, the nonprofit agrees to pay legal costs, settlements, and judgments on behalf of its volunteers. Most organizations include indemnification provisions for directors and officers in their bylaws. *Indemnification can be an empty promise if the organization does not have enough money to pay those expenses.* Many government grants or contracts may not permit an organization to use those funds for indemnification. Therefore, indemnification is only meaningful if the agency has a risk financing mechanism in place (such as a reserve fund, insurance policy, or access to a line of credit).

**If you are considering the use of contractual risk transfer mechanisms, consult an experienced attorney for advice.**

#### **Controlling property risks:**

- Weekly inspections of premises for fire, water etc. hazards and protective devices such as extinguishers
- Semi annual testing of sprinkler systems, alarms and smoke detectors
- Annual walk through with fire department

#### **Controlling workers' compensation risks:**

- Safety committee
- Quarterly review of claims
- Weekly inspections of premises for tripping hazards etc

- Periodic meetings with employees to discuss safety topics
- Many types of controls also apply to general liability risks

**Controlling general liability risks:**

- Life Safety committee
- Weekly inspections of premises for exit obstructions, exit signs, emergency lighting etc.
- Periodic fire drills

**Controlling employment related risks:**

Employment-related matters represent the largest share of claims filed against nonprofits under directors' and officers' liability policies. The Nonprofits' Insurance Alliance of California (NIAC) reports that lawsuits alleging wrongful termination represent 60 percent of all suits filed against nonprofit boards. Charges of sexual harassment and discrimination are the next leading causes of employment practices claims. Nonprofit managers and boards must carefully establish and follow employment policies and procedures to reduce the risk of employment practices claims.

The most common employment-related claims are:

- Wrongful Termination or Discharge***
- Sexual Harassment***
- Discrimination***
- Failure to Employ or Promote***
- Breach of Employment Contract***
- Wrongful Discipline Failure to Grant Tenure***
- Negligent Evaluation***

**Minimizing the likelihood of an employment-related claim:**

The claims described above arise from the perception by prospective, current, or former employees that an organization acted illegally or failed to treat them fairly. Organizations can avoid many potential employment-related claims by striving for clarity and consistency in the administration of employment practices.

The nonprofit should ground its personnel practices in legal, defensible practices. In addition, the foundation for all employment actions should be a strong commitment to treat employees fairly. It is important that all supervisors and managers be trained and coached in the implementation of the organization's employment practices. Training sessions should discuss potential problem scenarios and concerns.

- Develop concise, written policies on employment matters
- Conduct training on sexual harassment
- Follow a carefully documented procedure and exercise special care when handling terminations
- Carefully document all employment-related actions
- Conduct thorough, candid annual performance reviews
- Promptly investigate all allegations of harassment or discrimination

Seek the advice of counsel before taking action

### **Screening Paid and Volunteer Staff:**

***Position descriptions.*** The duties, responsibilities, required experience, and limitations of the position guide the screening process. Position descriptions lay the groundwork for establishing "bona fide occupational qualifications".

***Written applications.*** Application forms are the most common source of information about applicants for staff positions -- both paid and volunteer.

***Interviews.***

***Reference checks.***

***Record checks.***

### **Legal Duties and Screening**

The law requires that organizations use reasonable care in selecting staff -- both employees and volunteers. When the court finds that a lax screening process enabled a staff member to cause harm to a client, member of the public, or another staff member, it may hold the organization liable and financially responsible for the harm caused by its "negligence."

### **Resources for more information and help:**

- Marsh ([www.marsh.com](http://www.marsh.com))
- The Professional Risk Managers' International Association <http://www.primia.org>
- The Institute of Risk Management (IRM)
- Public Entity Risk Institute
- Alliance for Nonprofit Management ([www.allianceonline.org](http://www.allianceonline.org))
- Nonprofit Risk Management Center ([www.nonprofitrisk.org](http://www.nonprofitrisk.org))
- Risk and Insurance Management Society ([www.rims.org](http://www.rims.org))

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