

Risk Management & Loss Prevention Today

Risk management practice, unlike accounting and finance, is still in its formative stage and in a state of evolution. Duties and functions of risk managers vary widely because the specific categories of risks are widely different across organisations.

To the risk manager of a large hospital, legal liability issues could be of paramount importance while in a financial service institution such issues may have comparatively little significance. No matter what the variations in priorities among different organisations, risk management has clearly moved beyond its primary root. Though insurance buying still is a significant component of most risk managers' responsibilities, its importance has steadily diminished, giving place to other priorities. The insurance buying activity now blends with other components of the safety engineering, legal risk management, information systems security and so on.

The application of Risk management concept in developing countries nations is still not matured. While the concept is being adopted by a few large business houses and multinational companies, for the vast majority, risk management continues to be nothing but insurance and in some companies the concept, is totally unheard of.

The consultancy organisations in the field of, or rather, in the name of risk management, also tend to focus attention on insurance portfolio analysis only for reduction of premium, leaving aside all other areas of risk management. Perhaps this area, i.e. premium reduction, has appealed to many finance managers because of the obvious reasons; they see risk management purely as a means of reducing insurance premium to reduce overall cost of production.

The most important element in the risk management exercise is the step of **risk identification**. It is very important for risk management consultants to perfect the art of understanding of the process material flow, nature of raw materials, intermediate products and finished goods, surrounding companies, the law of the land (both local and federal laws) and the laws of foreign country/countries in case production is exported.

Once the risk managers perfect the art of risk identification, they will be successful in not only **reducing the risk** for their organisations but also in minimising the cost of risk transfer. A great deal of work is required to be done to induce the acceptance of the concept and awareness of the benefits of risk management in the minds of the Indian business management community.

In general following points can be used as a **guideline for risk management**, training and loss prevention programme.

1. Management's involvements in all safety function as a policy matter.
2. Periodic Training of Supervisory Personnel for all the matters related to safety

3. Periodic Inspection of Plant and Machinery.
4. Re-evaluation of fire protection and control system.
5. Incorporation of the control measures in the processes suggested as a result of accident investigation.

The field of financial or speculative risk management has a great future. Unfortunately, it is an almost neglected field. While it is a fact that major financial institutions do carry out financial risk management studies, industrial risk managers/management consultants apparently shy away from this field, may be due to the lack of infrastructure facility available to carry out such analysis. It is important that this area of **financial risk management** is added to the traditional scope of risk management to make it really comprehensive.

In line with the global concept of risk management, *Insurers of the developing nations should play a key role in inculcating the concept of risk management in the community of industrial managers.* The total acceptance of this concept by the Industrial leadership may take a little more time; the response is not yet very encouraging. A lot more is needed to be done to reap the benefits of the concept of risk management.

The application of Risk Management and Loss Prevention Concept in industries with the active participation of insurer can improve the claim ratio and also can help the insured by reducing down time of their organizations.

A survey of major fire losses:

Loss Prevention Association of India (LPA), a body promoted by public sector Indian Insurer in 1996 conducted analysis of Major Fire Loss occurred in Indian Industries for last five years. The analysis reveals following important factors

1. More than 50% of the fire had occurred in storage areas.
2. The quantum of loss involve in storage area fire accounted for approximately 70% of the total quantum of loss
3. Around 30% of fire occurred in process areas in the industries.
4. Fires mostly occurred in unattended areas during the night shift.

The causes for the above losses as per LPA, in general attributed by the following reasons:

1. Public Apathy towards fire safety
2. Inadequate Fire Protection System and Training
3. Building Deficiencies
4. Lack of R & D activities

The above analysis emphasizes the urgent need for risk management and loss

control measures in Indian industries. Since application of the concept of Risk Management starts with identification of risk and ends with control of risk, following guidelines may be applied for better storage area management.

1. Application of all Statutory Safety norms provided for the storage area.
2. Application of the norms Specified in local and International Standards for storage of goods in open and within the shades.
3. Redesigning of the storage buildings or reallocation of the storage from the safety angle
4. Segregation of storage areas from the process area.
5. Application of the hazard identification techniques like Hazop etc. specifically for the storage and distribution of hazardous liquids/gases in process industries and adopt remedial measures for control of risk after identification of the hazards.
6. Implementation of modern fire/explosion control system after carrying out the economic feasibility.

Since more than 30% cases of large fire loss occurred in process areas of the industries following guidelines are suggested for better identification and control of hazards in the process areas.

1. Review of all process control / safety interlocks and trip systems whenever any modification is carried out in process industries.
2. Strict adherences to safety norms during shut down and start up in process industries.
3. Continuous application of Hazop techniques for hazard identification and control whenever new machineries are incorporate and systems are modified.
4. Carrying out safety audit through professional organization periodically and incorporating suggestions prescribed in safety audit reports.
5. Carrying out R & D activities from safety angels whenever new materials are introduced in the process.
6. Dissemination of information related to safety to all the people concern with operation of the plant.

Indian Experience in risk management:

LPA had started Risk Management Consultancy Services in 1998 and so far conducted more than 50 Risk Management consultancy studies for industries located across the country. The industries availed LPA's Risk Management Services include companies like Godrej, Neyveli Lignite Corporation, Aurther Anderson, IMC Ltd., Hindustan Petroleum Corpn. Ltd., etc. which mostly comes under large industries category. However, there is hardly any taker in the area of medium and small scale industries.

LPA made considerable efforts within its means to popularize the concept of Risk Management amongst the industries but it is limited only to the large scale industries. LPA's experience somehow rather indicates that following could be the main reasons of hindrance for acceptability of Risk Management Concept in India.

- Insurance buying for industries is a mainly treated function of finance department and there is almost marginal involvement of Technical Services in the area.
- Insurance and insurance related products including safety system gets lower priority in the industry.
- Combined effect of above two reasons developed a negative mind set in Indian Industry on the aspect of Risk Management. As a result, even a large size of the Indian industries in general is reluctant to spend even 1% of their gross annual insurance premium for the Risk Management Studies

LPA's Risk Management studies reveals that even though these large size of Indian industries generally claim that adequate measure had been taken by them for the purpose of loss prevention and risk management but the practical scenario is somehow rather different from their claims. The reasons for the same could be due to following:

- Lack of professional approach in understanding the cause and purpose of loss prevention and risk management.
- Lack of initiative in learning from others experience or lack of dissemination of information on loss prevention and safety in the decision making authorities in Indian industries.

Insurer's initiatives a catalyst for risk management

It is well-established fact that the application of risk management and loss prevention measures in the industries is beneficial for both insurer and insured. Even though both the parties should take equal responsibility to implement the concept of risk management and loss prevention measures in the industries but from the ground realities in India and developing countries it appears that insurer should take more initiative for introduction of the concept particularly for the small and medium size industries as this industries lack in resources and expertise for risk management and loss prevention.

In light of the above, following approaches may be adopted by the insurer to inculcate Risk Management and Loss Prevention culture in the small and medium size industries.

- Set up a Committee represented by underwriters to form a technical team who will collect information related to different areas of loss prevention and Risk Management for different types of industries.

- Since the target group is small and medium sector industries, committee should be specifically equipped to address basic safety and loss prevention issues with low or no cost insolvent for the following industries to start with,
 - Engineering
 - Chemicals
 - Textile
 - Electrical/Electronic Assembly

The low cost or no cost safety related areas are generally involving the followings:

- Safe storage practices to be followed for small scale industries.
- Safe handling of materials
- Safety in electrical installations
- Housekeeping
- Security systems
- Committee should also take up the job of providing safety educational information to the insurer so that same can be passed on to the insured whenever they are purchasing the insurance.
- Committee should guide the insurer to organize Loss Prevention Training Programme both for Insurance Managers and Technical Managers of the small and medium scale industries so that both the functions of an industry can work together for the concern cause of safety and loss prevention
- The Committee should be also empowered to liaise with authorities for implementation of loss control measures like location, segregation, etc. at the initial stages.
- The Committee should also explore the possibilities to equip itself to provide guideline in the area of financial risk management at least for the medium size industries.

The concept of risk management and loss prevention assumes very great importance in open insurance market scenario. It is obvious that the organisations, which attach greater importance to risk management and loss prevention, should get better treatment while purchasing the insurance. But the question is what should be the yardstick of judgment by which the benefit in insurance rates can be passed on to the better-managed organisations. One way of course, is to go by the claims experience but that does not always reflects the true picture of a better managed company.

Conclusion:

Need for an objective oriented Risk Management Rating System

It is suggested to set up an **objective oriented programme** to evaluate the different industries by a uniform acceptable method to judge their concern and level of implementation of risk management and loss prevention systems so that a guideline is available to arrive at appropriate insurance rate to charged depending on commercial viability.

In view of the above followings are suggested for consideration.

1. Evaluation of system of rating of the risks from the implementation of the concept of risk management, which can be termed as **Risk Management Rating System (RMRS)**.
2. Grading of the risks based on **RMRS** like financial position rating of an organization.
3. Attach importance of **RMRS** grading of an organization while selling the insurance. ■