

"Notes - Class #1 - 1/28/14"

Topic 1- Intro and Overview- Risk, Risk Management & Uncertainty

Topic 2- Risk Management Process and Methods of Risk Identification

- **Risks at Temple University**
 - What Risks?
 - Personal Injury
 - Theft - (Tangible property, financial, employee diversion of funds, intellectual- patents- ideas, security breach, cyber security)
 - Natural Disaster/ Fire
 - Finance - tuition/ state of Pennsylvania
 - Reputation
 - Depreciation of *real* property
 - Separate Assets
 - Lawsuits
 - Sexual Harassment
 - Discrimination
 - Negligence- "slip and falls"
 - Malpractice- hospital
 - Professional Liability Negligence
 - Workers Compensation
 - Auto (fender bender)

 - **Types of Risk**
 - Traditional Risk Management Model
 - **Uncertainty of outcome**
 - Produces loss to you or the company
 - Loss is always financial impact
 - Loss with certainty
 - Risk ≠ Loss
 - Budget, Plan, Avoid
 - **Possibility of Negative Outcome**
 - No indication of likelihood
 - **Probability of Loss**
 - Likelihood of outcome or event.
 - Defining and Quantifying
-

Risk Classification: Pure Risk VS. Speculative Risk

- **Pure Risk:**
 - Chance of Loss or no loss—NO Gain
 - Example:
 - My house—it either burns, or it didn't.
 - Owner of commercial building—faces risk associated with fire loss.
 - ** No Change in Financial Condition
 - **Speculative Risk**
 - A chance of loss, no loss, or chance of gain
 - Example:
 - Apartment building—Rent out to tenants—might profit but also might incur loss
-

Static Risk VS. Dynamic Risk

- **Static Risk:**

- Does not change significantly over time—Always Present for an organization
 - Natural Disasters, death, fire, theft.
- **Dynamic Risk:**
 - Varies due to changing circumstances
 - New Law connected to benefits (Obamacare)
 - Dependents are covered until age 26
 - New Technology
 - Economic Crisis of 2008
 - Fuel prices, Foreign Exchange Rates
 - "Biggest Dynamic Risk"- *Terrorism*
 - Examples:
 - Recessions, Regulatory changes, Increased competition, Changes in consumer habits.

Subjective VS. Objective Risk

- **Subjective Risk:**
 - Perceived amount of risk based on an assessment of risk, based on company's opinion of the risk.
- **Objective Risk:**
 - Based on Facts—Usually quantifiable
 - Measurable Variation in uncertain outcomes based on facts and data

Subjective Risk & Objective Risk Differ Based On:

- Familiarity & Control
- Consequence over Likelihood
- Risk Awareness
 - If you or the company is not aware of the risk/impact on company—you will perceive the likelihood as low.

Diversifiable Risk VS. Non-Diversifiable Risk

- **Diversifiable Risk:**
 - Risk that affects some individuals or companies
 - ** (Random)
 - Example: Fire in a strip mall that affects one or a small number of businesses
- **Non-Diversifiable Risk:**
 - Risk that affects society at large (Large segment of society affected at the same time)
 - ** (Occur Simultaneously, Not Random)
 - Example: Inflation; Unemployment; Natural disasters such as hurricanes

- **Liability Exposure:**
 - Loss due to acts of negligence—"Torts"
 - Settlements/ Judgments → Cost \$
 - Legal Fees → Cost \$
 - Reputation → Cost \$

Factors Affecting Risk:

- **Peril:**
 - Immediate cause of loss
 - Random Event that causes loss to occur
 - Natural Disasters
 - Frequency of Loss—How often do losses occur?
 - Units of measurement
 - # of Injuries
 - Days out of work

- Days on light duty
 - Days overtime for coverage
 - Temporary Employees
- Example:
- Flood caused the loss to the beach house (only 1 peril)
- Low Frequency ≠ Low Severity
- High Frequency ≠ High Severity

Severity

- **Severity:** (The Size of a loss)
 - Given that a loss has occurred—How much?
 - Severity is always measured in \$
 - **Hazard:** (Condition that increases the frequency or severity of a loss)
 - Underlying condition behind the loss
 - Can increase frequency, severity, or both
 - **4 Classifications for "Hazards":**
 - **Moral**—Condition that increases the likelihood that a person will intentionally cause or exaggerate a loss.
 - **Morale**—Condition of carelessness or indifference that increases the frequency or severity of loss.
 - **Physical**—Condition of property, persons, or operations that increases the frequency and/or severity of loss.
 - **Legal**—Condition of the legal environment that increases the frequency and/or severity of loss.
 - Example:
 - Peril → Fire— Cause of loss
 - Hazard → The distance to the fire hydrant; combustible materials, lack of sprinklers in establishment.

Difference Between Hazard and Peril

- **Hazard** -
 - A condition that increases the frequency or severity of a loss.
 - Example:
 - Location of my beach house that got flooded
 - There are numerous hazards
- **Peril** -
 - Random event or immediate cause of loss
 - Example:
 - Flood cause the loss to my beach house
 - Only 1 peril

Moral Hazard VS. Morale Hazard

- **Moral Hazard:** (Condition that increases likelihood that a person will intentionally cause or exaggerate a loss)
 - Act differently because of the existence of insurance
 - Not Necessarily bad
 - Example:
 - Health Insurance—going to the Doctor more frequently → Healthier lifestyle
 - When is it bad to act differently?
 - Fraud → Epitome of Moral Hazard
 - *Insurance Fraud*—life insurance → Negative outcome—spread risks—share costs
 - *Home Insurance Fraud* → Negative outcome—spread risks—share costs
 - *Auto Insurance Fraud* → Negative outcome—spread risks—share costs