Managing Risk Is a Public Trust

> *"To trust everybody is as disastrous as to distrust everybody."*
> Hesiodus, ca 700BC, Greek epic poet

Laws and regulations require government to establish policy standards and practices to serve and protect citizens. Just what is Policy Management in a government context? Consider that all government agencies were created to fulfill a mission—which is typically accomplished through program delivery. Like most organizations, government agencies typically have too many competing priorities and not enough resources to accomplish them all.

Risk management comes into play here, as executives strive to balance funding priorities against not meeting program goals, and the impact that would have on social welfare. *How can scarce resources be applied for the highest social benefit?* What is the social benefit of 16 more teachers versus 16 more police officers? This is obviously an extreme example, but more subtle priorities need to be balanced continuously by government managers.

Policy Management in government is about identifying potential hazards and guiding effective action across multiple services or entities. In fact, as illustrated above, in order for a government organization to achieve its mission, it must manage potential risks with the goal of taking effective action to limit avoidable losses. This requires effectively balancing positive social outcomes through investment against negative outcomes from under-investing or not investing. The skills that government organizations use to balance alternative risk management strategies and corresponding programs will determine its ability to retain citizens' trust in the value of policies and programs.

In a world where globalization, economic volatility and structural change are increasing, government organizations need to manage policies and public services better and with greater transparency. The regulations and procedures established by government organizations are the standards that citizens and institutions rely on for fair and equitable results. Citizens expect their governments to practice good governance and facilitate effective coordination across government services in day-to-day operations and in times of crisis. Policy Management excellence enables citizens to evaluate which government organizations coordinate resources effectively and respond most effectively to their needs.

At a fundamental level, government needs to demonstrate effective planning and control for the inventory of policies and regulations impacting its mission. This requires developing and demonstrating that there are active risk management analysis processes in place for assessing potential hazards to the public's welfare. Programs must make it clear that there are sufficient oversight capabilities to detect or prevent actual losses. Contingency plans must outline that resources are positioned to take corrective action for predictable problems and potential catastrophes. Today there is great debate around unifying the regulatory parameters that monitor risk and support stability. Given the various risk parameters, the key is to identify specific risk indicators for where and how a government organization proactively manages its associated assets—physical, financial and human—to the benefit of all parties and related government programs and effectively serve the public good in the face of competing priorities.

Risk management strategies for loss control are a top concern for the leaders of public and private organizations. However, while risk management is an accepted priority, it also represents an unenviable task that can be very political, depending upon the culture and the magnitude of potential risks. The challenge is implementing an integrated, fact-based approach that can be ingrained seamlessly into operational practices. Without a coordinated policy management strategy, governments will continue to struggle with costly, unsatisfactory policy iterations before risk-handling procedures and controls are efficiently aligned to stabilize productive relationships among competing parties.

Government organizations need to tackle three important barriers to ensure a successful, integrated policy management process.

Barrier 1: ***Lack of consistent measurement methodology***

Policy impact measurement is complex, and no methodology will accurately capture the full picture for forecasting and monitoring results. Any risk evaluation process will, by definition, be imprecise. Government organizations need to remain open to new "learnings" as economic, demographic, market, climatic or other conditions change. Over time and through experience, organizations will gradually hone in on methods that better identify risk sharing patterns and adapt loss control and response procedures accordingly.

However, the issue of policy impact measurement is further complicated by the lack of consistency across various institutional approaches for reporting problem events and recording resolution activities. This has a direct impact on financial risk quantification and resource allocation decisions. For example, accounting methods may differ among federal, state and local agencies; a problem that is recognized in one institution may be rejected in another. It may fall below their threshold demanding action, either because of measurement variances—they don't measure the same things in the same way—or because the thresholds themselves are different. The more detailed and extensive the underlying loss control documentation, the more a government organization can devise granular risk management strategies based on informed insights into external forces and market segmentation.

Another measurement challenge flows from the above example. By standardizing the risk evaluation process at a high government authority level within an organization, the organization may lose its flexibility and the ability of frontline "troops" to identify opportunities for taking direct action. The danger in "hard-coding" risk management standardization is that it reduces the options down to a common denominator that will not apply to every program or service subsegment, despite the need to be able to evaluate risk at a fairly granular activity level.

Barrier 2: ***Hidden information gaps hinder the quantification of risk***

Three generic risk mitigation approaches exist:

1. Risks can be eliminated or avoided—e.g., policy and procedure process changes.
2. Risks can be transferred to other entities—e.g., regulatory responsibility re-assignment.
3. Risks can be actively managed.

To the extent that an institution has a good understanding of its policy risks and exposures—where, what and how much—it can be proactive in its policy and program management strategies. Clearly, to appropriately manage risk, you must firstly be aware of it, and then understand the context within which the risk is being evaluated. However, such transparency is not easy to come by without investing in systems, analytical tools and modeling techniques that can be applied at the risk event level.

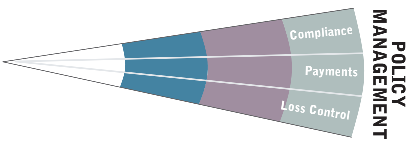
Frequently risk prevention measures are brought in after the event, in a reactive fashion. *To what extent is the policy or program manager fully aware of the existing risks, as well as the potential courses of action? Are government units still making decisions without coordinating and communicating exposures?* Such information gaps represent unknown risk exposures, and the government agency is not even in the position to decide how to mitigate these risks.

As risk events and program inter-relationships become more intertwined to address new problems, the challenge is to enhance and keep up with the necessary program monitoring information flow. Without serious management attention, investment and effective execution, success is likely to remain elusive. This leads naturally to the next barrier:

Barrier 3: ***Integrated risk procedures are not "owned" by specific functional roles and embedded in the organization***

Active policy management is also about ensuring that the full organization identifies with and takes ownership of its own risk mitigation responsibilities. Policy Management professionals cannot sit in an organizational silo and be disconnected from risk management decisions across the agency. Pushing risk awareness and loss control procedures down into various functional roles will help establish a coordinated and proactive approach to government risk management. In fact, different functional roles are directly associated with certain types of risk, including operational risk. The greater their ability to communicate risk concerns, identify risk patterns and support the development of appropriate risk controls, the more effective risk management capabilities will be for profitable long-term citizen relationships. An effective risk management process that is embedded in the organization and well executed will deliver measurable results and mission recognition.

Policy Management practices in government translate organizational oversight responsibilities into many types of risk management implementation areas, such as environmental risk, operational risk, human capital risk and financial risk. For the purpose of simplicity, this discussion will focus on three policy management decision areas that operate in tandem:



- **Compliance** ➔ Monitoring the details of implementation standards for laws, policies and risk events.
- **Payments** ➔ Managing the benefits and loss reimbursements for claims against government programs.
- **Loss control** ➔ Managing the activities that reduce the frequency and severity of losses.

Compliance

Compliance is the focal point for maintaining the policy documentation that specifies standards for government requirements, loss events, limits and exclusions for specific laws and regulations. Risk monitoring activities are defined to delineate methods and procedures for fulfilling legal contractual responsibilities and achieving program goals. Compliance threshold levels are set to mark the boundaries for audits and potential violations for noncompliance reviews.

GOALS	METRICS	DIMENSIONS	
Compliance Audit Activity Index Compliance Score	Regulations (#) Controls (#) Exceptions (#) Regulatory Audits (#) Audit Costs ($) Issues (#) Violations (#) Penalties (#) Penalties ($) Fines (#) Fines ($) Settlements (#) Settlement ($)	Reporting Period Year Quarter Month Organization Org. Code Regulation Regulation Type Regulation Examiner Examiner Compliance Audits Audit Type Audit Name	Compliance Locations Territories Geo Codes Risk Events Risk Types Risk Events Risk Frequency Frequency Risk Severity Severity

FUNCTION	DECISION ROLES	PRIMARY WORK	CONTRIBUTORY	STATUS
Regulatory/Compliance	Executives	•		
	Managers	•		
	Analysts	•		
	Professionals	•		
Legal	Executives			•
	Professionals	•		
Audit	Executives			•
	Managers	•		
	Professionals	•		
Services	Executives		•	
	Managers		•	
	Analysts		•	
	Professionals		•	
Risk Management	Executives		•	
	Managers		•	
	Analysts		•	
	Professionals		•	
Program Management	Executives		•	
	Managers		•	
	Professionals		•	
General Management	Executives			•
Finance	Executives			•

Compliance activities documentation enables government organizations to establish baselines for planning and controlling resource levels for mission requirements. Identifying automated vs. manual control activities provides the basis for estimating the capacity levels for implementing specific policies and regulations. When potential risk events are associated with specific control activities, organization leaders have the core information in place to evaluate the impact that resource gaps have on mission fulfillment and contingency readiness.

Most government agencies are faced with innumerable laws, acts and grant fulfillment reporting responsibilities. Merely keeping up-to-date on the reporting can be a significant challenge. On the downside, failure to comply can mean significant financial penalties. Also, failure to be able to report comprehensively can mean that a government agency is missing an opportunity for funding if certain goals are accomplished. It is not unusual for money to be made available through grants that are contingent on certain performance goals. If the agency cannot keep track of how it is performing, these can be missed opportunities.

Payments

Payments in the form of entitlements are for many citizens the public face of government. Many government agencies have responsibilities for processing entitlements, validating eligibility and settling claims for damages that are covered under the law. It is the operational hub for managing loss expenses and generating analysis for evaluating payment trends. Payments reporting controls are the backbone of detecting fraud and assuring that there is accurate information in place to adjudicate citizen disputes.

GOALS	METRICS	DIMENSIONS	
Program Recipient Growth (%) Payments Timeliness (%) Avg. Payment Processing Backlog (#) Payments Cycle Time Change (%) Payments Activity Index Claims Activity Index Claims Activity Growth (%)	Program Payment Recipients (#) Payment Value ($) Payment Volume (#) Claim Cases (#) Claims Pending (#/$) Investigation Time Settlement Time Litigation Activity (#/$) Repair/Rehabilitation Activities (#/$) Claims Paid (#) Incurred Claims ($) Claims Paid % Subrogration ($)	Reporting Period Year Quarter Month Entitlement Programs Program Types Program Types Programs Claims Claim Types Claim Case Number Claim Location Claim Location Claim Geo code Adjudicator Claim Adjudicator Documentation Documentation Types Documentation	Time to Investigation Time to Investigation Litigation Litigation Types Legal Cases Claim Service Providers Claim Service Types Claim Service Claim Service Providers Time to Settlement Time to Settlement Claim Status Claim Activity Status

FUNCTION	DECISION ROLES	PRIMARY WORK	CONTRIBUTORY	STATUS
Program Management	Executives	•		
	Managers	•		
	Analysts	•		
	Professionals	•		
Audit	Executives			•
	Managers	•		
	Professionals	•		
Legal	Executives			•
	Professionals		•	
Services	Executives		•	
	Managers		•	
	Analysts		•	
	Professionals		•	
Finance	Executives			•
	Managers		•	
	Analysts		•	
Risk Management	Executives			•
	Analysts		•	
General Management	Executives			•

A key challenge here is that, frequently, data for evaluating claims or for identifying fraud can be distributed across multiple disparate systems. The time lags between when one system is updated, and another system is synchronized can be many months. The time gap in between can represent an opportunity for fraud, where an enlightened fraudster can triage this gap to their advantage. This takes us back to the risk management discussion above, and the need to close the gap through a performance management system that is able to synchronize disparate data and related processes.

The payments organization must coordinate a network of relationships among other government agencies and external suppliers to assure policy-related work is performed in a timely and professional manner to fulfill contractual standards. Payment expenses are classified by service provider types to develop benchmark metrics that can be used reliably to plan and control government program-fulfillment activities. Cases in litigation are aged to reconcile settlement value and timing estimates with government accounting requirements recording payments and adjusting reserves.

Loss Control

Effective loss control is the key to achieving risk management success. Expense impact analysis is the most revealing indicator for assessing how well specific detective and preventative controls have reduced payment disputes and net losses. The best success is achieved when the internal controls process in place maintains the documentation needed for implementing contingency plans that take short-term and long-term action to identify and proactively mitigate damages.

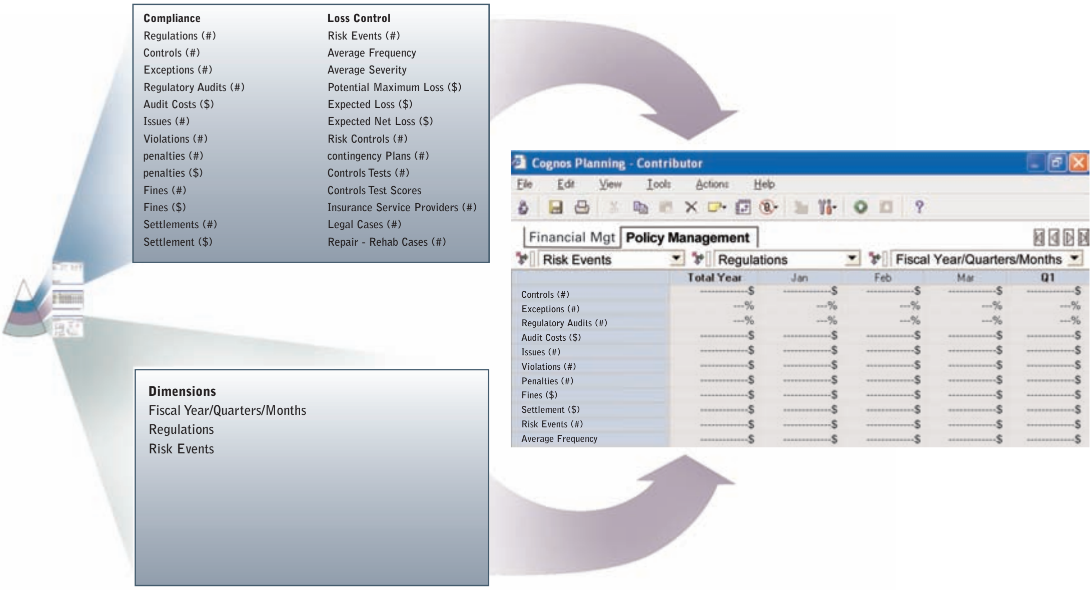
GOALS	METRICS	DIMENSIONS	

Risk Controls Assessment Score
Contingency Readiness Index
	Risk Events (#)
	Average Frequency
	Average Severity
	Potential Maximum Loss ($)
	Expected Loss ($)
	Expected Net Loss ($)
	Risk Controls (#)
	Contingency Plans (#)
	Controls Tests (#)
	Controls Test Scores
	Insurance Service Providers (#)
	Legal Cases (#)
	Repair - Rehab Cases (#)
		Government Programs
		  Program Types
		  Programs
		Organization
		  Organization
		Risk Location
		  Geo Code
		Risk Events
		  Risk Types
		  Risk Events
		Risk Frequency
		  Frequency
		Risk Severity
		  Severity
		Regulatory Standards
			Regulation Type
			  Reg Standard
			Control Activities
			  Processes
			  Control Activities
			Documentation
			  Documentation
			Contingency Tests
			  Test Types
			  Contingency Tests

FUNCTION	DECISION ROLES	PRIMARY WORK	CONTRIBUTORY	STATUS
Risk Management	Executives	•		
	Managers	•		
	Analysts	•		
	Professionals	•		
Legal	Executives			•
	Professionals	•		
Program Management	Executives		•	
	Managers		•	
	Analysts		•	
	Professionals		•	
Services	Executives		•	
	Managers		•	
	Analysts		•	
	Professionals		•	
Operations/Production	Executives			•
	Managers		•	
	Professionals		•	
Customer Service	Executives		•	
	Analysts		•	
IT/Systems	Executives			•
	Analysts		•	
Audit	Executives			•
Finance	Executives			•
General Management	Executives			•

The key issue is not simply to identify risk exposures, but to define the cycles and processes where potential damages are monitored to develop approaches or strategies to address them. One common valuation methodology is to review potential maximum losses in relation to the actual frequency and severity of specific events. Analytics are used to develop "value at risk" estimates which look at the likelihood of a program asset value's decreasing over a period of time. Others include shortfall probability, downside risk (semi-variance) and volatility. Government executives need to be aware of the inherent strengths, weaknesses and sensitivities associated with each method.

Whatever the method, government managers need to have access to better information that equips them to identify and mitigate risk. Only by clearly understanding the potential losses associated with noncompliance events can government organizations implement effective policy risk management strategies.



The Compliance and Loss Control decision areas illustrate how the Policy Management function in government can monitor risk exposure, allocate resources and set plans for future requirements to manage multiple risk types that cascade across the organization.