



# Risk management defined – part 3

ONCE the risks have been identified in step one (*NAEDA Equipment Dealer*, January 2008), the second step of evaluating the risks your dealership is exposed to can begin. This step gives you an important tool in prioritizing the risk as to its potential effect on your business.

## Step 2 – evaluate the risks

This step involves quantifying the risks and then prioritizing them. The two criteria normally used to analyze loss exposure are:

1. frequency – how often could the loss happen?
2. severity – how large is the loss likely to be when it occurs?

For reoccurring risks you will have historical data to help you identify the frequency and severity of the loss. However, for losses where you do not have any history, such as a new type of loss or a loss your business has not seen, you need to be able to quantify the loss in general terms of the probability that the loss will occur and the potential size of the loss. Industry statistics, if available, can help you determine the frequency and severity of the risk for your dealership. Using a graph can help you analyze and compare your risks.

Risks in the low frequency/severity quadrant are given a low priority status and the losses can be handled on an ad hoc basis. Risks in the high frequency/severity quadrant are accorded high priority status and are dealt with immediately. Some losses can be handled quickly and are given a slightly higher priority than normal because their “bang for the buck” is significant enough and warrants the higher prioritization.

- For example, from the chart you know that:
- Electrical fires caused by your new building’s wiring should be remote yet the severity could be catastrophic – you will need a plan of action.
  - At-fault single-vehicle accidents are possible; however, they tend to be low or moderate in severity – you will need a plan of action.
- In a perfect world all losses could be analyzed by their historical data, loss forecasting, and assumption based forecasting. However this is rarely the case. If the data or resources are not available, the risks have to be plotted on a more general basis using intuition and comparing them to known losses. Be careful as precious resources could be wasted on a remote risk or a risk could be more critical than originally thought.

Risk Management is not a one-time effort. Situations, technology, training programs, and loss prevention strategies can change the frequency and severity of the risk, which may change the prioritization of the risk. Continual monitoring helps identify any issues. At Federated Insurance, we believe loss prevention is a critical component of your risk management program. ■

The information provided is intended to be general in nature, and may not apply in your province. The advice of independent legal or other business advisors should be obtained in developing forms and procedures for your business. The recommendations are designed to reduce the risk of loss, but should not be construed as eliminating any risk or loss.

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## Analyzing Loss Exposures

FREQUENCY ↑	Expected					High Frequency/ High Severity
	Probable					
	Possible			Single Vehicle Accidents		
	Unusual					
	Remote	Low Frequency/ Low Severity				
		Negligible	Low	Moderate	Significant	Catastrophic
		SEVERITY →				