Bright Ideas
Supporting Organizational Excellence & Innovation

Risk and Benefit Management

A balanced approach

Mention "risk," and most board and management types picture a media feeding frenzy, funding being pulled, and the collapse of civilization as we know it… at least as far as the organization's future is concerned. Risk makes us feel unsafe because it focuses on what can go wrong if we pursue a particular course of action.

But just as things can go *wrong*, outcomes can also be *better* than expected. Life is full of surprises, and some of those surprises are very good indeed. Risk management is not just about preventing the bad surprises, but also about maximizing the good surprises. It's not just about putting out fires, but also about capitalizing on opportunities.

> *People are not rational when it comes to evaluating risk and benefit.*

Risk management strategies use your resources and activities to prevent or reduce losses and to make gains for your organization. We're going to look at three basic elements that put you in control of what happens as much as possible in an uncertain world.

Take out the Emotion

People are not rational when it comes to decisions with uncertain outcomes. First, an action's risks stand out in people's minds more than its benefits, so people tend to be *loss averse*. When a choice is framed in terms of gain, people are *risk averse*, preferring a smaller, sure gain over a bigger, potential win. People also tend to see change as riskier than the status quo, because its risks and benefits are less well-known to them.

By taking the emotion associated with loss and gain out of your thinking, you can approach risk and benefit management in a more balanced way.

Identify Key Risks and Benefits

When it comes to organizations, the important risks and benefits relate to the organization's mission, money, reputation and the safety or well-being of people. When deciding whether to pursue an opportunity, engage in an activity or operate a program, there are four questions to ask:

- How may the action help or keep us from fulfilling our mission?
- How may the action affect the money we have?
- How may the action affect our reputation?
- What impact may the action have on the safety or well-being of our staff, volunteers, members or clients?

Don't focus just on the risks—that's your emotions talking—consider the benefits. Also, think about the possible impacts if you *don't* pursue the opportunity or engage in the activity.

Once you've identified risks and benefits of both action and inaction, it's time to pick out the ones that are most important to plan for. Two factors determine importance: degree of impact and likelihood. Curing a deadly disease is a high-impact, positive outcome. Death of clients or volunteers is a high-impact, negative outcome. Most other outcomes have less impact.

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Bright Ideas is published quarterly by K. K. Biersdorff Consulting and provided free as a value-added service to clients.

Most people get the concept of impact, but panic when asked to estimate likelihood. Even when there are numbers available, such as the track record of a particular investment, past performance is a predictor but not a guarantee of future performance. So your discussion of outcome likelihood will usually involve terms like "pretty sure," "rare" and "50-50."

The key risks and benefits to manage are those identified as having a big impact or being highly likely or both.

Manage Key Risks and Benefits

Managing risks involves planning to make a negative outcome less likely, less costly or both. There are four basic strategies for dealing with potential risks; you can try to avoid, transfer, mitigate or accept the risk.

Avoiding the risk usually means not pursuing the opportunity or course of action. This also means missing out on whatever benefits might have followed.

Transferring liability or legal responsibility results from procedures like having participants sign waivers or release forms. Organizational policies and procedures or other communication strategies also work on this principle.

Mitigating risks means taking actions to reduce the likelihood of the risk or the size of its impact should it occur. For instance, a SWOT analysis identifies the internal strengths and weaknesses and the external opportunities and threats to an organization. An organization can draw on its strengths to mitigate a risk, just as it will want to make plans to ensure that its weaknesses do not increase the risk. In general, monitoring implementation and having a "Plan B" are the most common mitigation strategies. Having safety equipment and training staff in its use mitigates safety risks. Having an adequate financial reserve or money in the bank mitigates financial risks.

Finally, you can accept the risk. Not all risks can be avoided, transferred or mitigated. At some point the benefits will be valuable enough to an organization to accept a certain level and type of risk.

Managing benefits involves planning ways to increase the likelihood or impact of potential benefits by exploiting, sharing, enhancing or accepting them. Most of these strategies mirror those involved in managing risk. However, sharing the benefit is not as obvious. It involves partnering with another organization. This strategy generally reduces the resource load on your organization. Sometimes sharing the load increases the overall benefit, so that your organization gains more income, reputation, stakeholder well-being and mission fulfillment than if it acted on its own because of the synergy produced by the organizations working together.

Finally, keep in mind that risk management keeps organizations alive, while benefit management helps organizations thrive.

Check This Out

Extending the Risk Process to Manage Opportunities. http://www.theirm.org/events/documents/irm_innovation_sig_extending_risk_process_for_opps_df.pdf

The Framing of Decisions and the Psychology of Choice. http://www.sciencemag.org/cgi/rapidpdf/211/4481/453.pdf?ijkey=Qf67hM3Y0Ca2M&keytype=ref&siteid=sci

From Where I Sit

On the pleasure of re-reading classics

Once upon a time I had a really good memory. Even now, I surprise myself with what I can recall from the things I've read and learned over the years. But I rely more on an organized office and knowing where I keep the information on the shelf rather than in my head.

So it is a distinct pleasure when my work requires me to track down classics in the literature and re-read them, as I had the opportunity to do for the main article in this issue. Re-reading classics, such as Kahneman and Tversky's work on the many biases in our analysis of risks in decision-making, takes me back to days when learning was my full-time job and I was more concerned about wrinkles in my clothes than on my face. Re-reading the articles also reminded me of important studies that have influenced thinking, not only in psychology, but in economics and management theory.

So often we define "best practice" as what's new. Re-reading the classics reminds us that some truths have been around for awhile.

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