

## **Risk Management and Its Implications for Libraries**

### **What is risk management?**

Risk management is the process by which an organization establishes risk management goals and objectives, assesses and monitors its risk, and selects and implements measures to address its risks in an organized and coordinated fashion.(Young) The basic goal of risk management is ***to ensure the survival and continued operation of the organization.***

Other goals could include: *the maintenance of the organization's quality of operations, image and/or funding through anticipating and minimizing the consequences of acts of omissions; providing a safe environment for employees, volunteers, and patrons; providing better stewardship of library assets so that it can better pursue its goals and mission; ensure awareness and compliance with legal requirements; moderate the anxieties of staff or board concerning personal liability for decisions or actions.*(Berges)

Risk management is not just about preventing and controlling the bad things but also enhancing the likelihood of good things happening---all in the service of ensuring the viability of the organization. This is often referred to as “up-side” risk. In the case of public libraries, viability means fulfilling its contract with the community to provide materials and services that support lifelong learning, jobs and quality of life.

There are three basic tasks in the risk management process: 1) discovering and understanding your risks, 2) figuring out ways to prevent, control, avoid, transfer, or even enhance those risks, and 3) determining ways to pay for losses when they occur. In the

field of risk management, these tasks are referred to as *risk assessment, risk control and risk financing*.

### **Why do chief executive officers and governing bodies of organizations care about risk management?**

In recent years, governing bodies and chief executive officers of nonprofit and public sector organizations have begun to recognize, just like their counterparts in the private sector, that the risks their organizations face are pervasive and complex, and that these risks are not confined to insurable or accident-related situations. They may include risks arising from actions of the federal and state legislatures, financial decisions of a local funding body, the organization's policies, weather-related phenomena, and even changing preferences of customers and voters.

Risks come in different shapes and sizes. A hurricane could have a big impact, while the impact of a few books stolen from the library may be small. Some risks can result in real physical and economic harm---a fire can damage a library and disrupt services for an extended period of time; a liability suit for sexual harassment can deplete a library's financial resources and damage its reputation; employees can be injured in accidents. And, some risks can produce problems even when losses do not occur, as when the mere possibility of lawsuits influence library leaders' ability to make controversial decisions about library branch closings, staff reassignments or collection decisions, for instance.

Imagine a library board that would allow the fear of a lawsuit to stop it from re-designing the configuration of the library's branch locations to better serve the public. In the proposed re-design, several new larger branches, strategically located to be accessible by public transportation from a variety of neighborhoods, equipped with the newest technology would replace several neighborhood branches. The neighborhood branches being replaced are in buildings that are over one hundred years old. The buildings can not be retrofitted to accommodate the newest technology and their physical plants are in need of much repair. However, the library board fears they could be open to lawsuits from some members of the community if they close the older neighborhood branches. This fear is justified because in Baltimore, Maryland a lawsuit was filed because of branch closings.

Critics of Baltimore's Enoch Pratt Free Library filed a lawsuit when the library closed five branches. The lawsuit is trying to reverse the branch closings and change the composition of the library's Board of Trustees and its interlocking Board of Directors. [The Board of Trustees made the decision to close the branches.] The boards, based on Enoch Pratt's 1882 charter, are self-perpetuating. ACORN (Association of Community Organizations for Reform Now), the group that filed the lawsuit, wants term limits and a board that better reflects the city in terms of economics, geography and race. One result of the lawsuit, so far, has been the voluntary resignation of all trustees that live outside the city.(Order)

At one point in time, nonprofit and government agencies had no fear of liability. But in the last 30 years that has changed. There are no states or municipal entities [public libraries are often part of a municipal entity] that have total immunity and courts have ruled that governmental immunity does not apply to constitutional violations. This includes common occurrences such as discrimination and violations of freedom of speech and freedom of religion.(Palermo) In fact libraries can find themselves in a *catch 22* when it comes to freedom of speech; individuals or groups may sue because the library has installed filtering software on computers used by adults, but libraries run the risk of going against the values of its local community and/or losing federal funds if filtering software isn't installed on computers, in accordance with the Children's Internet Protection Act (CIPA).

### **How do organizations structure the risk management function within their organizations?**

When confronted with examples of their risk exposure, governing bodies and chief executive officers of organizations have seen the wisdom of setting up risk management programs in their organizations. Public sector programs have often been primarily concerned with the control of the cost of risks and financing. Hence, "cities with populations of 100,000 or more commonly have full-time risk managers," says Dennis Kirshbaum, executive director of the Public Risk Management Agency in Arlington, VA. He adds, "If a city does not have a risk manager, often an assistant city manager, the finance department or the personnel department handles risk management."(Cowans) A study entitled, "Cost of Risk Evaluation in State and Local Government," conducted by

the Public Risk Management Association, Deloitte & Touche LLP and the National Underwriter Company found that the practice of risk management is widely established in the public sector. The majority of the entities that responded to the survey employ professional risk managers. Survey respondents are located in 46 states. About 50 percent are municipalities, 25 percent are counties and the remaining 25 percent are states. Thirty seven percent of these respondents, who represent a cross-section of the country, indicated that their risk managers report to the chief financial officer, while twenty seven percent of the respondents said their risk managers reported directly to the chief administrator.(Pouzar)

In Montgomery County, Maryland, “the risk management function is located within the Finance department”, says risk manager, Terry Fleming. [Terry was cited as one of the reputational leaders/risk managers in an article entitled, “Taking the Lead in Risk Management” written by David Ammons and published in American City & County, so I called to ask him a few questions about risk management.]

### **The Risk Assessment Framework(Young)**

The objective of risk assessment (identification, assessment, analysis and ongoing monitoring) is to develop an understanding of an organization’s risks. Peter Young, Ph.D., who holds the E.W. Blanch, Sr. Chair in Risk Management at the University of St. Thomas, outlines a risk assessment framework in Limiting Small Town Liability: A Risk Management Primer for Small Town Leaders. He says, risk assessment is based upon an evaluation of:

- The environments in which risks are generated,
- The perils and opportunities that arise within those environments, and
- The organization's exposure to those risks.

According to Peter Young, risk management professionals have identified five external and two internal environments as sources of risk. [Were appropriate, I have inserted an explicit reference applicable to public libraries.] They are:

#### External

1. The physical environments (example: hurricanes, floods, earthquakes, snow)
2. The economic environment (example, state of the economy, monetary policy)
3. The political environment (example, legislative activity, pending elections)
4. The social environment (example, social attitudes and preferences)
5. The legal environment (example, court decisions, administrative/regulatory rules)

#### Internal

1. The operational environment (example, the day-to-day activities and actions within the organization), generally categorized as:
  - a. Professional (example, malpractice for dispensing legal advice at the reference desk of a public library)
  - b. Financial (example, misstatement of financial reports, poor fiscal policies, embezzlement)
  - c. Legal (example, actions and activities that might produce lawsuits)
  - d. Physical (example, fire risks to buildings, automobile risks)

- e. Contractual (example, risks arising from outsourcing collection of library fines)
  - f. Technological (example, information technology system risks, threats to the safety of hardware and software)
  - g. Environmental (example, risks arising from environmental protection rules and laws)
2. The cognitive environment (absence of information, the influence of attitudes toward risk on decision making)

Within environments there are *hazards* which raise the probability of a loss occurring or increase the potential impact of a loss. Hazards, however, do not produce losses. It is the perils created by the hazardous conditions that lead to loss. A “peril” is a cause of loss. Young gives the example of a winter storm being a hazard arising from the physical environment. The perils created by the winter storm are poor visibility and icy roadways. These perils can cause accidents. This same approach could be used to assess the “upside” risks that bring advantages or rewards to an organization. Instead of *hazards* the environment produces *risk factors* that can create opportunities rather than perils. Young’s example is that of the economic environment giving rise to a booming stock market as a risk factor, which produces investment opportunities that can favorably impact a community’s ability to finance big projects.

The perils and opportunities created from the hazards and risk factors don’t matter if the organization has no exposure to the risk. In other words, if a library does not have its

bookmobile out on the icy highways, the risk may exist, but the library has no exposure. There are, broadly two types of exposures---asset and liability. Asset exposures have three categories, *physical, financial and human*; and liability exposures have two categories, *legal liability and moral responsibility*.

The general categories of asset exposures are:

1. Physical assets are library buildings, books and other library material, computers, library vehicles. The impact of a physical asset loss is not just the cost of replacement, but the costs associated with its loss of use until replacement occurs.
2. Financial assets include stocks, bonds, letters of credit and other such instruments. Libraries don't hold or issue these types of assets, although local governments might.
3. Human assets are the managers and employees. They are subject to physical and economic harm in numerous ways: premature death, injury, unemployment, and old age, for example.

Young listed a number of legal liability categories which are relevant for a typical local government. I selected a few categories from his list and added a few to represent what I think are relevant categories of legal liability for a typical library:

1. premises liability (slips and falls)
2. employment liability (harassment, discrimination)
3. workers' compensation and employers' liability (injuries on the job)
4. motor vehicle liability (bookmobiles hitting pedestrians)

5. professional liability (reference librarians dispensing legal or business advice; librarians enforcing no loitering or patron behavior rules)
6. copyright infringement (challenges of adhering to electronic copyright provisions of licenses to subscription databases)
7. intellectual freedom and censorship (Internet access)
8. errors and omissions (library director and officers liability)

In addition to legal liability as an exposure there is moral responsibility, which is sometimes overlooked as a risk management issue. It should never be overlooked in libraries or any public sector entity because governing bodies and managers at every level of the organization have an obligation to manage the entity in the best interest of its citizens.

A formal process needs to be developed to collect information about environments, hazards and perils (risk factors and opportunities), along with asset and liability exposures, to use for risk assessment [it could be timed to coincide with the annual budget setting process or the annual strategic planning process]. Joe Palermo, a risk control specialist in Public Sector Services for St. Paul Travelers Companies gives these steps for identifying risk:(Palermo)

- Create consistent and easy-to-follow reporting forms
- Review contracts and other documents
- Conduct frequent inspections of property and equipment
- Meet with employees

- Review historic loss information [In the case of libraries, I would also advise reviewing the library literature for examples of risk exposure and loss sustained by other libraries.]

Once the data has been gathered, the risk manager (and risk management committee, if appropriate) uses the data to develop a broad summary statement to describe sources of risk in each of the relevant environments; to list the key hazards and perils (also risk factors and opportunities) specific to each environment summary; and to determine the asset and liability exposures appropriate for each environment, with their hazards and perils (also risk factors and opportunities).

The risk manager sorts or ranks the risks to reflect the level of seriousness they represent. Peter Young suggests risks can be placed in four categories based on the frequency and severity of the risks, they are:

- Category I risks are those which rarely occur and they produce losses of minor importance (low frequency/low severity).
- Category II risks are those which rarely occur but they produce severe losses, they tend to be classified as “catastrophic risks” (low frequency/high severity).
- Category III risks are those which occur frequently but they produce losses that tend to be relatively modest, they tend to be referred to as “operational risks” because they tend to be known and in some instances they can be anticipated. (high frequency/low severity)

- Category IV risks are those which occur frequently and produce severe losses (high frequency/high severity). It is rare to find examples of these risks when organizations conduct risk assessments.

The next step in the risk assessment process is to analyze the risks to understand how risky conditions produce losses. The results of this analysis could suggest possible remedies to prevent or avoid future losses. Risk managers also place a valuation on the risks. From the risk manager's point of view, exposures to risk have two bases of valuation. First assets might be valued based upon the cost to replace those assets. Or, second the assets may be valued based on what they "contribute" to the local organization. There could be some assets that have a low replacement value that contribute greatly to the local organization. For example, an old library bookmobile, which has depreciated in value as a motor vehicle, provides priceless service to a community which does not have a branch library.

Once the risk assessment process of evaluating the *environments, perils and opportunities* and *exposures* has been conducted, the risk manager decides which risk control techniques to employ.

### **Risk Control**

Risk control includes efforts to avoid, prevent, reduce or otherwise manage risk and its impact on an organization. The five basic techniques involved in controlling loss exposures and library examples from a few library practitioners are:

Risk Avoidance. Some activities and situations carry risks so great that the best way to handle them is to avoid the activity altogether. A library, for example, could decide not to permit the use of library facilities for karate classes because of the likelihood of injury and liability claims.(Brawner)

Loss Prevention. These measures seek to prevent, or at least reduce the likelihood of, losses. Examples of these measures, which could be employed by libraries, are: eliminating clutter, training employees, adopting policies and maintaining adequate files and records.(Berges)

Loss Reduction. These methods do not prevent losses from occurring. They minimize the impact of losses that do occur. A library may install a sprinkler system, for example, that will reduce the likelihood of a fire or reduce the amount of damage from a possible fire.(Brawner)

Uncertainty Reduction. Information management is a primary tool in reducing “uncertainty.” Library board members and library directors are in the information profession. They should always gather information to better understand a given situation, which should allow them to make decisions that are consistent with library objectives.

Contractual Risk Transfer. Some risks can be transferred to private or nonprofit organizations by contracting for services and products, thus making the other parties responsible for the risks, through the use of “hold-harmless” or “indemnity” clauses. Libraries may, for example, include these provisions in leases for storefront libraries, in lawn maintenance agreements, or in the use of library meeting rooms by a college conducting classes in the library.(Brawner)

## **Risk Financing**

No matter how successful the risk control efforts, libraries may still suffer losses than need to be paid. There are several methods of risk financing. Those used most commonly and library examples from a few library practitioners are:

Risk Retention. The term “self-insurance” is sometimes used when an organization decides to retain or assume some of its risks. In practice, a library, for example would establish a fund for the express purpose of handling a loss (e.g. a bookmobile fund, materials replacement fund, etc.). Or, the library could consider a particular loss as one of the regular expenses of doing business. In this respect many libraries assume the loss of stolen books, feeling that the heroic measures of insurance or increased security are more costly than any likely losses.(Berges)

Risk Financing Pools. In many states, risk financing pools provide municipalities, counties and other governmental subdivisions a viable alternative to insurance. In many cases, the costs are somewhat less than insurance and each participant is a partial owner, similar to a co-op. Refunds may be made once a sufficient base is realized if pay-outs have been modest during a specific insurance period. Libraries who are considering joining a risk sharing pool should look at such things as how the pool is capitalized and who is responsible for pool management. Also review the annual reports for the past two or three years to determine if the pool is a good fit for the library.(Berges)

Insurance. Regardless of the source of insurance, it is important to have a clear and specific idea of the library’s insurance requirements. Purchasing more insurance than is really needed is evidence of insufficient analysis, just as is buying too little.(Berges)

Insurance is a budget projection or leveling device that spreads the financial

consequences of loss out over a period of time. The library can trade unpredictable, unbudgetable losses for a known budgetable insurance premium.(Brawner)

### **Implications for the Library**

Governing boards and library directors in large and small libraries need to integrate the practice of risk management into their policy making and planning activities. Many activities, which have been described as *risk assessment*, *risk control* and *risk financing* are probably already occurring within libraries. However, these activities need to come together under a single manager or committee that reports to the library director, and ultimately the board of library trustees. Libraries in communities of 100,000 or more may have access to a risk manager in their local government. Libraries in smaller communities should identify the local official who has risk management responsibility. Library directors, or their designees, should coordinate their risk management program with these local officials. Terry Fleming, Montgomery County, MD risk manager says, “I work with the library department and other departments regarding their safety, employment and other practices to prevent exposure to risks. The risk management department also takes care of buying commercial insurance for property loss. We self-insure against employee injury claims, e.g. carpal tunnel injuries and other worker’s compensation claims.”(Fleming)

Library directors and chairs of governing boards should take steps to educate board members about risk management. Make trustees aware of the library’s risk exposure and their personal risk exposure; and make them knowledgeable about risk treatment (risk

control and risk financing). While there are no states or municipal entities [public libraries are often part of a municipal entity] that have total immunity, many libraries come under “charitable immunity” or tort immunities for nonprofit associations. These laws do not prevent a trustee from being sued, but these laws offer the trustee who has behaved as a reasonable trustee, even if she or he may have made an error in judgment, or discretion, a valid defense that can be asserted in answer to a complaint filed in a lawsuit. When this defense is asserted, the burden of proof shifts to the person bringing the complaint to prove that the trustee’s actions evidenced a reckless disregard for the duties imposed by the position. This is a harder standard of proof than just having to prove that the trustee acted unreasonably.(Miller)

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