SECTION 20 – RISK MANAGEMENT

Overview

All organizations are subject to liability and claims from a variety of risks arising from torts, property damage, errors and omissions, injury to employees arising from unsafe conditions or hazards in the workplace, and natural disasters. Risk management encompasses identifying risks, evaluating potential losses, and ultimately planning and developing a risk management program to mitigate these risks to an acceptable level. The importance of risk management has grown steadily in recent years for various reasons, including increased use of technology and higher litigation costs.

Local governments face unique risk challenges. Unlike many business organizations, local governments provide facilities and services for all residents of a given area. Additionally, the nature of some of the services provided, such as public safety, can be considered high-risk areas, which could make obtaining adequate insurance coverage difficult or cost-prohibitive. Additionally, each community has unique risk attributes that might not be a risk area for other communities. For example, two seaside communities might exhibit similar risk profiles, except one operates a seaport facility with petroleum storage. Given the heightened awareness of terrorism on domestic soil, the seaport community would possess a very different risk profile. Consequently, a comprehensive risk management program is a vital component of a local government's administration. For some local governments, this responsibility and other insurance-related matters often fall to the finance department.

To implement a risk management program, the local government must establish written risk management policies and procedures that identify the local government's goals and individuals responsible for carrying out risk-related functions and contain guidelines for making decisions about fundamental activities. Reviewing and updating a local government's overall risk assessment and insurance coverage can help ensure that the entity maintains the best mix of risk mitigation for the lowest possible cost to taxpayers.

Identifying Risks

The first step in creating an organization-wide risk management program starts with a comprehensive risk assessment, including identifying risks to understand the sources, types, and likelihood of risk. At a minimum, exposure to risks should be identified in the following areas:

- Economic environment (market trends)
- Internal environment (attitude of individuals towards risk)
- Legal environment (laws and legal procedures)
- Operational environment (day-to-day activities)
- Physical environment (e.g., natural disasters)
- Political environment (legislative activity, elections)
- Social environment (socio-economic composition of the community)
- Accurate insurance valuations on government owned properties via formal property appraisals (at least every 5 years) with annual increases for buildings and contents
- Cyber Liability risk analysis
- Employee Safety – review of Job Hazard Analysis' plus PPE (personal protective equipment) assessments

In most cases, such an assessment already exists; however, periodic re-assessment will provide a more current and accurate risk profile, reflecting the ever-changing risk environment. The purpose of this process is to ensure that all areas of significant risk have been identified and addressed, and that insurance coverage is adequate to meet potential claims.

Evaluating Potential Losses

To determine the level of coverage necessary for a given area, it is helpful to understand how the entity values particular assets. For instance, it would not make sense to insure a new civic center against hurricane damage for significantly more than its replacement cost. The entity's liability profile and recent claims experience also provide guidance on appropriate coverage. Relevant information includes the frequency and severity of claims, the number of open claims, amounts paid, and amounts reserved.

Florida law provides most Florida local governments with some relief from liability claims. Section 768.28, Florida Statutes, limits tort recovery to $200,000 per person and $300,000 for claims arising from the same incident or occurrence, unless a further act of the Legislature authorizes payment of an excess amount. However, a government may agree, within the limits of available insurance coverage, to settle a claim or judgment without further legislative action. Obtaining insurance coverage does not increase the statutory waiver of sovereign immunity.

Developing a Risk Management Plan

Based upon a completed assessment and a thorough understanding of the local government's risk profile, a risk management plan should be developed. A wide range of solutions are available to communities to combat each community's risk exposures. These include:

- Loss Prevention and Control: This involves education and training to employees to raise awareness of safety issues and other workplace hazards that can result in loss. It also involves instituting routine inspection programs that detect, deter, or prevent unsafe conditions or practices that can result in accidents, theft, property damage, or other losses.
- Risk Transfer: This involves acquisition of insurance, either directly by the local government or requiring others to do so contractually (e.g., construction contractor). Insurance can be obtained directly by local governments through:
- Traditional Insurance Coverage: Many insurance carriers provide property damage and liability coverage policies for local governments. Chances are an all encompassing policy can be formulated for your entity. To reduce insurance company credit risks, it is advisable to deal with established A. M. Best Company rated "A" insurance companies.
- Public Entity Risk Pools: Government associations may offer members participation in a variety of risk pools, which provide the opportunity to participate with other local governments and diversify self-insurance coverage geographically.
- Self-Insurance: This involves the local government assuming financial responsibility for all or a portion of specified losses. Depending on the government's size and risk exposure, self-insurance can be a cost-effective method of managing workers' compensation, property, liability, and other risks. Claims experience, premiums, reserve requirements, and coverage needs should be evaluated to determine whether self-insurance is appropriate. Self-insurance may be combined with excess or catastrophic coverage for claims above an established retention.
- Risk Avoidance: This involves a local government avoiding the provision of specific services if the risk management costs are excessive. For example, a local government may decline adding a swimming pool in a recreational area.

Funding Policy Considerations for Risk Management

As part of its risk-management policies and procedures, a local government may adopt a written funding policy describing how risk-related costs—such as premiums, deductibles, reserves, and mitigation expenses—will be

evaluated and funded over time. Clear funding principles can help ensure that the government is financially prepared to meet obligations when risks materialize and can support long-term resilience.

A risk management funding policy may balance several key objectives:

- Ensuring actuarially sufficient reserves are available to cover expected claims and liabilities.
- Managing funding volatility, especially in years with large claims or premium increases.
- Supporting transparency and accountability in how risk costs are allocated and tracked.

Local governments that self-insure or participate in pooled risk programs should fund their insurance reserves based on actuarial analysis, which may include confidence levels (for example, funding at an 80% confidence level suggests that funding will be sufficient in 8 out of 10 years). Confidence levels are developed by actuaries to reflect the probability that reserves will be adequate to meet future claims. Governments may choose a confidence level that aligns with their risk tolerance, financial capacity, and policy objectives. Funding to the actuarial central estimate may be appropriate for some, while others may prefer higher confidence levels to reduce the likelihood of underfunding.

Funding mechanisms such as internal service funds may be used to centralize and allocate risk-related costs across departments. These structures can improve cost tracking and support reserve planning.

References

- Section 768.28, Florida Statutes – Waiver of sovereign immunity and recovery limits. Official link
- Chapter 440, Florida Statutes – Workers' compensation. Official link
- Florida Department of Financial Services – Division of Risk Management. Official link
- Government Finance Officers Association – Risk assessment and internal service best practices. Official link
- AM Best – Insurance company ratings and information. Official link