Risk Identification

Learning Outcomes

By the end, of this unit, the learner will be able to

- ✓ outline the phases involved in Risk Identification.
- ✓ describe Risk Identification Process.

Risk Identification

Introduction

For more effective risk management, an organization needs to ascertain and evaluate the risks it faces.The first step in building a company's risk profile is to identify the risks. Documentation is very important for effective risk management; however, there is no single correct way to document an organization's risk profile. An analysis of the business, or Stage 1, is a prerequisite to identifying risk.

Risk identification can be placed into the following two phases:

- **Initial Risk Identification** is used for a new company or an enterprise which has never identified its risks in a structured manner. It is also usedfor a new project or activity within a business.
- **Continuous Risk Identification** is required to identify new risks that did not exist previously, fluctuations in existing risks, or risks which did exist but are no longer relevant to the company. This should be a routine activity for every organization.

In either event, risks should be related to goals. Risks should only be evaluated and prioritised in relation to objectives, which can be done for any type of objective, ranging from personal objectives to organizational objectives. It is important to identify generic risks that will affect the company's objectives but are not immediately apparent when evaluating specific business objectives. A risk may apply to a number of the organization's objectives, and its potential impact may vary in relation to different objectives. The best way to address any particular risk may be different in relation to the objectives; however, a single treatment may address the risk in relation to several objectives adequately.

When stating the risks, one should avoid stating that the impacts that may arise are the risks themselves. Risks that do not affect the objectives should not be identified. Care should be taken not to define risks with statements, which are simply the opposites of the objectives. Statement of a risk should include the cause of the impact, as well as the impact to the objectives, or the cause and consequence which might occur.

Objective – To travel from A to B by train for a meeting at a specified time

Failure to get from A to B on time for the meeting.	**X** This is simply the converse of the objective.
Being late and missing the meeting.	**X** This is a statement of the impact of the risk, not the risk itself.
There is no buffet on the train, subsequently I get hungry.	**X** This does not have an impact on achieving the objective.
Missing the train causes me to be late and miss the meeting.	This is a risk which can be controlled by ensuring that I allow sufficient time to get to the station.
Severe weather prevents the train from running and me from getting to the meeting.	This is a risk which I cannot control, but for which I can make a contingency plan.

The individual risks that an enterprise identifies are generally not independent of each other and form natural groupings. For example, there may be several risks that can be grouped together as *resources*, while others may be grouped together as *environmental*. Some risks could be applicable to any number of the company's goals. These groupings of risks will include related risks at operational, strategic and programme levels. A grouping of risks should never be confused with the risks themselves. Risks should be identified at a level where a specific impact can be identified and a specific action to manage the risk can be identified. Once identified, all risks should be allocated to an owner who is responsible for ensuring that the risk is monitored and managed on an ongoing basis. The risk owner is accountable for managing the risk and should have sufficient authority to make sure that the risk is adequately managed. The risk owner may not be the person who actually takes the action to address the risk.

The primary process objective of risk identification is the identification of both the risks to the organization, which would decrease or eradicate the probability of the company reaching its objectives, and the opportunities, which could improve business performance. The risk and opportunity identification process is sufficient when it satisfies the following subgoals:

- Understanding of the overall management of the business activity is achieved.
- The risk identification process is started only after the business objectives or the objectives of the activity being studied are defined. Risks are only threats to objectives. It is impossible to identify risks without understanding the objectives.
- Risk identification is not started until the business objectives, success criteria, and deliverables are aligned.
- Risks are not identified before the map or flow chart of the business processis created.
- The process used to identify risks is extensive, investigating all major sources of opportunity and risk. The process of identification is undertaken with the help of a risk breakdown structure or process map that includes all essential business actions.

- Staff members from all appropriate company departments are involved, and no departments are forgotten or excluded.
- Department representatives taking part in the identification process are senior enough to be knowledgeable in their area of specialisation and are aware of company risk exposure and previous corporate lessons learnt.
- Where appropriate, non-executive directors are consulted and included in the risk identification process.
- Descriptions of risks are wide-ranging and understandable to all the participants in the identification process. More specifically, they are and will be readily understood and considered significant weeks after the identification process is completed.
- The risks described are pure risks and not a combination of causes and effects. For example, programme overrun is not a risk itself but the effect of a risk.
- The interdependencies between the risks are acknowledged.

Risk Identification Process

A suitable approach or tool must be used to identify the risk. Two of the most commonly used approaches are:

Commissioning a Risk Review

A designated team will be established to evaluate all the activities and operations of the company in relation to its goals and to identify what the related risks are. The team, which may be in-house or contracted, should conduct a number of interviews with key staff at all levels of the organization in order to develop a risk profile for the entire range of activities. However, it is important that this approach should not create a misunderstanding for line management, who should understand they are still responsible for controlling the risks which are applicable to their objectives.

Risk Self-Assessment

A section of the company will be invited to assess business activities and to contribute to the analysis of the risks that the company faces. This could be done through a documented approach where a framework for diagnosis is set out with questionnaires. However, it is often more effective to conduct a facilitated workshop where facilitators with appropriate skills help the staff to identify the risks influencing their objectives. Better ownership of risk tends to be created when the owners themselves identify the risks affecting them, which is why this approach is quite strong.

As these approaches are not mutually exclusive, a combination of approaches to the risk identification process will yield better results. This often highlights important differences in risk perception within the company. These differences in perception need to be addressed in order to attain efficient integration of risk management at all the levels of the company.

CATEGORY OF RISK Illustration / issues to consider

External risks are those that arise from the external environment, not from within the organization's control, but where action can be taken to reduce the risk.

This analysis is based on the "PESTLE" Model:

Political - Change of government; cross cutting policy decisions (e.g. the Euro); machinery of government changes

Economic - Able to attract and retain staff in the job market; exchange rates which affect costs of international transactions; effect of global economy on UK economy

Socio-cultural - Changes in demographics affect demand for services; stakeholder expectations change

Technological - Current systems become obsolete; expense of procuring the best technology available; opportunities available due to technological development

Legal/Regulatory - EU requirements; laws that impose requirements, e.g. employment legislation or health and safety

Environmental - Buildings need to adhere to changing standards; disposal of surplus and rubbish.

Inputs

- Assumptions are statements of belief about the result of future events. These future events may be aspects of a business venture or project. Assumptions may include issues such as market size, competitor behaviour, market fluctuations, increases in fuel or energy costs, and resource availability.
- Uncertain events can be described as known events that are sure to occur, but their scale is unknown. The expense to be incurred on bored-pile foundations of a new building is an uncertain event. Although soil surveys can be carried out, the ground-bearing ratio may be calculated and a piling design completed and the required depth of a pile be ascertained only when the auger has bored the hole due to different ground conditions across a site.
- Lessons learnt are those lessons learnt from a completed project or activity in terms of which segments went well and should be repeated and which did not go well and should be improved upon if a similar activity is embarked upon in the future. Maintaining records of lessons learnt is necessary for informed decision-making and organizational improvement so that repetition of actions that had an unfavourable outcome may be avoided and the positive outcomes may be capitalised on.
- Issues are problems that are identified and recorded to be unresolved with reference to the approach to be adopted. With the passage of time, an issue may be eliminated or converted into a risk, fixed cost or an uncertainty.

- Business analysis is the group of findings reached after conducting the activities described in the previous unit.

Process Activities

Activities of the risk identification process are those tasks considered essential to capture uncertainties and risks and are documented in a risk log, list or register. These include:

- Defining and recording the business objectives or the business objectives subset, which is being examined;
- Risks to the objectives cannot be identified without knowing what the objectives are in the first place. Although this is rather obvious, it is surprising how often the objectives are unclear or project team members have different views on what the objectives are.
- Reviewing the business analysis;
- Identifying the risks and opportunities of the objectives as comprehensively as possible using the facts obtained from the business analysis as prompts,
- Achieving a consensus on the opportunities and risks, their description, their interdependencies, and how they will make an impact on the organization, and
- Recording the risks and opportunities.

Clarifying the Business Objectives

From the beginning of the risk identification process, the business or activity objectives must be identified.The main objective of the process is to identify the opportunities or threats to these objectives. Stated objectives, deliverables and success criteria must be aligned. The deliverables and success criteria must originate directly from the objectives. The lists of objectives should not be a combination of primary and secondary objectives.

Typical Contents of a Risk Register

Document Control

Title of the register

Author of the register	Originator of the register and point of contact for any questions regarding the content
Date register compiled	Date of issue
Issue number	Unique issue number
File reference	The location of documents on the server

Register content

Risk identifier	Unique number to identify the risk
Risk category	Risk subject area

Risk description	Full description of the risk that will be easily understood by all after the completion of the process of identification 12 months later.
Risk status (overtaken by events)	The commonly used descriptions are *Active*, *Closed* and *OBTE* (Our biggest thing ever).
Probability	Assessment of how likely the risk is to occur. The probability can be recorded as a percentage, a category or both.
Impact	Impact can be measured in terms of cost, duration, quality or any other business or project objective.
Proximity	Reflects the timing of the threat of the risk. For instance, does it occur at a specific point in time?
Risk response category	The terms adopted here are reduce, retain, remove, or transfer.
Manager	The person responsible for agreeing on and managing the implementation of the risk response action
Actionee	The person responsible for implementing the risk response action under the auspices of the risk manager
Risk response action	Description of the specific action or actions decided upon to address the identified risk to remove, reduce or retain the risk
Expected value	Calculated by multiplying the average impact by the probability percentage

Reviewing the Business Analysis

This process activity will review the business analysis findings described in the previous unit. Based on the objectives of the study, one or a combination of the following areas will be studied for sources of risk and/or opportunity:

- business plan
- market
- change management
- acquisition
- regulatory compliance
- resources

Risk processes:

- value chain
- financial ratios
- audit committee roles and responsibilities
- Process map

Risk and Opportunity Identification

The requirement for a systematic identification of risk and opportunity in the risk-management process is based on the following expectations:

- All business activities including change management, acquisitions, capital projects, supply chain management, and counterparty contracts are exposed to risk.
- Business risks are usually understood by the management, but are not communicated to other staff members effectively.
- Ad hoc approaches lead to unidentified risks and blind spots.
- A formal open-minded, non-attributive environment is a prerequisite for providing a setting whereby controversial or alternative views can be heard.
- Identifying opportunities is just as important as identifying risks.
- An organised and repeatable system of risk identification is required for consistent and measurable risk management.
- Identification and presence of risk is not a criticism of the administration's performance.

Risk identification is a facilitated process and can be conducted in several ways. One or more techniques can be used, such as questionnaires, including the Delphi technique, and interviews or interactive workshops including brainstorming or the nominal group method. Identifying risks and opportunities is generally a group-oriented technique that relies on the combined knowledge and experience of the individuals designated to take part in them. Based on the size and geographical dispersion of the company, identification activities maybe done by one-on-one interviews, meetings, e-mail or video conferences.

The aim of these group activities is the identification of the major risks across the enterprise, understanding the interconnectivity between them and creating a risk management strategy that takes the organization's appetite for risk into consideration.

The following techniques are useful for identifying business risk:

- interactive workshops
- roundtable discussions
- strategic risk reviews
- checklists or questionnaires
- specific studies / surveys
- structured interviews
- management reports

Facilitation

The facilitator must plan how to acquire information from participants and record the risks to the business or project being studied and their assessment. Therefore, the responsibilities of the facilitator of interactive workshops and interviews are the following:

Timing

Select the date and time of the workshop in conjunction with the study sponsor.

Physical Environment

Select an appropriate area large enough to accommodate the specified number of attendees comfortably. The venue should be away from the attendees' work place to prevent interruptions. For this reason, conference facilities are often selected. Decide on a suitable seating arrangement that encourages discussions, such as a horseshoe formation. The room should have all the amenities required, such as blackout facilities, plug points and pin-up space. There should also be a white wall or screen for using a notebook computer with a projector, as well as a whiteboard and/or flip charts.

Selecting Attendees to Maximise an Effective Outcome

In collaboration with the study sponsor, decide who the suitable attendees may be to ensure that the right mix of skills and experience are present. This will help make the risk and opportunity identification as broad as possible to avoid blindspots.

Producing an Agenda

Set up a structured and realistic agenda that is not overambitious. It must identify the workshop objectives, examine the aspects of interest and include adequate breaks.

Preparing and Forwarding a Briefing Pack

The briefing pack should include the date, time, venue, objective of the workshop, status and background to the business activity or project, agenda, attendees, workshop rules, presentations, preparation required, risk-management terminology that will be used, outputs, and any other applicable information.

Managing the Process of the Workshop

- State the purpose of the workshop at the beginning of the workshop.
- Talk about the workshop rules, such as no mobile phones, all participants are equal, one person talks at a time, every idea is valid, and no criticism or judging, etc.
- Walk through the agenda at the start to give attendees a clear idea of the intended course of events.
- Ensure that everyone understands the terms that will be used during the workshop.

- Provide direction and a common purpose.
- Obtain participants' buy-in on the desired workshop results.
- Ensure that speakers who have been requested to describe part of an activity or project to set the scene do not overrun their allotted time.
- Ensure that all skills and subject areas are represented.
- If the discussion stays for too long on a detailed issue, bring it back to the core objectives.
- Don't allow individuals to have discussions with neighbours.
- Maintain momentum.
- If necessary, be prepared to change the content of the workshop.
- Ensure that all participants take part in the discussion.
- Manage dominating individuals who try to impose their views.
- Be aware of differences in attendees' hierarchical position within the company and how this affects their degree of participation.
- Be aware of interpersonal relationships among the attendees to avoid point-scoring games.
- Record the risks and opportunities as they are identified and get consensus on how to describe them in a manner that will stand the test of time. In other words, department heads should be able to understand what was meant by the risk description three months later.
- Ensure that everyone agrees with the conclusions; for example, making certain that everything recorded on the notebook, flip chart, board or electronic display is a record of what is agreed on.

Facilitation is different from chairing a meeting. The facilitator is generally not a business employee or a project team member. He or she uses only the facilitating skills and has no vote in the decision making. There are several very obvious advantages of selecting a facilitator outside of the the organization, as this avoids issues such as lack of independence, bias, hidden agendas and distortion of focus in pursuit of personal or departmental goals.

To achieve the objectives of facilitation, the facilitator can use one of the three following techniques:

Brainstorming

The brainstorming process, used in standard business management, involves redefining the problem, creating ideas, identifying possible solutions, developing selected feasible options and conducting an evaluation.

Developed by Alex Osborn in the early 1950s, brainstorming was created as a problem solving technique which would produce a far greater quantity of ideas in less time than the group problem-solving techniques which existed at the time. In the third revised edition (1963) of his text entitled *Applied Imagination* originally issued in 1953, Osborn argues that the effectiveness of brainstorming is derived from two essential components. These are briefly described by Johnson (1972); first, group thinking is more productive than individual thinking, and second, the avoidance of criticism improves the generation of ideas.

Osborn maintains that a creative environmentfor brainstorming is achieved only by strict observance to the four rules of brainstorming, which are:

- Criticism is ruled out; evaluation of ideas must be postponed for later.
- Free-wheeling is encouraged; the wilder the idea the better.
- Quantity is sought; the more ideas, the better the opportunity of finding useful ones.
- Combination and development, try to build on other participants' ideas.

Nominal Group Technique

The Nominal Group Technique (NGT) was developed by Delbecq in 1968 (Delbecq 1968). Delbecq *et al.* (1975) describethe operation of the NGT method as beginning with group members, a group ranging from seven to ten,who will write ideas related to the problem on paper without discussing them. Approximately five to ten minutes later, each person presents one of his or her ideas concisely. These ideas are written on a flip chart in complete view of the participants. This process continues until all members are sure that they have no more ideas to contribute. After all the ideas are recorded, each one discussed. Finally, each person notes down their assessment of the risks, ranking them in order or rating them for being the most serious risks. These ratings are mathematically aggregated to provide a group decision. Delbecq*et al.* summarise the NGT decision-making process as follows:

- There is silent generation of ideas in writing.
- Round-robin feedback from participants is recorded in a brief phrase on a flip chart.
- Each recorded idea is discussed for clarification and evaluation.
- Individual voting takes place to prioritise the ideas generated. The group decision is mathematically derived through rank ordering or rating.

Delphi Technique

The Delphi Technique is less commonly used to assess expert opinion. The technique, originally developed by Dalkey, Helmer and others of the Rand Corporation, was specifically for technological forecasting, but has been widely applied. It is a technique for systematically collecting and organizing judgements on a particular topic from domain experts. These experts work independently of each other and reply anonymously to a set of carefully-designed, sequential questionnaires. The second and any subsequent questionnaires are preceded by feedback in the form of summarised information assembled from earlier responses, with the aim of arriving at a consensus. Turoff (1970) suggests that at least three separate groups of individuals are required to perform three different roles:

Decision maker(s)	The individual or individuals expecting data or results to use for their purposes (Client/Sponsor).

A staff group	The group which designs the initial questionnaire summarises the data received and prepares the feedback information and subsequent follow-up questionnaires (the facilitator).
A respondent group	The group whose judgements are being sought and who are asked to respond to the questionnaire (leading business representatives).

The elementary principle of this multistage method is to eliminate direct social contact and provide unattributed contributions, provision of feedback, and an opportunity for revising opinions. Generally, by mailed or e-mailed questionnaires, the participants are individually asked for their estimates regarding the variables that are being investigated.

These responses are then aggregated and summarised in a manner that conceals the origin of the original estimates. The outcomes are then disseminated and participants are asked if they wish to review and revise their earlier forecasts. This continues until the estimates stabilise, though normally no more than three questionnaires are issued.

Gaining a Consensus on the Risks, the Opportunities and Their Interdependencies

To assign risks to the risk owners and managers in the risk management process, it is quite important to achieve consensus and buy-in to the risks and opportunities, their descriptions and the interdependencies.

Risk Register

The risk register is updated with the findings of the process activity. The risk register will be useful only if it is used as a proactive tool to manage the business and not just be placed on a shelf to collect dust.

Further Reading:

- ✓ ***Linda S. Spedding, Adam Rose, (2008), Business Risk Management Handbook: A Sustainable Approach***
- ✓ ***Edmund H. Conrow, (2003), Effective Risk Management: Some Keys to Success***
- ✓ ***David Vose, (2008), Risk Analysis: a Quantitative Guide***