How Lean Six Sigma Can Increase Productivity and Profitability By Improving Risk Management Efficiency

Introduction

Companies are under intense pressure to become more efficient, doing more with the same or fewer resources. Eroding operating margins, declining revenues, and the need for new streams of growth are converging. At the same time, companies are concerned about compromising quality and customer service. The risk-management function has not escaped this "squeeze." Many risk-management departments are working with reduced budgets while being pressured to reduce overall company costs. This pressure extends to outside consultants and vendors that assist the risk-management department.

A Lean Six Sigma process-improvement strategy can help companies to stay competitive, and extending this strategy to risk management is a must to optimize overall benefits. This white paper explains how risk managers can use Lean Six Sigma methods and tools to control costs, reduce inefficiencies, and quickly develop solutions to problems while expanding value-adding activities that help to protect the company's profit margins and support top-line growth.

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Lean Six Sigma

Lean Six Sigma is a combination of Six Sigma and lean process improvement:

- *Six Sigma* is data-driven and uses statistical variation to identify the causes of poor-quality results so those causes can be addressed. Six Sigma projects follow five phases to resolve a problem: Define, Measure, Analyze, Improve and Control, known as *the DMAIC process*.
- *Lean process improvement* is process-driven and uses *value-stream mapping* to identify wastes[1] that inhibit a process from creating the maximum amount of value that it could; and rapid improvement events (known as *kaizens*) to eliminate the non-value-adding waste and redirect assets to value creation.

Lean Six Sigma combines the DMAIC principles with focused rapid improvement, which results in a systematic framework that teams can use to:

- Identify the root cause of unacceptable results and/or non-value-adding waste in *any* process;
- Eliminate the root cause and/or waste using collaborative problem-solving tools and techniques in order to free up assets for new growth opportunities; and,
- Repeat the cycle as they work, thereby continuously improving the overall performance of the company.

Lean Six Sigma fundamentally changes the way employees think and teams collaborate. Instead of just accepting processes as unchangeable and problems as inevitable, employees become empowered to change the processes they use for the better—making their work safer, less frustrating and more meaningful; and strengthening the sustainability of their company through improved performance, i.e., financial results.

It is important to understand, however, that a Lean Six Sigma strategy will not be successful if it is limited to one function or department. In this scenario, two things commonly erode resulting benefits: Problems end up being "passed on" to an adjacent function instead of being solved; and/or decision-makers in upstream or downstream functions unknowingly reverse improvements through unrelated decisions or actions because the are "left out of the loop."[2]

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1 [1] The seven wastes that impede a process' optimal performance are unnecessary transport, excess inventory, motion, time (waiting), over-production (making more than the customer wants), over-processing (doing more than the customer wants), and defects/rework.

2 [2] The importance of enterprise-wide application has its roots in the foundation of lean process improvement, the Toyota Production System (TPS). The fathers of TPS aimed to do much more than reduce waste and solve problems. They envisioned a self-learning culture and a company that's most powerful competitive tool is knowledge created through ongoing process improvement via hands-on, collaborative learning in every process in every function. This is what has made Toyota Motor Company the most sustainably profitable automaker in the world.

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Lean Six Sigma in Risk Management: Significant Business Results

When applying Lean Six Sigma to risk management, consider both a company's culture and the processes that are specifically part of the risk-management function.

Fostering a Risk-Averse Culture

Process-efficiency improvement and risk reduction tend to occur simultaneously even when the inefficiency does not appear to have directly associated risk. For example, eliminating duplication of paperwork not only improves efficiency but also reduces the risk of information leaks by reducing the opportunity for such a violation to occur.

Every employee, from an hourly part-timer to the CEO, should have a risk-accountability objective by which performance is measured. Ideally, employees conduct business in a risk-aware manner as second nature; identify, assess and manage the risks within the context of their specific job functions; review existing safeguards to identify any gaps; and have the freedom to escalate any risk issues to management.

Lean Six Sigma provides the system employees can use to make a practice of:

- objectively analyzing a process to fully understand how it works;
- identifying issues, problems, waste and improvement opportunities in the process;
- prioritizing improvement opportunities;
- employing tools and techniques to solve priority problems or capture significant improvement opportunities; and,
- controlling the newly designed process so it delivers the anticipated benefits.

Improving the Risk Management Function

One of the key areas of focus for Lean Six Sigma must be reducing waste in the risk-management department. Risk managers should understand every activity in the processes they use, determine whether these add value, and remove those activities and processes that don't add value for the company. Waste is inherent in all processes and has significant cost consequences.

Sometimes problem resolution or waste removal falls into the "just-do-it" category because the fix is obvious and easy to make without disruption. Other times, a team-based focused improvement effort is needed.

Lean Six Sigma helps by enabling risk-management departments to streamline their claims-management process, which normally is comprised of various other sub-processes, and therefore prone to complexities and time delays.

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An important Lean Six Sigma tool for doing this is value-stream process mapping, which helps to identify the biggest improvement opportunities. The value-stream map depicts reality, warts and all. It allows everyone on the team to understand what activities are happening, in what order, and with what levels of performance.

With value-stream process mapping, a team constructs a flow chart that documents—in detail—every step in a process. The visual result helps teams to determine which process steps are important and which can be eliminated or modified. The goal is to gain agreement on a process from end-to-end, the source of its biggest expenses, and where inefficiencies or performance gaps exist. Boxes depict important process data, such as elapsed time, at each step.

Completed map in hand, teams determine the value of each step, based on three categories.

- *Customer value-add:* An activity essential to deliver a service to the customer, a feature that the customer is willing to pay for, or a function that enables on-time delivery or enhances price competition.
- *Business value-add:* An activity that improves effectiveness or efficiency in a process, or addresses safety or regulatory requirements.
- *Non-value-add:* An activity not required to meet customer needs or run the business.

The non-value-adding steps should be attacked first (eliminated or automated) to generate time and cost savings. Then, teams improve business-value add tasks as much as possible by removing waste. Finally, they optimize value-add steps by removing waste, reducing variation, and fixing problems that cause defects.

Identifying Priorities and Setting Benchmarks

Applying Lean Six Sigma to risk management will have a big impact on business priorities because risk managers will be evaluating each aspect of the company's risk management program to Define what can go wrong.

The DMAIC process has been used to evaluate a company's claims-management services. The claims-noticing process was identified as an improvement opportunity, i.e., a place where, if something "went wrong," there could be problems.

When a claim is made against a company, it must provide its insurance companies with "notice" of the claim, which entails sending a letter to the insurance companies describing the circumstances surrounding the claim. The first notice initiates the claims-handling process at the insurance company and serves to give the insurance company sufficient information to conduct an adequate investigation and to gather information necessary to prepare a defense of the underlying claim. Insurance companies sometimes argue that the Insured failed to give timely notice of the claim and if they are successful with the argument, the Insured could forfeit coverage.

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Value-stream mapping can be used to evaluate the claims-noticing process step-by-step. Then, multiple process points can be identified where steps (waste) can be eliminated and technology could be incorporated to get more notice letters into the mail to insurance carriers faster. The result is significant savings of cost and time for clients.

In addition to revealing potential problems and improvement opportunities, value-stream making can help risk-management departments establish internal benchmarks. Benchmarking can help track costs by activity and allows a company to better understand its risks and manage the claims-management process using best practices.

Achieving best practices in claims administration is the most reliable leading indicator of good risk-management performance outcomes. Adherence to true outcomes-focused best practices requires a risk-management department to perform at a clearly specified level, i.e., a benchmark. Best practices must focus on the qualitative aspects of performance as well as on the process, and, ultimately, on improved outcomes. The goal is to create a "Best Practice" claims department that is focused on identifying and managing claims; teaching the employees to think and operate as claims managers, and to foster a culture of accountability and transparency

Conclusion

Risk managers who apply Lean Six Sigma methods are likely to experience significant benefits beyond quick-win process improvements because this management approach promotes new ways of thinking and drives operations to higher levels of effectiveness and efficiency. To be effective, there are a number of lessons to be learned when applying the Lean Six Sigma methodology:

- Senior management must be dedicated, visible and provide vocal support for Lean Six Sigma.
- Lean Six Sigma requires extensive training, both internal and external, in the use of quality tools and statistical measures.
- Projects should be carefully selected with goals that relate to improving the bottom line. Priority should be given to those projects that will have a higher impact throughout the company and contribute to meeting the company's strategic goals.
- It's important to communicate results and share improved risk-management best practices learned from improvement efforts throughout the company. Doing so works to build momentum for continued change.

Understanding the company from end to end allows risk managers to identify areas of particular importance that need to be scrutinized for process improvement. Risk managers must understand what their company is doing, how it is doing it, and, finally ask why certain steps are taken. In breaking out the problem, risk managers can clearly identify areas to create solutions using Lean Six Sigma process improvement that helps drive value.

Risk managers with significant experience in quality and productivity improvement have found Lean Six Sigma to be the next logical step in their ongoing efforts to eliminate waste and to provide superior service. Lean Six Sigma provides the means to develop a stronger process and focus; and, in so doing, reduce inefficiencies and improve the bottom line.

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