

THE CONCEPT OF RISK

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My two most recent Atheneum papers, the first on ambition and the second on utopian societies, failed for basically the same reason. Neither paper fully answered why there is always a certain percentage of people that always want "more", whatever "more" may be. The resulting consequence is that such individuals cause themselves, and their respective societies, to remain in a constant state of agitation and uncertainty.

Then, while attending my high school's 20th year reunion, the answer suddenly occurred to me. The answer was simple--- I was asking the wrong question. The question is not "why do some people want more" but instead "why are some people willing to take risks in order to obtain more". "More" is relative, dependent upon an individual's society, geographical region, and time in history. Isolating the concept of risk, it becomes clear that individuals will not always react the same way in all situations. In any situation, every person's reason for action or inaction can be examined in terms of what that person is willing to gain or lose in relation to the benefit received.

When human behavior is viewed in terms of risk, it becomes apparent that every person does not automatically want "more". Although every individual may not be perfectly content, this approach recognizes that every person has at least attained some degree of contentment in his life. Thus, if there is a common denominator to understanding why some individuals seek "more", one basic question can be asked:

Why are some individuals risk-takers and others risk-avoiders?

With this thought in mind, this paper will attempt to examine the importance of risk in shaping individual and societal behavior. The primary premise of this paper is that, depending upon the situation and an individual's values, an individual adopts either a risk-taker or a risk-avoidance position. Hopefully, this paper will demonstrate that an individual's approach to risk affects every situation with which he is involved, and determines to an even greater extent how he will respond to that situation. In an overview, five distinct questions concerning risk will be examined:

- I. Does it make any difference how risk is defined?
- II. Who fears what and why?
- III. How can additional risk be justified?
- IV. How can the consequences of risk be allocated?
- V. What is the greatest risk?

I. Does it make any difference how risk is defined?

Obviously, regardless of how an individual or a society defines risk, one's response to risk is affected by the type of risk involved. Whether real or imagined, the types of risk with which we are constantly confronted include health, political, economic, historical, legal, religious, safety, education, environmental, military, psychological, family, and cultural. In the truest sense of the word, we are at risk at any given moment, threatened from all sides. As a defensive mechanism, we all develop some form of mental scanning device to distinguish those risks that might harm us in some way. As few of us are true independent thinkers, which risks we fear are largely determined by the institutions in which we place the greatest trust. Such institutions would include our government, religion, culture, family, employer, and close acquaintances. To a large extent, most of us allow institutions to serve as our mental scanning device in differentiating risk. In terms of defining risk, the question changes from "What does a person fear and why?" to "Who does a person believe and why"?

As everyone's perspective of risk is always different, risk may be perceived as short-term or long-term, outside of our interest, or outside of our control. Arguably, it would appear that we examine all information concerning any risk as to whether the new information reinforces our own values and beliefs. That is, one person may perceive a situation as an insurmountable problem whereas another person may perceive a tremendous opportunity. The truth is, whatever the situation, what and how we perceive risk provides tremendous insight into the current values, past experiences, and future goals of that individual and society.

Along these lines, it is important to be aware of how the different definitions of risk affect our lives. In terms of a strict dictionary definition, risk has three different connotations:

- (1) There is the possibility of suffering a harm or loss, i.e., danger. As in "There is a risk we will not return". This definition stresses the possibility that a person may be in a worse position after a risk is taken than before. Also, inherent in this definition is the realization that danger can be avoided if the additional risk is not taken.
- (2) A factor, element, or course involving an actual danger, i.e. a hazard. As in "The stormy weather is a risk that we will have to take". This definition emphasizes a particular type of risk, such as the risk of physical danger (mountain climbing) or business (bankruptcy). and,

- (3) There is the implication of a wager, as in "I'll risk \$100 the brown horse wins". This definition emphasizes the possibility that the probability of an outcome can be calculated in advance.

Using these three definitions, it is interesting to distinguish how individuals and societies define risk differently. In business, the loss of \$10,000 would be devastating to an unemployed worker but yet considered acceptable to Donald Trump. Or, in a war between China and Australia, China might consider the loss of 20,000,000 men acceptable whereas such a loss would represent Australia's total population. In this case, China might decide that the risk of loss (human life), the hazard (doing without those men) and the expected worst possible outcome is an acceptable risk. In both situations, what is at risk and the magnitude of the risk are perceived differently by each involved party. Further, so long as individuals and societies have a common definition of risk, all involved parties can prioritize the available alternatives. Such a common understanding allows for an objective assessment of the benefits, in terms of success or failure, of competing courses of action. Once aware of the true dimensions of risk, individuals are then able to better choose those activities which they believe will bring them the greatest chance of success.

A common definition of risk further allows a society to accomplish two important functions if that society is to survive. One, the society is able to recognize its winners and losers, and two, to reallocate the desirable resources within that society. The short-term consequence is that risk-takers are able to apply their energies toward those efforts which best allows them to achieve the benefits to which they attach the highest value. Such short-term benefits may include profit, fame, power, control, or freedom. However, the long-term consequence is that that society is able to accommodate the inevitable struggle between individuals and societies for desirable resources. By example, children aspire to be opera singers rather than astronauts in Italy, doctors rather than goat-herders in the United States, and communist party leaders rather than taxi-drivers in China.

In the truest sense of the word, our heroes are simply risk-takers that took a risk and succeeded, whatever the game being played. Perhaps without realizing it, individuals and societies seek-out successful risk-takers as heroes, regardless of the activity being pursued. As an example, contrast America's sudden interest in hockey during the 1972 Winter Olympics. Perhaps this is why societies recognize and individuals seek out the opportunity to be risk-takers, successful risk-takers are considered the exception to the

rule. Historically, it is interesting to note how our heroes change as their success increases or decreases. Although Donald Trump was held in high esteem during the 1980's, this does not appear to be the case for the 1990's. If there is a constant concerning risk, time alone eventually provides a level playing field for those that do not continue to succeed as the level of risk increases. In the attempt to determine why people want "more", perhaps "more" is not in itself the ultimate objective. Instead, perhaps risk-taking activities are pursued simply because they provide the opportunity to be recognized as different or special.

Also, rather than perceiving its national character in a positive light, a society's common understanding of risk can just as easily be seen to defined in a negative manner. In a recent issue of the Economist, America was perceptively described as now having "a decadent puritanism: an odd combination of ducking responsibility and telling everyone else what to do". Time expanded this observation by observing:

It is also the age of the all-purpose victim: the individual or group whose plight, condition or even monetary setback is not a matter that needs be solved by individual effort but constitutes a social problem in itself. "We're not to blame, we're victims" is the increasingly assertive rallying cry of groups who see the American dream not as striving fulfilled but as an unachieved entitlement. Crybabyhood is all blame, no pain, for gain. And all too often it works.

Gone is the principle of accepting individual responsibility for one's actions. At least in America, society wants the best of all worlds, to live in a risk-free world and to share equally in the benefits produced by those who take additional risk.

However, whatever terms are used to define risk, the decision to take a risk must still be made. Perhaps this critical factor is what differentiates a risk-avoider from a risk-taker: successful risk-takers are willing to make a decision which directly places their interests at risk. Arguably, in any situation 50% of the involved parties have consciously decided to not be aware of the problem, 25% of the people recognize the problem but do not care, 20% of people are concerned and will offer advice, and only 5% will actually assume the risk and make a decision. This is not to say that the 75% that have elected to not become involved are incapable of understanding the risk, only that they have decided to be risk-avoiders rather than risk-takers. As it is impossible for everyone to benefit equally in all transactions, people by necessity must pick and choose those activities which best offer them the best opportunity for success. Thus, risk-avoidance does not indicate a resigned

approach to life but only that the decision to avoid risk is made at an earlier point. Although both situations involve calculated decisions, by definition risk-takers are provided with many more opportunities, involving both complexity and magnitude, than risk-avoiders.

This is the realization that occurred to me at my high school reunion--although most people understand risk and the resulting benefits, most are unwilling to consistently make decisions which place their interests at risk. Perhaps without even realizing it, at some point most people decide to accept the status quo and to live their life within their own particular comfort zone. Judging from our high school class, it is important to note that risk-takers are not necessarily those with the most personality, intelligence, or athletic ability. More often than not, risk-takers are exactly the opposite, but whose value system and energy level allow them to justify the many sacrifices required to accomplish a particular goal. Such sacrifices include time away from family, increased personal stress, and the postponement of more enjoyable activities.

In this context, it is interesting to contrast the contradicting manner in which society compensates risk-avoiders and risk-takers. Whether based upon legal, religious, or philosophical grounds, human life is more highly valued than the gain or loss of property. Yet, in a free market economy, compensation is not based upon one's exposure to physical harm but upon one's willingness to risk tangible assets (money, property) in the pursuit of additional tangible assets. By example, contrast the monetary rewards of a policeman with that of an entrepreneur. Without exception, compensation dramatically increases as existing assets are placed at risk. Expressed in terms of a risk-reference point, any job can be seen as having a certain value to society as to what assets are at risk and what additional societal value might be produced through that job. By example, a salary of \$20,000 might be seen as a risk-reference point in our local economy. In New York City, this figure might be \$30,000. It is only when the possibility of increasing or losing one's assets comes into play does a society compensate in excess of the risk-reference point. Rather than being paid to maintain the status quo or do work that can be duplicated, society pays risk-takers for their ability to create new assets or for increasing the value of existing assets. Ironically, society advocates that a person's value lies in his value as an ethical and law abiding citizen. However, if compensation is used as an objective measure, it would appear that society places a higher value on a person's willingness to take risks which will increase the assets of that society.

II. Who fears what and why?

Realizing that everyone perceives risk differently, the question must then be asked: who fears what and why? In this regard, there are more questions than answers. What is our source in determining risk and what are the motives of our sources? (How much did William Randolph Hearst really know about the sinking of the Maine prior to the Spanish-American War?) Is the risk relative--what is our self-interest and are we too close to make an objective decision? (Do we really care what happened at the Middle East peace talks?) What is our knowledge of the risk--what are the real facts and are we open to new facts which may disagree with our pre-conceived opinion? (Do we really want to know how many more lives are lost by driving over 55 miles per hour?) Are we willing to seek out new information which may create additional risk or stress? (Do we really want to know which chemicals in our food may be hazardous to our health?)

Further, in seeking out knowledge that would affect our behavior toward risk, several important questions must be asked: would we understand the new information, would we follow it, how much credibility should be given to the new information, and how long should the new information be followed? (Should we really eat more fiber?) Obviously, every question increases the frequency which risk must be confronted and further increases the number and magnitude of the decisions which must be made. No wonder that 75% of all people are risk-avoiders. One simply does not have the time or the intellectual ability to mentally scan every risk that in fact does or might exist.

Traditionally, at least four different theories have been put forward to help explain why people perceive risk differently. The most widely held theory is the "knowledge theory", i.e., people perceive situations to be dangerous because they know them to be dangerous. (I know that dog will bite). That is, people worry most about the risks that seem most directly to threaten their well-being at that particular moment. This theory parallels Maslow's stages of wants--complex threats materialize only if the most direct and immediate threats are successfully resolved. After an individual feeds and shelters himself, and perhaps has sex, only then is he willing to worry about his prestige or to help his community. Another theory explains risk perception as totally dependent upon the personality of the individual. That some people, like motorcycle racers or airplane stunt flyers, take extreme risks because of certain intrinsic personality characteristics. Another explanation of risk perception follows two versions of economic theory. In one, the rich are more willing to take risks because they benefit more and are better shielded from economic consequences. In the other, the rich are less interested in taking risks

because they have affluence and are more interested in the improvement of their personal health or social relations. A final explanation for taking additional risk is based on political theory. This approach assumes that a person views any risk as a struggle between competing political philosophies. i.e., the haves versus the have-nots.

However, although all four theories may work in certain situations, risk perception cannot automatically be pigeon-holed. Instead, all four explanations combine to provide every individual with a cultural bias. It is this cultural bias, oftentimes not even realized, that allows every individual to perceive, make a decision, and act on any risk. In its simplest terms, people choose what to fear and how much to fear in order to support their own lifestyle and view of the world. Arguably, people's first response to any new risk is to defend their way of life and to find some justification for their existing perception of the world. Although this approach represents a cynical view of human nature, once most people get past their basic wants, risk perception largely depends upon the degree of their cultural bias. Much to the chagrin of Plato and other utopian thinkers, logic does not appear to play any significant role in the perception or resolution of risk.

III. How can additional risk be justified?

Once a new risk is identified, why would anyone want to assume additional risk? When examined closely, few people will habitually take risks unless certain minimum conditions already exist. Ironically, individuals who consider themselves as risk-takers are anything but risk-takers. Before additional risk is undertaken, risk-takers seek a high level of predicting the outcome of a certain event. This "edge" may include information from The Daily Racing Form, a stock tip from a trusted friend, or the knowledge gained through self-study. Also, risk-takers will proceed only if certain prerequisites are in place. Such prerequisites include some provision for law and order, the protection of property rights, some provision for the enforcement of contracts, a medium of exchange, a public infrastructure system, and the assurance of a capable labor force.

In addition to prerequisites which lessen risk, additional risk can be justified by asking the question: does the risk affect me or someone else? Obviously, given the opportunity to place the risk of loss on the F.D.I.C., many banking executives were quick to take risks within the savings and loan industry. Against this background, we respond differently to risks that we choose for ourselves and over which we believe we have some degree of control. Also, from a moral point of view, the question becomes not "What should

I do about risk?" but "Which risks do I want on my conscience?". Arguably, was Charles Keating willing to accept the risk of going to jail because of the tremendous profit he could make or because he knew that all bilked depositors would eventually receive \$100,000?

Clearly, whether for fame, profit, or not knowing any better, additional risk can be justified if all involved parties consent. This does not imply that all parties have equal knowledge or experience, but only that there is some degree of informed consent. The key is that consent has been provided by such risk-takers and that the consequences are understood by all parties. However, in the over-all scope of things, such clearly defined risks and resulting consequences are the exception to the rule.

IV. How can the consequences of risk be best allocated?

Thus, in any risk situation the interests of three parties conflict: the winner, the loser, and those persons that have not consented. Realizing that these competing interests are inevitable, the question becomes: how does an individual or society accommodate such risks? Individually, John Stuart Mill's doctrine of utilitarianism can be followed. That is, "This is my body or money and I'll do with it what I want." However, a related question becomes: how does a society handle the unintended consequences of risk to those persons that did not give their consent? Examples include exposure to pollution in our drinking water or acid rain? In these situations, it is impossible to obtain individual consent forms or to identify all of the sources of additional risk. To protect those that cannot consent to additional risk, society has several options. Society can hope the risk goes away, ignore the risk, blame others, transfer the risk to private entities (insurance companies), or have government intervention.

Arguably, the immediate parties to any risk are capable of protecting their own interests or of accepting the consequences. Although the lack of prerequisites discussed earlier would inhibit risk-taking if an independent enforcer did not exist to settle disputes, risk-takers could survive. However, no society has historically been able to make the world 100% risk-free, equally educate all of its members, or equally share the benefits with everyone. Such across the board equality is by definition impossible. Although risk-takers may argue that the sole purpose of government is to impede risk-takers, this is not the case. Whether risk-takers like it or not, it is only through government regulation that the interests of the majority (those people that did not consent and are by definition risk-avoiders) can best be protected.

However, if an independent force is necessary to provide the prerequisites for risk-takers and to protect risk-avoiders, what is the best form of government? Although Plato would disagree, democracy provides the best over-all solution to the allocation of risk. Simply put, majority vote solves the problems of who decides and what interests are represented. Although the majority's solution may not be the most efficient, the solution is recognized as legitimate among the inevitable competing interests. Also, a democracy has the advantage of being able to educate its members and in obtaining a broader base of consent. However, any government (including a democracy), must overcome certain inherent problems concerning risk allocation. The government must distinguish between the important and the trivial, involve more members during all stages of the decision-making process, and reconcile the expectations of those who vote on matters outside of their own experience.

V. What is the greatest risk?

Realistically, one risk cannot be isolated and described as the "mother of all risks". However, as successful risk-takers at some point control a society's resources, risk-takers eventually define risk within that society. The ultimate effect is that self-serving risk-takers are able to exploit a society's most trusted institutions to their own advantage. The unfortunate consequence, and what I consider to be the greatest risk of all, is that the majority's cultural bias is then manipulated by the minority risk-takers to the dis-advantage of the majority.

OVERVIEW:

As you can imagine by now, with these thoughts in my head, I was probably not much fun at my recent high school reunion. But indirectly, these thoughts helped to explain why the best and brightest of our class have yet to make a \$1,000,000 or be honored as a Nobel Prize winner. Also, these thoughts helped to explain why there appeared to be little correlation between the personal achievements and the success of my high school classmates. In both situations, many class members were certainly intelligent enough but for some reason had been unwilling to become consistent risk-takers and to make the ongoing decisions that accompany risk-taking. During our twelve years together, our high school class apparently failed to read those books, participate in those sports, or act in those plays that would have provided the motivation to spend the rest of our lives seeking "more".

Whatever values that were needed to clearly establish ourselves as true winners in the real world, no class member appeared to have made the necessary sacrifices. Over-all, an outsider might have described our class as just a bunch of ordinary people who had been given the ability to survive 20 years of life's daily challenges. Perhaps not the most noteworthy or glamorous accomplishment, but what "more" could a high school graduating class want?