Balance Sheet Protection in Incident Response

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"We survived the accident, the business returned to normal, and everyone lived happily ever after." When it comes to environmental pollution incidents, that ending is often more fantasy than reality. But it doesn't have to be the case. It is possible to manage responses and mitigate resulting liabilities to reduce the financial and reputational threats to an organization. The C-suite perspective is focused on protecting corporate assets and limiting liabilities — including intangibles such as public perceptions and business reputation. This focus also should be implemented within the company's Finance Section of the Unified Command ("UC") structure. Under the Unified Command (the organization established under the National Contingency Plan to manage oil spill response), the Finance Section is generally tasked with accounting for resources, addressing claims and managing cash outflows; but the UC structure includes outside organizations, such as the United States Coast Guard and state responders, and these outside organizations will not necessarily be focused on the same goals of the Responsible Party. However, in a response the Finance Section can provide the information necessary for the company's C-suite to set goals and develop a strategy, the objective of which is to protect corporate assets and limit liabilities.

The intent of this discussion is to begin to pull back that veil of mystery associated with incident-related liabilities. These include, among others, uncertainties of costs & cost recovery, environmental damages & related penalties, damages to property & income and all manner of litigation liability exposures. Managing these to protect the corporate balance sheet is a process that begins long before the first alarm bell rings or siren sounds.

KEY POINT #1, ANTICIPATE YOUR WORST CASE – AND BEST CASE – SCENARIOS

Perhaps the U.S. energy and shipping industries have been fortunate to be so highly regulated. The requirements of OPA 90 and various regulatory agencies to plan — and practice — for responses to pollution release events has mandated that attention be focused on spill risks. Energy companies, as well as oversight agencies, devote large amounts of time, manpower and money to stage very elaborate spill drill exercises.

In order to drill effectively, companies should anticipate realistic release event potential. Each event will be very different in the details and yet very similar at the highest levels. However, in general, drill scenario planning in the U.S. has historically focused on operational responses, including working with government agencies. These regulatory-required drills are short in nature, and for many reasons do not give a full representation to the concerns faced by the C-suite in the case of a "real event." Unlike many types of general business risks, spill risks are often location dependent. A best practice is to consider demographic, environmental, seasonal, and other factors in anticipating incident scenarios. In doing so, firms should develop an understanding of the potential nature and magnitude of impacts to biota, land, water & air resources, residences, commerce, transportation, reputation, regulation, and general disruption of "normal" life that a release at a particular spot could entail. We refer to such an analysis as a liability risk profile. By assembling profiles for a number of locations, businesses naturally begin to better understand their exposures, and risk managers have better data to craft policies and devise protections. And yes, size matters, although location matters even more. A 15-barrel oil spill in a nearshore area impacting sensitive environmental resources will likely be far more costly than an open-water offshore spill of hundreds if not thousands of barrels.

For locations anticipated to be higher risk, consider maintaining a database of liability profiles. Such a database allows a risk manager to quickly comprehend the possible nature and magnitude of exposures. Energy companies have detailed Facility Response Plans. They should also have detailed location liability risk profiles.

KEY POINT #2, PLAN FOR THE BUMPS IN THE ROAD

Plans involve goals and processes. From a corporate standpoint the end-point goals should be similar for each incident: safety first, then balance sheet protection. How to reach these goals given the details of incident realities is always the question. The tendency for the government-led Unified Command is to concentrate more on planning efforts of rapid response & efficient cleanup and less on the longer-term liabilities issues. It shouldn't be a surprise to learn that goal-setting with respect to environmental recovery is also out of the responsible party's ("RP") hands; it is the role of the Natural Resource Trustees. Likewise, goal-setting for financial, insurance and litigation matters is often a (far-too-distant) afterthought. There are no good excuses for this. Pre-establishing endpoints empower RP personnel and responders to act timely and cohesively in alignment. Everyone pulls in the same direction.

Typically, accounting scrutinizes costs. Corporate counsel focuses on potential litigation actions. HSE wants to eliminate the hazards, and the Board of Directors is concerned with market value. From the C-suite vantage point the goal is higher than any of these. It is, or should be, to control, limit, and/or mitigate those liability exposures that could most seriously impact a business' ability to continue operations. The Finance Section should identify those exposures for a location and establish goal(s). With a large crude release in the Louisiana coastal zone during oyster harvest season, a goal could be to avoid class litigation by the oyster fisherman, as well as the restaurants that depend on them.

The “secret sauce” for achieving goals is to have clearly developed processes by which to maneuver through the hard realities of a variety of incident circumstances. Processes need to be flexible enough to accommodate location variabilities, environmental sensitivities, demographics, differences in litigious environments (including both state and local authorities), public sentiment and routine public interactions. The process will also need to be effective and well-documented. Afterall, insurers and attorneys could be combing through files for years. Regarding the example in the preceding paragraph, the processes might include working with the local associations of oyster fisherman to establish a common formula for settling loss of income claims.

The passage of time, assessment and restoration of environmental damages, operational costs, legal liabilities and public perceptions are all intertwined. A best practice is to game plan goals and processes for many situations. Goals for controlling liabilities from a pipeline leak in a flat corn field are different from that of a well blowout in environmentally sensitive wetlands. Likewise, depending on the incident particulars, the processes will vary. It may be most urgent to “get money on the street” as soon as possible or to ensure the public has a chance to observe progress in cleanup operations. It could be more important to be seen responding to social media outcries. Finding temporary housing for displaced families could be most pressing. Simply spending lots of money in lots of directions until problems go away isn’t an effective strategy. Yet, this happens time and again with consistently predictable results: waste and frustration. No organization can afford either.

Each event is very different. However, for the C-suite, the ultimate endpoint goals are similar for each response. The art of goal-setting and process planning is to understand the liabilities involved with your range of potential incidents and the types of actions needed to mitigate them.

KEY POINT #3, PRACTICE

Unlike a sporting event, in a response situation there is no “big win” for the C-suite, but there can be great success. Here success looks like a process of increasing understanding and control over the various liability components day by day. With that in mind, how does one practice? The answer is: consistently, regularly, with established procedures, with knowledgeable personnel and with realistic scenarios. For best success from the C-suite perspective, it is imperative that finance, insurance, legal, claims, environmental components be practiced. In reality, these are not drilled enough.

Practice doesn’t have to be elaborate. In fact, many of the concepts discussed herein should happen within the walls of the C-suite, and NOT in a spill response drill with multi-agency participation. But it is imperative that companies go through the process of stepping through response scenarios to understand exposures and liabilities. At every step, participants need to ask (and be able to answer) the question, “What is the next step in moving toward the goal?” Most of those answers have to do with gathering, assessing, and reporting information. Are costs being accumulated and projected accurately? How and by whom are environmental damages assessments being conducted? What is the magnitude of liability claims exposures?“ Knowing what information to gather and to whom and how to ask for it can make all the difference. For example, it’s not enough to know that a waterway is closed to marine traffic; you also need to understand how many commercial vessels have been delayed. In practically every aspect of understanding spill risk and exposure, to get the big picture, you need to ask the right questions.

It is best practice to expand response exercises for finance section responsibilities beyond the limited one or two operating periods of most drills. Typical short-duration exercises don't allow enough time for in depth thought about liabilities and how to address them. Often organizations with elaborate and detailed drill exercises have very limited practice in analyzing potential exposures from the spill scenario. The reality should be just the opposite. For example, an evacuation is often the most high-profile and complicated part of an actual incident. Yet how many drills get to the point of detailed tracking of evacuees? How many drills consider options for housing evacuees? We recommend conducting drill follow-up sessions to take the scenario to the next level and allow the C-suite and their internal response organization to drill deeper into understanding spill liabilities in order to gain clear insight on managing towards both operational and financial success.

SUMMARY

An organization's long-term financial well-being is not necessarily captive to unknowable variables of an incident response. The largest and most intimidating of those variables are liabilities: costs incurred, environmental damages, damages to third parties, and litigation exposures. Anticipating, planning for, and practicing incident responses can help an organization address Finance Section data needs that in turn can support the C-suite's longer-term strategic needs. Add to that some guidance by experienced professionals and the C-suite executives may be able to rest assured that incident liabilities are being mitigated and their business' interests are being cared for.

What should be involved in extended-scenario drills and what happens when it all hits the fan in an actual incident? Those are subjects of future discussions.

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