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PG&E’s lack of prevention leaves California communities up in smoke and possibly footing the bill

Ignoring the risk that erratic environmental climates can pose for companies worldwide can have catastrophic consequences for supply chains and the communities they serve. Climate can disrupt production, affect the workforce, alter shipping routes and, in one of the most dramatic examples, literally turn off the lights.

The Pacific Gas and Electric Company (PG&E) is being held responsible for hundreds of fires in California, including several major fires that burned hundreds of thousands of acres and killed at least 22 people. The consequences of failing to meet the risk of forest fires with an adequate response has the utility filing for bankruptcy, considering blackouts during severe drought conditions and raising costs for consumers down the pipeline.

The company spent years trying to shore up its equipment in the face of a years-long drought, but a lack of resources, commitment and urgency led to a situation in which PG&E now faces “billions of [U.S.] dollars in legal claims, the specter of bankruptcy, a federal judge forcing his way into utility operations, the possibility state regulators will break it into pieces, and potential state criminal charges including homicide, due to its continued inability to stop the fires from starting.”

PG&E lags far behind other California utilities, such as Sempra Energy’s San Diego Gas & Electric and Edison International’s Southern California Edison unit, in its efforts to implement fire-prevention measures along thousands of miles of power lines. Whereas the other two utilities had installed weather stations, replaced old power lines and poles, and cut down trees that stood in the path of power lines, PG&E has reportedly said that its own improvements won’t be completed until 2022. Despite a multi-year campaign and expenditures in the hundreds of millions of U.S. dollars to trim and cut down trees and replace old lines, the utility was unable to prevent fire after fire.

California has been suffering under a decade-long drought that, along with an increase in people moving deeper into the forested areas of the state, created a perfect storm of fires, power lines and loss of property and life.

Climate change risks and costs

The U.S. Securities and Exchange Commission issued guidance in 2010 on disclosure requirements related to climate change matters. The guidance identifies four main categories of climate-related risks to supply chains that companies should disclose:

- Legislation and regulation.
- International accords.
- Indirect consequences of regulation or business trends.
- Physical impacts.

The most obvious danger that climate change poses to supply chains is the physical impact of severe weather. In

2014, the top three disruptions were all due to extreme weather:

- Typhoon Halong, Southeast Asia (USD 10+ billion in damage, 41 week-long disruption).
- Severe flooding; Long Island, New York, U.S. (USD 4+ billion in damage, 38 week-long disruption).
- Typhoon Rammasun, Southeast Asia (USD 1.5+ billion in damage, 38 week-long disruption).

More recently, Hurricane Florence ravaged the eastern coastline of the United States, while the California wildfires ravaged the west coast. This kind of damage can cost insurers billions of U.S. dollars, and companies with global supply chains can face greater risk of disruption and huge losses if storms, floods or wildfires wipe out a supplier or close down transportation routes.

Regulations and international accords present a less dramatic risk than a raging wildfire, albeit with similar consequences if ignored. The recent International Maritime Organization's reduction of the marine fuel sulfur cap is an example of how international accords related to climate change can force companies to incur costs in the many billions of U.S. dollars. Indirect consequences can be even more damaging and long-term: A known polluter could face reduced demand for products, as well as damage to its reputation and brand.

These risks are already being assessed by insurers, who are now seeing that the premiums they should charge to protect against climate-related issues could be much higher. Several insurers are currently filing suit against PG&E for its role in starting the fires, adding to the overall liability cost of roughly USD 30 billion, more than triple its current market value.

Where to start?

The first place to begin is an overall risk assessment. What environmental risk does your company face? Does the company rely on shipping routes and coastal logistics? Is the industry particularly prone to polluting the environment? Is the environment your company works in susceptible to floods, droughts or fires? What about hurricanes or earthquakes? Which aspects of the supply chain would be susceptible to extreme weather?

Systematically answering questions like these can help to provide a framework for risk mitigation. This framework is the foundation for the policies and procedures that will help ensure a company has mechanisms in place to deal with environmental challenges, and can adapt quickly to fast-moving threats. The policies devised at headquarters can then be sent out to suppliers, contractors and other third-party vendors to start the process of integrating the entire supply chain into the framework.

PG&E faced an unforeseen issue during its tree-trimming campaign: a lack of qualified workers to do the job. The reliance on less-qualified workers was most likely a factor in why PG&E was found to be consistently behind schedule. These are the types of problems that can be mitigated with the help of a thorough risk assessment, followed by deep dives into the supply chain, vendor list and other third parties.

Finally, the C-suite has to be onboard. The 2018 Global Dangerous Goods Confidence Outlook report, sponsored by Labelmaster, the International Air Transport Association and the Hazardous Cargo Bulletin, found that a compliance officer's ability to do the job well and add value to the company is inextricably linked to the leadership's view of compliance.

With PG&E, climate change and wildfires were reportedly placed fifth on the list of top enterprise risks. Although executives noted that placement on this list doesn't matter, for insurers, investors, politicians and the public, it doesn't look good as long as a risk is on the list.

The largest utility in California faces insolvency, criminal investigation and a massive reputation hit. It is unlikely it will ever recover, and there is discussion of splitting the utility into several smaller, more easily managed companies. The billions of U.S. dollars in costs, however, may be passed down onto business and home owners through energy price increases. Not only have the communities that PG&E served had to deal with wildfires and death, but PG&E's downfall may cost those communities deep into the future. If that is indeed the track that the state takes to pay for the damages, then the company can never expect to regain its standing or reputation with the people of California.

Takeaways

- Climate change is a real risk that, if unaddressed, can cause incredible amounts of damage to a company's bottom line and reputation. Climate must be taken into consideration when doing business.
- Proper risk mitigation and response strategy is essential to the survival of companies that do business in regions vulnerable to erratic climate. Just one incident can be enough to destroy a company.