Managing Reputational Risk: How senior leaders can build trust in their organizations

by Melissa Lackey

> *It takes 20 years to build a reputation and five minutes to ruin it. If you think about that you'll do things differently."*
>
> WARREN BUFFETT, CHAIRMAN AND CEO, BERKSHIRE HATHAWAY

Building, protecting and maintaining reputation is undeniably the most important responsibility of today's senior executives. The pace of technology and business change has profoundly altered the role of senior leadership and what is expected of them. Transparency has taken on a new meaning—and level of importance.

Following scandals at Enron, WorldCom and others, corporate governance became political, resulting in an increase in government regulation and changing executive oversight. Sarbanes-Oxley went into effect to reform public accounting and protect investors. The government stepped in again after the financial meltdown of 2008, leading to bailouts of several automotive and financial companies. These actions led to the Wall Street Reform and Consumer Protection Action of 2010, better known as Dodd Frank, providing the most significant changes to financial regulation in the United States since the Great Depression.

These business scandals and the economic crises have resulted in a growing mistrust of capitalism and business. According to an annual Gallup poll, business executives have for the past five years been rated among the lowest professions for honesty and ethical standards.

The advancement of technology, especially social media and mobile devices, compounds reputational pressures for senior executives. Information from multiple sources and media channels is now available 24/7/365. The world has become smaller—yet more complex.

These business realities have not gone unnoticed by senior leaders. Boards are seeking more effective oversight and governance of business risk. For the second year in a row, reputational risk is No. 1 on the list of concerns by boards of directors, in a 2012 study conducted by EisnerAmper.

Although organizations are seemingly gaining a greater understanding of the importance of reputation and its value, most continue to struggle with identifying the risks and developing strategies to mitigate them.

Today, we live in the "Reputation Economy," a world where who you are as an organization matters as much—and possibly more—to consumers than what you sell. According to a study conducted in June 2012 by the Reputation Institute, 60 percent of the public's willingness to buy, recommend, work for or invest is driven by their perception of an organization and the values it represents. Yet, few organizations can clearly articulate or meet that challenge.

Putting a Price on Perception

> *In a market system based on trust, reputation has a significant economic value."*
>
> ALAN GREENSPAN, FORMER CHAIRMAN, FEDERAL RESERVE

Trust is today's currency. Reputation is not a single line item on a company's financial statement. Rather, it's a series of intangible assets that are linked to business outcomes, such as market value, revenue, market share, customer revenue, market share, customer and employee retention, and price tolerance. It shouldn't be surprising that in the EisnerAmper study, when asked to expound further on types of reputational risk, directors first identified quality, liability and customer satisfaction, followed by integrity, fraud and ethics, and then public perception. IT issues and security, regulatory compliance and environmental risk also were highlighted.

According to a 2007 BusinessWeek Magazine article "What Price Reputation?," a company's reputation can be measured by its ability to deliver growth, attract top talent and avoid ethical mishaps. This can account for the 30 to 70 percent gap between a company's book value and its market capitalization.

So, it's critical that organizations identify all key stakeholders, clearly understand their expectations, benchmark how they perform against those expectations and measure the gaps. These gaps also shed light on vulnerabilities. Strategies can then be leveraged to not only identify, but mitigate the risk.

What is Reputation Management?

"Reputation Management is about creating influencer strategies that deepen understanding, build trust and mitigate risk."

STANDING PARTNERSHIP

Building a positive reputation doesn't happen by accident or by luck. It requires discipline, focus and more than an understanding of how the organization wants to be perceived—but how it is perceived. This is achieved by listening to key stakeholders (including an ongoing open dialogue with both internal and external stakeholders), identifying gaps and assessing risk.

Effective reputation management starts by having a clear vision, mission and values for the organization and ensuring the organization lives them. The board of directors, CEO and senior leadership must take responsibility for setting the strategic direction, based on the vision, and demonstrate to stakeholders what the company values.

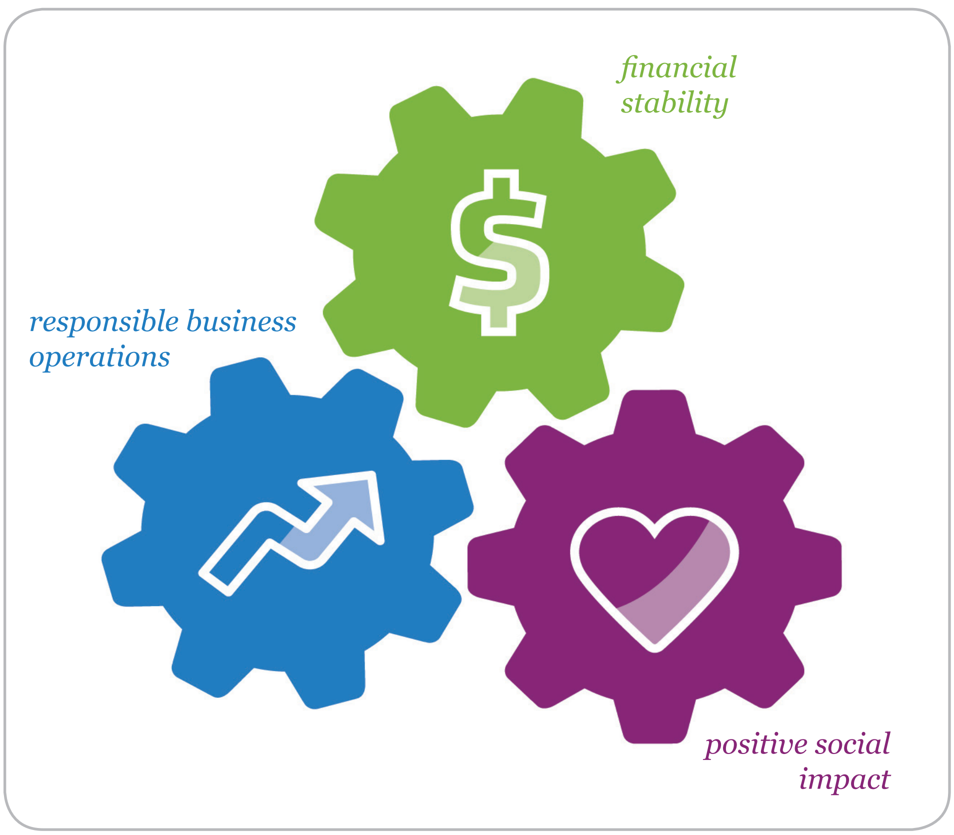
Too often reputation management is characterized as crisis management. These are not one in the same. Reputation rests at the intersection of three key areas of business strategy and governance that build trust when aligned:

- Responsible Business Operations translate into minimal negative impact and maximum positive impact. This includes areas such as environmental, health and safety, and human rights.
- Positive Social Impact ensures that a company's expertise and assets address social issues and support social well-being that engages the organization's communities.
- Financial Stability is the result of providing products and services that are both socially beneficial and economically profitable for the company and its stakeholders.

If any one of these three is out of alignment with the others, the risk of a reputational mishap rises significantly.

Take, for instance, Johnson & Johnson who, until recently, enjoyed a positive reputation for decades. Since 1943, the company has lived a creed that opens with "We believe our first responsibility is to the doctors, nurses and patients… and all others who use our products and services. In meeting their needs, everything we do must be of high quality." But, since September 2009, Johnson & Johnson has experienced a series of product recalls and other operational issues, which have eroded customer and investor confidence. Clearly its operations are not aligned with its values. The result, in January 2012 Johnson & Johnson landed on 24/7 Wall St.'s "The 10 Most Hated Companies in America" list. The following month, William Weldon, its CEO of 10 years, stepped down.

Certainly, organizational crises occur. And when they do, a well-thought-out, documented and rehearsed crisis plan can be the difference between simply surviving or thriving. Recognizing vulnerabilities and developing strategies



that address and mitigate them in advance is true reputation management. This approach can minimize damage and shorten the duration of a crisis.

Operationalizing Reputation Management

Unfortunately, organizations continue to struggle with how to manage reputational risks. Simply recognizing them isn't enough. So what do companies need to do? Centralize and create accountability for execution of the function, including:

- Articulate organizational values.
- Evaluate what's important to stakeholders.
- Assess how the organization performs.
- Inventory gaps (vulnerabilities).
- Build strategies to mitigate vulnerabilities.
- Monitor the change in beliefs and expectations.

Vulnerabilities exist within the supply chain, operations, the marketplace, internal culture, etc. As such, oversight has to be at the highest levels within an organization and be comprised of a cross-functional team who can create alignment with overall risk assessment.

A June 2009 article in The McKinsey Quarterly, "Rebuilding Corporate Reputations," agrees that companies must establish a multidisciplinary, cross-functional effort. The article further surmises that while the CEO has ultimate accountability for an organization's overall reputation strategy, a senior executive must own and oversee its execution.

Of course, this can be operationalized in a myriad of ways depending on organizational structure. Some organizations include reputation management in their Enterprise Risk Management system. Others turn to their internal audit departments for help, according to almost 80 percent of respondents to the 2012 EisnerAmper survey of directors.

Regardless of how an organization elects to manage reputational risk, it's clear it must be central, cross-functionally integrated and part of an overall risk management system.

Achieving a Good Reputation

"The way to gain a good reputation is to endeavor to be what you desire to appear."

SOCRATES

A stellar reputation is achieved when an organization consistently lives its purpose, its values are evident in all aspects of its operations, and it seeks to continually adapt based on meeting the needs—and expectations—of its multiple stakeholders. Sharing these stories with frequency and transparency builds credibility and trust.

When a crisis happens—and it will—an organization that operates in alignment with its values, is aware of risks and has strategies to mitigate those vulnerabilities will be in a position to draw on its positive goodwill and trust equity.

Reputations can be managed, but doing so requires diligence and integration into the overall operational and risk management structure. It requires governance and leadership to succeed.

Standing Partnership specializes in reputation management, creating influencer strategies that deepen understanding, build trust and mitigate risk in complex, ever-changing environments. The firm's comprehensive approach drives strategy and helps clients build, protect and restore reputations.

Melissa Lackey is Standing Partnership's President and CEO. Drawing upon her extensive business acumen, Melissa develops reputation management strategies for leading organizations in health care, education and other complex industries. In addition to serving as senior counsel to clients and account teams, Melissa is responsible for managing the day-to-day operations of the firm. Holding a master's degree in business administration and a bachelor's degree in journalism, Melissa has a strong command of both business and communications strategies.

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