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Understanding Reputation Risk

PART V: CASES & OVERVIEW

ANDREA BONIME-BLANC, JD/PH.D.
CEO AND FOUNDER OF GEC RISK ADVISORY

LEONARD J. PONZI, PH.D.
MANAGING PARTNER, REPUTATIONINC

"A reputation once broken may possibly be repaired, but the world will always keep their eyes on the spot where the crack was."

-- Joseph Hall, English Bishop

(1574-1656)

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INTRODUCTION

In this 5-part series on "Understanding Reputation Risk", we have sought to accomplish two main objectives:

1. Provide our readers with the first and most comprehensive understanding of a combined quantitative and qualitative approach to reputation risk analysis
2. Point to a solution for a better qualitative/quantitative (qual/quant) approach to this issue in the age of hyper-transparency and super-connectivity where companies and all forms of organization can better manage their reputation risk….and reputation opportunity

In this final Part 5, we provide a summary overview as well as a series of snapshots of real world cases of reputation risk and how a qualitative / quantitative approach might help an organization deal with this complex issue.

There are a multitude of cases at any given time of companies that may not have properly identified and/or managed their most important underlying risks and challenges in the marketplace. When that happens such underlying risks can blossom into bigger risks with additional and serious reputation risk implications and consequences for the company or organization layered on top of their existing core risks. This is the worst-case scenario for a company.

The better case scenario is for an organization to have a robust system of enterprise risk management, customized to its footprint, purpose, mission, needs, etc., and able to surface the principal and most important risks confronting it. When companies have such an effective system in place, they can then layer on the necessary reputation risk analysis that will enable them to:

1. Know who their high priority stakeholders are
2. Manage their key stakeholders' principal expectations
3. Manage the inevitable crises that may come in an effective manner that does not erode reputation or brand
4. Understand how to transform the experience (risk and crisis) into an opportunity for better business and even value creation

REPUTATION RISK: CASES AND SOLUTIONS

Below are several actual cases of reputation risk from companies around the world in which we provide a brief summary of the risk and illustrate how a qualitative/quantitative approach to reputation risk management would help the company overcome the challenge and even create an opportunity for value creation.

CASE 1:

STARBUCKS TAX REPUTATION RISK IN THE UK

The Facts:

- To avoid taxes in the UK, Starbucks allegedly used its coffee bean roasting plant based in the Netherlands to minimize profits for 7 years.
- The Starbucks roasting firm had been charging inordinately high prices for roasting and for knowledge transfers.
- Starbucks approached the Dutch government to test whether this practice was legal.
- An investigation by the European Chamber of Commerce into this practice (which included other companies like Fiat) found it illegal and Starbucks had to pay an additional £30 million in taxes.

The Qualitative Analysis

This case is an example of the possible downside effects of borderline or cutting edge practices. On the one hand, Starbucks undertook a practice that is widespread amongst international companies who would all probably consider the tax planning to be cutting edge and even aggressive but not over the edge (illegal).

However, such practices can also backfire in this age of hyper-transparency and the growing importance of other key global topics such as the growing role of income inequality, populism, and aversion to tax avoidance schemes, all of which could provide potential additional reputation risk to multinational companies who don't properly mind their tax risk exposure.

On the other hand, Starbucks, unlike many other companies, asked the relevant government agencies whether their practice was legal and in doing so demonstrated relatively good core tax risk management which undoubtedly helped them to ameliorate and lessen the potential for more extensive reputation risk associated with the underlying tax risk.

Net/net, while Starbucks acted aggressively for 7 years regarding this issue, they also demonstrated proactivity and sensitivity to the reputational risk consequences of the underlying tax risk and resolved their issues with minimal negative reputational effects.

CASE 2:

GSK BRIBERY REPUTATION RISK IN CHINA

The Facts

- Starting in 2007, GSK allegedly engaged in the bribery of government officials, hospitals and doctors in China.
- In June 2013, Chinese authorities began investigating GSK, laying bare a tale of intrigue involving a mysterious sex tape, whistle-blowers, private investigators and a culture of bribery and graft in China's vast medical industry.
- At first, GSK denied being involved in such practices. After public pressure and the revelation of additional details, the company admitted wrongdoing.
- In 2014, they were fined £300M and suspended prison sentences were meted out to several top managers.

The Qualitative Analysis

This is a case where a company, like many others that entered the Chinese market over the past two decades, may have had what appeared to be a sufficient global corporate compliance and anti-corruption program that satisfied, at least on paper, the requirements of the U.S. Foreign Corrupt Practices Act and other applicable extra-territorial anti-corruption laws under the OECD Anti-Bribery and Anti-Corruption Convention of 1997.

However, GSK and others during this period may not have anticipated another critically important corruption risk: that of the Chinese government enforcing its own national and local anti-corruption laws – something that didn't happen often if at all to multinationals doing business in China prior to the actions against GSK in 2013.

In this case, GSK (and we're sure other MNCs) missed another serious and important consideration in the global marketplace: the fact that nations that may not have enforced their existing national anti-corruption laws before may suddenly start to enforce them.

The key lesson learned from this case is that no global corporation or other form of organization like a university or NGO can do business around the world thinking that specific nations in which they are doing business will not enforce their own laws just because there has been lax or non-existent enforcement in the past. The reputation risk and other consequences can be dire, as the GSK case has demonstrated.

CASE 3:

BHP BILLITON OLYMPIC GAMES CORRUPTION REPUTATION RISK IN CHINA

The Facts

- At the 2008 Beijing Olympic Games, BHP hosted a number of government officials. The guests where mainly from Asia and Africa and were offered up to four days of hospitality at the event, which included tickets, a luxury hotel stay and excursions with a total value of between $12,000 and $16,000 per guest.
- In 2013, the US SEC investigated the case and fined the company a total of US$30 million. The company paid the fine without admitting any wrongdoing.

The Qualitative Analysis

These facts illustrate a very common corruption / bribery problem that most global companies face: where is the line between courtesy and non-corrupt business development activities or client service and the appearance and/or reality of bribery and corruption?

The 41 nations that have adopted extra-territorial anti-corruption laws pursuant to the OECD Anti-Bribery and Anti-Corruption Convention of 1997, have issued guidance or laws that provide parameters (some more than others) to help their companies understand when business development involving government officials becomes bribery. Lavish entertainment does not fit within any of these laws and guidelines and in fact is considered to be corrupt regardless of local practices including in some cases (like the UK Bribery Act) between two private parties. Companies know or should know better that, if they are caught, they will not only suffer the legal but also the reputational consequences of being considered bribers or corrupt by their stakeholders and the public in general.

CASE 4:

BARCLAYS INTEREST RATE MANIPULATION REPUTATION RISK IN LONDON/GLOBALLY

The Facts

- Dating back to 2005, Barclays (like a number of other banks) was found to have manipulated LIBOR (the London Inter-Bank Offered Rate) with the intention to fix the rate and hence gain higher profits from mortgage and loan trading.
- In 2007, employees internally cautioned management against these unethical practices. Nothing happened.
- In 2008, the Wall Street Journal revealed these practices in an investigative report.
- Barclays, as was the case with the other banks involved, continued to deny their involvement until 2012, when they were fined £290 million.

The Qualitative Analysis

This case provides a very clear illustration of "reputation risk contagion" a term coined in The Reputation Risk Handbook. The LIBOR cases more than anything else illustrate the power of the race to the bottom within a sector or industry. If one leading player is known to be at the cutting (unethical) or even bleeding (illegal) edge of a practice (in this case LIBOR rate manipulation), frequently other members of that sector catch on to that practice, in order to compete effectively (the argument goes), and then everyone indulges in the unethical or illegal practice. This is in effect what happened with the LIBOR cases.

Lessons learned? Companies and organizations generally need to mind their own store when it comes to risk management and have a clear concept of the key reputation risks that are associated with their primary risks in the marketplace. The slippery slope that reputation risk contagion encourages can lead companies that otherwise have decent risk management in place to dangerous zones where unethical or illegal activity might take place. Hence the great importance of including reputation risk analysis and assessments in an enterprise risk management program that not only understands the risks directly challenging the company itself but also the overall sector.

The Quantitative Analysis

In each case above, the company's corporate communications, marketing, legal, risk and crisis management functions would have benefited from a robust reputation risk management program enhanced with the quantitative inputs similar to the ones proposed in Parts 3 and 4 of this series.

In those two Parts 3 & 4, we outlined the importance of improving the **Risk Analysis** phase of any risk management process. We proposed that the results of these analyses be strengthened with independent and objective third party analyses and measures.

As described in Part 3, the first additional measure we suggest is to visualize the **Risk Register** through a **Risk Heat Map**. The **Risk Heat Map** is a 2-by-2 mapping of the risks. Its purpose is to visualize the potential impact of each risk event derived from answers to two key questions:

1. What is the perception of a **Reputation Risk Event** occurring?
2. If this **Reputation Risk Event** occurs, what is the resulting scale of the negative impact on the company's reputation and supportive or adverse behaviour by key stakeholders?

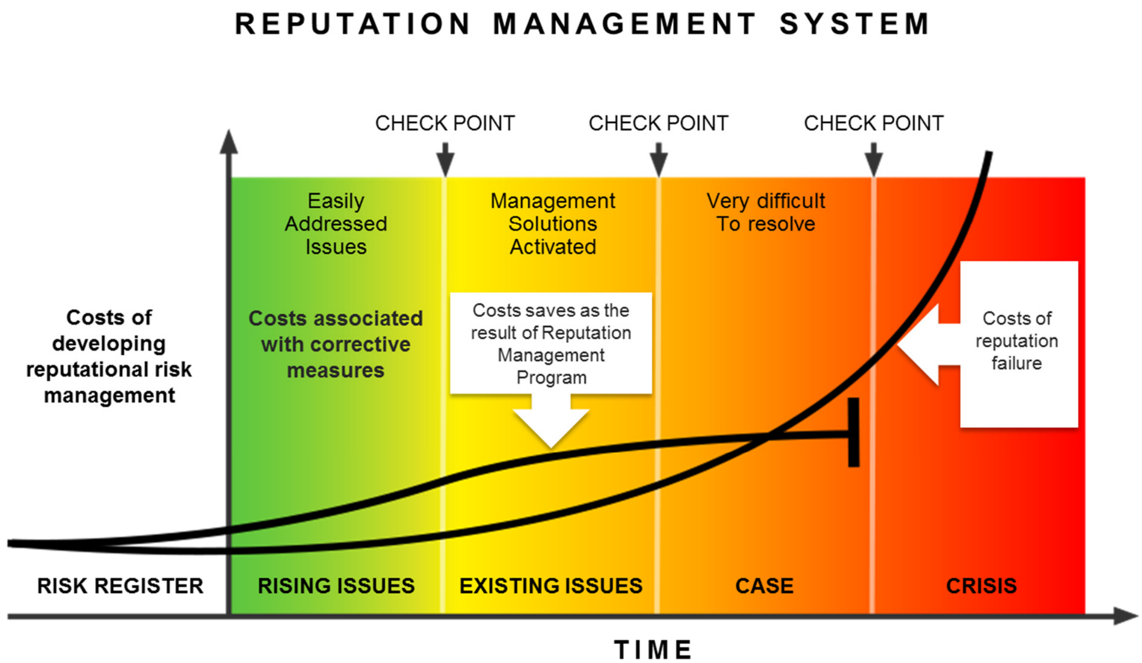
The key inputs of this analysis are:

- **Stakeholder Reputation Studies** – These research studies are based on a variety of stakeholder respondents that rate a company on customized reputation attributes. These attributes are then associated or mapped to specific risks. This approach has several advantages such as refiguring the associations to risks as they change or as new risks are added.
- **Media Studies** - A media-tracking tool is used to build the model in terms of the likelihood and impact of Reputation Risk Events.

In Part 4, we propose the second analysis that illuminates the dollar value of reputation as well as values that lead to specific event/risk planning. More specifically, this analysis addresses the following topics:

1. What is the **Total Value of Reputation Risk** to our company?
2. For each specific risk or event, what is the **reputation value at risk**?
3. What should be our **budget** for mitigating a risk?
4. What is the **ROI**?

It is our view that these additional analyses will allow reputation risk strategists to adopt better risk management parameters and curb the cost of managing reputation risk (see graphic below).



We also fully acknowledge that quantifying intangibles is the 'holy grail' and that our approach will also have its flaws - as every methodology has subjectivity.

What we are saying, however, is that because of the inherently complex, ever-changing and intangible nature of reputation risk, to be as highly effective as possible, both the "quant" and "qual" sides need to be robustly considered, combined, and applied.

CONCLUSION

In this five-part series on "Understanding Reputation Risk" we have attempted to convey a simple message about a complex problem:

> *Reputation risk will continue to be a core issue for global companies in the foreseeable future. While it is a difficult intangible topic to grasp in concrete terms and is not easily susceptible to scientific analysis, it is a subject that can be submitted to a rigorous quantitative/qualitative methodology combining the best of both worlds to provide a disciplined analysis and methodology and a practical set of recommendations and solutions.*

We have stated elsewhere in this series that our qual/quant approach to reputation risk analysis and recommendations is neither art nor science. Or perhaps stated more accurately – it is part art and part science. We believe that this era of hyper-transparency, super-connectivity, and the current and coming digital transformation of almost everything we do, requires that we apply the best of both worlds to this changeable, complex and ever-amorphous issue.

We look forward to engaging in a robust conversation on this important topic and assisting friends, colleagues and clients with solving their reputation risk challenges.

About the Authors & Their Firms

Dr. Andrea Bonime-Blanc
CEO & founder of GEC Risk Advisory

For more information, visit: https://gecrisk.com/
Andrea can be reached at abonimeblanc@gecrisk.com

Dr. Leonard J. Ponzi
Managing Partner at Reputation Inc

For more information, visit: www.Reputation-inc.com
Len can be reached at LJPonzi@Reputation-inc.com