

Supporting strategic success through enterprise-wide reputation risk management

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Abstract

Purpose – The purpose of this paper is to present a coherent and effective enterprise risk management (ERM) framework that includes necessary steps and processes for integrating reputation risk management into an organization's overall ERM approach which is intended to support corporate strategic success. In particular, reputation creation, enhancement, and protection are critical to an organization's success, yet highly challenging given the wide ranging and somewhat opaque nature of the concept. These qualities call for a strong ERM approach to reputation that is holistic and integrative, yet existing knowledge of how to do so is limited.

Design/methodology/approach – The paper evaluates and synthesizes existing reputation literature in developing an enterprise-wide reputation risk management framework incorporating necessary steps, processes, and considerations. We address risk strategy, risk assessment, risk governance, and risk culture as key elements of ERM and conclude with suggestions for future research.

Findings – The results suggest several important ideas which are of great relevance when integrating reputation risk management into an ERM framework. Among these are the importance of: identifying and understanding the purpose of key stakeholders, appreciating the multidimensional and layered effect of events on organizational reputation and monitoring the influence of technological advances.

Originality/value – The authors contribute to the literature by developing a framework for enterprise-wide reputation risk management that applies across industries. In contrast to previous work, the authors offer a broader perspective on the underlying causes and consequences of reputation damage based on empirical evidence and insight from the academic literature and provide additional detail in identification of reputation determinants, antecedents, and drivers. While much of this information exists in various places in the literature, it has not been organized into a cohesive framework nor used in developing an ERM strategy.

Keywords Corporate reputation, Reputation risk, Reputation risk management, Reputation risk response

Paper type Research paper



1. Introduction

Reputation broadly is considered at the core of organizational value, with one study estimating that reputation's asset value represents 22% of the S&P 500's total market capitalization (Decyk, 2015). The enormous effects of reputation-damaging events on firm value can also be seen when considering the experiences of BP (2010 oil spill) and

TEPCO (2011 Fukushima Daiichi nuclear power plant accident)[1]. Scott and Walsham (2005) further suggest that changing social norms combined with advanced communication technologies make reputation more fragile than ever, a notion supported by surveys of executives who list reputation as a top strategic business risk (Deloitte, 2014).

Academics have noted the relevance of reputation to corporate value. Numerous empirical studies suggest that investment in positive reputation creation (and maintenance through risk management) yields strong returns. In general, a good reputation, including investment in reputation building, serves as a signal regarding the quality of products and services offered. This is especially relevant against a background of information asymmetry (Shapiro, 1983; Klein and Leffler, 1981). Firms with a high reputation are further assumed to have potentially significant competitive advantages as compared to competitors with low reputation (Fombrun and Shanley, 1997), which is why it is also considered as a strategic intangible asset (Hall, 1992).

In particular, strong empirical evidence indicates that a positive corporate reputation positively affects stakeholder behavior. Especially important is the effect on customer behavior. Among the findings are that positive reputations imply a higher “willingness to pay” by customers (Graham and Bansal, 2007), positively impact spending and share of wallet (Walsh *et al.*, 2012) and generate purchase intention (Yoon *et al.*, 1993). They also positively affect customer loyalty (Walsh *et al.*, 2009, 2012), word of mouth (Walsh *et al.*, 2009) as well as trust and identification (Keh and Xie, 2007).

Similarly, suppliers are affected by a buyer’s positive reputation, often offering better contractual terms because of the impression of lower credit risk (Van den Bogaerd and Aerts, 2015). When investors perceive an organization positively, they often allow easier access to capital (Shane and Cable, 2002; Dollinger *et al.*, 1997) and lower financing costs along with more flexibility with respect to the type of financing instrument (Wang *et al.*, 2012). Firms with a better reputation also generally have an advantage in hiring employees, generating more job applicants as well as a higher quality of applicants (Turban and Cable, 2003).

In line with the positive effects of better reputations on stakeholder behavior, several studies demonstrate empirical evidence for a significant positive relationship between the level of reputation (over time) and firm performance using various measures of reputation and financial performance (McGuire *et al.*, 1990; Deephouse, 2000; Roberts and Dowling, 2002; Raithel and Schwaiger, 2015). Roberts and Dowling (2002) and Raithel and Schwaiger (2015) further observe that non-financial components of reputation may even contribute more to financial performance than do financial components.

Given the wide array of influences on reputation, the fact that many researchers from a wide range of fields have studied reputation is not surprising. Much of that research is focused on the definition and measurement of reputation, however, and much less on risks associated with reputation and their management (Gatzert *et al.*, 2015). A few exceptions exist, including an entire issue of the *Geneva Papers* devoted to insurer reputation risk exclusively, including Eccles and Vollbracht (2006) with focus on the relevance of strategic management communication based on empirically observed long-term media reputation, and Gaultier-Gaillard and Louisot (2006) with respect to definitions and drivers of reputation (risk). Others are similarly focused in perspective, such as considering the reputational effects of accounting restatements along with the

effect of reputation repair programs (Chakravarthy *et al.*, 2014), reputation as part of social responsibility (Hogan and Lodhia, 2011) and the relationship between reputation management and crisis management (Coombs, 2007; Kim *et al.*, 2011). Some focus on the strategic use of resources to create and protect reputation (Eccles *et al.*, 2007; Louisot, 2004), while still others focus on governance aspects including the role of the Board of Directors (Tonello, 2007) or how organizations can improve the value of their enterprise risk management (ERM) taking into account corporate reputation (Rogers *et al.*, 2010). The closest work to our paper is Regan (2008) who offers a broad reputation risk management approach.

In this paper, we contribute to the literature by presenting a framework for enterprise-wide reputation risk management that applies across industries, thereby addressing risk strategy, risk assessment, risk governance and risk culture as key elements of ERM. In contrast to previous work, we offer a broader perspective on the underlying causes and consequences of reputation damage based on empirical evidence and insight from the academic literature and provide additional detail in identification of reputation determinants, antecedents and drivers. While much of this information exists in various places in the literature, it has not been organized into a cohesive framework nor used in developing an ERM strategy. The framework is intended to support overall organizational strategic objectives through identification of successful methods to protect and support an organization's reputation.

To achieve this outcome, we begin with a discussion of ERM generally, and then follow with specific consideration of each element, focusing on reputation risk. Detail includes extensive consideration to important questions such as how to define and measure reputation and reputation damage, as well as reputation's determinants, antecedents and drivers. We follow with a presentation of an enterprise-wide reputation risk management including risk strategy, identification, assessment and response, as well as risk governance and risk culture based on an evaluation and synthesis of existing reputation literature. We conclude with consideration of the most relevant areas for future research in this field.

2. Reputation definition and fundamental ERM framework

2.1 Reputation definition, measurement and antecedents

2.1.1. *Reputation definition.* The definition of corporate reputation typically incorporates the concept of a multidimensional social construct involving the aggregate perceptions of a firm's stakeholders on financial and non-financial aspects of a firm (Fombrun, 1996). Fombrun and van Riel (1997, p. 10), for instance, define reputation as "a collective representation of a firm's past actions and results that describes the firm's ability to deliver valued outcomes to multiple stakeholders." Reputation can differ across stakeholder groups (Walker, 2010), where key stakeholders often include customers, suppliers, (potential) employees, and investors.

Conducting a meta-study of research published between 2000 and 2003, Barnett *et al.* (2006) define reputation as "observers' collective judgments of a corporation based on assessments of the financial, social, and environmental impacts attributed to the corporation over time" (p. 34). Reviewing literature published in heavily cited management journals from 1999 to 2008, Lange *et al.* (2011) conclude with a three-pronged conceptualization as: being known, being known for something and

generalized favorability. They note that most authors start with the notion first proposed by Fombrun (1996) that reputation “exists in the minds of beholders.”

Definitions of “reputation risk” incorporate implied definitions of reputation as well. For example, Solvency II and Basel III define reputation risk as the “loss in confidence in the integrity of the institution” (Solvency II definition, see CEA, 2007). Scott and Walsham (2005, p. 311) suggest a broader definition of reputation risk as “the potential that actions or events negatively associate an organization with consequences that affect aspects of what humans value” to take into account social, political and ethical aspects of relevance for “a wide range of stakeholders” and thus beyond shareholder value. In particular, reputation risk often results from other underlying risks such as operational risk events[2]. The focus of each tends to be on reputation generating from the perspective of various stakeholders.

2.1.2 Reputation measurement. Given the multiple definitions of reputation, it is not surprising that its measurement is equally varied. In general, the most appropriate measure depends on how reputation is being viewed. Measurement is affected as well by who is perceiving the reputation such as an investor, employee, customer, regulator, or other (Lange *et al.*, 2011). Several commonly-used reputation measures are listed in Clardy (2012), including surveys or questionnaires (in case of reputation as general knowledge or beliefs), external rankings (in case of reputation as evaluative judgment)[3], interviews (reputation as brand knowledge and beliefs, or as personality), as well as Tobin’s q, Goodwill, or Brand Equity (reputation as a financial (intangible) asset). Deephouse (2000) and Rindova *et al.* (2007) measure media reputation based on a content analysis of print media statements about the firm, including the extent of coverage, favorability of coverage, and content of coverage. Ultimately, the proper measurement technique will depend on the organization’s purpose and the situational context, including relevant stakeholders.

2.1.3 Reputation drivers and antecedents. In addition to understanding what reputation *is*, and some sense of methods to measure reputation, successful management of it also requires identification of drivers and/or antecedents through which reputation is developed (Rindova *et al.*, 2005, 2010) and which can contribute to reputation building and reputation repair (Rhee and Valdez, 2009). These drivers and/or antecedents, if adversely affected (or positively affected), will in turn harm (or enhance) the organization’s underlying reputation. In risk management terms, these may be considered “hazards”, which are conditions that make losses more likely and/or of larger value. Table I shows a list of selected determinants, antecedents and risk drivers of corporate reputation from the literature. Ultimately, these concepts of reputation definition, measurement, determinants, antecedents and drivers are key components to a successful ERM process.

2.2 Key elements of ERM

At its best, ERM manages risk across the entire organization in an integrated and holistic manner, considering interdependencies across risk situations. ERM is a critical support of the firm’s business strategy and is intended as a means to manage opportunities and risks in a coordinated process for purposes of increasing firm (and stakeholder) value[4].

When comparing various ERM frameworks and standards[5], one can derive that organizational ERM encompasses four key elements. They are: risk strategy, risk

Table I.
Selected
determinants,
antecedents and
drivers of reputation
from the literature

Determinants, antecedents, risk drivers	Reference/described in (e.g.)
<i>Determinants (Fombrun et al., 2000)</i>	
Financial performance	Fombrun et al. (2000), Roberts and Dowling (2002), Rhee and Valdez (2009, p. 151)
Emotional appeal	Fombrun et al. (2000)
Products and services	Fombrun et al. (2000)
Vision and leadership	Fombrun et al. (2000)
Workplace environment	Fombrun et al. (2000)
Social responsibility	Fombrun et al. (2000)
<i>Antecedents</i>	
High status affiliations (borrowing reputation from affiliates, distinguish from competitors); especially relevant for new firms	Rhee and Valdez (2009), Rindova et al. (2005, 2010), Lange et al. (2011, pp. 180f)
Media (as an information medium, network approach and reputation endorser)	Scott and Walsham (2005, p. 309), Rhee and Valdez (2009, p. 151, 153)
Rankings/certifications from institutional intermediaries (as an information medium, network approach)	Rhee and Valdez (2009, p. 153), Rindova et al. (2005)
Firm characteristics [institutional ownership, advertising intensity and diversification, specialization, organizational age, longevity and past performance, (complexity of) firm's market action profile, corporate culture and identity]	Rhee and Valdez (2009, p. 151, 152f), Lange et al. (2011, p. 177), Basdeo et al. (2006), Fombrun and van Riel (1997, p. 8)
Reputation spillover ("reputation commons" problem; spillover within and across sectors)	King et al. (2002), Cummins et al. (2011)
Congruence between reputation claims and context	Scott and Walsham (2005, p. 312)
<i>Risk drivers</i>	
Internal risk drivers (corporate governance, human rights, human resources, community involvement, environment and business behavior)	Scandizzo (2011)
External risk drivers (project, counterparty, country and sector risks)	Scandizzo (2011)
Changes in technology and social norms	Scott and Walsham (2005), Eccles et al. (2007)
Reputation-reality gap	Eccles et al. (2007)

assessment, risk governance and risk culture. These are discussed in detail below, with a focus on integrating reputation risk management as depicted in Figure 1. In this context, we note that a Canadian survey by Rogers et al. (2010, p. ii) shows that firms on average need "more than five-and-a-half years of ERM experience before exploring ways to integrate the management of corporate reputation into the ERM process".

Reputation risk is considered a "risk of risks", meaning that it generates from other sources of variability. A successful ERM process, therefore, manages reputation risk effectively, and a successful process to manage reputation risk will be an effective ERM effort. In addition, managing corporate reputation can generate substantial value for firms by positively influencing various stakeholder groups as described in the

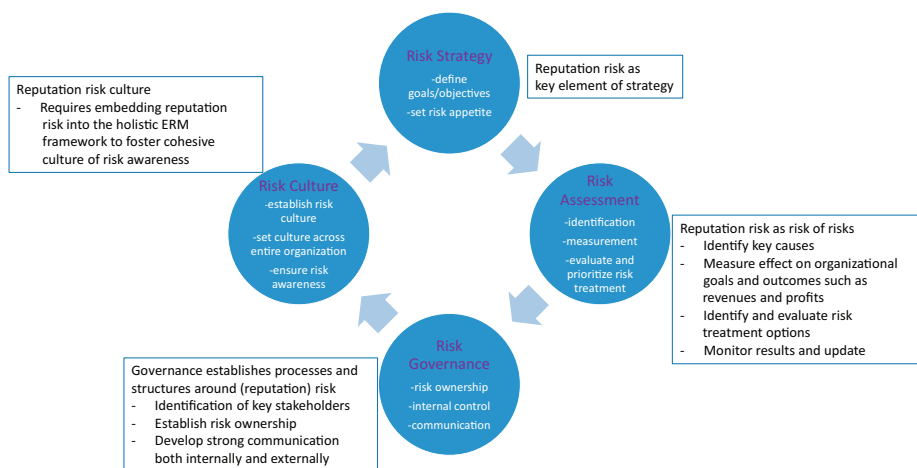


Figure 1.
Embedding
reputation risk into
an ERM framework

introduction, which is exactly in line with the goals of ERM. Conversely, a not well-managed reputation can induce costs for firms, including from redundant or inconsistent risk identification and risk management processes (Tonello, 2007; Regan, 2008).

Tonello (2007, p. 23f) further raises the question whether reputation risk should be treated separately from other business risks. He cites a survey where 55 per cent of the participants responded that it should be considered as a “failure to manage other risks effectively” and should thus not be managed separately. We note as well that the few insurance policies providing protection against reputation events tend to require the occurrence of an underlying loss (Gatzert *et al.*, 2015).

3. Integrating reputation risk management in a holistic ERM framework

3.1 Risk strategy

The purpose of any unit or activity within an organization is to support the organization’s overall strategic objectives, where ERM is a critical element. In defining the activities and procedures for ERM, therefore, coordination and alignment with the organization’s objectives is imperative (Rogers *et al.*, 2010). One important step is to *identify* the set of key stakeholders that are vital for achieving the company’s long-term strategic goals and objectives (Tonello, 2007; COSO, 2004). In this regard, Lange *et al.* (2011, p. 165) point out that the identification of an organization’s key stakeholders is generally highly complex (Mitchell *et al.*, 1997).

To define the organization’s risk appetite in regard to reputation requires defining how to measure reputation and reputation risk, e.g. by examining the impact of a changing stakeholder behavior on a chosen financial performance measure (Regan, 2008). Based on their characteristics, objectives and experiences, organizations may choose to accept quite different levels and types of risk; therefore, evaluation of risk management options must be made based on the defined risk appetite.

All of these elements associated with risk strategy requires the involvement of the Board of Directors as well as a strong communication plan to ensure support of

the defined strategy throughout the organization (Regan, 2008; Tonello, 2007), which is also of high relevance when implementing risk culture.

3.2 Risk assessment

Risk assessment encompasses risk identification, measurement, evaluation/response and monitoring. The intention is to have a full sense of the organization's exposures to risk, the opportunities and challenges posed by those risks and sufficient detail regarding risk dimensions and dependencies to evaluate possible risk response solutions.

3.2.1 Risk identification. A risk source not identified is one managed well only by accident. A rigorous, extensive and thoughtful identification process, therefore, is crucial to an organization's success.

Specifically, the organization ought to identify exposures, perils and hazards. An exposure is what can be lost, the peril is the cause of loss, and hazards are conditions that make loss more likely and/or larger. Gatzert *et al.* (2015) describe these elements within a reputation risk situation with focus on reputation-damaging events. In this case, the "crisis event" is the peril causing loss, while reputation is the exposure, and the financial effect of a damaged reputation is the measurement of loss. Successful reputation risk management requires identification of potential crisis events taking into account that reputation risk is a risk of risks, their financial implications and the factors that affect their occurrence and effect, especially in regard to the impact of events on the behavior of the firm's key stakeholders as identified in the risk strategy definition step (see previous subsection).

As a risk of risks, reputation risk identification is a multistep process: First is to assess reputation-relevant underlying business risks and understand how these underlying risks may affect reputation, i.e. the perceptions of stakeholders. In this regard, it is also vital to understand the possible ways in which such reputation-damaging events affect stakeholder outcomes and ultimately stakeholder behavior, thus causing a financial loss for the firm, e.g. due to lost revenues or higher costs of capital. The intention ultimately is to ensure that these underlying risks are managed effectively. As Regan (2008) indicates, a thorough risk identification process also requires a team at all levels of the company with sufficient knowledge about the company and the environmental conditions.

In particular, Regan (2008, p. 191) suggests interviews with internal and external experts, brainstorming sessions or event inventories to identify reputation relevant underlying risks. These activities need to consider not only risks present within the organization (market and credit risks, underwriting/insurance risks and operational risks) but also risks that may arise from outside the firm due to reputational spillover effects within and across the industry (Cummins *et al.*, 2011) for an empirical analysis in the financial services industry, or due to misconduct by business/trading partners (Regan, 2008).

An overview of selected empirical evidence in the event study literature regarding reputational crisis events that can significantly affect financial performance as well as trigger events (perils) often used in reputation insurance policies is provided in Table II, and we refer to Gatzert (2015) for a more comprehensive review of this literature.

Of the existing empirical studies, we note that quite a few have focused on the influence of operational risk events on financial reputational losses in the sense of

Underlying risk/crisis event with impact on ...	Empirical evidence/reference in ...
... <i>financial performance (non-financial industry)</i>	
Fraudulent earnings restatements	Palmrose <i>et al.</i> (2004)
Allegations of illegal activities	Murphy <i>et al.</i> (2009), Alexander (1999)
Criminal fraud charges	Karpoff and Lott (1993)
Corporate illegalities	Davidson and Worrell (1988), Reichert <i>et al.</i> (1996)
Military (defense) procurement fraud	Karpoff <i>et al.</i> (1999)
Environmental violations	Karpoff <i>et al.</i> (2005)
Financial misrepresentation	Karpoff <i>et al.</i> (2008)
Public disclosure of allegations of price-fixing	Skantz <i>et al.</i> (1990)
Legal disputes	Bhagat <i>et al.</i> (1998)
Unethical business behavior	Long and Rao (1995)
Technical and product failures	Rubin <i>et al.</i> (1988), Borenstein and Zimmerman (1988), Mitchell and Maloney (1989)
... <i>financial performance (financial industry)</i>	
Operational risks (especially fraud); effect depends on type of firm, firm characteristics, sequence of triggering events and timing of market reaction	Perry and de Fontnouvelle (2005), Cummins <i>et al.</i> (2006), Gillet <i>et al.</i> (2010), Biell and Muller (2013), Sturm (2013), Fiordelisi <i>et al.</i> (2013, 2014) Cummins <i>et al.</i> (2011)
Operational risk implying inter- and intra-sector spillover effects (banks and insurers)	
... <i>corporate reputation</i>	
Layoffs	Flanagan and O'Shaughnessy (2005) Love and Kraatz (2009)
Downsizing (conflicting signals to stakeholders: potentially positive for shareholders, negative for (potential) employees or customers)	
Corporate crime	Williams and Barrett (2000)
<i>Exemplary trigger events (perils) used in reputation insurance policies (e.g. Munich Re)</i>	Gatzert <i>et al.</i> (2015)
Product recall	
Discrimination or harassment of clients or employees	
Breach of data privacy	
Loss of key persons	
Misconduct of key persons	
Breach of UN global compact principles No. 3, 4, 5, 6 (<i>labor</i>) and 10 (<i>anti-corruption</i>)	

Table II.
Selected underlying causes with potential impact on corporate reputation and financial performance: insight from the event study literature

market value losses. Some of this research has been done in the financial services sector, given the regulatory requirements to identify, report and assess a variety of risk sources, including reputational risk sources. In general, a positive association between the occurrence of operational risk events and financial reputation loss is found. Most

consistently found is the positive association with fraud-related events. Outside of the financial services sector, studies have shown a negative market impact of a variety of events/behaviors, which also include fraudulent and criminal activities, unethical behavior, legal disputes as well as product failures (see [Table II](#)). In addition, regarding the impact of reputation-damaging events on corporate reputation, the empirical literature should be taken into account as well when assessing risks for the respective firm. See also Section 1 for a short overview of empirical evidence regarding the consequences regarding stakeholder behavior and financial performance for firms with strong (or weak) corporate reputation, and [Gatzert \(2015\)](#) for a review of the respective empirical literature on stakeholder behavior.

If we stop at the list above, however, we miss the opportunity to identify new sources of risk. That is, successful risk management requires anticipation of events that have not yet happened and that is active rather than reactive. [Scott and Walsham \(2005\)](#) in particular highlight the combined effects of continuously changing social norms with technological advances in communication capabilities as requiring anticipation of what could happen based on new conditions.

To identify the specific reasons for losses in reputation and/or financial reputational losses, an analysis of the effect of reputation-damaging events on various adverse behavioral changes of different stakeholder groups is vital[6]. For instance, customers may switch to a competitor implying a reduction in revenues, suppliers or business partners require higher contracting costs due to an increasing monitoring effort, employees may leave the company or are less motivated, investors increase their costs of capital due to a reassessment of the firm's business risks or regulators impose an investigation along with sanctions or require a reorganization, thus implying additional costs as well ([Cummins et al., 2006](#)).

3.2.2 Risk measurement. In line with the risk identification process, the measurement or assessment of reputation risks starts with an evaluation of the underlying risk sources. Most often, reputational losses result from operational or strategic loss events (see previous subsection), which often are difficult to quantify due to a lack of historical data. In these cases, qualitative approaches such as risk workshops and the derivation of risk maps may be used based on likelihood and severity assessments ([Regan, 2008](#), p. 192). In general, however, a holistic approach is needed when quantitatively and/or qualitatively assessing the underlying risks (financial, underwriting, hazard and operational risks) by taking into account potential reputational damages, e.g. done by the risk owners, given that the underlying risk event occurs.

Typically the triggering event is reported in the media; otherwise, stakeholders are unlikely to be aware of the event and therefore will not alter their perceptions. One element of risk quantification, as a result, is to assess the likelihood of negative publicity from various potential events. [Tonello \(2007, pp. 32-33\)](#) states specifically that the probability that an event breaks the news in the first place is increased if:

[...] management does not meet public expectations in terms of ethical standards (risk of fraud), the board's oversight is ineffective (governance risk), or the company does not avail itself of a thorough compliance program (compliance risk).

Furthermore, once negative publicity does occur, the actual effect of that publicity on corporate reputation and thus the perception of stakeholders may depend on various factors. For example, [Love and Kraatz \(2009\)](#) find that prior reputation serves as a

moderating factor in that firms with a stronger reputation suffer less reputation damage after a downsizing. Other empirical work show that firm size and organizational age strongly affect the impact of a reputation event (Flanagan and O'Shaughnessy, 2005). Eccles *et al.* (2007) further describe the reputation-reality gap, changing beliefs and expectations, as well as weak internal coordination as factors impacting the level of reputation risks.

Financial losses in case of a reputation-damaging event typically have been measured in the event study literature as the difference between the resulting market value loss (requiring consideration of listed companies) and the original loss. Other financial measures include a loss of revenue, operating margins or market share, all of which allow consideration of instances beyond just that of stock listed corporations.

An interesting item to note regarding this approach to measurement of reputation losses is that it does not measure directly the effect on stakeholder perceptions, which is how most commentators refer to the notion of reputation. More research is needed to understand the relationship between perceptions and behaviors across various stakeholders and then further to understand the relationship between those perceptions and organizational outcomes (Gatzert, 2015). For instance, while a particular event might not have an immediate effect on profit, it might form the basis for future changes in perceptions that could have devastating effects on the organization's long-term results.

A damaged reputation, however, does not necessarily result in actual financial loss. After the trigger event happens, response and communication are vital (Chakravarthy *et al.*, 2014), including a firm's social media capabilities (Lee *et al.*, 2015). Furthermore, insufficient risk prevention measures, e.g. insufficient internal controls, operational risk management, crisis communication strategy, can amplify the likelihood and/or severity of reputational losses. Moderating factors may further impact the extent of the financial loss after a crisis event. For instance, Rhee and Haunschild (2006) find that organizations with stronger prior reputations experience greater financial reputation losses upon the reporting of relevant events (product recall). They actually receive more media attention when those events occur as well, likely contributing to the larger negative effect of the event itself. On the other hand and as described above in case of reputational effects, market analysts and consumers may resist changes in reputation ordering because the ordering is collectively regarded as appropriate. Highly reputed firms, therefore, may be more resilient to the revelation of product defects (Pfarrer *et al.*, 2010). Reputational effects are also moderated by substitutability and generalism or specialism, as Rhee and Haunschild (2006) show that "having few substitutes with an equivalent level of reputation, or a focused product identity stemming from specialism, buffers the negative market reactions to product recalls". Furthermore, antecedents and risk drivers such as changing norms and technological progress can impact reputation.

If there is a financial effect, however, it can lead to a downward spiral. The loss of resources will dampen the organization's ability to undertake its strategic initiatives; furthermore, lower resources are themselves taken as a sign of poor quality, thereby affecting reputation negatively (Fombrun and Shanley, 1990; Roberts and Dowling, 2002).

3.2.3 Risk response. Following measurement of possible reputation risk outcomes, incorporating not only likelihood and severity but also the influence of moderating risk management techniques, decisions about risk treatment must be made.

Risk avoidance is the complete elimination of potential harm. Achieving avoidance, therefore, requires giving up potential benefits as well as harms, and as a result is a “last resort”. *Risk mitigation* measures are intended to achieve a risk reduction in terms of likelihood and/or severity of reputation risk, whereby one can distinguish between preventive measures before and after the occurrence of a reputation-damaging event. If during the risk assessment process, the firm found that a certain business risk can result in severe reputational (and financial) damage, the risk response strategy and designated preventive measures for this business risk should be adjusted or extended accordingly. Furthermore, most literature that addresses reputation suggests that communication strategies affect reputation considerably, contributing to the reduction of the likelihood and severity of the reputational damage (see also the previous subsection). The young field of reputation risk insurance has taken this route as well, focusing on providing support for a “crisis communications” strategy, both before and after an event is known to the public (Gatzert *et al.*, 2015). Industry studies also highlight the value of a well-planned and robust communications plan in limiting reputation event losses (Aon, 2012).

In this context, Coombs (2007) presents the application of situational crisis communication theory as a framework to help managers protect reputation by anticipating stakeholder reactions to crisis events as well as responses to crisis strategies, presenting guidelines for crisis communication strategies based on results from evidence-based research. Coombs (2007) emphasizes that the first priority and ethical responsibility of firms in case of a crisis is “to protect stakeholders from harm, not protect the reputation”, especially in case of physical dangers such as contaminated food (p. 165). The type of crisis event and the framing in the media as controlled by the firm’s crisis manager plays an important role for the reputation threat. He points out three clusters:

- (1) the victim cluster where the firm is viewed as a victim of the event (natural disasters, workplace violence, product tampering and rumor);
- (2) the accidental cluster where the event is unintentional or uncontrollable for the firm (technical-error accident, technical-error product harm and challenge); and
- (3) the preventable/intentional cluster, where the firm caused the event purposeful (human-error accident, human-error product harm, organizational misdeed and violation of law) (p. 167).

Of relevance is also the firm’s crisis history (signal for ongoing problems) and unfavorable prior reputation, which may intensify a reputational threat.

The crisis response plan, therefore, should involve a plan to address different stakeholder groups as well as the media (Rogers *et al.*, 2010, p. 15). In this regard, Chakravarthy *et al.* (2014) conduct an empirical study based on 94 US firms’ press releases one month before and after a serious accounting restatement/intentional misreporting and identify 1,765 reputation building activities. Types of actions identified in the literature in regard to investors include improving governance, firing senior leadership, improving incentive or internal control systems, reorganizing the firm

and repurchasing stock. In regard to customers, the authors name major new advertising campaigns, rebranding and “external validation of product quality via third-party awards or certifications”, and with respect to employees the firm’s offer of “ethics training or mentoring programs to help prevent employee turnover and to reinforce the firms’ commitment to integrity”, as well as “improving benefits programs and investing in winning ‘best employer’ awards” (p. 1338). Based on these activities, the authors find a significant increase in reputation building activities after a serious restatement and that reputation repair strategies indeed address multiple stakeholder groups that depend on firm characteristics:

- firms that sell durable products target customers;
- firms with organized or highly skilled workers target employees; and
- firms operating in many locations undertake more community-focused actions (p. 1331).

They further show to what extent value can be derived from reputations with the respective stakeholder group and that these stakeholder-oriented strategies have a positive effect on abnormal market returns. With respect to further reputation repair strategies, we refer to [Rhee and Valdez \(2009\)](#), who point out that the level of difficulty of the reputation repair process is also affected by antecedents of reputation (see Section 2.1.3).

Apart from risk mitigation, *risk transfer* instruments have recently become available by means of new reputation risk insurance policies. Most of the very few policies, however, only provide coverage for preventive and crisis communication measures, while coverage of actual financial losses in terms of lost revenue is scarce. We refer to [Gatzert et al. \(2015\)](#) for a comprehensive presentation and analysis of reputation insurance policies. Finally, the firm may decide to *accept* reputation risks and to retain certain risks depending on their relevance and materiality for the firm and the costs of risk transfer techniques ([Eccles et al., 2007](#)).

3.2.4 Risk monitoring. As a last and important step in the risk assessment process, regular and proactive risk monitoring and updating of risk identification and assessment are highly relevant, especially due to a rapidly changing environment and its impact on new forms of reputation risk, whereby observed deviations should be reported within the firm. This final step may be even more relevant for reputation risks than other risks because of the rapidly changing landscape and the influence of social media on organizational reputation.

3.3 Risk governance

Risk governance refers to the establishment of risk organization, processes and structures within the organization that allows an adequate risk strategy, risk assessment and risk treatment, including a strong compliance function, internal audit, as well as a business continuity management plan. This also encompasses processes that support the identification of key stakeholders who are critical for the firm to achieve long-term strategic goals ([Tonello, 2007](#), p. 27). Of high relevance in reputation risk management is to keep an integrated perspective that takes into account risks across the entire enterprise without being segmented from other risks and processes, which is the case if a firm decides not to manage reputation risks separately from other business risks ([Tonello, 2007](#)). Furthermore, independent internal risk controls and internal audit

have to be established to evaluate the quality of risk identification, analysis and valuation processes.

In addition, risk governance comprises a clear definition of risk management principles as well as roles and responsibilities, i.e. the process of determining who are the “risk owners”. Given the organization-wide nature of reputation risk, the individuals given responsibility for managing it ought to have broad organizational experience, perspectives and authority. Moreover, [Eccles et al. \(2007\)](#) suggest that the firm appoints one person to be responsible for overall management of reputation risks, such as a chief reputation officer (alternatively the COO, CFO or CRO), who should have sufficient control, credibility and resources, and whose position is not in conflict with his or her own work, e.g. heads of marketing, corporate communication. This appointed person is responsible for building and defending corporate reputation, for crisis and post scandal management, to define strategies that reduce damages to reputation and simplify reputation repair activities ([Rhee and Valdez, 2009](#)), especially regarding prompt and effective communications within the firm (reporting to the board) and public relations ([Tonello, 2007](#)), and who accounts for the interaction between reputation and communication.

In general, internal and external risk communication is vital, especially an effective communication and response strategy to any business risk with a potential of causing reputational damage. For example, the internal reporting system should ensure that all material risks regarding reputation risks, along with the results of a potential reputation risk mitigation process, are communicated not just to the Board but throughout the entire organization ([Regan, 2008](#)). Vice versa, [Rogers et al. \(2010, p. 5\)](#) also point out that “organizations need to focus more on communicating the role of ERM in protecting corporate reputation to their employees.”

Regarding external crisis communication and the establishment of a response system, [Regan \(2008\)](#) suggests that the firm appoint a specific spokesperson responsible for all communication. This person addresses the media as well as the various affected stakeholders in a timely, truthful and open manner. As [Rhee and Valdez \(2009, p. 165\)](#) emphasize, the:

[...] adoption of legitimate formal policy, such as a compensation system for error-related performance, can serve as a tangible buttress for verbal communication to meet shareholders’ greater demand for managerial accountability for reputation-damaging events.

3.4 Risk culture

As part of the corporate culture, a strong risk culture ensures general risk awareness and accountability for integrity in daily operations throughout the entire organization, thus improving decision-making by “considering risk and reward on an informed basis” ([Brooks, 2010, p. 87](#)). From the board level to senior management to each individual employed within the organization, roles and responsibilities ought to be defined, along with organizational norms and rules. In particular, risk culture includes all aspects of how corporate culture affects risk management, thereby constituting the basis on which risks are identified, analyzed and controlled[7]. Risk culture should be supported and actively lived by senior management, and a strong internal communication mechanism

should be in place to ensure effective decision-making among the Board as well as full awareness throughout the organization. Furthermore, the COSO (2004) framework suggests that a common language of risks is essential for a risk culture and gives hints regarding implementation, such as incentives (Brooks, 2010).

In support of strong risk awareness across the enterprise regarding reputation and reputation risk, many organizations are considering education and training to make employees aware of changing social norms and to sensitize them toward newly evolving risks. These programs also provide input regarding processes to report risks and concerns, as well as return information about the results of management's actions in response to such reports.

According to Tonello (2007, p. 9), the failure to embed reputation risk in a holistic ERM framework might hamper the firm's ability to "foster a cohesive culture of risk awareness". Given the fundamental goal of strategic alignment as well as effective coordination, creation of an organization-wide risk culture is considered paramount to successfully creating value through ERM (Brooks, 2010).

4. Summary and implications

Our purpose with this research is to present a coherent and effective ERM framework that includes necessary steps and processes for integrating reputation risk management into an organization's overall ERM approach, which is intended to support corporate strategic success. The framework takes into account current knowledge from the existing literature on the definition and measurement of reputation and reputation risk as well as reputation's determinants, antecedents and drivers, as well as effective methods to respond to reputation-damaging events. Our results suggest several important ideas which are of great relevance when integrating reputation risk management into an ERM framework. Among these are the importance of:

- identifying and understanding the purpose of key stakeholders;
- appreciating the multidimensional and layered effect of events on organizational reputation; and
- monitoring the influence of technological advances which allow for incredibly rapid distribution of perceptions to millions of others, whether accurate or not.

This is highly relevant as reputation is a social construct, and social norms are apt to change more rapidly in an era of widespread technological connections.

Future research, therefore, ought to focus on the specific influence of social media when developing effective risk management techniques. So far, only first steps have been undertaken in the literature and without focus on risk management purposes [Lee *et al.* (2015) in the context of consumer product recalls]. At a more fundamental level, research is needed on the general effectiveness of various risk management techniques, including the specific situations (pre and post the event) in which they are most effective. Part of that research ought to focus on reputation loss measurement and prediction, both of which currently limit the availability of insurance.

An organization's reputation has always been valuable. What is new today is its vulnerability due to technological advancement in communication combined with changing norms. Those same conditions which increase risk, however, may also provide opportunities to protect and enhance reputation. An effective communication strategy,

strong governance and expansive risk culture can protect and enhance an organization's reputation. ERM is the framework to generate these results.

Notes

1. BP is said to have lost 50% of its market value, while TEPCO lost 80% (Aon, 2012).
2. This is also one reason why the reputation risk policy by Allianz insures risks (crisis events) that are covered by other insurance policies, which also ensures that the risk is well defined (Gatzert *et al.*, 2015).
3. External rankings typically exhibit further limitations due to an overweighing of financial aspects, among other aspects (Fombrun and Shanley, 1990), and due to its public availability, the construction may influence the ranking, which is why representative surveys are more recommendable (Lange *et al.*, 2011).
4. Grace *et al.* (2015) demonstrate that ERM adds to an organization's cost and revenue efficiency; see Gatzert and Martin (2015) for a survey of the empirical literature that shows that ERM generally has a (significant) positive impact on firm value.
5. See, for example, KPMG (2001); FERMA (2002); COSO (2004) and ISO (2009).
6. In this context, firms should also distinguish between financial and non-financial components of reputation, which can have a different impact on financial performance (Roberts and Dowling, 2002) due to different effects on different stakeholder groups.
7. See Zeier (2014) for a review of the literature with special emphasis on the insurance context.

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