Corporate reputation:
perspectives of measuring and managing a principal risk
Most of us would agree that reputation matters – it can explain why customers choose your product or service in preference to somebody else’s and can make the difference between success and failure.

But it is arguable that there are few issues that are quite so challenging to manage as reputation. Consider the following:

• A well-deserved reputation that has been diligently built up over many years can be damaged beyond repair in a day by circumstances that are relatively insignificant when seen against the overall picture. Think of businessmen and politicians whose reputations founder on issues related to their personal rather than professional lives.

• A good reputation can, perversely, be built on ‘bad boy behaviour’ or notoriety.

• Although a company’s reputation may be harmed by adversity, it may emerge from the episode with its reputation enhanced – simply due to the way it handled the situation. On the other hand, an organisation can squander golden opportunities for building reputation through inept management.

Added to such challenges is the fact that there are no hiding places any more. The internet, blogs and mobile technology have made it possible for anybody to broadcast information to large audiences in a very short space of time. The media of course plays a powerful role in the making and breaking of reputations.

Furthermore, the ever-increasing shift towards greater corporate accountability and transparency through enhanced narrative reporting means that organisations need to understand and report on all those issues that have a significant bearing on their future prospects and their risk profiles. We would argue that reputation is one such key issue.

However difficult, it is important for organisations of all sizes and sectors to be aware of the importance of reputation and the attendant risks. Simply put, a good reputation can:

• help the organisation to optimise shareholder value by enabling it to attract customers and high quality staff

• enhance the business in good times and protect it during the bad ones.

Reputation is a major risk issue for all organisations and needs to be considered alongside all the other major risks such as operational, strategic and financial risks. What this means is that organisations need to mitigate against the effect of loss of reputation, but they also need to be looking for the upside opportunities to enhance their reputations.

Against such a background, CIMA has commissioned this Executive Report to explore various perspectives on corporate reputation. It has been prepared by Dr Arlo Brady and Garry Honey, two leading experts on corporate reputation. Their approach was to interview a number of key industry players to obtain insights from a range of perspectives such as governance, legal, human resources and the public sector. The interviewees represent some of the stakeholders that chief financial officers should be aware of and may even have to engage with. This report gives some of their views on reputation and how they believe the risk to reputation should be managed and reported on. It should provide a tool to help members in business work with these different stakeholders. Profiles of the authors and interviewees can be found in Appendices 2 and 3.

The report is in two key parts. Each part is supplemented by insights from the interviewees together with a number of case studies.
Part 1 explores reputation in terms of ten different aspects:
- perceptions of control
- quality
- stakeholders
- reputation versus brand
- reputation as an asset
- the value of reputation
- reporting on reputation
- ownership
- trust
- damage.

From these, the report identifies the following principal findings:
- Organisations have no direct control over stakeholders’ perceptions, but they can influence them.
- The quality of reputation must be monitored across all stakeholders. Organisations must look for opportunities for positive news especially in the midst of adverse situations.
- Organisations must understand who their stakeholders are and what impact they have on the organisation.
- Reputation and brand are not the same thing.
- Reputation should be seen as an asset to the organisation.
- It is difficult to value reputation in monetary terms.
- Reputation should be covered in narrative reports. It is best dealt within the risk section as ‘reputation risk’.
- It is important to assign ownership for reputation – the board has prime responsibility for the organisation’s reputation.
- Reputation is ultimately a measure of trust.
- The extent of damage to reputation caused by an event will depend on how easily trust can be recovered. This will depend on the prior state of reputation, the nature of the threat and the way that the situation is handled.

Part 2 looks at reputation risk in more detail. A risk to reputation occurs where the organisation fails to meet the expectations of a specific group. The key to effective reputation risk management is therefore the management of expectations.

The report explores:
- how reputation risk relates to the organisation’s risk appetite
- causes of reputation risk
- effects of reputation damage
- identification of reputation risk
- measurement of reputation risk
- management of reputation risk
- reporting of reputation risk.

A key finding is that organisations do not identify reputation risk specifically as a risk. Nor do they assign responsibility to a dedicated individual to manage the risk. Organisations tend to claim that reputation risk is covered adequately through existing operational and strategic risk reporting procedures. However, notwithstanding this, it remains important to devote dedicated attention to protecting and enhancing reputation. Most interviewees agreed that reputation risk represents a principal risk that needs to be included in narrative reports such as the Business Review, Directors’ Report of the Companies Act 2006.

The report concludes with an overview of possible future trends with suggestions for further reading.
Although the report suggests some possible approaches to identifying and managing reputation risk, including reputation measurement models, its main focus is to understand and explore the key issues surrounding reputation to stimulate discussion and debate. CIMA hopes that this will make a meaningful contribution towards the development of good practice principles in terms of reputation risk management.

As a starting point, CIMA believes that the significance of reputation is such that it should receive dedicated and specific attention by an organisation’s board and management despite the challenges associated with identifying and measuring the risks related to it. It is only by shining such a spotlight on the subject and assigning responsibility for it within the organisation that progress towards commonly agreed principles is likely to be made.

The next challenge will be to put a value against reputation risk. This would identify reputation as a value at risk and would show that reputation risk is a topic that management accountants should be concentrating on.

We would very much welcome your comments and feedback on this report. We would also be interested in hearing about your experiences and challenges of managing your corporate reputation.

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Reputation is a word much used today. Pick up a newspaper and turn to the business, sport or travel section and you will find the word reputation in relation to a person, organisation or place. Many use the word casually with little regard for its meaning especially in the context of our celebrity-fixated culture where diary or gossip columns talk of fame and notoriety as a goal in its own right. When Andy Warhol claimed everyone would be famous for 15 minutes he clearly didn’t anticipate YouTube or Big Brother.

What then is reputation and moreover why should CIMA members take an interest in it?

The short answer is that for a business or commercial organisation reputation has a bearing on value. Reputation may not be identified as an asset on the balance sheet but it affects investor confidence, staff recruitment, supplier attitudes and a myriad of other stakeholders in its capacity as relationship capital. Reputation represents a principal risk to any business and as such falls within the Business Review, Directors’ Report of the Companies Act 2006.

Guy Jubb remarked that corporate reputation as a concept embodies the image and values of a company, and was therefore intimately linked with the concept of corporate responsibility.

There are at least ten aspects of reputation to consider when defining it:

1.1 Perceptions of control
A brand is created and controlled by an organisation, but a reputation is something that is attributed to it by others. This fact raises the thorny issue of ‘control’. The reputation of an organisation is influenced by its performance, policies and people, but ultimately it is the stakeholders who decide what the reputation of the organisation actually is. Thus although stakeholders expect the management of an organisation to protect and enhance its reputation, this is something management has only indirect control over.

Reputation is a perception of past actions and future behaviour viewed not in isolation but in the context of what others are doing in the marketplace. This relativity is important: if all the companies in your sector have a policy of charitable donations but yours doesn’t then by this omission your company will appear mean-spirited. A company with a poor reputation for employee relations might decide to improve and upgrade its HR policy but it will take time for that company to acquire a reputation as a good employer, because so much of its reputation depends on past performance.

Reputation is a perception of character. For a person or place it is what you expect them to be like based on what you know of them. For a business or organisation this character is also a reflection of behaviour, what it has done in certain situations and can be expected to do in future occasions. Behaviour is a good indicator of management priorities, as any dissatisfied passenger of a suburban rail network will confirm.
Bill Connell referred to a report published by IFAC in 2002 entitled ‘Managing Risk to Enhance Shareholder Value’ in which Steve Marshall, former Chief Executive Officer (CEO) of Railtrack, wrote on reputation risk. Now replaced by Network Rail, Railtrack endured the media spotlight for 45 consecutive days during 2001 in the light of the Hatfield rail crash. Steve Marshall is quoted as saying that: ‘If you haven’t got clear control and you have great complexity, then things will go terribly wrong and your reputation with it’.

Management has no control over how an organisation is perceived by its stakeholders but it does have control over the behaviour of the organisation and can influence the perceptions of stakeholders through this.

1.2 Quality
Reputation is a fluid concept. A good one is earned through hard work yet can be quickly lost through misfortune or incompetence; a bad one can take a long time to lose especially if the cause is not fully appreciated by the hapless owner.

Apart from the dynamics of reputation, the quality depends on the relative values of the sector or its stakeholders. An airline might be judged to have a good reputation on punctuality but passenger safety is a business-critical ‘given’. Similarly a bank might have a good reputation for interest rates on savings, but deposit security is likewise a business-critical ‘given’ (see also section 1.9 on Trust).

Grocery retailers in the UK traditionally fought over the reputation for ‘best value’ or ‘cheapest’, yet this can lead to a good reputation with customers but a bad one with suppliers. Furthermore consumer values change with added concerns over product sourcing (food miles), mode of production (organic farming), labour conditions (fair trade) or packaging (waste control). As the grocery market evolves so reputations change.

Fear of reputation damage can lead to a risk adverse corporate mindset blind to opportunity. Too often strategic risk issues are met with an attitude of ‘what could go wrong?’ rather than an attitude of ‘how can we harness this situation to our advantage?’ A mobile communications operator in the UK fearful of the way access to the young could be exploited by predators, decided to develop user protection software to create a claim for competitive advantage in the marketplace. By turning a threat into an opportunity the manufacturer offered users a real benefit.

Quality of reputation according to Mark O’Connell of Skandia depends on HR policy. For a large employer the reputation among existing and potential employees is paramount. HR policy maybe sensible and logical but the risk comes in how it is applied at a local level by managers. The aim of HR is to avoid litigation which damages an employer’s reputation in the eyes of the employees and customers. Certain types of claims such as sex discrimination can incur unlimited damages and certain types of industry attract more media attention for the sums involved. This can be seen in the City with some high profile and costly tribunal cases. Companies need to be seen to learn from any inevitable exposure and hence switch a potentially bad news story to the company’s advantage.
To manage the quality of their reputation, organisations must constantly monitor and evolve their policies to avoid reputation damage and ensure that they look for opportunities for positive news especially in the face of bad.

1.3 Stakeholders
A stakeholder is anyone affected by the organisation. Commonly grouped by interest group, some organisations have as many as 30-40 stakeholder groups; most have 12-15. It is of course possible to have a good reputation with one group and a poor one with another. Most stakeholder interest categories fall into five super groups (see Figure 4 Ownership of stakeholder super groups) each of which can be managed by a board director. Note that stakeholders are pertinent to issues not companies and that with each issue they are likely to differ.

Bill Connell considers that organisations with a large number of stakeholders or employees should identify reputation as a value at risk and management accountants should be able to help express this.

While it is true ‘you can’t please all of the stakeholders all of the time’, your reputation is likely to be better among those to whom you give preference rather than among those you ignore.

Many businesses still focus primarily on two groups, customers and shareholders, as these are business critical. Case studies of Ratners Jewellers and Jarvis demonstrate the importance of customers (Ratners) and shareholders (Jarvis) to reputation.

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**Case Study: Ratners Jewellers**

**Background:** Ratners was a well-known high street jewellery chain, headed by the entrepreneur Gerald Ratner. The business was successfully selling ‘affordable’ merchandise in the mass market.

**Tipping point:** Gerald Ratner, at the Institute of Directors, incautiously referred to his merchandise as ‘crap’, primarily to get a laugh and attention. The quote found its way into the tabloids where it was seen by his customers, who didn’t see the joke.

**Outcome:** Customers turned their back on Ratners’ stores, sales plummeted and the chain ultimately folded.

**Moral:** It is not wise to ridicule your customers. Even those who knew the goods were not top quality wanted to believe they were buying a bargain. Reminding them of the commercial reality only made them feel foolish. Once insulted, customers are lost forever.
Stakeholder relationship mapping is not new but it does provide a valuable strategic planning tool to establish the relationship between the organisation and its diverse stakeholder interest groups. It can be a basis for a stakeholder engagement programme to help manage stakeholder relationships.

Organisations should therefore understand who their stakeholders are and the impact that each group of stakeholders has on the organisation.

For a government department there are many different stakeholders, each of whom will judge your performance in relation to their own expectations. One of the most important is invariably the Treasury as that is where your funding comes from. Nemat (Minouche) Shafik.
1.4 Reputation versus brand

Reputation is not the same as brand. A brand is created by an organisation to symbolise a set of values; it is consciously designed for consumers or purchasers. It is a cluster of attributes associated with a particular product. The brand might be a tangible product or an intangible concept that is ‘bought’ as an idea, but a brand is designed to be sold. A corporate brand might be targeted at fund managers and institutional investors, who are relevant consumers of the brand message. Consider the acronym BRAND and what it offers.

The image of an organisation is its immediate external perception, a snapshot frozen in time. The reputation of an organisation is the historic and cultural dimension of that image, the ‘social memory’ of the stakeholders which acts as a platform for expectation. A reputation is created by stakeholders and attributed to an organisation (person or place), in response to their expectations of it. By contrast a brand is manufactured by an organisation to sell to one stakeholder group, consumers. Brands are more controllable than reputations.

Brand owners should be aware of the growing trend for altering a business’s brand website or publicity material and then using the so called ‘spoof brand’ to negatively impact consumer behaviour. This is a form of hijack in which the positive associations of the brand are supplanted by negative ones created by those with malicious intent or grievance. The website www.adbusters.org provides an interesting insight into this trend, and profiles a number of the more famous.

According to Richard Carpenter of Radley Yeldar, brands can have a reputation and leading consumer or high street brands are more vulnerable to reputation damage because the general public at large represent a key stakeholder group of potential customers. Once a brand is deemed newsworthy it is susceptible to reputation damage through a failure to appreciate its vulnerability.

<table>
<thead>
<tr>
<th>Figure 1 Brand</th>
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<tbody>
<tr>
<td>Buyable</td>
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<tr>
<td>Reassurance</td>
</tr>
<tr>
<td>Association</td>
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<tr>
<td>Name</td>
</tr>
<tr>
<td>Difference</td>
</tr>
</tbody>
</table>
1.5 Reputation as an asset
Is reputation an asset? Well it certainly isn’t a fixed asset or depreciable. It can be claimed to be an intangible asset but valuing it is controversial (see section 1.6 The value of reputation). For reputation the label ‘asset’ is more emotive than financial, like its opposite ‘liability’ which indicates that there is a problem.

‘Balance sheets are for stuff, not people or ideas. People aren’t assets because you can’t own them, you can only rent them. Ideas are not assets because the people who generate them can’t be owned and because you can’t keep ideas bottled up for very long. If you want to measure the value of people and their ideas, you need to look at cash flows not assets. Balance sheets measure the value of stuff you own, cash flows measure the value of things you rent.’ This has been attributed to an anonymous banker but sums up the view of many accountants and auditors towards intangible assets.

The reputation of CIMA is an asset to the institute because it is vital to the success of any membership organisation in recruiting and retaining members. Both members and employers recognise the standard set by CIMA and its assurance of quality and integrity.

Charles Tilley of CIMA.

So although reputation cannot be classed as an asset for balance sheet purposes; a good reputation can be seen to be an asset to the organisation.

1.6 The value of reputation
How do you determine the value of a reputation? Can you put a figure against it? Putting a value on a brand was once thought impossible so valuing a reputation should not be discounted for the future. However, one has to consider why anyone would want to fix a value on reputation. No insurer will offer a premium as the moral hazard is just too great for claims control. There are just too many factors which influence the value of reputation to make this viable.

In most cases value is taken for granted until threatened, and depreciation results from damage to reputation. A good reputation is an asset and a bad one is a liability. The aim of management should be to enhance a good reputation and build it into the marketing strategy of the organisation. This requires an understanding of the factors which contribute to a good reputation in the eyes of stakeholders.

Where reputation is regarded as a liability then the objective should be to contain or reduce the threat of damage. This leads to a protection policy and ultimately a turnaround of fortune. This will take time and skill but can be achieved. A brand like Skoda has achieved this with considerable investment from the Volkswagen Group and a determination to address the cause of a poor reputation.
Bill Connell considers that the next major thrust of interest for management accountants will be getting a handle on what creates stakeholder value. Fifteen years ago, before the internet revolution, on average 80% of a company’s value was contained in the balance sheet, whereas today it is nearer 30%. The difference lies in value that has no immediate financial expression such as intellectual capital. This may be knowledge, culture or some other intangible but when more of your enterprise value is off-balance sheet than on it, there is an urgent need for enterprise risk management.

Reputation influences consumers in a far greater way than could ever be measured on a balance sheet. Intuition tells you more about the value of a business and this can be wrapped up in personalities: ‘what is the value of The Body Shop without Anita Roddick or Virgin without Richard Branson?’ Reputation also has a different dynamic; it can change value faster than most other assets. It isn’t just good or bad but valuable because of its inherent volatility.

The value of reputation varies according to sector. In the private sector reputation is vital for inspiring and sustaining investor confidence; damage to reputation reduces the share value and ultimately market capitalisation. In the public sector reputation for a service provider in health, education or transport is vital to maintain public trust in the provider. For professional service and partnership businesses, reputation is valued for its ability to attract and retain clients as damage to value results in loss of client confidence.

1.7 Reporting on reputation
How should you report reputation? There are some who consider it falls under the section of intellectual capital, where it could be recorded as reputational capital. Intellectual capital reporting is in its infancy, although with increasing value wrapped up in off-balance sheet entities, it is worth investigating along with items such as workplace practices, knowledge management and human capital.

Managing reputation requires both an understanding of its drivers and a method of measuring changes in it. Given that any attempt to calculate financial value for reputation is spurious, then the best way to express it is via non-financial or narrative reporting. This however sets up the challenge for a vocabulary of meaningful language. Once chosen this needs to set the objectives for future value as well as current, in order to aid investors and management along with other stakeholders.

David Loweth suggested that the balance sheet does not reflect the total resources available to many organisations and wants to see how management will overcome this through narrative reporting. Directors who show a clear understanding of where value lies within a business should inspire confidence and thus encourage investment. Articulating risk and uncertainty shows not weakness but honesty and realism. Reluctance to report on soft issues can indicate denial of their impact on the business.
Reputation doesn’t fall within risk reporting as, in itself, it doesn’t constitute a risk. Should reputation be identified as a risk? In itself no, but damage to reputation can cause value depreciation of a high magnitude, hence a protection policy ought to be specified or its omission be flagged as a risk. Too few organisations really understand the constituents of their reputation or how the different interdependent strands relate and how quickly they can unravel in a time of crisis. Risk to reputation exists in most organisations and many auditors believe it is undeniably a principal risk requiring more diligent narrative reporting. Thus, as the Companies Act requires the reporting of ‘principal risks’ within the Business Review of the Directors’ Report, it is under this category that we consider reputation to be best expressed, despite the fact that the word ‘risk’ has acquired negative connotations.

1.8 Ownership
Who owns the reputation of your business? It is rarely identified within the remit of a board member and ownership is usually shared. The company secretary might take responsibility for protecting reputation within a compliance remit. Conversely the Director of Corporate Communications may take responsibility for promoting and enhancing reputation, often aided by an external agency.

When asked about accountability and ownership of reputation, Guy Jubb was clear that the ‘buck stops with the board’. He suggested that it should be their responsibility to maintain checks and balances, ensuring that the right focus is achieved between current performance and future risk.

The acid test of where responsibility lies is the answer to the question – ‘who stands to lose most when reputation suffers?’. For this the answer is most commonly the CEO or the Managing Director (MD). The risk firm Aon conducts regular surveys on the types of risk that concern CEOs of global firms and 80% of respondents claim that risk to reputation is the single greatest risk keeping them awake at night. When probed to determine the response to this concern less than 30% admitted to doing anything about it.

Heather McCallum described a model used in many professional firms to manage ownership of reputation risk. Decisions relating to the taking on of new business are centralised to help prevent commercial aims compromising the firm’s integrity. The potentially conflicting interests of different clients, business sectors and internal practice groups are considered as part of a central process and the balancing of those various interests forms part of the strategic risk which is considered at board level.

Reputation rarely features in the risk register or on the agenda of risk committees. It is difficult to forecast damage cost or the probability of occurrence, hence it tends to evade scrutiny. Moreover it is difficult to attribute responsibility to a single individual or department with the result that when reputation is damaged there is no internal procedure for containment and repair. It is often left to the Corporate Communications department to implement a crisis management team.
1.9 Trust

Reputation dictates how people behave and in whom they place their trust. Once trust is gone it is very difficult to regain and in some cases its loss is irredeemable. Reputation is ultimately a measure of trust. As the CEO of a leading advertising agency said ‘reputation has never been as important as it is today ... to reassure the world that you are safe to talk to, deal with or rely on, there can be no complacency.’

The figure below illustrates the five levels of stakeholder reactions along with some examples of what could have caused these reactions and what impact this has on the stakeholder’s trust in the organisation.

In the public sector trust is extremely important as this defines the licence to operate. Through the Department for International Development (DFID) the UK government contributes aid to end global poverty.

Charles Tilley confirmed that trust is critical to CIMA. The reputation of any professional institution rests on integrity. Any body which sets itself up to be an authority must set standards and demonstrate consistency. Furthermore, as with all risk, it is always the one that hasn’t been considered that eventually causes most damage, hence a culture of trust protection is essential.

The reputation of the department is of vital importance to the UK’s standing in the world. The manner in which the UK allocates and controls its overseas aid budget is a critical ingredient of the reputation of the UK among its peers within the UN and EU.

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**Figure 2 Stakeholder reactions to the loss of trust**

<table>
<thead>
<tr>
<th>Level</th>
<th>Stakeholder reaction</th>
<th>Characterised by</th>
<th>Trust damage</th>
</tr>
</thead>
<tbody>
<tr>
<td>5</td>
<td>Outrage</td>
<td>Fraud, embezzlement, illegal activity.</td>
<td>Trust completely lost; not recoverable</td>
</tr>
<tr>
<td>4</td>
<td>Disgust</td>
<td>Incompetence, poor management decisions.</td>
<td>Trust severely damaged; never fully recoverable</td>
</tr>
<tr>
<td>3</td>
<td>Concern</td>
<td>Accident or safety issue, for example product recall.</td>
<td>Trust diminished; recoverable at heavy price</td>
</tr>
<tr>
<td>2</td>
<td>Surprise</td>
<td>Poor judgement or control, for example supply chain problems.</td>
<td>Trust dented; Recoverable with good PR</td>
</tr>
<tr>
<td>1</td>
<td>Disappointment</td>
<td>Inconsistent behaviour, for example gap between policy and reality.</td>
<td>Trust questioned; but speedily recovered</td>
</tr>
</tbody>
</table>
1.10 Damage

'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.

Damage to reputation is almost impossible to cost before an event and always easier after it. This is partly because the magnitude is dependent on so many variables. The three main ones are the prior state of reputation, the nature of the threat and the way the situation is handled.

Damage is not just about financial cost, immediate or deferred, but is about what it leaves in the way of diminished trust.

The extent of damage to reputation caused by an event or crisis will depend on how easily trust can be recovered. Figure 3 below illustrates some of the aspects that could determine how quickly trust could be restored; along with a brief description of what a good reputation should possess to limit the amount of damage done.

Richard Slynn observed that with professional firms the selection process for partners is in itself a quality control process designed to protect the firm’s reputation. Each and every partner bears some responsibility for reputation risk. Damage would be anything that destroys the external trust in the integrity of the firm. Clients pay for ‘sound judgement’ and any example of poor judgement could cause some reputation damage.

Damage to reputation and its recovery depends on the culture of the organisation, claims Alan Knight. If the particular problem is endemic then it will take a long time to resolve, whereas if the problem is an isolated event recovery will be easy and damage slight. For any company, large or small, reputation damage could come from a public safety incident or accident but the real damage would depend on how much that revealed about the safety culture in place prior to the accident.

### Figure 3 Aspects of recovery

<table>
<thead>
<tr>
<th>Recovery determinants</th>
<th>Relevant aspects</th>
<th>Damage limitation</th>
</tr>
</thead>
<tbody>
<tr>
<td>Existing goodwill</td>
<td>Quantity and quality</td>
<td>... money in the bank as goodwill for a rainy day on which to draw.</td>
</tr>
<tr>
<td></td>
<td>Dependent conditions</td>
<td></td>
</tr>
<tr>
<td>Prior state of trust</td>
<td>Cause</td>
<td>... a robustness to tolerate drawbacks and the unexpected.</td>
</tr>
<tr>
<td></td>
<td>Preventability</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Contain-ability</td>
<td></td>
</tr>
<tr>
<td>Nature of threat</td>
<td>Efficiency</td>
<td>... the confidence to put a hand up promptly and issue a mea culpa.</td>
</tr>
<tr>
<td>Impact event / crisis</td>
<td>Comprehensiveness</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Sensitivity</td>
<td></td>
</tr>
<tr>
<td>Responsiveness</td>
<td></td>
<td></td>
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<tr>
<td>Situation handling</td>
<td></td>
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</tbody>
</table>
1.11 Principal findings

- Organisations have no direct control over stakeholders’ perceptions, but they can influence them.
- The quality of a reputation must be monitored across all stakeholders. Organisations must look for opportunities for positive news especially in the midst of adverse situations.
- Organisations must understand who their stakeholders are and what impact they have on the organisation.
- Reputation and brand are not the same thing.
- Reputation should be seen as an asset to the organisation.
- It is difficult to value reputation in monetary terms.
- Reputation should be covered in narrative reports. It is best dealt with in the risk section as ‘reputation risk’.
- It is important to assign ownership for reputation – the board has prime responsibility for the organisation’s reputation.
- Reputation is ultimately a measure of trust.
- The extent of damage to reputation caused by an event will depend on how easily trust can be recovered. This will depend on the prior state of reputation, the nature of the threat and the way that the situation is handled.
2 Reputation risk

Reputation has a value even if it cannot be expressed financially. The possibility of this value being reduced represents a business risk. Most organisations do not know enough about the drivers of their reputation to identify or protect against this risk from devaluation. Any incident that reduces trust among any single stakeholder group has the possibility to create reputation damage. The severity of this damage and the cost will depend on the influence of the stakeholder group and its impact on the organisation. Not all stakeholder groups are benign and some secondary ones are by their nature hostile.

A risk to reputation occurs where the organisation fails to meet the expectations of a specific stakeholder group. The key to effective reputation risk management is therefore the management of expectations. It has been said that reputation risk lies in the gap between expected and actual behaviour. This is why stakeholder mapping is useful to ‘mind the gap’.

Responsibility for stakeholder handling is spread across the board of a corporation and so there is scope for expectation shortfall in many areas. Consider the table in Figure 4 which shows the spread of ownership within a corporation across all the stakeholder groups and also what the most common failures are to satisfy stakeholder expectations.
Any one of the failures listed in the chart above has the capacity to cause reputation damage and thus erode value. Most would be classified as operational or business risks but their damage to the value of reputation is rarely acknowledged by a risk or internal audit committee. This is because most organisations view reputation risk as a consequence of operational risk, not an identifiable risk in its own right.

To better understand reputation risk it is necessary to look at its appetite, causes, identification, effects, measurement, management and reporting in the following sections.
2.1 Appetite for risk
Risk management as a discipline has grown in recent years to such an extent that the Turnbull report (Internal Control: Guidance for Directors on the Combined Code) recommended that major public companies embrace a risk awareness culture. The aim for management is to identify risks and classify them into acceptable and unacceptable. Problems arise with a risk averse culture because not all risks can be avoided, some must be faced and managed. There are four strategies for handling risk – transfer, avoid, manage and mitigate.

The word risk has acquired a negativity it doesn’t deserve and to many corporate executives, especially those involved with compliance, risk is generally something to fear. It is a warning about a threat and sounds a note of caution to risk managers, internal auditors and lawyers. It is nevertheless worth remembering that to a different audience, for example investors and entrepreneurs, risk represents opportunity and an invitation not a caution.

Cary Depel of IFX Markets Ltd, a leading firm of financial traders and market makers and Chairman of The Institute of Risk Management explained: ‘The nature of the business is risk taking so risk aversion is not really an option. Risk assessment is an ongoing process in trading with a culture of classifying decisions as high, medium or low risk. The measurement and constant assessment of reputation risk is an active process’.

Effective risk management requires a change in mindset from a negative one looking to create bureaucracy, to a positive one looking for opportunities. Bill Connell has a proactive view on risk management: ‘you have more control if you manage into a situation rather than trying to manage out’. The challenge for management is to create a control environment that is not stifling but empowering. He calls this liberation: ‘intelligent risk taking within structured risk management’.

Richard Carpenter of Radley Yeldar believes that risk tends to be poorly covered in narrative reporting. Some of the information derives from internal auditors who may have an introspective focus and are not best placed to assess external risks. Reporting on risk tends to be included because the Turnbull report requires a statement rather than as a result of detailed analysis. Insufficient thought goes into the reporting of corporate risk, few companies admit any reputation risk or talk about it in relation to identified operational risks.
2.2 Causes of reputation risk

An analysis of reputation damage to corporations over recent years yields a categorisation of causes under the headings: cultural, managerial and external. This classification was tested through a survey with the Strategic Risk magazine in August 2006 and found to be valid. A summary of these causes can be found in Figure 5.

2.2.1 Cultural risk

These are risks which tend not to be identified as they are embedded in the culture of an organisation and relate to workplace practices and policies. In short, these relate to codes of conduct and rules of operation, some of which are imposed by a third party as mandatory and some are discretionary or volitional codes which are self imposed. These are risks that can be avoided and should be identified.

Legal risk relates to regulator imposed rules and codes, for example reporting regulations, company law, statute law, professional negligence or legislative compliance. Financial organisations have systems and procedures but these alone do not provide reputation protection, remember Barings Bank. Accountancy firm Arthur Andersen also fell foul of regulatory rules, blinded by the complex auditing for a lucrative client like Enron. Barings suffered reputation risk from poor internal controls which destroyed customer confidence. Enron suffered loss of reputation because it had been illegally exaggerating its assets.

Ethical risk relates to self imposed standards via a professional institute or association to advise members on behavioural norms and ethics. All professional fee earners have to balance commercial aims with ethics and there can be a temptation to earn commission through cutting corners. Codes of conduct exist to reinforce trust and should not be viewed as an impediment. Ethical risk occurs in organisations that demonstrate some inconsistency between what they say and what they do. Google suffered reputation damage in entering the Chinese market and accepting censorship; The Body Shop suffered reputation damage in selling its business to L’Oreal.

2.2.2 Managerial risk

These are risks that are frequently identified as they fall under the radar of the risk or internal audit committee. The fact that these risks still present substantial reputation damage only goes to show how important it is to have a handle on operational risk. It is not enough just to have systems and procedures in place, they must also work effectively. These are risks that cannot be avoided or transferred and so must be managed.

Executive risk is about performance indicators, meeting financial targets and satisfying clients. This should be easy enough to control but Equitable Life is proof that this is sometimes less so if the right questions are left unanswered by shareholders. Apart from incompetence this type of risk can arise from arrogance. Coca-Cola tried to launch bottled water called Dasani on to the UK market which was subsequently found to be tap water. This disclosure led to a hasty and expensive recall. Bechtel Corporation had tried to sell Bolivians their own water at Cochabamba until they were shown the door by the Bolivian government. This proved a reputation disaster for the Bechtel Corporation throughout Latin America.
Operational risk is about performance expectation and how well the ‘product’ works. For manufacturers this is simply a matter of quality control and distribution, yet mistakes happen and batches need to be recalled. The reputation damage depends on the way this is handled. In the US the gold standard is Tylenol which was recalled promptly after a tampering scare. In Europe the most famous recall was Perrier following a benzene scare, this was also judged to have been well handled. In the UK Cadbury recalled Creme Eggs in 2006 but only after what the public took to be a delay in acting on evidence. The fact that health laboratory tests took time was lost to a public who had lost confidence in their favourite chocolate manufacturer, who felt that Cadbury should have recalled the product much earlier.

2.2.3 External risk
These are risks to your organisation from the outside. They can be quite close in the form of a partner, supplier, agent or contractor or distant in the form of a natural disaster on the other side of the world. The common thread is that these risks can neither be controlled nor avoided so they must be mitigated.

Association risk is where part of your product or service is delivered by a third party on whom you rely. This might be on a permanent or temporary basis but your reputation depends on their standards of client service meeting yours. In the case of British Airways (BA) an industrial dispute with the contract catering firm, Gate Gourmet, spilt over to contaminate the reputation of BA as a passenger service. In the case of Jarvis, the contractor to Railtrack, the poor supervision of subcontractors led to a critical safety issue that destroyed investor confidence. There are risks in using sub-contractors which cannot be directly managed but threaten to contaminate your reputation. Outsourcing has been popular but it offers an association risk.

Environment risk can be from the natural or commercial environment. New technology alters the marketplace or a new competitor from overseas enters your market. Critical data may be lost through an IT virus. Business continuity can be insured but not when the viability of the business comes into question. One online fashion retailer suffered disruption from the Buncefield fire that almost caused the business to close. Sometimes insurance is not enough and the risks from the marketplace need to be recognised. High street travel agents are finding the popularity of online booking for flights and holidays a real threat to their business model. Reputation damage from the environment is very difficult to anticipate.
2.3 Effects of reputation damage

Damage to reputation will differ depending on the nature of the business and the basis for stakeholder trust. In each of the 14 interviews conducted for the CIMA study, respondents were asked to describe what would damage their reputation. The answers have been grouped by role and sector to demonstrate the diversity of perspective on damage.

In the Financial Services sector reputation damage would result from a financial irregularity, for example an insurer unable or unwilling to meet claims, or considered irresponsible in over or mis-selling product. In the trading world reputation would be damaged following the downgrading of stock by analysts; this would signal a loss of confidence. The Chartered Insurance Institute (CII), the Association of British Insurers (ABI) and the British Insurance Brokers Association (BIBA) are all working towards higher standards of customer service through the Treating Customers Fairly (TCF) scheme launched by the Financial Services Authority (FSA).
### External risks to mitigate

<table>
<thead>
<tr>
<th>Associations</th>
<th>Environment</th>
</tr>
</thead>
<tbody>
<tr>
<td>Related brands:</td>
<td>Unpredictable:</td>
</tr>
<tr>
<td>• In same group</td>
<td>• Marketplace industry sector</td>
</tr>
<tr>
<td>• Trading partners</td>
<td>• New competitor</td>
</tr>
<tr>
<td>• Suppliers/agents</td>
<td>• Technology</td>
</tr>
<tr>
<td>• Subsidiaries</td>
<td>• Global markets</td>
</tr>
<tr>
<td>• Sub-contractors</td>
<td>• Environment change</td>
</tr>
<tr>
<td>• Outsource risk</td>
<td></td>
</tr>
<tr>
<td>• Contamination of your reputation</td>
<td>• Business continuity threat</td>
</tr>
<tr>
<td>• Third party lets down your customers</td>
<td>• Business viability questionable</td>
</tr>
<tr>
<td>BA/Gate Gourmet</td>
<td>• Internet shopping</td>
</tr>
<tr>
<td>Jarvis</td>
<td>• Online booking</td>
</tr>
</tbody>
</table>

In professional firms of accountants and lawyers reputation damage would certainly accrue from any act of impropriety with a client or unprofessional conduct. Clients engage professionals for their ‘sound judgement’ and any question over integrity threatens the client’s trust in the integrity of the firm. Damage to reputation would also be caused by the defection of key talent to a rival or by poor management of junior staff leading to gaps in the firm’s client service capability.

For manufacturers of consumer and retail brands the greatest risk to reputation is customer safety. A former director of a major company stated the most feared headline was ‘customer killed in store’. For a major retailer damage could come from a public safety incident or accident, but the real damage to reputation would depend on how much that revealed about the safety culture which was in place prior to the accident. Damage to reputation could also be caused by treating suppliers unfairly or forcing them to treat their labour unfairly in order to meet your unreasonable demands.

For HR directors in large corporations the greatest risk to reputation is a costly legal battle with a former employee via a tribunal. Whether the case is subsequently won or lost is less relevant than the bad publicity which accrues from media interest in the corporation. Firms with a large number of employees are exposed to reputation risk inherent in the activities of each and every one of them. Staff behaviour can only be controlled so far by codes of conduct and beyond that exists the risk of damage to the employer organisation.

In the public sector reputation risk exists in the execution of any public service and its ability to meet the expectations of the general public. Those expectations are often set nationally through politicians and the media leaving the delivery at local level in the hands of a local or regional authority. Public services are exposed to reputation risk given the capacity for expectation to exceed delivery. Local delivery of education, health and transport services is exposed to reputation risk based on nationally set expectations.
ALARM is a not-for-profit company governed by elected directors. It is funded by members and sponsors. It exists to promote public risk management and assist members in career development and professional training, as many members lack a formal qualification in risk management. ALARM aims to be the UK voice for public service risk management. Withdrawal of financial support from members or sponsors could damage our reputation so it is vital to offer good service and value-for-money as an association. Lynn Drennan.

Reputation damage can be traced back to the three generic causal types: cultural, managerial and external (mentioned in 2.2 Causes of reputation risk). Most of the risks mentioned by respondents can be classified as managerial, such as product safety, and are down to managing the operation effectively. Where staff behaviour sets up a ‘people risk’, this is essentially cultural and can be avoided through careful selection of senior management to ensure that the organisation’s values are not compromised by the activities of its people. Externally caused risk to reputation is inherent in supply chain partnerships and must be monitored and mitigated.

2.4 Identification of reputation risk

Does any organisation specifically identify reputation risk? So far the authors have not identified any organisation claiming to do this; all claim that it is adequately covered through existing operational and strategic risk reporting procedures. Reputation risk tends to be seen as an outcome from operational risk and thus not singled out for attention. This was found in both the interviews conducted for CIMA and in the online survey for the Strategic Risk magazine.

This does not mean it is correct to leave reputation as an outcome devoid of any pro-active protection or enhancement policy. The authors feel this approach is a function of two things: the absence of ownership and the challenge which reputation as a category represents to conventional risk assessment methodologies.

Why does reputation rarely feature on the risk register? This appears to be because it is so difficult to evaluate the cost of any damage. The post-Turnbull thinking on risk reporting is that risks must have a damage cost and an owner; reputation offers neither. The cost of reputation damage is only ever known after the loss of future business has been considered. Cadbury has said that the cost of the Creme Egg recall damaged their reputation by £20m but, even if this is based on a revised market capitalisation, it is impossible to adequately factor in lost future sales. The reputation damage cost can only be really known five to ten years after an event, and even that might be too soon.

Reputation risk escapes scrutiny for four basic reasons:
• the nature of the subject means that as it is a perception of character determined by others, it is intangible and not financially anchored
• the damage cost depends on a myriad of other factors such as competitor behaviour and market conditions; to calculate a figure requires so many suppositions that it is ultimately meaningless
• the probability of occurrence cannot be forecast as reputation is linked to human behaviour which is notoriously difficult to factor into models
• the lack of ownership means that responsibility for vigilance is unclear.

Organisations tend to react to crises rather than proactively identify and manage the risks to reputation.
The Institute of Risk Management suggests three headings under the risk analysis section of the risk management standard. These are identification, description and evaluation. Without any individual taking ownership for the identification of reputation risk it is hardly surprising that both description and evaluation are so often missing. In many organisations a description of reputation risk would be helpful as it would articulate the nature of and the extent of the risk. Evaluation could prove more difficult as it assumes an impact cost that can be calculated to signal magnitude.

The most significant finding of the CIMA study is that reputation risk is not specifically identified, despite the fact that most interviewees agreed that it represented a principal risk which should be reported in the Business Review to comply with the new Companies Act.

Identifying reputation risk in social care is closely linked to political risk and for a government agency it is important to succeed and to be seen to do so. Several agencies set up at the same time as the General Social Care Council (GSCC) have been wound up or absorbed into other areas, and there is undoubtedly a political dimension to reputation risk in any aspect of health provision. With regard to social services, many abuse cases hitting the headlines reflect on poor practice, and the GSCC was set up to improve public confidence in social care provision. Terry Butler.

2.5 Measurement of reputation risk

Most corporate risk reporting uses a standard matrix of either four or nine boxes to plot two determinants of any identified risk: the damage cost or severity and the occurrence frequency or probability. For reasons mentioned previously reputation rarely features in this grid matrix. There is a belief in some quarters that ‘what gets measured gets managed’ but this is not universally accepted by those working in non-financial areas such as social responsibility or accountability where reputation doesn’t have to be measured in order to be managed.

How are other risks measured? The risk matrix offers a simple management decision making tool to determine what is important and what is urgent in order to prioritise action. Risk management as a discipline has tended to focus on the negative impact of risk rather than the positive. This is because it was designed by insurers not entrepreneurs, thus risk tends to be viewed in the UK as something to be avoided not embraced. The fact that some risks, like employment risk, are unavoidable and thus require good management tends to get forgotten. It seems that many risks are measured with the explicit purpose of avoiding or reducing them; a view that most investors and entrepreneurs who actively seek risk find bizarre.

Measurement of reputation itself has been possible for over ten years and there are several methods available. There are two basic types: one is a ranking model used by some analysts which uses published information to compare reputations; the other is bespoke and uses internal client information as an aid for reputation owners. The ranking model has the advantage of providing a comparative score, but the disadvantage is that this fails to be stakeholder or issue specific. The relationship model has the advantage of being a management tool but it cannot provide a comparison between different reputations. Appendix 1, reputation measurement models, gives some examples of different measurement models.
In common with many senior management teams, the BT Board is strongly committed to accounting for significant social, environmental and ethical matters that relate to BT’s business.

The challenge over the last few years has been to develop a tool to assess and quantify the risks that these issues may present that has an output in a concise and familiar format to present to the board.

The BT Corporate Social Responsibility (CSR) risk register, setting out their most significant social, ethical and environmental risks, was therefore recently re-developed and reviewed by the Corporate Responsibility Team to align with the more rigorous Risk Frontier Methodology introduced by the Risk Management Team to report BT Group’s strategic risk profile.

The initial determination of what risks and opportunities should be considered was undertaken by the CSR Practitioners Forum whose members, drawn from across the business, have responsibilities including business ethics, health and safety, environment, age and disability, internal audit and digital inclusion. In addition, an external perspective was obtained from the CSR Leadership Panel, an external advisory group of experts renowned for excelling in their field chaired by Jonathon Porritt. The risk register was then reviewed and approved by the Corporate Social Responsibility Steering Group (CSRSG), a senior management committee which oversees the strategic implementation of all social and environmental programmes across BT.

Each risk is defined in terms of vulnerabilities, triggers and consequences, with the purpose being to understand the range of the risk in greater detail. In many cases the risk is broken down into a number of sub-risks. The seriousness of each risk is then determined by assessing both its likelihood and financial impact as a risk frontier. The figure opposite illustrates the resulting CSR risk matrix – highlighting visually the potential impact of each risk from a likelihood and financial risk perspective. Quantification on the graph (in terms of likelihood percentages and financial measurements) has been removed for commercial confidentiality.

For further details of each of the risks see the BT 2005-06 Annual Report and Accounts.
2.6 Management of reputation risk

There are four strategies for tackling risk and, depending on cause, reputation risk necessitates understanding three of these – avoidance, management and mitigation (as explained in 2.1 Appetite for risk). The fourth option to transfer risk is denied to risks which cannot be insured or in some other way handed over. It could be argued that in employing an agency to manage a reputational crisis an organisation is transferring risk, but it could also be argued that this is not strictly speaking risk transference but policy execution or damage limitation.

It is also worth repeating that reputation itself cannot strictly speaking be managed. Because it is determined by stakeholders, the reputation owner can only influence their expectations as an act of risk management and this is not technically reputation management. Therefore reputation risk management is actually expectation management through stakeholder engagement.

Organisations manage reputation risk in different ways. There appear to be four different levels of commitment to this, as shown in Figure 6.

<table>
<thead>
<tr>
<th>Commitment level</th>
<th>Sophistication level</th>
<th>Management process in place to handle risk to corporate reputation</th>
</tr>
</thead>
<tbody>
<tr>
<td>Controlled</td>
<td>• Managed by Chief Risk Officer (CRO) • Executive interest</td>
<td>Reviewed regularly by the Chief Financial Officer (CFO) as a strategic risk and discussed at board level. Supported by independent tracking of diverse stakeholder group attitudes. Sophisticated and sensitive.</td>
</tr>
<tr>
<td>Managed</td>
<td>• Managed by Risk Manager (RM) • Operational interest</td>
<td>Reviewed as part of a corporate risk register but not measured or monitored by the corporate strategy committee. Compliant with Turnbull guidelines in risk identification but little control over reputation risks.</td>
</tr>
<tr>
<td>Supervised</td>
<td>• Managed on an ad hoc basis responsively</td>
<td>Managed on a severity of risk basis by senior management alongside all other operational and strategic risks. Tends to be crisis only, reactive not proactive: fire fighting approach.</td>
</tr>
<tr>
<td>Unmanaged</td>
<td>• Not managed at all</td>
<td>Reputation risk is not measured or managed in any way – it is not considered a risk worth measuring or trying to manage, other than by having an agency retained to handle any problems if/when they arise.</td>
</tr>
</tbody>
</table>
Most of the organisations interviewed claimed to manage reputation risk at the higher controlled level but in no case was there a dedicated individual responsible for ownership of the risk. Executive interest was claimed yet without an ownership or measurement protocol, it is hard to see this as significantly better than one of the lower levels of management handling.

It follows that damage to reputation and its recovery depends on the culture of the organisation. If the particular problem is endemic then it will take a long time to resolve, yet if the problem is an isolated event, recovery will be easy and damage slight.

Tim House of Allen & Overy observed that clients, and especially major banks, are acutely aware of reputation risk. In the last five years many have recruited at CEO level from the ranks of regulatory lawyers to protect their interests in the emerging world of regulator power. Business leaders tend to be selected for their experience in managing risk rather than their industry sector service. Increasingly sophisticated financial products increase ethical risk and the probability of regulator scrutiny, thus reputation becomes more important.

Alan Knight says ‘you can’t manage a reputation, you earn a reputation’. Organisations that preserve a good reputation do so because they are managing the issues or challenges which are business critical not necessarily reputation critical. ‘If you manage the challenges just for reputation alone you will fail to get the benefits you seek, it becomes obvious to your stakeholders that reputation matters more than the challenges you should be addressing’. People try to over-manage reputation and sometimes focus on the wrong issues.

2.7 Reporting of reputation risk

Reputation risk is best expressed through narrative reporting. Attempts to attribute a financial cost is unlikely to reflect the risk accurately, so many activities of an organisation have the potential to impact upon reputation so any numerical expression is unreliable. Given the nature of reputation, and that its value can differ among stakeholders, it is best expressed as a qualitative rather than quantitative element.

Guy Jubb said that despite there being no imperative to report, businesses have a responsibility to allude to uncertainties that they face in their operations, both now and in the future, and to draw investors attention towards issues that have potential reputational implications. He predicted that narrative reporting will have an increasing importance in the coming few years – particularly as businesses strive to build it into the shareholder relations process.
The Business Review in the new Companies Act places more emphasis on narrative reporting with a requirement for a ‘description of principal risks and uncertainties facing the company’ and ‘a balanced and comprehensive analysis’ of the business. For auditors and accountants the skill set required in compiling company accounts will in future require ‘more story teller than bean counter’ as one interview respondent put it.

David Loweth said that a good narrative puts the issues of the business in context and itself represents a management challenge; information of value to potential investors might also be of value to competitors and so there is always a balance between transparency and confidentiality. Describing this non-financial value must be left to the individual companies and their investors for they alone know what their value drivers are and how to harness them to increase shareholder value.

CIMA is part of the Report Leadership group which has demonstrated practical and effective ways to improve narrative reporting. Those involved with reviewing the annual accounts of FTSE100 companies felt that risk reporting was generally poor as it tended to express the view of internal auditors familiar with operational or managerial risk but unused to looking at either external or cultural risk. It was also felt that value, where expressed, was both subjective and performance based as opposed to objective and prediction focused.

Both the expression of risk and value will need to be improved. The Association of British Insurers (ABI) expressed their views on narrative reporting in November 2006. They identified specific types of information the insurance industry would like to see in narrative reports; specifically ‘investors consider the priority areas for improvement should be the delivery of forward-looking information and non-financial key performance indicators... also welcome the provision of more information on how boards approach their work.’

Investors want to have information to help them make a judgement about the future value of the business, yet most are supplied with only the opinion of company management on where value actually resides. Many investors inherently know where the value lies in a company, especially if it lies off-balance sheet within intellectual capital and other intangibles, yet companies now have a duty to identify and express this value to all stakeholders.

Compilation of the annual report normally falls to the audit committee or Finance Director as it traditionally comprises a statement of financial performance. Auditors can be uncomfortable reporting intangibles due to their non-financial nature and so this type of value often goes under-reported. It is because ‘value reporting’ lacks any universally agreed metric that it continues to be a challenge for auditors and accountants.

Risk reporting in corporate accounts is generally poor. In Turnbull compliant companies information comes from the internal audit function and thus has a limited focus on what constitutes risk to an organisation. External risk and cultural risk tend to be omitted, yet these risks are important to investors and other stakeholders.
Reporting obligations alter with ownership as does the appetite for risk. A publicly listed company is accountable to its shareholders and other stakeholders, but a privately owned company is accountable only to its owner. Private ownership tends to reduce transparency. Private equity ownership is not the same as private ownership; the investors are focused on selling the business on at a profit, and thus have a vested interest in reputation and compliant risk reporting. This was a view offered by Cary Depel among others.

For some companies reporting risk outside the boardroom is seen as a weakness signalling an opportunity for competitors to exploit. This reflects a misconception of the purpose of the annual report: it is not meant to be a promotional document but a year end statement and an indication of management competence. Far better therefore to honestly demonstrate a recognition of risks rather than simply a lack of awareness of them.
3 Future trends

There is no doubt that reputation will play an increasingly important role in all decisions concerning in whom to place trust. Managing your reputation has always been a key business objective. The internet age of electronic instant information is yet another medium that an organisation needs to consider and monitor. A good reputation can be hijacked by a malicious fraudster and identity fraud is a major worry to financial institutions. It is very easy to find out what a reputation is worth after damage has been caused, the challenge is to pro-actively measure and protect it.

There is a new generation of people who use electronic media as a medium of choice, not only for communication but opinion forming. Blogging is opinion broadcasting without censorship or codes of conduct. Reputations depend on stakeholder perceptions and truth is often a victim of sensationalism. Protecting a reputation will require a level of pro-activity previously unseen and unwarranted. Investor confidence has always relied on rumour, now the medium for spreading rumour is accessible to all.

The risk industry has grown as new risks arise that were unknown five years ago. Political risk, computer virus risk and other forms of business continuity risk are evolving. Fear of uncertainty breeds new products for security, both electronic and physical. The business environment of the future will have new competitors from new markets and established reputations within the western world will be challenged.

Future trends in reporting indicate that intangibles will be included not by regulatory requirement but through the adoption of the principle of transparency and good governance. In Australia there is a move to introduce a Risk Management Standard (version 3, number 4360) and it is likely that the UK will soon adopt a similar protocol. The British Standards Institute is looking to create a global risk management standard with the ISO (International Organisation for Standardisation). The aim is to embed risk management within the culture so that it is not just a process but part of the philosophy and management thinking.

There is an increasing demand to understand value drivers, both financial and non-financial. Once these are known it is a simple step to identify the value at risk. The next major thrust of interest for management accountants will be getting a handle on what creates stakeholder value. Thus reporting non-financial value is a future trend of enormous relevance to CIMA and its membership. The International Accounting Standards Board (IASB) has expressed a desire to have a reporting protocol for value drivers in place by 2010.

Value reporting is a hot topic both in the public and private sectors. In the public sector it seeks to express the societal benefit of investment in public services, and in the private sector value reporting seeks to express the soft, intangible, off-balance sheet values that stakeholders seek. Reputation is a value that currently goes unreported despite being a highly influential value driver. Organisations with a large number of stakeholders or employees should identify reputation as a value at risk and management accountants should be able to help express this.
Auditors will continue to try to monetise assets for reporting in a controlled environment. There is a danger that reputation reporting will suffer in the same way as sustainability reporting before it due to a lack of common measures to satisfy auditor reporting requirements. CIMA members will find it a challenge to express reputation and other intangible assets like intellectual capital. There is a real need for a metric to express stakeholder value because there is a view that many accountants and auditors ‘just don’t get it’ when it comes to non-financial values like responsibility, sustainability and reputation. Accountants will need to find ways of expressing non-financial value using language that is helpful to both investors and the regulator.

The future of transparency is linked to the legal status of companies. For the professional partnership that becomes a public company to protect partners with limited liability, there will be greater financial transparency. Conversely for the trading company that is acquired by a private owner there is likely to be a reduction in transparency as reporting requirements are less stringent under private ownership. As more businesses are bought by private equity firms accountable only to their owner/investors it is quite possible there will be a reduction in the amount of information provided to other stakeholders.

So far the UK has avoided being too rule-based like the Securities Exchange Commission (SEC) in the US where Sarbanes-Oxley has only succeeded in producing a compliance culture. A principle-based approach works best in a mature marketplace served by both a strong legal and accounting professional structure. A lesson from Enron is the need for these advisory professions to maintain an independence from their clients and be alert to conflicts of interest within their own service portfolio.

In the UK there is a balance to be found between reporting for good governance and regulator compliance. The European and US reporting cultures are largely understood. The issue for a global market is how the emerging markets will interpret reporting requirements. How will China, India or Russia act when it comes to regulations for company reporting? These are where the traders, analysts, investment funds and other institutional investors are looking now. Such is the view of Cary Depel of IFX Markets Ltd and Chairman of The Institute of Risk Management.
Further reading


ASB Reports. See http://www.frc.org.uk/asb


Chiron consultants. See www.chiron.uk.net


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Larkin, J. (2003), Strategic Reputation Risk Management, Palgrave Macmillan.


Peters, G. (1999), Waltzing with the raptors, John Wiley and Sons Ltd.

Rayner, J. (2003), Managing Reputational Risk: Curbing Threats, Leveraging Opportunities, John Wiley and Sons Ltd.


Reputation Institute. See www.reputationinstitute.com

The Companies Act 2006. See www.opsi.gov.uk

The PRISM Group. See www.euintangibles.net


Appendices

Appendix 1

Reputation measurement models
The RepTrak™ and RQ models for measuring corporate reputation were developed by Dr. Charles Fombrun and further details about them can be found on the website of the Reputation Institute www.reputationinstitute.com This model is useful for analysts to compare reputation between organisations as its output is a ranking score. Detractors point out that this model fails to address different stakeholders and thus is of limited value.

Fombrun’s RepTrak™and RQ models
RepTrak™ creates a comparative rating of corporate reputation on a 0-100 scale. The instrument measures corporate reputation by asking observers to rate a company on a set of 23 key performance indicators classified into seven dimensions: products and services, performance, innovation, governance, ethics, workplace and citizenship.

RepTrak™ is a refined version of the Reputation Quotient (RQ) measure that Dr Charles Fombrun (1966) originally developed. RQ measures reputation on 20 attributes classified into six dimensions:

- Emotional appeal – how much a company is liked and respected.
- Products and services – perceptions of quality, innovation, value and reliability.
- Vision and leadership – clear vision, strong leadership and initiative.
- Workplace environment – management quality, culture and employee quality.
- Social responsibility – high standards in dealing with people, causes etc.

NB: RepTrak™ weights dimensions in terms of their derived importance to a specific stakeholder group. Neither Reptrak™ nor RQ give specific weights to stakeholder groups.
The Brady model is designed to show an organisation where its sources of reputation lie and was developed by Dr Arlo Brady. It was not designed to contribute to a comparative ranking system and any organisation employing this model must design its own relevant quantification methods for tracking change over time.

<table>
<thead>
<tr>
<th>Brady model</th>
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</thead>
<tbody>
<tr>
<td>Seven elements of reputation management (2005).</td>
</tr>
<tr>
<td>Seven sources of reputation:</td>
</tr>
<tr>
<td>Knowledge and skills – employee talent pool, drivers of innovation.</td>
</tr>
<tr>
<td>Emotional connections – consumers’ perception of value, stakeholder alignment.</td>
</tr>
<tr>
<td>Leadership, vision and desire – governance style and practice, motivation and vision.</td>
</tr>
<tr>
<td>Quality – product or service delivery history, consistency.</td>
</tr>
<tr>
<td>Financial credibility – history of creating better than average returns.</td>
</tr>
<tr>
<td>Social credibility – good citizen, licence to operate etc.</td>
</tr>
<tr>
<td>Environmental credibility – must not be seen to add negative legacy for future.</td>
</tr>
<tr>
<td>NB: Not designed as a basis for a commercial ranking system.</td>
</tr>
</tbody>
</table>
The MacMillan SPIRIT model was founded by Keith MacMillian. This model is designed to be used by a reputation owner to help improve relationship quality with different stakeholder groups. It is a relationship managing tool.

<table>
<thead>
<tr>
<th>MacMillian SPIRIT model</th>
</tr>
</thead>
<tbody>
<tr>
<td>SPIRIT – Stakeholder Performance Indicator (SPI) Relationship Improvement Tool (RIT) (predetermined dimensions).</td>
</tr>
<tr>
<td>16 attributes across four categories.</td>
</tr>
<tr>
<td><strong>Past performance:</strong></td>
</tr>
<tr>
<td>Experience indicators (7) – service and material benefits, shared values etc.</td>
</tr>
<tr>
<td>Influence indicators (1) – outside influencers; media, peer and pressure groups.</td>
</tr>
<tr>
<td><strong>Future performance:</strong></td>
</tr>
<tr>
<td>Behaviour indicators (5) – intention to support, recommend or subvert.</td>
</tr>
<tr>
<td>Emotional indicators (3) – trust and other emotional support indicators.</td>
</tr>
</tbody>
</table>

NB: Measures relationship quality to show where improvement is needed.
The Honey model was designed as a strategic planning tool for use in management decision making and action prioritisation. It is based on only four attributes but is the only model to attempt to address the issue of expectation which is so important to reputation risk.

<table>
<thead>
<tr>
<th>Honey model</th>
</tr>
</thead>
<tbody>
<tr>
<td>CSSE – a strategic planning tool – (stakeholder determined dimensions)</td>
</tr>
<tr>
<td>Several attributes across four categories.</td>
</tr>
<tr>
<td><strong>Performance:</strong></td>
</tr>
<tr>
<td>Stewardship indicators – board quality, succession planning, decision taking etc.</td>
</tr>
<tr>
<td>Sustainability indicators – environmental, social and economic combination.</td>
</tr>
<tr>
<td><strong>Expectation:</strong></td>
</tr>
<tr>
<td>Attention indicators – media magnetism, generic or specific.</td>
</tr>
<tr>
<td>Association indicators – family linkage, corporate or trading brand names.</td>
</tr>
<tr>
<td>NB: Highlights potential risk areas for management’s priority attention.</td>
</tr>
</tbody>
</table>
Appendix 2
Author profiles

Authors

Dr Arlo Brady is Special Advisor at the strategic marketing and communications consultancy Freud Communications. In his role Arlo provides counsel on sustainable development, corporate responsibility and reputational issues to a range of senior business leaders, consumer brands, public sector bodies and global corporations, including, for example, Sony, the Greater London Authority, Eurostar, Volkswagen, Warner Bros, The Climate Group and American Express.

Arlo is also an associate at the Judge Business School, Cambridge University, author of the 2005 book ‘The Sustainability Effect’, and contributor to the 2007 book ‘Corporate Strategies for Climate Change’. Arlo holds a Ph.D. in business from Queens’ College, Cambridge University; an M.Sc. from Imperial College; and is a lecturer on a number of MBA programmes. Arlo was originally trained as a petroleum geologist. For further information about Arlo please visit his website at www.arlobrady.com or his blog at http://greenlightbulb.blogspot.com

Garry Honey is Visiting Senior Fellow of Southampton University in the Centre for Risk Research and a Fellow of Kingston University in the Centre for Stakeholding and Sustainable Enterprise. In 2006 he founded Chiron www.chiron.uk.net the only consultancy in the UK dedicated to identifying and measuring reputation risk. He writes regularly for Strategic Risk magazine and conducted an online survey on reputation risk among their readership.

He has over 30 years industry experience as both a marketing director and strategy consultant. He spent 12 years in the toiletries and cosmetics market rising to Marketing Director of the L’Oreal subsidiary Vichy in both UK and Germany. As a strategy consultant for the past 20 years he has worked with a variety of global clients interested in measuring intangible assets. At KPMG he helped develop a brand valuation methodology and his interest in reputation measurement comes from his experience as a brand strategist.
Appendix 3
Interviewee profiles

Interviewees
The interviewees were chosen from a range of industries to provide insights from different perspectives on measuring and managing the risk to corporate reputation. They represent stakeholder groups that finance professionals should be aware of and may even have to engage with.

Insurance perspective
Derek Atkins is non-executive director for the international insurance group Trust Holding Ltd and former UK strategy director for Royal & Sun Alliance (RSA). With over 30 years experience of the UK insurance industry, he lectures at Cass Business School and writes risk management and insurance textbooks for both the Institute of Financial Services (IFS) and the Chartered Insurance Institute (CII). He recently co-authored ‘Reputation Risk: Responsibility without Control’.

Governance perspectives
David Loweth is Technical Director of the Accounting Standards Board (ASB), part of the Financial Reporting Council (FRC), responsible for corporate reporting and governance; acting as regulator for the accountancy and actuarial professions. The FRC is not a public sector body; it is funded with one third from the government, a third from the accountancy profession via the Combined Codes Accounting Board (CCAB), and a third from business via the FSA levy from listed companies. As a result it has a number of stakeholders to consider with regard to its own reputation.

Bill Connell was Chair of the IFAC committee for Professional Accountants in Business (PAIB) between 2000 and 2006. The International Federation of Accountants (IFAC) is an umbrella body for accountants worldwide. CIMA is a member of IFAC and Bill served as a council member until June 2006; he has also previously chaired both Technical and International committees at CIMA. Bill spent 40 years working for the BOC Group in a variety of management roles, his last before retirement was Director of Risk Management for the Group.

Investor perspective
Guy Jubb is Head of Corporate Governance at Standard Life Investments. Guy’s team has frequent one-to-one meetings focused on corporate governance issues with directors of companies and company secretaries. These discussions are used as an opportunity to raise any concerns that he and his team have expressed in companies that they invest in. These concerns might range from executive compensation and compliance with legislation through to conflicts of interest and direction of strategy.

Legal perspective
Richard Slynn is a partner at the law firm Allen & Overy LLP and advises clients on corporate reporting. Allen & Overy, as a professional firm, has a responsibility to both its own reputation risk as a law firm and that of its clients, many of whom are leading international banks and financial institutions. Richard was assisted by two other partners, Heather McCallum, Head of Risk and Compliance, who spoke for risk from the firm’s perspective, and Tim House, a litigation partner and chair of the audit committee, who spoke for risk from the client’s perspective.
Risk perspective

**Cary Depel** is Compliance, Risk and Legal Director for IFX Markets Ltd, a London based firm of financial traders and market makers with offices in Boston, Sydney and Shanghai. He sits on the board, the Executive Committee and the Credit Risk Committee. He is also Chairman of the Institute of Risk Management (IRM) and a non-executive director. He has been a Director of a major UK stockbroker; Chief Legal Officer for the largest UK insurer; Special Counsel to Lloyd’s; and was in private legal practice in London and San Francisco. At the time of interview IFX Markets Ltd had just been acquired by City Index and his view on reputation covers broking and market making in equity derivatives and foreign exchange.

CIMA perspective

**Charles Tilley** is the CEO of CIMA which redefined its strategic purpose around creating employability for its members. CIMA is a lead partner in the Report Leadership group launched in November 2006 which aims to challenge established thinking on corporate reporting.

Corporate Communications perspectives

**Alan Knight** was the former Head of Social Accountability at SABMiller, a global brewer and bottler with a diverse number of issues from water supply to labour relations. Prior to that, he was Head of Social Responsibility for Kingfisher plc responsible for coordinating social and environmental policies, and before that Head of Sustainability at B&Q, part of Kingfisher plc. Alan is a member of the Sustainable Development Commission, a government think tank which reports directly to the Prime Minister. He is also an independent advisor to business on sustainable development.

**Richard Carpenter** is development director at Radley Yeldar, a corporate communications agency that specialises in corporate reporting. Radley Yeldar is one of the founding organisations behind the Report Leadership best practice guide on corporate reporting along with CIMA (Charles Tilley), PwC (David Phillips) and Tomkins (Ken Lever). Radley Yeldar publishes various reviews of narrative reporting, including a detailed critique of the content of the FTSE 100 reports.

Human Resources perspectives

**Mark O’Connell** is HR Director of Skandia UK, part of the Skandia group of insurance and investment companies, now part of Old Mutual Group. Skandia is a provider of investment and savings products for High Net Worth Individuals (HNWIs). The Skandia culture is based on five values: commitment, creativity, contribution, courage and passion. Skandia has no direct sales force and sells investment products through Independent Financial Advisors (IFAs), thus it is dependent on their competence, professionalism and probity to preserve its reputation. **Pauline Colvin**, the Chief Risk Officer for Skandia, was also interviewed.

**Margaret Gildea** is Executive Vice President of Human Resources – Operations and UK Employment and Skills Policy for Rolls-Royce and is responsible for 12,000 employees based in operation sites worldwide. Rolls-Royce is a global business providing power systems for use on land, sea and in the air. The group has a balanced portfolio with leading positions in the civil and defence aerospace, marine and energy markets. There are approximately 54,000 Rolls-Royce gas turbines in service. The group provides high-value, product related services to customers throughout the operational lives of their gas turbines. Rolls-Royce is a technology leader, employing 38,000 people in 50 countries.
Public Sector perspectives

**Terry Butler** was formerly Head of Social Services for Hampshire County Council and is now self-employed as an Adviser in Public Services and Social Care. He is a non-executive Director of the NHS South Central Strategic Health Authority and a non-executive council member on the General Social Care Council (GSCC). He is also the social care advisor for the National Patient Safety Agency (NPSA). Public health and social care provision at a national level incur reputation risk not only for government agencies but for ministers and politicians.

**Lynn Drennan** took up the post of CEO at ALARM (the national forum for risk management in the public sector) in 2006. Formed 16 years ago, ALARM has 1,800 members, two thirds of whom come from local government, the remaining third comprising members from the police, fire and other ‘blue light’ national public organisations. Prior to this Lynn was Head of Risk at Glasgow Caledonian University and co-author of *Reputation Risk: Responsibility without Control*.

**Minouche Shafik** is the Director General for Country Programmes at the Department for International Development (DfID) which is leading the British government’s fight against world poverty. DfID works in over 20 countries to address specific UN goals such as reducing hunger and infant mortality, and increasing access to education. DfID works with multilateral institutions such as the World Bank, United Nations and the European Commission, as well as its own offices in 67 countries. Prior to joining DfID Minouche worked for the World Bank.
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