

Reputation Management: Strategically Targeting Opportunities & Risks



Professor Paul Argenti
Tuck School of Business at Dartmouth

Goodwin Procter's 3rd Annual Director's Forum
March 3, 2009

“If you’re not managing your corporate reputation, you’re wasting a global corporate asset.”

-- Roy Vagelos, former CEO, Merck

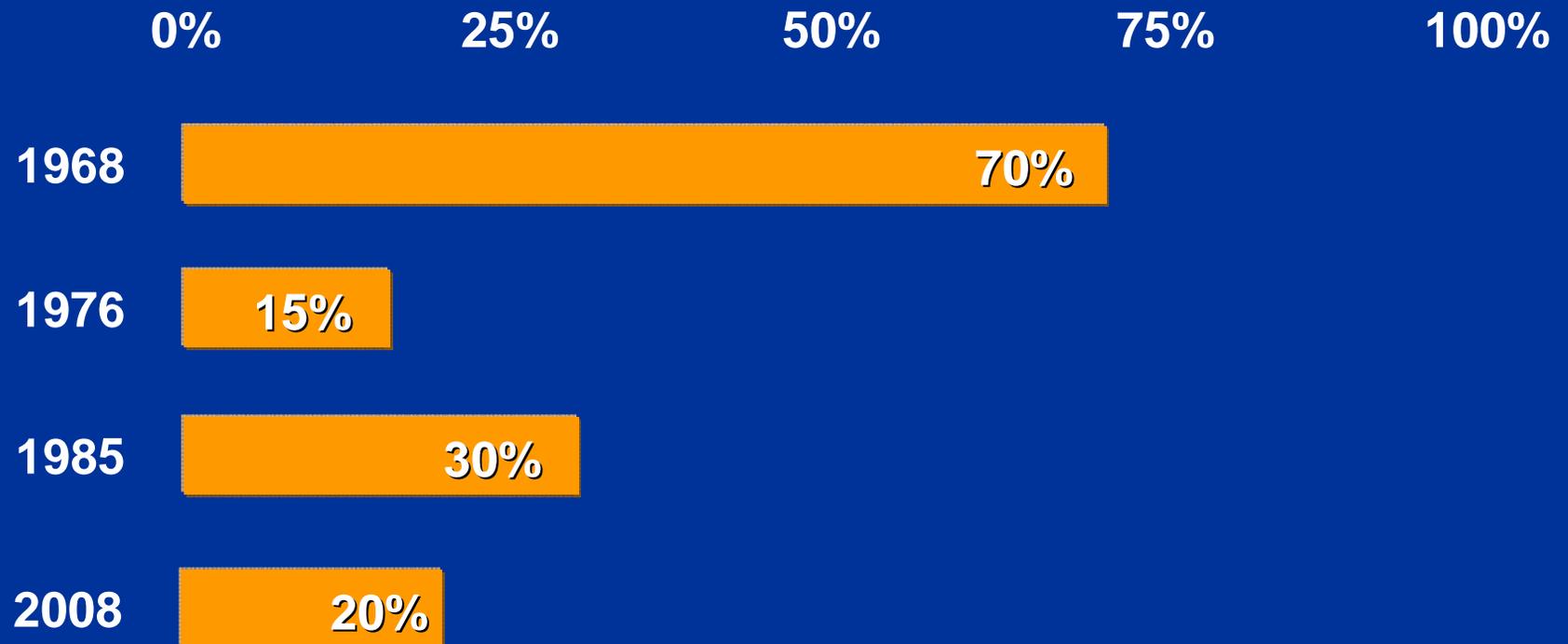
Reputation Management: Strategically Targeting Opportunities & Risks

- Understanding the uncertain environment for business
- Building reputation through strategic communication
- Engaging in reputation management as a director

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Does business act responsibly?



Business critics abound

- **64% say:** “Giant companies are too big to give reliable service to customers.”
- **65% say:** “Even well-known, established companies cannot be trusted to make safe, durable products without government standards.”
- **67% say:** “The quality of products from big companies has been slipping.”
- **88% say:** “Business is too concerned with profit and not concerned enough with responsibilities to workers, consumers, and the environment.”

2009 Edelman Trust Barometer: Trust in business down globally

- **62%** of people globally trust corporations less this year than they did last year
- **65%** of people globally want more government control over business to restore trust

Variety of factors go into building reputation & trust

How important is each of the following factors to building reputation?

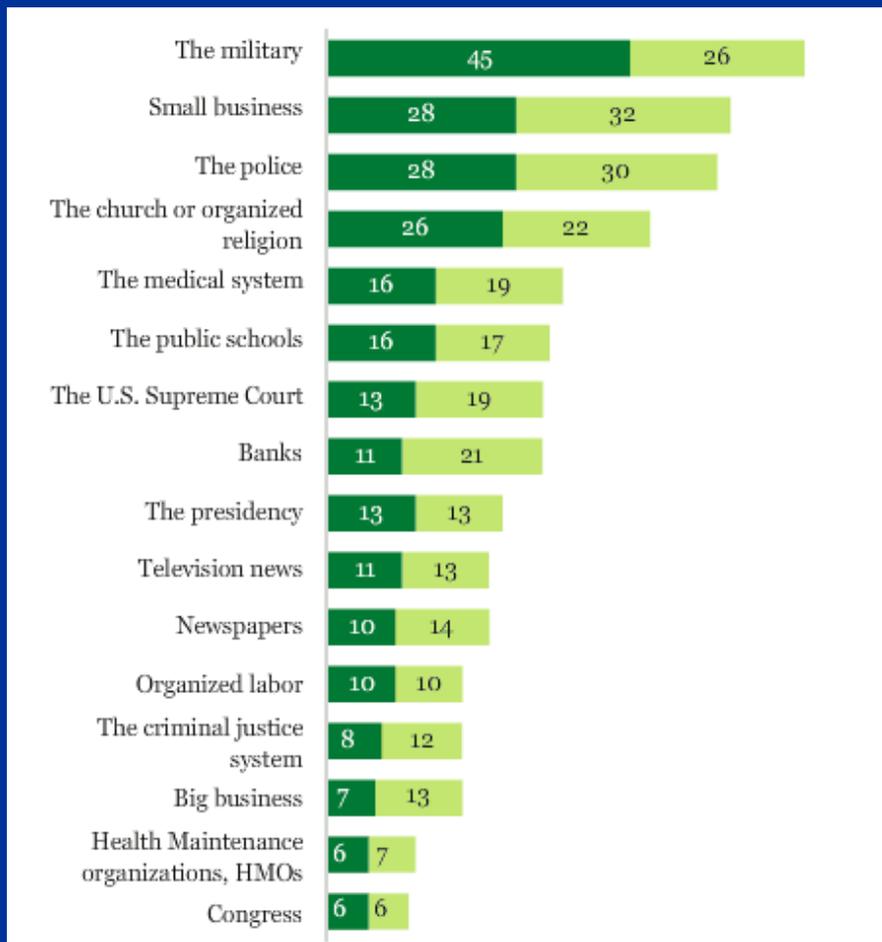


2009 Edelman Trust Barometer: Importance of constant communication

“The old order, in which business had the freedom to operate autonomously and without government restraint, is over”

- **Europe:** 75% of respondents want government to step in to prevent future financial crises
- **United States:** less than 50% of respondents think that the free market should be allowed to function independently
- Top factors in the reputation of a company include:
 - Communicating frequently and honestly on state of the business
 - Having a strong financial future
 - Committing time, money and resources to greater public good
 - Creating and keeping jobs in your area

Limited confidence in big business



Only 20% of US citizens say they have a “great deal” or “quite a lot” of confidence in big business

■ % Great deal ■ % Quite a lot

Gallup Poll—June 9-12, 2008

ARGENTI

Trust in institutions to operate in society's best interests

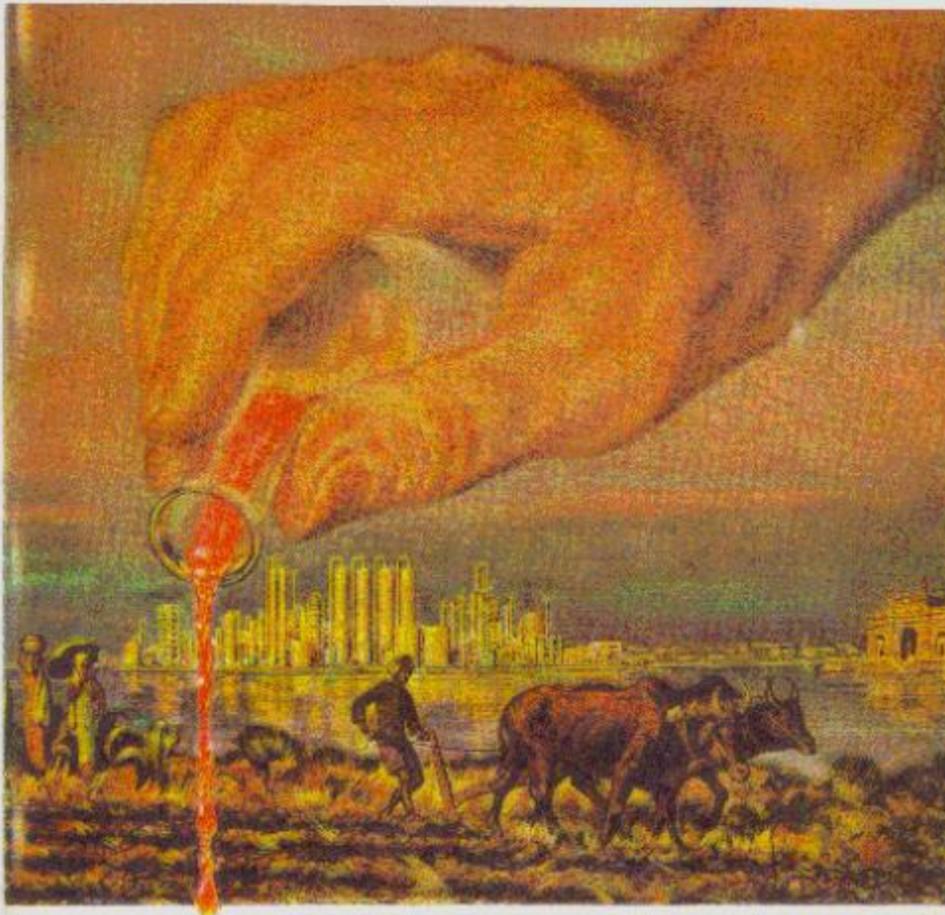
Armed forces	+43%
NGOs	+27%
Education system	+26%
Health system	+17%
Trade unions/labor	+2%
Legal system	-2%
Global companies	-9%
Large national companies	-10%

***“What matters is what the public thinks,
and the public trust is what’s
really crashed.”***

—Pete Peterson, Chairman of Blackstone Group

***“I blame the system, I blame greed.
Wall Street is really predicated on greed.
This could happen to any firm.”***

—Stephen Raphael, former Bear Stearns board member,
following J.P. Morgan Chase & Co.'s deal to buy Bear
Stearns for \$2 a share



Science helps build a new India

Oxen working the fields . . . the eternal river Ganges . . . jeweled elephants on parade. Today these symbols of ancient India exist side by side with a new sight — modern industry. India has developed bold new plans to build its economy and bring the promise of a bright future to its more than 400,000,000 people. ▶ But India needs the technical knowledge of the western world. For example, working with Indian engineers and technicians, Union Carbide recently made available its vast scientific resources to help build a major chemicals and plastics plant near Bombay. ▶ Throughout the free world, Union Carbide has been actively engaged in building plants for the manufacture of chemicals, plastics, carbons, gases, and metals. The people of Union Carbide welcome the opportunity to use their knowledge and skills in partnership with the citizens of so many great countries.

A HAND IN THINGS TO COME

WRITE for Sample R-2 "The Story of Union Carbide," a booklet describing the role of carbons, chemicals, gases, metals, plastics and nuclear energy being brought to you. A limited supply only. Write Union Carbide Corporation, 220 Park Avenue, New York 17, N. Y.





Tons of Toxic Waste Still Mark Bhopal Gas Leak

July 2, 2008: Nearly a quarter-century after gusts of poison gas leaked out of the Union Carbide pesticide factory here, killing thousands and turning this ancient city into a notorious symbol of industrial disaster, hundreds of tons of toxic waste still languish inside a tin-roofed warehouse in a corner of the old factory grounds, with a rolling, padlocked shutter for a gate.

At least now it is locked. For 20 years, it lay out in the open, in small mounds scattered around the compound. The waste has yet to be carted away. The factory grounds have yet to be cleaned up.

[Protestors] insist that the Dow Chemical Company, which bought Union Carbide in 2001, should pay for the cleanup. **Dow, based in Michigan, says it bears no responsibility to clean up a mess it did not make.**

"As there was never any ownership, there is no responsibility and no liability—for the Bhopal tragedy or its aftermath," Scot Wheeler, a company spokesman, said by e-mail.

Somini Sengupta, International Herald Tribune, July 2, 2008



Free flowing for instant protection

plus quiet power and performance you can feel at the wheel

New Mobiloil Special is the easiest year-around motor oil that flows freely over all cars and trucks. This means instant protection for vital engine parts—no matter how long it's been since you last changed oil. New Mobiloil Special keeps you other troubles away. It means less wear. It can even give your mechanical parts so completely new life you actually don't need to buy them. It means no more trouble, no more noise and quick plug fixing—in effect, it means the new look and feel of new parts. Your engine will run more quietly and smoothly—despite the same power and gas mileage. Get New Mobiloil Special—*feel the difference at the wheel!*



**New Mobiloil
SPECIAL**

*Best for older cars —
a "must" for new cars!*

Mobil Oil Co., P.O. Box 100, Dallas, Texas

Sold at Mobilgas Service Stations, Gas Houses

The New York Times

Justices Cut Damages Award in Exxon Valdez Spill

June 26, 2008: The Supreme Court on Wednesday reduced what had once been a \$5 billion punitive damages award against Exxon Mobil to about \$500 million. The ruling essentially concluded a legal saga that started when the Exxon Valdez, a supertanker, struck a reef and spilled 11 million gallons of crude oil into the Prince William Sound in Alaska in 1989.

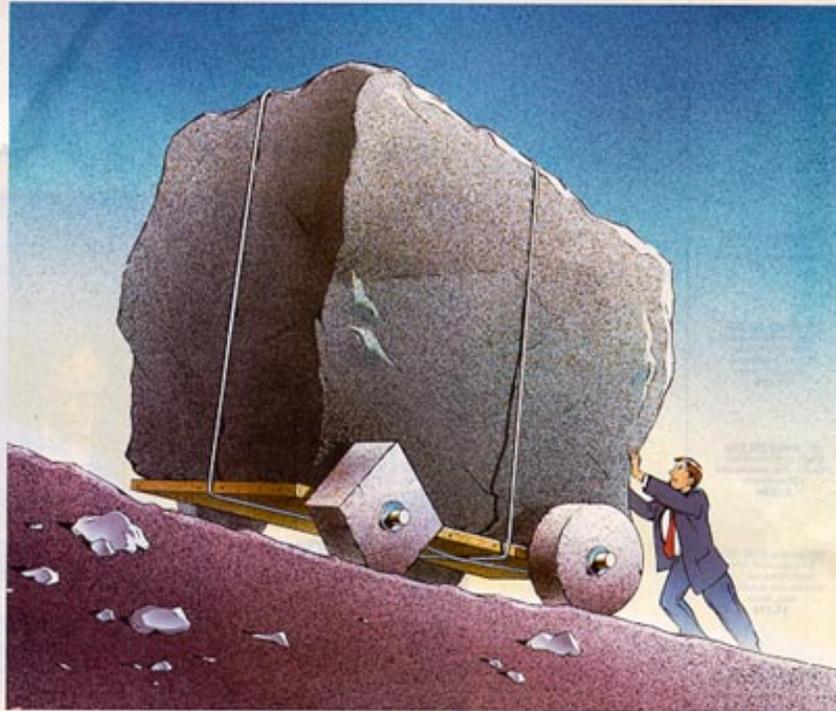
The Exxon Valdez spill was the worst in American history, damaging 1,300 miles of shoreline, disrupting the lives and livelihoods of people in the region and killing hundreds of thousands of birds and marine animals. It occurred after the ship's captain, Joseph J. Hazelwood, left the bridge at a crucial moment. Mr. Hazelwood, an alcoholic, had downed five double vodkas on the night of the disaster, according to witnesses.

When communication misleads

- Enron misrepresents reality and its values

When communication misleads

- Enron misrepresents reality and its values
- Arthur Andersen disregards regulators and clear signals



What's really holding your company back?

You'll find out when you discover your real business problems—the ones hidden in your underlying business practices.

And that's where our proprietary knowledge base of Global Best Practices can help.

In our trained hands, it lets us compare your operating practices to the best in the business world—within your own industry, and across the board.

So we can gain insight into what's slowing you down. And roll out more creative ways to help you reengineer your operations.

It's designed to be the most thought-provoking resource of its kind. Driven by an advanced application of CD-ROM technology. Updated

throughout our global network. And unsurpassed in its depth and scope.

To see a demonstration of our knowledge base or receive a brochure, call 1-800-445-5556, today. And find out how we can help you make lasting progress—on paper and in practice.

*Best Practices.
Putting insight
into practice.™*

**ARTHUR
ANDERSEN**



When communication misleads

- Enron misrepresents reality and its values
- Arthur Andersen disregards regulators and clear signals
- KPMG creates tax shelters that are illegal
- JetBlue vows to “bring humanity back to air travel” then cancels 1,000 flights in five days
- BP talks green but appears to be false

Cars should eat their vegetables, too.

Demand for low carbon transport fuel is growing. Fortunately, so are crops such as sugar beet, corn and wheat. At BP, we're partnering with DuPont to develop an advanced generation of biofuels made with local homegrown crops. The first of these, biobutanol can be blended in gasoline or co-blended with ethanol and gasoline. This new fuel has the potential to lower overall greenhouse gas emissions while reducing dependence on oil and expanding agriculture markets. It's a start.



beyond petroleum®

SPECIAL
Tech Buyers Guide

The ImClone
Mystery

7 Ways to Make
Flying Safer

More Fuzzy
Math at AOL

FORTUNE

Oink!

**CEO Pay
Is Still Out
Of Control.
Here's
Why.**

PLUS
The
Latest
Way to
Hide
Millions

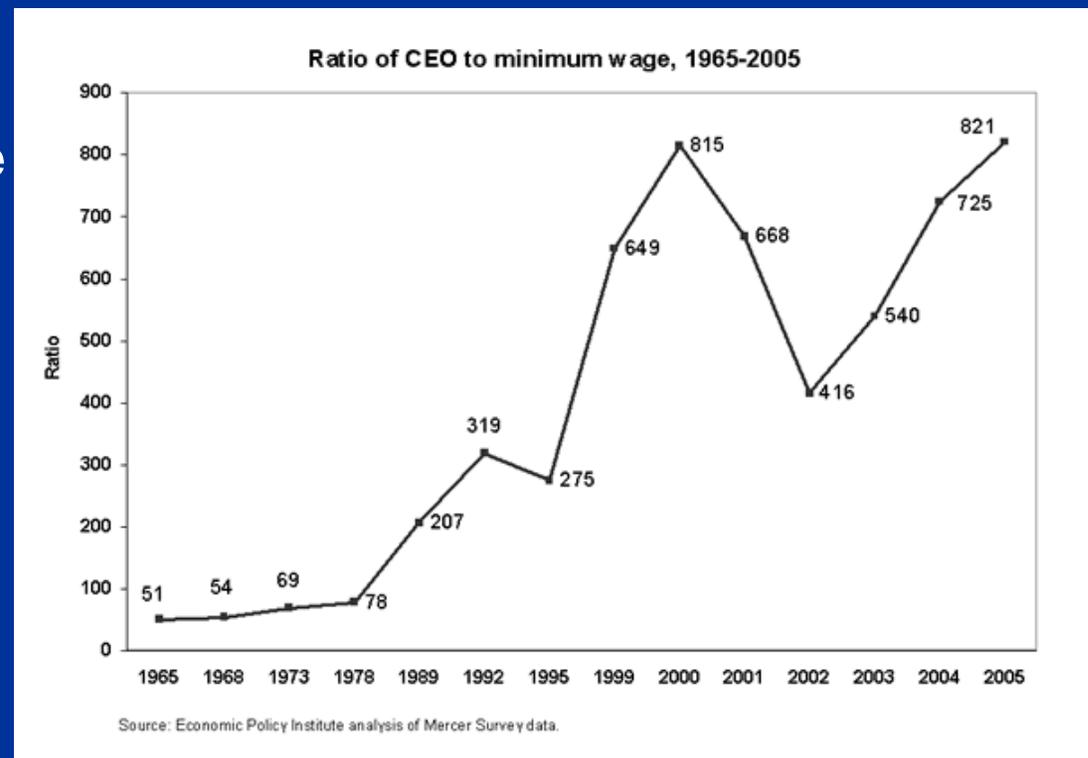
APRIL 28, 2003 \$4.99

www.fortune.com (AOL Keyword: Fortune)



Ratio of executive pay to worker pay

- An average CEO earns more before lunchtime on one day of work than a minimum wage worker earns all year
- Last year, the CEO of a Standard and Poor's 500 company made on average \$15.25 million in total compensation



Thanks for the memories



Bank CEO pay packages in the wake of the 2008 subprime mortgage crisis:

- **\$120 million** for Countrywide Financial CEO Angelo Mozilo
- **\$161 million** retirement package for ex-Merrill Lynch CEO Stanley O'Neal
- **\$39.5 million** in stock, options, bonus for ex-Citigroup CEO Charles Prince

(In the last two quarters of 2007 alone, the three executives' firms lost more than **\$20 billion** on investments in subprime and other risky mortgages)

Reputation affects not only firms but employees as well

- Employee quotes on working on Wall Street from recent *New York Times*:

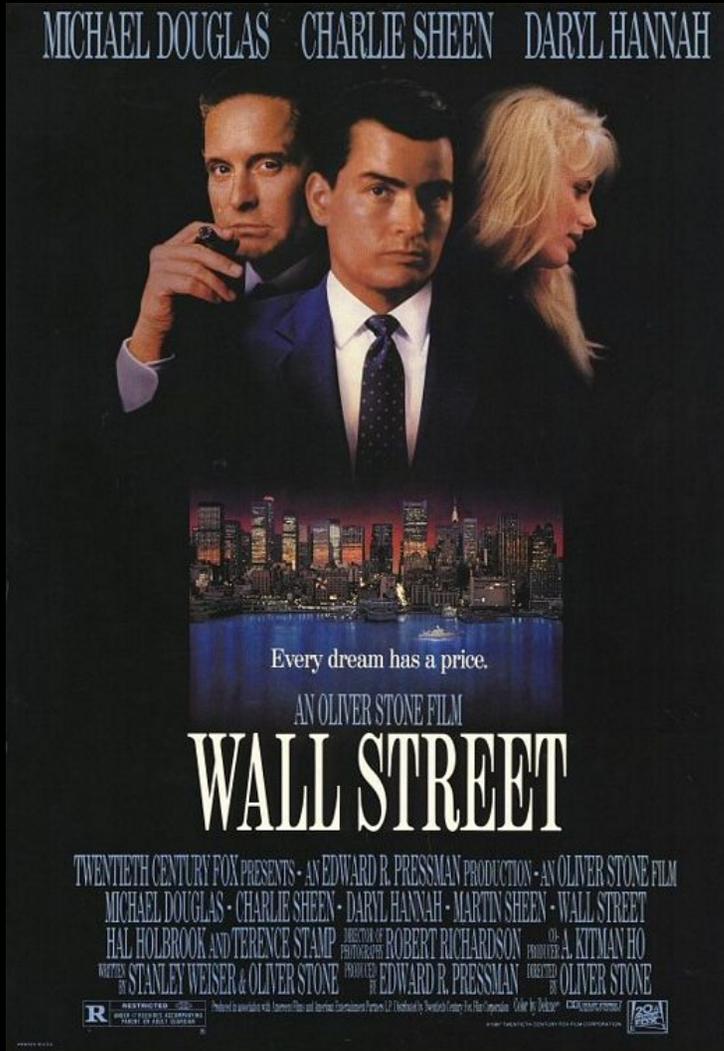
“Oh, you’re one of *THEM*...”

“I’d almost rather say I’m a pornographer,”
said a retired Wall Street executive who, for self-evident reasons, asked not to be identified.

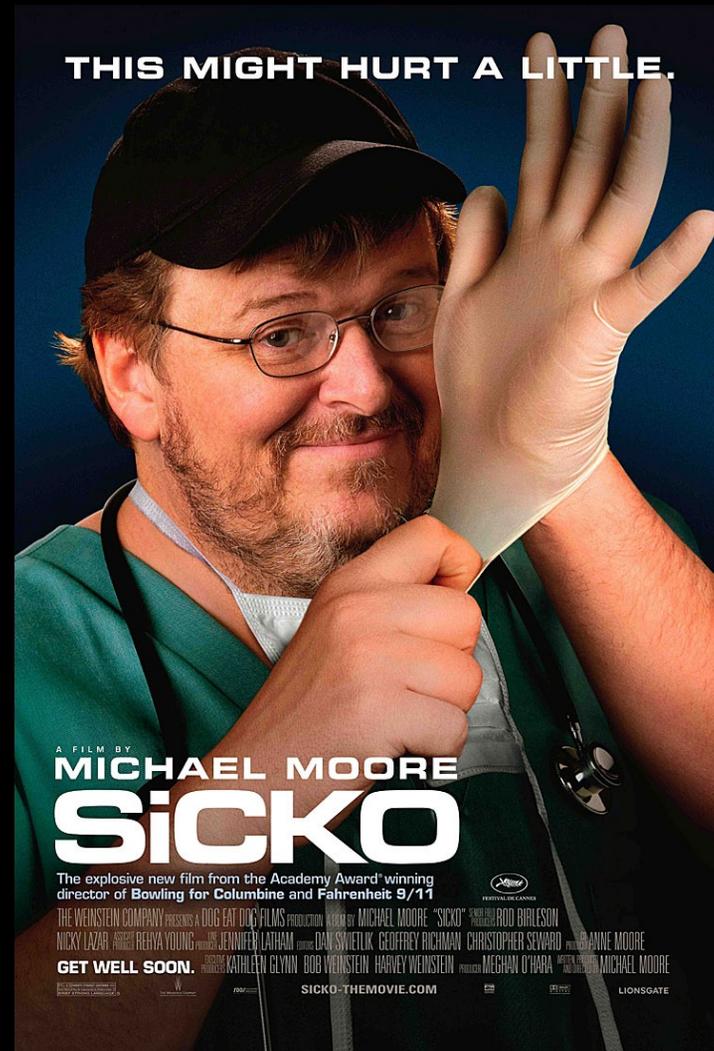
“At least that’s a business that people understand.”

Are executives overpaid?

Paris Hilton	\$6.5 Million
Britney Spears	\$9.1 Million
Alex Rodriguez	\$28 Million
Gisele Bundchen	\$35 Million
Rolling Stones	\$88 Million
Tiger Woods	\$100 Million
Oprah Winfrey	\$260 Million



1987



2007

Triggers of reputation failure

- In a Weber Shandwick survey, business executives cited these causes of reputation failure:
 - Financial irregularities 72%
 - Unethical behavior 68%
 - Executive misconduct 64%
 - Security breaches 62%
 - Environmental violations 60%
 - Health and safety product recalls 60%

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- Engaging in reputation management as a director

What is strategic communication?

Communication is strategic when it is completely consistent with a corporation's hierarchy of statements and able to enhance its strategic positioning and competitiveness.

A hierarchy of company statements

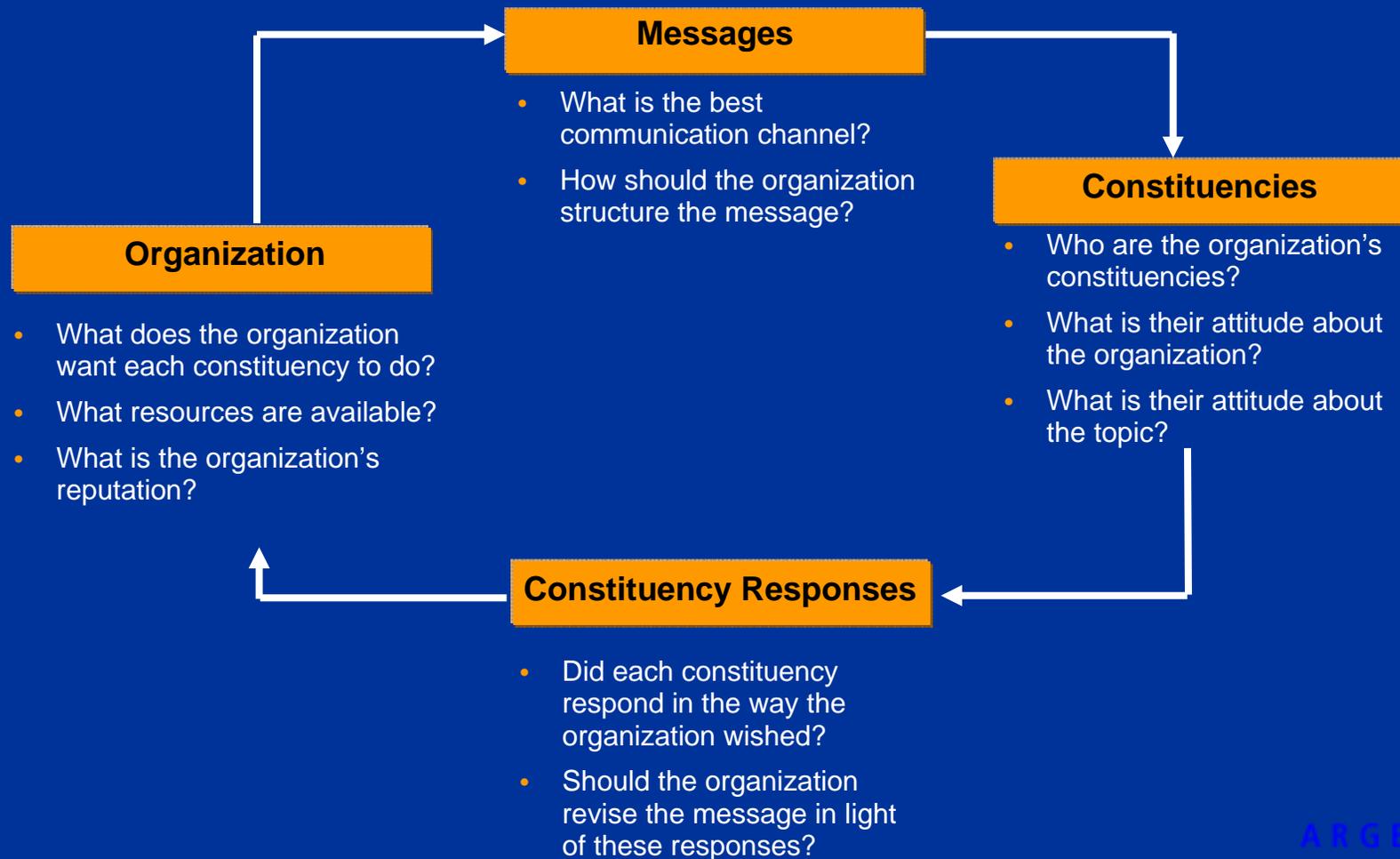
Mission: Why we exist

Values: What we believe in and how we will behave

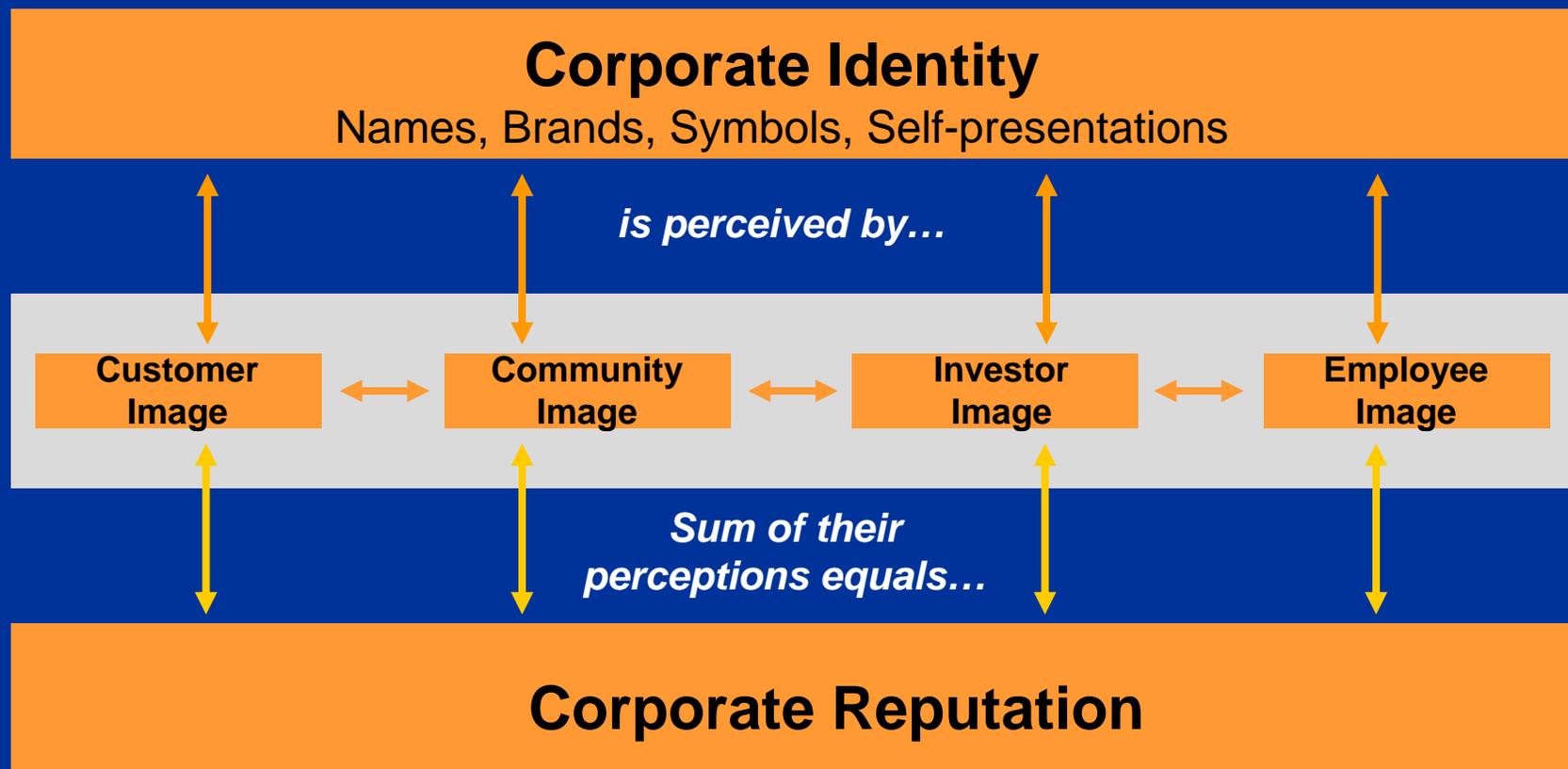
Vision: What we want to be

Strategy: What our competitive game plan/advantage will be.

Corporate communication strategy framework



What are Identity, Image and Reputation?



Why does reputation matter?

**Price
Advantage**

**Competitive
Advantage**

Stability

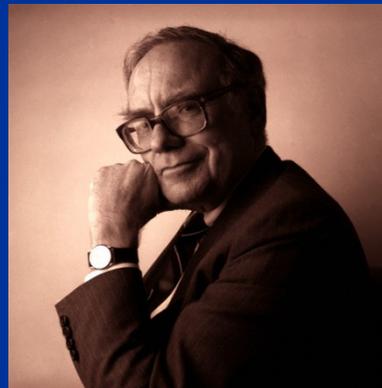
Companies with better reputations:

- Command premium prices
- Pay lower prices
- Entice top recruits
- Have more stable revenues
- Face fewer risks of crisis
- Experience greater loyalty internally and externally
- Are given greater latitude by constituents: Opportunity to operate
- Have higher market valuation and stock prices
- Have greater loyalty of investors, less stock price volatility

Measures of reputation

Fortune's Global Most Admired Companies 2008

1. Apple
2. Berkshire Hathaway
3. General Electric
4. Google
5. Toyota Motor
6. Starbucks
7. FedEx
8. Procter & Gamble
9. Johnson & Johnson
10. Goldman Sachs Group



BETHANY MULLAN ON
GOLDMAN
ON PAGE 130

FORTUNE

SEPTEMBER 2006 \$6.99

"Was there any
chance he'd find
more things and more
and go on? In reality
conditions like to bring
and how much... to get
more to take good?"
—Steve Jobs

AMERICA'S MOST ADMIRABLE COMPANIES

APPLE IS NO. 1!

IN AN EXCLUSIVE
INTERVIEW STEVE JOBS
TELLS HOW
HE GOT THERE.

(PAGE 62)

PLUS

THE TROUBLE WITH STEVE JOBS

YES, APPLE'S ON TOP BUT DOES
THE CEO'S RECKLESS BEHAVIOR
PUT THE COMPANY AND
ITS SHAREHOLDERS AT RISK?

BY PETER BRKIND

(PAGE 58)



The tangible value of strategic communication and reputation

Interbrand & *Business Week's* Best Global Brands

<i>Brand</i>	<i>Value (\$M)</i>
1. Coca-Cola	\$65.3
2. Microsoft	\$58.7
3. IBM	\$57.1
4. GE	\$52.0
5. Nokia	\$34.0
6. Toyota	\$32.1
7. Intel	\$31.0
8. McDonald's	\$29.4
9. Disney	\$29.2
10. Mercedes-Benz	\$23.6

Relationship between reputational capital & risk

- The fluctuating value of the company's reputation is its **reputational capital**
- “**Reputational risk**” is the range of possible gains and losses in reputational capital for a given firm.

Reputational capital

- Provides a platform from which other investment opportunities may arise—similar to R&D in this respect:
 - **Upside example:** sound corporate citizenship improves relations with constituency groups and provides a holistic approach to implementing strategy
 - **Constituency groups** include Community, Employees, Customers, Activists, Regulators, Suppliers, Partners, Investors, and Media
 - **Downside example:** Loss of reputational capital comes from these same constituency groups; threats include rogue behavior by employees, defection by partners, and the threat of legal action by regulators



Toyota U.S. Operations	
Plants	10
Jobs	386,000*
Investment	\$13 B



Being a good corporate citizen starts with hiring lots of good citizens.



WHAT'S A GOOD CORPORATE CITIZEN? It's not about awards or mission statements or press releases. It's about people. People who care about what they do and how they do it. And at Toyota, we know these people pretty well, because we hire them every chance we get. You see it in every vehicle we build here.** Our over 32,000 team members

take pride in everything they do. Quality, teamwork and dependability, that's what they are all about. Our team members care about doing what's right; at work as well as in their local communities. They really are good citizens. Which in turn makes Toyota a better corporate citizen. Isn't it nice when things work out?



TOYOTA
toyota.com/usa



"This is our drop."

Water sustains us. Conservation unites us.

Although water is one of the earth's most plentiful natural resources, less than 1% is available fresh water. Today, over 1 billion people lack access to safe drinking water, and water shortages threaten thousands of animals and habitats that could be lost forever.

Water is critical to sustaining nature, communities and businesses. Our organisations, The Coca-Cola Company and WWF, have come together to conserve and protect freshwater resources in key ecoregions around the world. By bringing our networks, people and brands together, we believe we can achieve meaningful and large-scale results.

With WWF as a key partner, The Coca-Cola Company will further improve the use of water across our bottling operations and with our agricultural partners. Committed to reducing our environmental impact, we are setting measurable targets for these improvements. In addition, we are collaborating on climate protection as we recognise the impacts of climate change on the water cycle.

For several years, we've been working together on freshwater conservation projects to protect river systems that are vital to the people and the wildlife that depend on them. Now, as part of our global partnership, we are focusing on seven watersheds from Asia to the Americas.

Water is a top priority for both our organisations, and drop by drop, we know we can accomplish far more together than we can on our own.

If you'd like to join us on this journey or want to find out more about our partnership, visit the-coca-cola-company.com and panda.org/water/cocacola.

The Coca-Cola Company



Reputational risk

- *Commercial Bank Examination Manual* says reputational risk:
 - “is the potential that negative publicity regarding an institution’s business practices, **whether true or not**, will cause a decline in the customer base, costly litigation, or revenue reductions... can also cause liquidity constraints and significant depreciation in market capitalization.”
- Product offerings affect reputation risks. Reputational risk (along with credit risk and legal risk) increases the more controversial a product is
- Companies need to manage reputation risks in the same way as operational or financial risks are assessed, audited, and managed

A CNBC ORIGINAL PRODUCTION



THE DESPERATE STRUGGLE
AND THE PLANS TO REGAIN GLORY



All industries are susceptible to reputational risk

Life Sciences

- Animal rights
- FTC/FDA action on drugs already approved
- Lack of transparency around drug pricing, “price fixing” allegations

Financial Institutions

- Loss of client information / privacy and data security
- Now seen as greedy and responsible for current financial crisis

Airlines

- Safety concerns surrounding any news of accidents
- Union strikes and fear of service delays
- Perceived handling of changing security threats

Technology

- Customer privacy and data security
- Monopoly allegations and legal issues during M&A
- Revenue recognition and financial scrutiny

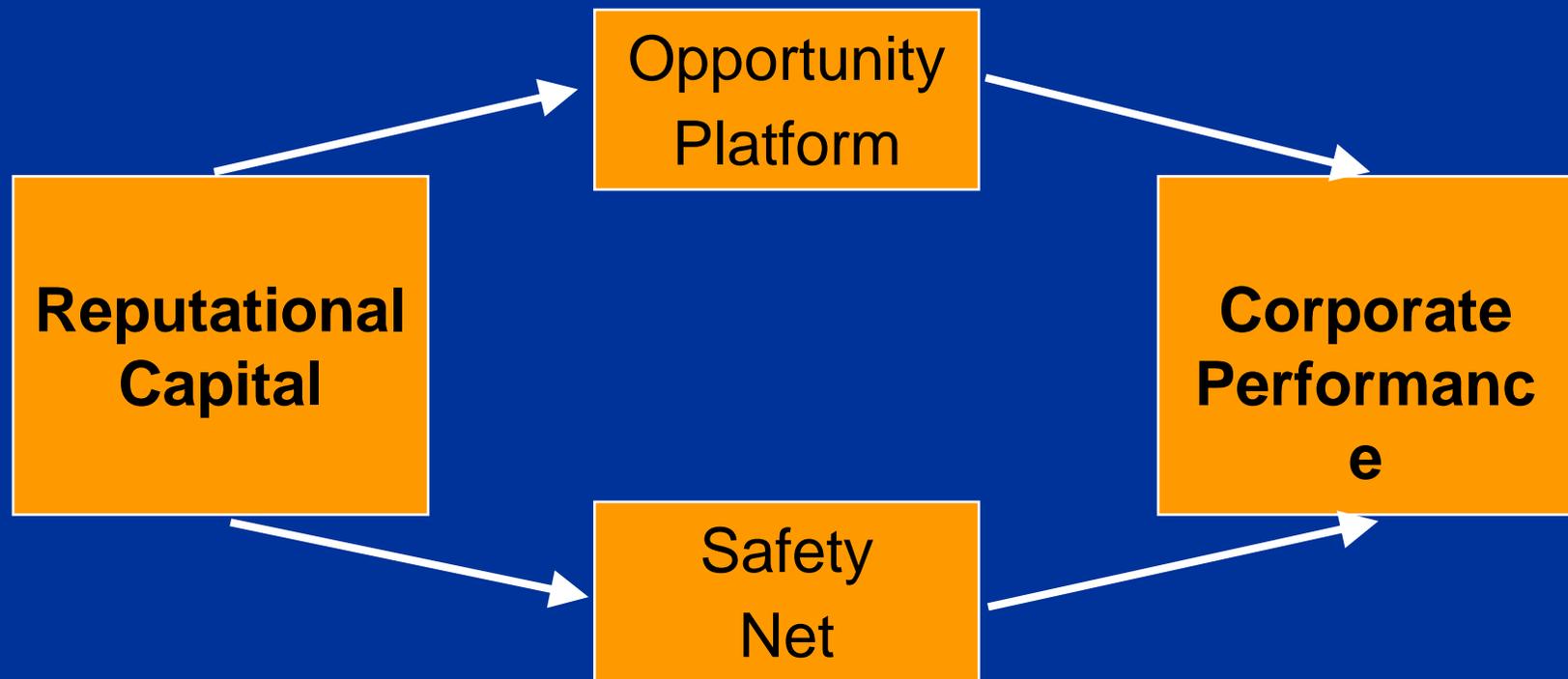
Energy

- Environmental concerns
- Consumer price backlash
- Service interruptions

Automotive

- Safety/Recalls
- Environmental issues and natural resource fears
- Labor issues
- Fears of bankruptcy

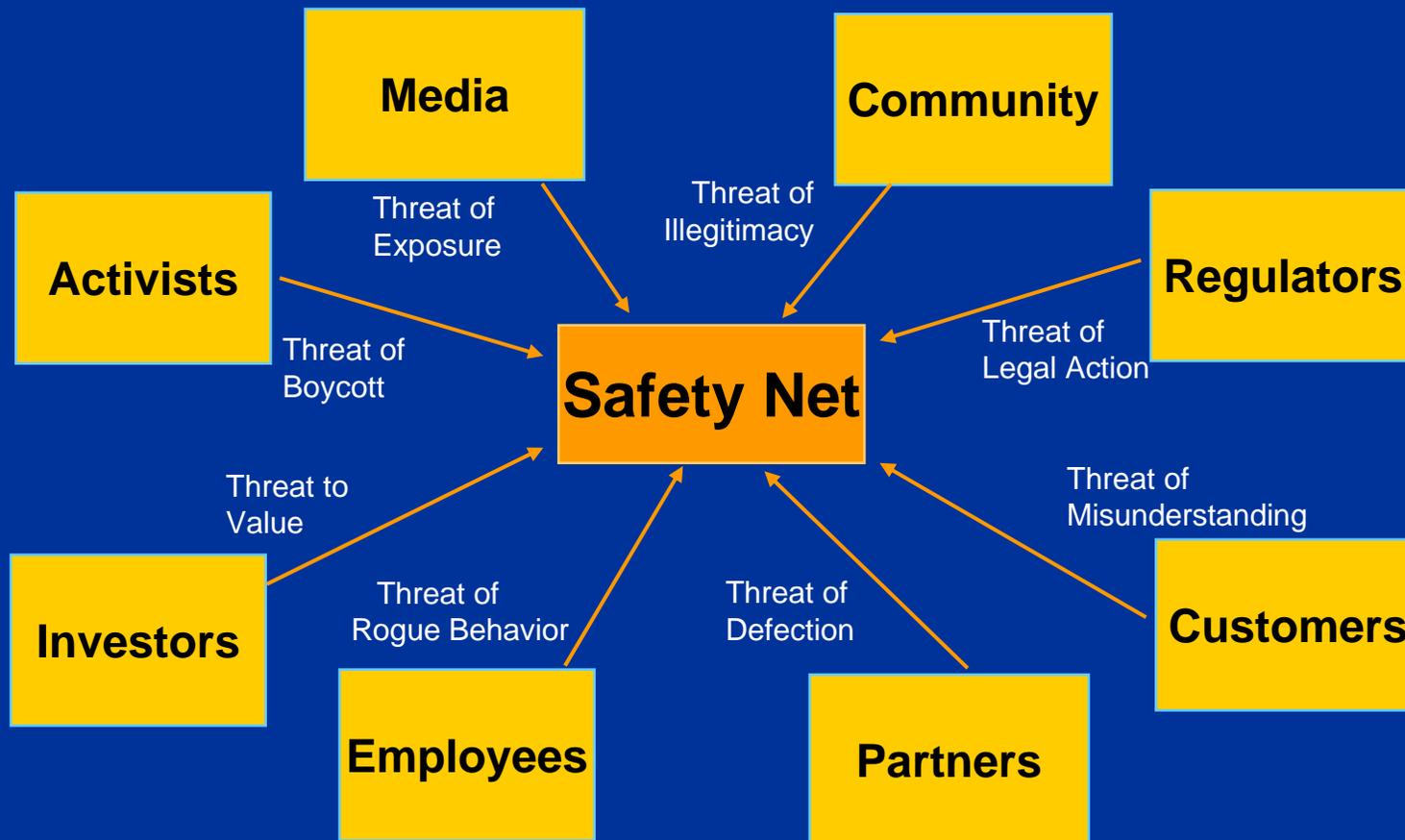
Reputational risk management cycle



Managing the upside of reputational risk



Managing the downside of reputational risk





THE MOST HATED MAN IN NY

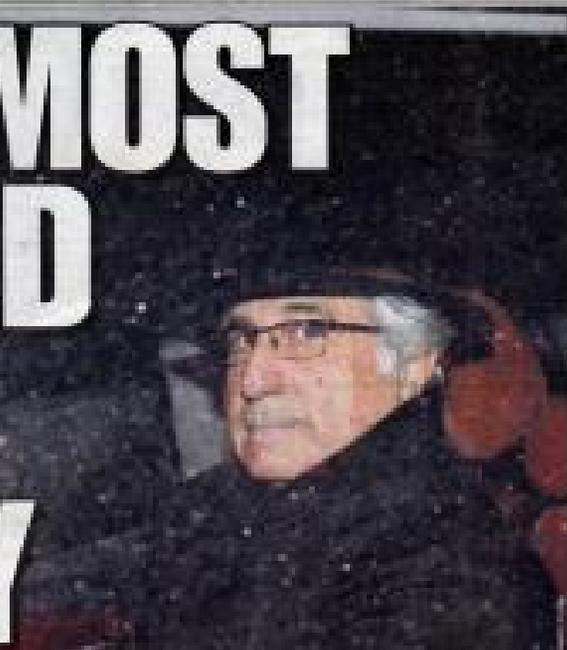


PHOTO EXCLUSIVE

Bernie Madoff skulks from his Manhattan penthouse



CAROLINE: I WANT HILL'S SENATE SEAT

PAGE 3

How to manage a company's reputation

- Assess company's current reputation
- Assess key constituencies' perceptions of company
- Determine who influences them
- Create forum to manage reputation
- Locate reputation in the context of issues management
- Determine key areas of reputational risk
- Measure effectiveness of communications on reputation
- Invest in opportunity platform

Reputation environment is changing

The evolution of communications requires a new approach to reputation measurement



“So for us – and for all like-minded companies – our past behavior was like money in the bank. It gave us a reservoir of good will that we could draw upon in our hour of need.”

--Anne M. Mulcahy, chairman and CEO, Xerox Corporation

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The Board and reputation

- The Board of Directors can help prevent reputation crises by setting a strong tone from the top emphasizing:
 - **Strong governance and internal controls:** making investments in strong risk management, internal controls, and compliance systems
 - **Accountability:** to this end, the Board should keep good records of all Board actions and involvement, including detailed minutes of all meetings
 - **Transparency:** ensuring full cooperation during internal and external audits and investigations
 - **Objectivity:** the Board should always strive for an objective, thoughtful, and thorough decision-making process

A board gone missing: Lehman Brothers 2008

LEHMAN BROTHERS

- **March 2008:** Veteran corporate governance researcher The Corporate Library rated Lehman's governance risk "high" after examining its annual proxy statement
- The Corporate Library's main concerns included executive compensation and Board composition:
 - The Board awarded CEO Dick Fuld \$71.9 million earlier in 2008, ranking him in the top 2% of American CEOs
 - Half of Lehman's 11 directors are over the age of 70; nine are retired; one is a theater producer; another a former Navy admiral; only two have direct experience in the financial services industry
- **"Our board is a joke,"** said one Lehman executive who asked to remain anonymous

A board gone missing: Lehman Brothers 2008

LEHMAN BROTHERS

- **Sept. 10, 2008:** five days before Lehman Brothers filed for bankruptcy CEO Dick Fuld said the Board had been “wonderfully supportive” in a conference call
- The Board’s eerie absence before and after the bankruptcy announcement prompted many to question whether they played any role monitoring the company’s ongoing risk accumulating its fatal portfolio of real estate assets and securities

Lehman Brothers employees’ graffiti on a portrait of Lehman Brothers CEO Richard Fuld, Jr. outside the NYC headquarters
(Sept. 15, 2008, *Associated Press*)



Boards need to be more proactive about reputation & long-term management

- **According to a recent McKinsey survey:**
- Directors want to spend more time developing long-term strategies to maximize shareholder value
- Yet directors say they need more information...
 - Only 45% of directors report that they have “good” access to key company performance data and leading industry indicators
- ...and rarely have substantive discussions with management about reputation & long-term management
 - Less than half of directors consider global trends and future scenarios when developing value creation plans

To meet the challenges of our current business environment, boards must change

- As companies grapple with uncertainty of a magnitude that few have experienced before, their boards should begin by questioning fundamental strategic assumptions:
 - Is our view of the market realistic?
 - Does our financing strategy take into account the new conditions?
 - Should we reset the incentive scheme or abandon any approach based on share prices?
 - Can we exploit the current glut of talent?
 - How can we take advantage of the pain our competitors are experiencing?
 - **How can we preserve and strengthen our reputation during these challenging times?**

How should companies manage reputational risk?

- Prepare for potential problems
- Develop a response *before* a crisis hits
- Look for ways to create an opportunity platform
- Analyze constituencies reactions in advance and respond appropriately
- Get managers to see that waiting for problems to happen is more costly in the short run and potentially damaging to your reputation in the long run
- **Keep the board involved and engaged throughout the process**

Why building reputation matters

- Today's dynamic business environment poses substantial risks to corporations
- Reputational risk assessment and management—evolving in this dynamic environment—is critical
- Corporations must tie corporate communication closely to core strategy and values
- Building an opportunity platform based on reputation can protect against risks, prevent crises, and build a trust reservoir with stakeholders
- The board of directors plays a key role in preserving, building and managing reputation

After our break...

**From Theory to Practice:
Reputation Case Study Breakout Session**

Reputation Management: Strategically Targeting Opportunities & Risks



Professor Paul Argenti
Tuck School of Business at Dartmouth

Goodwin Procter's 3rd Annual Director's Forum
March 3, 2009

Reputation Management: Strategically Targeting Opportunities & Risks

- *From theory to practice:* introduction to today's case breakout sessions
- Break into industry groups to discuss cases
- Re-convene to review insights from breakout sessions
- Review key takeaways on reputation management

Reputation Management: Strategically Targeting Opportunities & Risks

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Reputation management: From theory to practice

- This session will allow you to put what you have learned into practice:
 1. We will break into industry interest groups so you may work on a case that is relevant to your industry
 2. In your groups, read the instructions and the case and discuss
 3. Focus on the questions posed to you and incorporate concepts from earlier this afternoon
 4. Have someone record your ideas and prepare a brief presentation for the larger group about the case

Overview of cases

Financial Services

Hanover Investments

New England-based investment management firm trying to preserve business while navigating the financial crisis

Life Sciences

GENECO

Small Cambridge biotech company in the process of bringing its first revenue-generating drug to market

Technology

Abraxis Systems

Mid-sized hardware manufacturer preparing for a challenging quarterly earnings announcement

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Case review for life sciences:

GENECO

- Small Cambridge biotech company in the process of bringing its first revenue-generating drug to market
- Preliminary data from Phase 2 drug trials raises cause for concern and company must decide how, if at all, to disclose this information
- Then, the company's key development partner and main investor, Jetson & Jetson, comes under FDA scrutiny for unexplained side effects with one of its drugs

Case review for technology: Abraxis Systems

- Mid-sized hardware manufacturer preparing for a challenging quarterly earnings announcement
- Faced with some important issues regarding questionable revenue recognition processes as it prepares 2008 taxes
- Then, CEO, who is figurehead of company, raises concern when he is unable to work due to long-term unexplained but serious illness

Case review for financial institutions: Hanover Investments

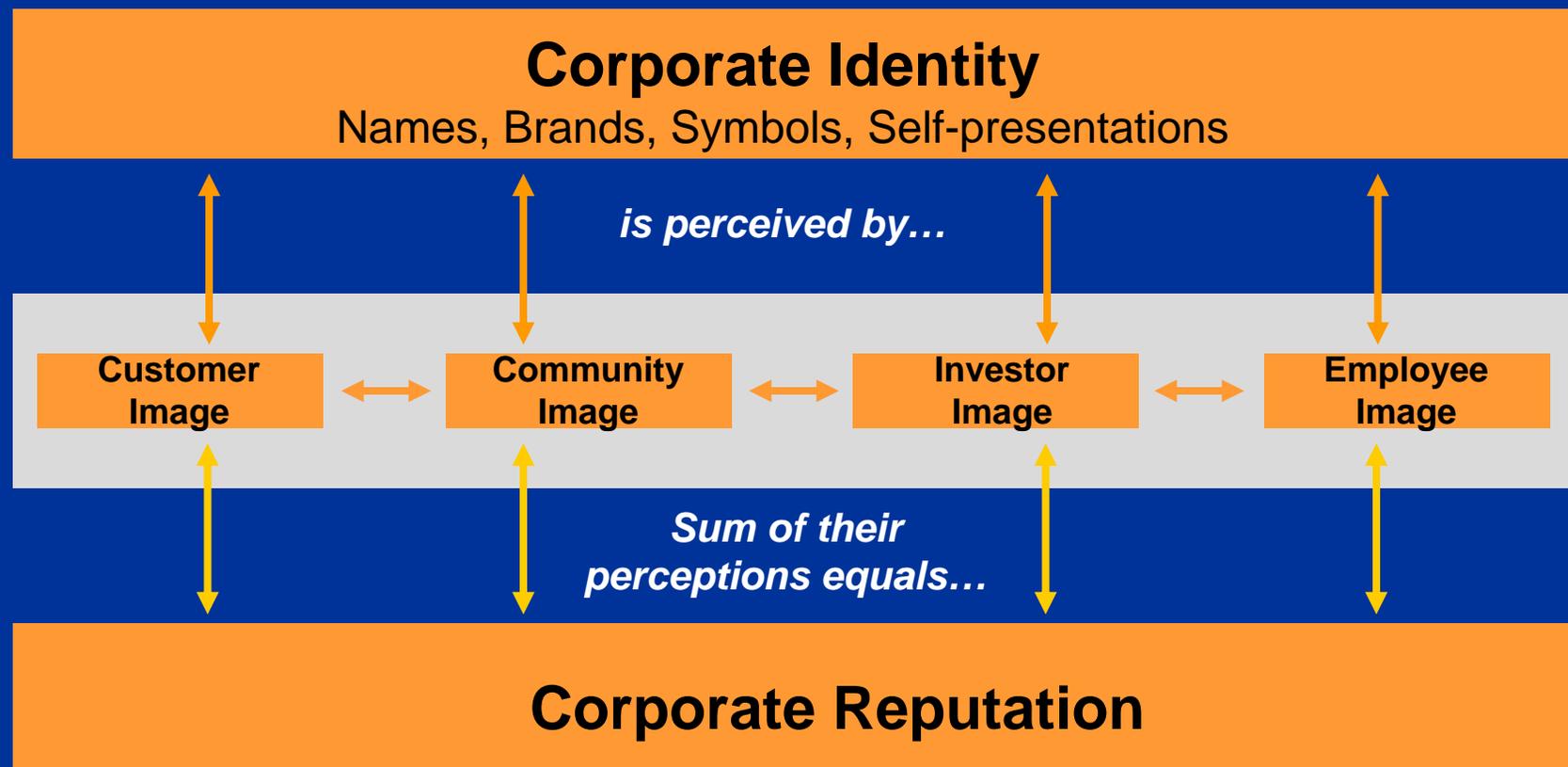
- New England-based investment management firm trying to preserve business while navigating the financial crisis
- Its owner, a bank holding company which has a similar name, is under intense scrutiny and has accepted TARP funds; confusion exists among constituents between the two companies
- Then, CEO falls victim to the Maxell ponzi scheme and clients are increasingly concerned about the security of their funds

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Review

What are Identity, Image and Reputation?



Review

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Review

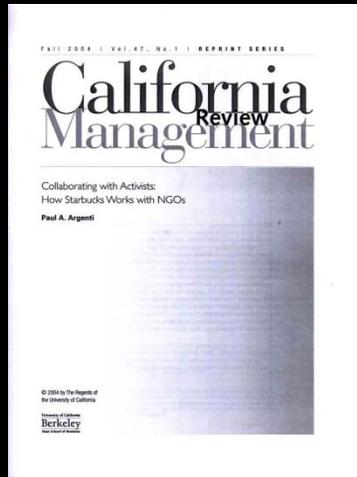
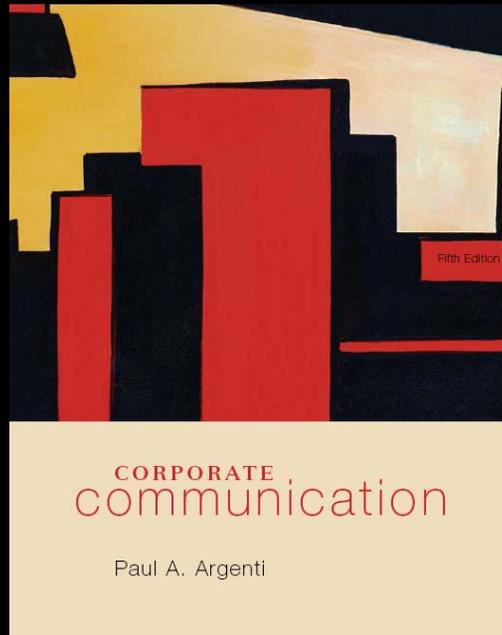
Why building reputation matters

- Today's dynamic business environment poses substantial risks to corporations
- Reputational risk assessment and management—evolving in this dynamic environment—is critical
- Corporations must tie corporate communication closely to core strategy and values
- Building an opportunity platform based on reputation can protect against risks, prevent crises, and build a trust reservoir with constituents
- **The board of directors plays a key role in preserving, building and managing reputation for all constituents**

“If you lose dollars for the firm by making bad decisions, I will be understanding. If you lose reputation for the firm, I will be ruthless.”

-- Warren Buffet, CEO, Berkshire

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