



## Can't Run, Can't Hide: New Rules of Engagement for Crisis Management

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The corporate apologies are piling up. Mattel CEO Robert Eckert apologized before a Senate subcommittee on September 12 for lead paint found in millions of the company's toys. On September 14, TD Ameritrade CEO Joe Moglia apologized for a database breach that compromised customer addresses, phone numbers and email addresses. Apple CEO Steve Jobs apologized on September 6 for cutting the price of the high-end iPhone to \$399 just weeks after die-hard customers waited in long lines to pay \$599. Dell executives apologized in August on the company's corporate blog for delayed deliveries of certain laptop and desktop models. And in February, Jetblue apologized for canceling 250 flights during an ice storm and leaving some passengers on the tarmac for as long as 11 hours.



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The common thread linking these apologies: Executives were moving quickly to stem damage to their companies' reputations. And while not all corporate crises are created equal, there is a playbook to handle these events, according to professors at Wharton. First, a corporate response should take hours, not days. It should include a well-thought out apology delivered through multiple mediums and it should feature some remediation so that the event won't happen again.

The stakes are high. Companies that manage these events well tend to preserve a good reputation. Those companies that take a long time to respond to a crisis may be permanently scarred by customer perception. What's different these days, say Wharton experts, is the speed with which the Internet and globalization have facilitated the dissemination of information. This means that word of mouth -- both good and bad -- travels farther and faster than ever.

An example of this is Jobs' open letter, which came with a \$100 credit at Apple's retail or online stores for those who bought the iPhone on its June 29 launch. It was posted on Apple's site a day after the company announced the iPhone price cut. "We want to do the right thing for our valued iPhone customers," the letter said. "We apologize for disappointing some of you, and we are doing our best to live up to your high expectations of Apple."

### Three Categories of Crisis

Customized responses to a crisis are critical given that not all crises are the same. [Maurice Schweitzer](#), a Wharton operations and information management professor, puts crises in three primary categories: Customer service issues, "failures of competence" and "screw ups that aren't related to core competence." The third category refers to incidents such as Martha Stewart's stock trading scandal. Although Stewart served jail time, the incident didn't reflect on her core competence, which is giving advice on home decorating, food and entertaining.

Dell's inability to fulfill orders for some laptops and Apple's iPhone price cuts are customer service issues, says Schweitzer. The goal here is to keep customers from giving up on the company. "When

Apple unveils its next product, it wants to avoid having people feel like suckers," says Schweitzer. "Apple doesn't want customers to wait [to make their purchase] the next time they launch a new product."

JetBlue's failure to get customers to their locations in February and Mattel's manufacturing troubles in China are examples of "failures of competence," says Schweitzer. Both companies had problems that should have been prevented. In Mattel's case, "the last thing parents want to worry about when they give a child a toy is safety."

Mattel's safety issues, adds Wharton marketing professor [Lisa Bolton](#) require a response that appeals to consumers' emotions. Indeed, Mattel's Eckert addressed parents' concerns directly in his September 12 testimony before the Senate Committee on Appropriations Subcommittee on Financial Services and General Government. "Like many of you, I am a parent," he said. "I, like you, care deeply about the safety of children. And I, like you, am deeply disturbed and disappointed by recent events. As to lead paint on our products, our systems were circumvented, and our standards were violated. We were let down, and so we let you down. On behalf of Mattel and its nearly 30,000 employees, I apologize sincerely.... We are doing everything we can to prevent this from happening again."

### **Literate in Multiple Media**

To get its message out to its customers, Mattel utilized online media, its web site and video. More importantly, Mattel reacted quickly. Of those steps, speed may be the most important factor, says [Yoram \(Jerry\) Wind](#), a Wharton marketing professor and author of the forthcoming book, *Competing in a Flat World* (Wharton School Publishing). "The Internet means that there is full transparency and you cannot hide. Anything can be distributed worldwide. Management has to respond fast and effectively."

Ron Culp, a managing director at public relations agency Ketchum, agrees, noting that the traditional news cycle, where daily newspaper deadlines dictated how companies managed crisis communications, doesn't exist any more. A company facing a crisis used to have at least a day to respond, but now the timetables are speeded up as blogs and online news operations report stories faster than traditional media outlets. "Just a few years ago, I knew if I got a call at 10 a.m., I would have until 5 p.m. to respond with an answer (to an inquiry)," says Culp. "Today, I need to respond by 10:05 a.m."

Culp also notes that companies have to be literate in multiple media. Traditional outlets, for example, are increasingly monitoring blogs, or online diaries, for tips. By reaching customers directly via blogs, companies in crisis can deliver a more effective message. "The best approach is posting the corporate response on the company's web site and allowing the bloggers to take it from there," says Culp. "The traditional media follow." Given the new dynamics, he recommends that companies continually monitor all news sources, especially blogs, where potential problems may surface. "Companies have to be all over the Internet as a starting point."

To remain nimble enough to react to a never-ending stream of online chatter, [Thomas Donaldson](#), Wharton professor of legal studies and business ethics, recommends that companies create a team devoted only to crisis communication. The team can then tailor a company's response quickly and is able to avoid corporate bureaucracy. When a crisis strikes, a CEO can't ask his corporate counsel for advice because it only slows up the communications process, says Donaldson. "Companies must take the hit, get all the dirt out and move on. That means letting corporate lawyers into the office, but saying 'no' to them even though a corporate response may raise liability issues."

Finally, companies -- especially those that are multinational -- need to consider how a message will be received globally. For example, Mattel has to consider American attitudes about Chinese workers taking jobs away from the U.S. manufacturing sector just as much as it has to consider how to craft its safety message, says Donaldson. "Mattel must assure people that the company is going to source globally and do it safely. The problem is, a lot of people don't want to believe that."

### **Anatomy of an Apology**

The linchpin of any reputation recovery process is a believable apology. According to Wharton marketing professor [Lisa Bolton](#), three key components ensure that an apology will work: The CEO must deliver the message, a solution to a problem must be outlined and some remuneration should be in place. The initial response is the most important," she says. "The general advice is to admit mistakes and try not

to be defensive. Get out in front of the story. Get your admission and mitigation out there as well, and consider financial compensation. Also, customize your response in relation to the magnitude of the failure."

Schweitzer says an apology that isn't sincere and doesn't offer a solution won't be effective. "People have to believe an apology is credible." Bolton agrees that credibility and likeability are key, but, she adds, remuneration may be most important. "You have to ... consider financial compensation as well as the emotional response." She suggests that one of the things that made Apple's apology effective was Jobs' offer of a \$100 credit. Adds Schweitzer: Jobs' apology and the Apple credit went a long way "to convincing customers that the company cares about them."

Wind, however, has a different take on the Apple case, noting that many recent apologies have been hampered by inadequate remediation steps. Jobs' remuneration, he says, could have been better. "Apple gave a \$100 credit against future purchases. The sum is pretty arbitrary. These are your best customers. They waited all night [to buy the phone] and you give them half of what a new customer got. Why not \$200? Why not \$250 to show that Apple really values its pioneers? Imagine how much bang Apple would have gotten if they had given those customers a \$250 discount."

Companies need to consider these various crises as ways to win over customers, Wind adds, suggesting that if Dell has to delay a shipment, it should offer a loaner PC or laptop. "Most companies don't appreciate the incredible value of the customer. They look at these events and panic. They are missing new opportunities."

### **Building Reputation Points**

Experts at Wharton say the success of a corporate reputation reclamation project depends on the company's image when a crisis hits. "The starting point matters a lot," says Donaldson. "The old saw that a reputation takes years to accumulate, but can be destroyed overnight, is only half true. If you have a good reputation, you are given the benefit of the doubt. If a company has a bad reputation, it gets the detriment of the doubt."

Donaldson cites Warren Buffett's Berkshire Hathaway as an example of a company that benefited from a good reputation when a crisis occurred. In 2005, Maurice Greenberg, CEO of insurer American International Group (AIG), was forced to resign over questionable transactions. Berkshire Hathaway's insurance firm General Re had a role in the AIG transactions. Although Buffett wasn't directly involved, he could have been tarnished, says Donaldson. "The reputation of Berkshire Hathaway really mattered when General Re was getting hammered. The media gave Berkshire Hathaway every benefit of the doubt because of Buffett."

In other words it makes sense for companies to "build up a reservoir of goodwill," says Thomas Dunfee, a legal studies and business ethics professor at Wharton. Dunfee studies corporate social responsibility (CSR) and whether it has an impact on business results. "There's an argument that companies should make the extra investment in doing good and [engaging in] philanthropy," says Dunfee. "The idea is that a company can build up social credits if something goes awry."

The issue with this line of thinking is that it is hard to quantify what social activities provide the most protection, Dunfee acknowledges. "The common assertion is that CSR activities can provide some inoculation [from future crises], but there hasn't been anything empirically established." Most companies, he adds, invest in their local communities, but it's unclear whether that makes a crisis any easier. Other activities -- such as contributing to the arts -- may provide little or no effect.

According to Bolton, a big part of reputation management is anticipating problems and then heading them off before they become lingering issues. For example, Disney on September 10 said it will independently test for lead paint those toys that feature its characters, such as Mickey Mouse figurines. "Disney is testing to try and get ahead of the Mattel story," says Bolton. "That's how you get a good reputation in advance. This testing will help: If there are future problems, at least the customer will know Disney was being proactive. It's much better to prevent something and get a good reputation than to try and fix it later."

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