Managing Risks for Corporate Integrity:
How to Survive an Ethical Misconduct Disaster

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Headlines:
Scandals, Diminished Trust, and Ethical Disasters

☆ Corporation Fined $3.4 Billion
☆ EEOC Slams Business
☆ Share Value plummets
☆ Dept. of Justice Investigations and Indictments
☆ Ponzi Scheme CEO Arrested
☆ Company Shuts Down in Wake of Scandals
☆ Customers and investors lose confidence
☆ Business Reputation Tarnished
Corporate Ethical Misconduct Disasters

Is your company prepared for preventing, mitigating, responding, and recovering from serious employee ethical misconduct (EMD) contingencies?

Estimates of Direct and Indirect Business Losses in the US from MAJOR Natural Disasters

- 2008 Hurricane Ike $12 billion
- 1993 Midwest Floods $19 billion
- 1992 Hurricane Andrew $30 billion
- 1988 Midwest Drought $39 billion
- 1994 Northridge Earthquake $44 billion
- 2005 Hurricane Katrina $108 billion
- Total 2005 Atlanta Hurricane Season $128 billion
Estimates of Direct and Indirect Business Losses from MAJOR Ethical Misconduct Disasters

- Sears $6 billion
- Marsh $16 billion
- Coca-Cola (1999) $34 billion
- Coca-Cola (2002) $15 billion
- Health South $27 billion
- Tyco $40 billion
- AIG $70 billion
- ENRON/Arthur Anderson >$188 billion

ENRON as the Hurricane Katrina of Ethical Misconduct Disasters

- The Cost of Corporate Recklessness calculated direct business/value losses related to the Enron disaster at more than $200 billion.

- These estimates include lost investment savings, jobs, pension losses and tax revenue. The report estimated that more than a million workers lost their jobs at the affected companies and those indirectly impacted.

- Further, the costs to businesses, stakeholders, and management include hundreds of millions in litigation costs; punitive and compensatory fines; tarnished brands, images, and reputations; and loss of consumer and investor confidence.
ENRON as the Hurricane Katrina of Ethical Misconduct Disasters

- In the 2 ½ years following the implosion of Enron, it is estimated that world capital markets lost between $4 and $7 trillion, believed to be attributable to the ENRON ethics disaster scandal which ruined pension plans, crashed equity value, costing jobs, wiping out investments, and left an enormous hole in the US and world economy.

Loss Risk of an Ethical Disaster

- Ethical breakdowns can disrupt your business operations just as significantly as can natural disasters, data loss, accidents, and deliberate malevolent acts.

- Such scandals can have enormous costs, impact your business, wound your reputation and brand, anger your stakeholders, and potentially land senior management in prison.

- No company is immune from these threats. Prudent businesses must plan to manage integrity continuity by assessing their vulnerability to ethical disasters, taking proactive measures, and preparing their organizations to mitigate and survive when such scandals break.
Real Risks of Ethical Misconduct Disasters?

- Recent revelations about ethical misconduct scandals make the prospects of the “unthinkable ethical disaster” a realistic concern.
- NBES data suggest that once the economy rights itself and business difficulties recede, misconduct is likely to rise.

Disastrous Scandals are not far-fetched possibilities for any organization

- Mutual Fund industry Scandal
- Health South
- Omnimedia
- Olympic Figure Skating Judging
- Head coaching resume fraud at Notre Dame and Vanderbilt
- Helmsley Hotels
- Sunbeam
- National Baptist Convention
- Roman Catholic Church
What is an Ethical Misconduct Disaster “worth?”

- Disrupt Business Operation
- Negatively Affect Performance
- Depress valuation, credit worthiness, and market value
- Litigation costs
- Criminal Charges – fines and prison
- Labor Problems
- Fraud costs
- Brand, Reputation and Image damage
- Some companies never recover and cease operations leading to loss of pensions, jobs, and regional economies

Catastrophic Impact of an Ethical Disaster
The Costs of Ethical Misconduct
Disasters

Integrity and the Value of your Image, Brand, and Reputation

Texaco Settles Race Bias Suit for $176 Million

EEOC
U.S. Equal Employment Opportunity Commission

SMITH BARNEY
CITIGROUP
The Costs of ignoring the Risks of Ethical Misconduct Disasters are Significant

Major Categories of EMD

- Harassment (Ethnic, Sexual, etc.)
- Criminal & Illegal Activities
- Fraud & Falsifying Records
- Discrimination
- Customer/Client Deception
- Bribery & Improper Influence
- Failure to Adhere to Policy/Regulations
- Corruption & Unethical Decisions
- Undisclosed Conflict of Interest
EMD Risks

• 62% of companies experienced a significant EMD (enough to disrupt routine operations) between 1986-1996.

EMD Risks

• One study found that 76% of MBA graduates anonymously reported that they were willing to commit fraud to enhance their profit reports to management, investors, and the public.

• Nationally, less than 50% of employees believe that their employers are people of high ethical integrity.
EMD Risks

- One study found that 30% of all employees “know or suspect ethical violations such as falsifying records, unfair treatment of employees, and lying to top management.”

EMD Risks

- The Ethics Resource Center (www.erc.org) reported in its National Business Ethics Survey that “one in two employees witnessed at least one specific type of misconduct.”

- At least 52% of employees observed at least one type of misconduct in the past year, while the percentage of employees willing to report the misconduct has dropped by 10 percentage points.

- CFO.com projection forecasts up to 20 “major” business EMDs every year.
Public vs. Private Sectors

- Employees who report that they know of significant instances of ethical misconduct or illegal activities:
  - Private Sector – 41%
  - Public/Government – 57%

EMD Is Under-reported

- 60% of employees know of instances of misconduct but have not reported violations.
  - They cite the lack of confidentiality policies or the fact that existing ones won’t protect them.
  - They fear “whistle-blower” retaliation.
Passive “Ethical Policies” Alone Are Inadequate

- Formal Codes of Conduct and Ethics Statements alone are insufficient.

- Active not Passive Ethics Efforts

- Ethical concerns must be regarded as on par with other business disruption/resumption concerns

Integrity Continuity

- *Integrity continuity* planning is also a due diligent policy and business continuity priority.

- Such planning must go beyond compliance issues and reactive disciplinary policies to actually manage integrity.

- Employees who know that certain workplace decisions, behaviors, and processes exist in an ethically judged context are more aware and motivated to act ethically.
Integrity Management

- LeClair (1998): “If your organization is dedicated to integrity management, then training and education should be used to reinforce the core values, cultural elements, and policies that buffer misconduct. In fact, there is little chance of creating a high integrity workplace without training, educating, and reinforcing ethical values … Your organization must create a solid connection between its mission, ethical values, and culture and the policies and systems designed to prevent legal violations.”

Managing Ethical Misconduct
Disasters: The RADAR© Model

- **Recognize** - by defining the issues, threat forecasting, risk assessment, anticipate
- **Anticipate** - by developing proactive ethical leadership, ethics/compliance programs
- **Discover** - by actively communicating and monitoring, formal and informal means
- **Answer** - by on-going oversight, integrated systems, and rapid actions
- **Recover** - by diligent restoration, repair image, stabilize situation, and resume work
The Value of Protecting against the Risks of EMDs

- Good business strategy
- New Federal Sentencing Guidelines
  - UFSGO
  - SOX
- Stakeholders demand it
- It is the right thing to do

Resources

Managing Risks for Corporate Integrity
E-businessethics.com provides a source of information on business ethics, corporate citizenship and organizational compliance.

The goal of e-businessethics.com is to create a virtual community of organizations and individuals that share best practices in the improvement of business ethics.

Much of the content is being provided by businesses, nonprofit organizations, government agencies and academics that support interactivity and accessibility of information.

The ability to access research, publications, resources, linkages and training devices provides an opportunity for both academic and business communities to support business ethics.

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- Ethics Inserts in NASBA Publications
- Student Centers for the Public Trust on college campuses
- Scholarship Programs
Jeff Immelt, CEO of General Electric

• “One concern that keeps me up at night is that among the 300,000-plus GE employees worldwide, there are a handful who choose to ignore our code of ethics. I would be naïve to assume a few bad apples don’t exist in our midst.”

• 2002 letter to GE shareholders
Managing Risks for Corporate Integrity: How to Survive an Ethical Misconduct Disaster

By Brewer, Chandler, and Ferrell

Managing Risks for Corporate Integrity helps readers identify, illustrate, and define the business problem of ethical misconduct as it lays out a practical guide to develop plans to prevent, mitigate, cope with, respond to, and survive ethical disasters in organizations across industry. It also illustrates how the process of ethical disaster recovery planning involves an assessment of an organization’s values, development of an ethics program, an ethics audit, and the ability to create contingency plans for potential ethical dilemmas.

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  • Released December 2009
  • visit www.amazon.com

• Forthcoming
  • From Praeger Publishers, anticipated Summer 2010

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Dr. Chandler is available for consulting or to provide on/off-site presentations, seminars, training, development workshops and more. Please contact him with RFP or scheduling sessions

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