CLEANING UP YOUR ACT

An Ethical Approach to Crisis Management

By MARK S. SCHWARTZ, WESLEY CRAGG & W. MICHAEL HOFFMAN

One of the biggest concerns for CEOs, senior executives and board members is waking up one morning to discover they are facing a crisis that could potentially threaten the very existence of their firms.

What would you do, for example, if you were the CEO of a major chemical company, and you discovered that a poisonous gas leak from your pesticide plant had led to the deaths of thousands of people living in the vicinity? Or if you were the CEO of a major global beverage chain, and it came to your attention that one of your employees had charged an ambulance crew for cases of bottled water that were needed for survivors of the 9/11 terrorist attacks?

Far from being hypotheticals, these are all-too-real cases faced by the CEO of Union Carbide in 1984 and the CEO of Starbucks in 2001.

In the Union Carbide case, the CEO insisted that company operations in Bhopal, India, met all existing safety standards that were

LIFESAVING
TOOLS FOR CRISIS
MANAGEMENT

legally mandated in India at that time, and he blamed sabotage instead. That commenced long and messy legal battles that continue to this day, with some $470 million paid in compensation and several executives convicted for causing death by negligence.

In the case of Starbucks, calls to management were initially ignored – until the story was published, stirring up an Internet-based consumer boycott of Starbucks. Only then did the ambulance workers get their money back and the CEO apologized.

It didn't have to end up this way. Consider another case of a major pharmaceutical company that discovered people were dying from one of its most popular medicines: How did it respond? And when the media accused a producer of canned tuna of killing dolphins that were getting caught in its fishing nets, did it simply ignore the complaints or did it take immediate action?

These well-known stories of Johnson & Johnson and StarKist are still held up as textbook cases of how one should respond to a crisis.

In 1982, when seven deaths were linked to the taking of Tylenol capsules, the CEO of Johnson & Johnson ordered a nationwide recall of all Tylenol products. While the poisoned capsules appeared to be an isolated criminal act limited to the Chicago area, the company took no chances. Although costly, the openness and honesty with which Johnson & Johnson handled the incident transformed the Tylenol brand into one of the most trusted on the market, and led to the development of tamper-resistant packaging and safety seals.

For its part, StarKist announced in 1990 that it would no longer purchase tuna captured in nets that trapped dolphins, and then added "Dolphin Safe" to its labels, gaining significant competitive advantage over other tuna companies in the process.

Fortunately, more firms are realizing the importance of preparing for potential crises like these. The academic and consulting worlds have also entered the arena, providing both theoretical and practical guidance for firms.

However, most of the information related to crisis management is treated within the field of strategic management or disaster/risk management. This has resulted in less attention being paid to the ethical dimensions of crisis management, in spite of the fact that ethical considerations lie at the core of most crises.

Based on our combined decades of experience and research in the areas of ethics, compliance and responsible business, it is our contention that executives who ignore the ethical dimensions of crisis management expose themselves to serious risks that can lead to the collapse of their firms. In this article, we analyze the 2010 BP oil spill in the Gulf of Mexico to highlight some key principles that can help executives to skillfully manage the crises they may face during their professional lives, with greater responsibility and integrity.

What Is a Crisis?

The definition of an organizational crisis by the academics Christine M. Pearson and Judith A. Clair remains as relevant today as it was when proffered in their 1998 paper, "Reframing Crisis Management": "An organizational crisis is a low-probability, high-impact event that threatens the viability of the organization and is characterized by ambiguity of cause, effect and means of resolution, as well as by a belief that decisions must be made swiftly."

To this definition of a crisis the dictionary adds these nuances: "the turning point for better or worse" and a "decisive moment."

Building on these definitions, we focus our discussion on one type of crisis that an organization can face – an ethical crisis – which we would define as a decisive moment caused by a severe ethical lapse, requiring the firm and its leadership to decide whether it will react based on a set of ethical values and principles, or based primarily on financial objectives.

Examples of such crises include: product defects that risk causing serious harm;

EXECUTIVE SUMMARY

Executives who ignore the ethical dimensions of crisis management expose themselves to serious risks that can lead to the collapse of their firms. The authors use the 2010 BP oil spill in the Gulf of Mexico as a cautionary example of what happens when a company fails to make decisions based on and directly connected to a set of core ethical values, such as trustworthiness, responsibility, caring, citizenship, respect and fairness. They outline how to construct an ethical corporate culture, which will make firms better equipped to deal with a crisis when it occurs, so that they emerge stronger and more respected as a result.

environmental disasters; illegal conduct, such as bribery; and breaches of human rights.

While ethical crises do threaten the viability of an organization, our view is that they also present important opportunities for organizations to strengthen and communicate their commitment to the responsible management of their business activities and their potential impacts.

Moreover, firms that demonstrate their ethical commitment through their response to a crisis not only are more likely to survive, but can emerge stronger and more productive as a result.

In this regard, we concur with Peter Snyder et al. who stated in "Ethical Rationality: A Strategic Approach to Organizational Crisis" that "crises challenge the explicitness of a firm's ethical beliefs and the level of its top management team's conviction to them."

In other words, it is not merely the competence of executives and managers that determines whether a firm's response to a crisis will be successful, but the extent to which the firm's executives and managers ground their responses in a set of core ethical values.

A Case to Remember

To illustrate this point, let's analyze a real-life case that put one company's commitment to ethical values to the ultimate test.

The facts are these: On April 20, 2010, an explosion occurred aboard the Deepwater Horizon, an oil drilling rig connected to the oil company BP in the Gulf of Mexico, which resulted in the death of 11 workers.

A lengthy struggle to plug the oil leak ensued, until the well was finally capped on July 15, 2010, by which time upwards of five million barrels of crude had been discharged into the ocean.

Outcomes of the disaster – the largest offshore oil spill in U.S. history – included significant environmental damage to the wildlife in the region, severe damage to the fishing and tourism industries along the Gulf coast, as well as a collapse in the value of BP shares on international markets.

What lessons can we learn from BP's management of this crisis?

Core Ethical Values

While there are many possible ethical values, we believe that the following core ethical values are both universal in nature and critical to a firm that desires to take an ethical approach to crisis management. In fact, as Jim Collins and Jerry I. Porras assert in their best-selling book, *Built to Last*, companies that are guided by core values similar to those we list here, and that have a sense of purpose beyond just making money, tend to enjoy superior returns over many decades.

1. TRUSTWORTHINESS. This implies several other associated values: honesty, keeping promises, integrity, transparency and loyalty. If a firm does not act in a trustworthy manner throughout the entire response to a crisis, it has failed from an ethical standpoint.

In the wake of the BP Deepwater Horizon oil spill, U.S. President Barack Obama set up a National Commission to investigate what went wrong. The findings are available for viewing or downloading at www.oilspillcommission.gov.

▪ ABOUT THE AUTHORS

Mark S. Schwartz is Associate Professor of Law, Governance and Ethics at York University's School of Administrative Studies in Toronto, Canada. He received his J.D. from Osgoode Hall Law School at York University, and his MBA and Ph.D. specializing in business ethics from the Schulich School of Business at York University. He has received numerous research and teaching awards in the field of business ethics. His most recent book is *Corporate Social Responsibility: An Ethical Approach* (Broadview Press, 2011).

Wesley Cragg is the Director of the Canadian Business Ethics Research Network, Senior Scholar and Professor Emeritus of Philosophy and Business Ethics at York University and the Schulich School of Business in Toronto, Canada. He received his B.Phil. and D.Phil. from Oxford University, U.K. His academic specializations include: business ethics; corporate social responsibility; sustainability; the ethics of resource extraction; and business and human rights.

W. Michael Hoffman is the founding Executive Director of the Center for Business Ethics and the Hieken Professor of Business and Professional Ethics at Bentley University in Massachusetts. He earned his Ph.D. in Philosophy at the University of Massachusetts/ Amherst. He has published 16 books and over 100 articles, and received awards for his contributions to the field of ethics and compliance.
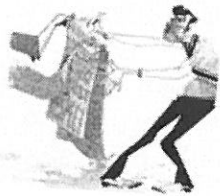
> As BP learned the hard way, having noble aspirations to behave in an ethical manner is one thing, putting them into practice is another. How we behave is what ultimately earns the trust of others.

The Chief Counsel's final report noted that the disaster "was not, as some have suggested, the result of a coincidental alignment of disparate technical failures," but rather each technical failure could be traced back to "an overarching failure of management."

According to the report, the litany of management failures included: ineffective leadership at critical times; ineffective communication and siloing of information; failure to provide timely procedures; poor training and supervision of employees; ineffective oversight of contractors; inadequate use of technology; and failure to appropriately analyze and appreciate risk.

All of these undermined trust and represented the failure of BP to live up to its own professed commitment to safety, people development and doing no harm.

Since the crisis, BP's new Group Chief Executive Bob Dudley has tried to redress these failures. As he states in the foreword to BP's Code of Conduct: "Laws vary from country to country and we must always comply with them, but as a global company, we need to go further. To be a trusted company, year after year, we need to work to a consistent and higher set of standards and follow them in everything we do and say, every day, everywhere we work."

As BP learned the hard way, having noble aspirations to behave in an ethical manner is one thing, putting them into practice is another. How we behave is what ultimately earns the trust of others.

As such, in addition to the existence of a Code of Conduct, it is necessary to support it with mechanisms that ensure it is being upheld. To this end, BP has set up OpenTalk, a confidential helpline to facilitate people being able to speak up, ask for help and do the right thing whenever they have a question or feel that the code is being violated.

2. RESPONSIBILITY. This value is the foundation for any response to a crisis – yet it is often one of the most difficult to live up to. It requires taking all necessary and reasonable steps to respond to the immediate crisis as well as ensure that it does not happen again.

Acting responsibly also means not trying to shift the blame for your mistakes. It requires that you apologize, and you need to be prepared to compensate those who have been harmed as a result of your actions or inactions.

At first, BP did none of these things. The CEO at the time, Tony Hayward, blamed the rig owner, Transocean, and then the cement contractor, Halliburton. Later, reports emerged that BP was trying to coax coastal residents into signing settlement agreements and waivers that would limit the company's liability and cap compensation at $5,000.

When the government got wind of this, Hayward admitted it was "an early misstep" and the company stopped. However, the fact that BP had sent letters urging affected residents to give up their right to sue made Hayward's earlier comments that "we are responsible for the oil and for dealing with it and cleaning the situation up" sound rather hollow.

3. CARING. This means caring about the impact of your actions on others. Against this standard, available evidence suggests that BP's actions both before and following the crisis did not measure up.

According to *The Wall Street Journal*, BP apparently chose not to install a remote-control shut-off valve that is required in Norway and Brazil and used by other oil companies, including Royal Dutch Shell and France's Total SA. The cost of installing such a safeguard device would have been $500,000 – which is not an extortionate amount in relation to BP's reported operating revenues of $240 billion, and far less than the billions that BP now has to pay out for the resultant disaster.

Beyond not using available technology to reduce safety risks, other reports emerged that BP did not appear to be responsive to the safety complaints of its workers.

According to CNN interviews with oil rig survivors, "It was always understood that you could get fired if you raised safety concerns that might delay drilling."

The New York Times obtained a copy of a confidential survey commissioned by Transocean just a few weeks before the accident, in which workers voiced concerns of "drilling priorities taking precedence over planned maintenance."

Quoting from the same research, the Final Report to the President noted: "Some 46 percent of crew members surveyed felt that some of the workforce feared reprisals for reporting unsafe situations."

This lack of caring revealed itself again in Tony Hayward's ill-judged comment about how the disaster was affecting him personally, when he said, "I'd like my life back." He later had to apologize to the families of the 11 men who had actually lost their lives in the accident and would never be given their lives back.

Later, in defense of going sailing on his yacht as the recovery effort faltered, a BP spokesperson tried to justify the jaunt on the basis that "it was the first break that Mr. Hayward has had since the spill began," reported the BBC.

4. CITIZENSHIP. This includes abiding by the law in the jurisdictions in which you operate, taking reasonable steps to protect the environment and pitching in to help your community as needed, especially during an emergency.

One way that BP could demonstrate its commitment to responsible corporate citizenship could be to join with others in the oil and gas industry to promote a safety culture by creating a self-policing body, in much the same way that those in the nuclear power industry did in creating the Institute of Nuclear Power Operations (INPO) after the Three Mile Island incident in 1979.

However, as the Final Report to the President acknowledges, certain features of the oil and gas industry make it harder to believe that companies like BP could ever be completely trusted to police themselves without some external government oversight.

"To be credible, any industry-created safety institute would need to have complete freedom from any suggestion that its operations are compromised by multiple other interests and agendas."

For this reason, BP's track record of working through its trade body, American Petroleum Institute (API), raises doubts over its commitment "to drive a safety revolution in the industry."

The Final Report states: "API's long-standing role as an industry lobbyist and policy advocate – with an established record of opposing reform and modernization of safety regulations – renders it inappropriate to serve a self-policing function. In the aftermath of the Deepwater Horizon tragedy, the Commission strongly believes that the oil and gas industry cannot persuade the American public that it is changing business-as-usual practices if it attempts to fend off more effective public oversight by chartering a self-policing function under the control of an advocacy organization."

5. RESPECT. The philosopher Immanuel Kant interpreted respect to mean treating people as an end and never merely using people as a means. For Kant, what mattered was whether one's actions were motivated by respect for others, which he regarded as a basic moral duty.

Against such a standard, how did BP's actions stack up? Again the evidence available is not encouraging, and the BP case is symptomatic of a bigger problem that has long plagued the oil and gas industry: putting profit before people.

The Final Report to the President reiterates this point: "Project profitability depended on how soon production could be brought online. Drilling vessels were contracted on day-rates, increasing time pressures. Production processes were highly interdependent: delay in one place could cause delays elsewhere. So there were relentless demands to drill the wells, install the platforms, and get the oil and gas flowing. 'When I first started working, they didn't care whether they killed you or not!' remembered one offshore veteran … 'If you got hurt, they just pushed you to the side and put somebody else in.'"

6. FAIRNESS. This final core value is also related to justice. It could be argued that BP, in establishing a $20 billion compensation fund in June 2010, has met this standard at least in terms of

> Through the CEO, your firm must emphasize that, when there is a conflict between your stated values and the bottom line, the ethical values must take priority. Such values must be embedded in your firm's corporate culture.

its obligation as a responsible party to provide compensation for the harm done. However, whether BP's total response now estimated to be around $40 billion meets this standard is yet to be determined.

Constructing an Ethical Corporate Culture

By seeing where the ethical lapses were in the BP case, we can begin to construct ways to reduce the risk of a crisis happening, respond adequately to a crisis when it occurs, and emerge from a crisis stronger and more respected.

1. ESTABLISH A SET OF CORE ETHICAL VALUES. The starting point for any firm, big or small, to develop an effective ethical corporate culture is to establish a set of core ethical values that are infused throughout the policies, processes and practices of the organization. We believe our suggested list of trustworthiness, responsibility, caring, citizenship, respect and fairness will provide a solid foundation.

Whatever your core values, they should be present and stated upfront in your firm's code of ethics. They should also be included in your annual report, public accountability statement and/or social responsibility report, and should be indicated as clearly as possible on the home page of your corporate website.

Through the CEO, your firm must emphasize that, when there is a conflict between your stated values and the bottom line, the ethical values must take priority.

For example, in Scotiabank's "Guidelines for Business Conduct," President and CEO Richard E. Waugh makes his ethical priorities clear: "Each of us must always do what is right. This is always in the bank's best interests, even when doing the right thing seems to conflict with meeting sales or profit targets. We do not compromise our ethics for the sake of other goals."

Core values that are embedded in a firm's

corporate culture are much more easily operationalized during a crisis. These values will guide your media strategy and the issuing of any apologies or admissions of fault, and they will help in planning ways to ensure that the same problems don't happen again.

In the case of the tainted Tylenol capsules, because Johnson & Johnson prized the safety and trust of consumers so highly, the recall of its products became a no-brainer for managers, above thinking about the negative financial implications for the stockholders.

Consider the opposite extreme: Ford's infamous leaked memo that led to lawsuits over the safety of its Pinto car during the 1970s. In that memo, Ford had calculated and compared the cost of a recall and product design changes ($137 million) versus the estimated cost to society of the accident victims ($50 million) and decided that a human life was cheaper. More recently, when safety concerns arose over its Explorer vehicle, Ford shifted the blame to the tire maker, Firestone, instead of immediately assuming responsibility. A nearly 100-year-old business relationship between Ford and Firestone ended in acrimony.

Your core ethical values should also be applied during hiring and firing, as well as in compensation and promotion decisions.

There is perhaps no more fitting example of living up to your stated ethical values than when the software firm Veritas – which is the Latin word for truth – chose to fire its CFO after it was discovered that he had lied on his résumé about having an MBA from Stanford Business School.

2. IMPLEMENT A COMPREHENSIVE ETHICS PROGRAM. Once you have agreed upon a set of core ethical values and developed your code of ethics, then you need to engage in some ethics training for all employees and managers.

You will need to designate an ethics officer, or some person responsible for the code of

Signs of Ethical Leadership Failure

EXHIBIT 1

BY RECOGNIZING THESE SYMPTOMS AND SEEKING THE PROPER ANTIDOTES, YOU CAN MINIMIZE THE OCCURRENCE OF AN ETHICAL CRISIS AND IMPROVE YOUR CHANCES OF SUCCESS.

SYMPTOM	ANTIDOTE
Lack of Vision: Not seeing the ethical issue in front of you	• View the world through "moral glasses," so to speak • Raise your awareness level • Sensitize yourself to the underlying issues
Keeping Quiet: Having ethical values, but saying nothing	• Proactively communicate your values to others • Publicly state your values in corporate documents
Incoherence: Behaving in an incoherent way, e.g., basing performance evaluations totally on hitting economic targets, or not following your values through to their rightful conclusions	• Seek better understanding of the issues • Develop your expertise in ethical decision-making • Prioritize respect for people over profit
Inaction: Not putting your values into action, either because you don't know how or you fear the consequences	• Actualize your values and manage their implementation to boost your effectiveness
Hypocrisy: Not being committed to the values you espouse • Saying one thing but doing another: "Do as I say, not as I do"	• Walk the walk: fully commit yourself to a unified set of guiding principles and operate accordingly, with integrity
Double Standards: Using a different set of values in one situation than those used in another, e.g., lobbying for something at work that you would not tolerate at home with your own family	• Be consistent in all realms of your life
Complacency: Allowing yourself to become complacent, believing that you are already ethically complete and mature • Having an organizational mind-set and culture that believes it has achieved a perfect state of ethical nirvana	• Be humble • Appreciate your own vulnerability and susceptibility to failure • Recognize that ethical management is a continual process or journey, not a one-time destination

ethics, who has direct access to the board of directors. In addition, there must be some reporting channels in place, via which concerns can be relayed without fear of any reprisals.

In most cases, crises can be avoided if employees feel comfortable about reporting their concerns, and then if firms take appropriate and immediate action as soon as those concerns are brought to their attention.

In a May 2012 National Public Radio interview, Peter Solmssen, a managing board member and general counsel of Siemens, explained what his company did after it was discovered that some of its employees were routinely paying bribes to win contracts.

First, Siemens hired outside investigators to reveal the extent of the problem. Then, they offered amnesty to employees who were willing to come forward and help weed out corruption. Those who didn't come forward and were later found to have been involved in shady dealing were fired and then prosecuted.

Changing the corporate culture is not as hard as it seems, Solmssen said, adding that employees will generally opt to make things right if given half the chance. "Our employees are thrilled not to be part of the problem and to be part of the solution."

3. GIVE ETHICAL LEADERSHIP. This is potentially the most critical element of an effective ethical corporate culture. The starting principle must be not to let short-term personal financial gain – otherwise known as greed – outweigh

considerations of the potential negative impact on other people.

Unfortunately, in too many companies, the narrow pursuit of profits and fat bonuses has prevented many leaders from setting the right ethical tone at the top. WorldCom's Bernie Ebbers and Enron's Kenneth Lay and Jeffrey Skilling are obvious examples. But besides those holding *Time*'s dubious honor of "Top 10 Crooked CEOs," there are many less well-known examples that may not make international headlines but are no less egregious – perhaps in your own company?

Check out **Exhibit 1** and see if you recognize any of the telltale signs of ethical leadership failure. Addressing these shortcomings and failings is key for boosting your level of ethical leadership.

Guiding Principles

Every firm faces the risk of an ethical crisis, no matter how serious an attempt has been made to build an ethical corporate culture. As such, being prepared to address potential crises effectively and ethically is a crucial element of strong and responsible management. We suggest the following principles to guide crisis management planning.

- Be honest, transparent and disclose all relevant information.
- Remain visible and available at all times throughout the crisis.
- Don't hide behind company media statements or "no comment."
- Accept fault and assume responsibility if indeed you are or your firm is at fault.
- Don't act defensively or try to deflect the blame.
- Take all reasonable steps to fix the problem and help ensure that it won't happen again.
- Apologize when the situation calls for it.
- Demonstrate sensitivity to those who may have been harmed.
- Ensure that the natural environment and local community are protected.
- Focus on respecting the rights of other stakeholders, not merely the shareholders.
- Ensure timely and fair compensation for the injured parties where and when appropriate.

Most importantly, everything said to any stakeholder – whether shareholders, employees, customers, governments, citizens, the media or special interest groups – and everything undertaken by the company should always be directly based on and directly connected to its core ethical values, such as those mentioned earlier like trustworthiness, responsibility, caring, citizenship, respect and fairness.

Exclusive or excessive reference to, and emphasis on, other values – such as profit maximization or protection of share value – have led to many of the most heavily criticized crisis management decisions that have occurred in recent years. Besides those cases already mentioned, think of the mess Nike found itself in when relying on local norms and business conventions as the standard-bearer for supplier decisions on the use of child labor in Asia.

Instead, we believe that a crisis can serve as a defining opportunity for a company to demonstrate its commitment to a higher set of core ethical values. This will put you in a much better position to survive a crisis, and moreover generate long-term goodwill for your enterprise. Firms that establish and sustain ethical corporate cultures also reduce the potential of other crises happening again in the future. □

⁚ TO KNOW MORE

- Schwartz, M.S. "Universal Moral Values for Corporate Codes of Ethics." *Journal of Business Ethics* 59, no. 1 (2005): 27-44.

- Driscoll, D.M., W.M. Hoffman and E.S. Petry. *The Ethical Edge: Tales of Organizations That Have Faced Moral Crises.* New York: MasterMedia Ltd., 1995.