Corporate Management of a Major Crisis

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The way a company manages a major crisis can literally spell the difference between life and death – both for the immediate victims of the crisis and for the company itself. Over the past decade, several major crises have had severe environmental, health, and safety consequences, as well as drastic implications for the companies involved:

• The near-meltdown of the reactor core at Three Mile Island in 1979 cost Metropolitan Edison more than a billion dollars in repairs (while it was paying to produce electricity by other means) and traumatized most of eastern and central Pennsylvania as well as the rest of the United States.

• The deliberate contamination of dozens of Tylenol capsules with cyanide by an unknown person in 1982 caused eight deaths and cost the parent company, Johnson & Johnson, $100 million in recalled packages (a second incident in 1986 caused the company to withdraw Tylenol capsules altogether at a loss of another $150 million).

• The widely publicized chemical leak at the Union Carbide plant in Bhopal in 1984 and the Chernobyl nuclear plant accident in 1986 caused extensive illness and numerous deaths.

• In the less-publicized 1985 Jalisco cheese incident in California, deadly bacteria caused the deaths of 84 people and bankrupted the company.

• More recently, the Sandoz warehouse fire in Europe and the ruptured Ashland Fuel tank on the Monongahela River in Pennsylvania have had major effects on the companies involved in terms of both cleanup costs and serious – if perhaps temporary – damage to company reputations.

• Finally, the last year alone has witnessed the *Exxon Valdez* oil spill in Alaska; the Phillips refinery explosion in Pasadena, Texas, that killed more than 20 workers; and the Huntington Beach oil spill in California.

What distinguishes a major crisis? First, in terms of its physical effects, it either threatens to or actually does severely affect people, property, and/or the environment. Effects might include multiple deaths, dis abling injuries, epidemics, or widespread destruction or contamination. Second, in terms of its impact on the corporation, a major crisis threatens material loss of control over the context in which the corporation operates. The events of a major crisis transcend an individual plant or facility and may endanger a company's reputation, a specific product line, an entire manufacturing operation, or even a company's survival. Operationally, a crisis demands fast decision making, often on the basis of incomplete information.

Not surprisingly, few executives like to think about crises. Many corporate leaders are proactive, „take-charge" people, who expect to shape events, not react to them. Some are too preoccupied with the normal course of business to make time for anything so unlikely as a major crisis. Still others can't accept the possibility that a crisis could happen to them. The very idea challenges their competence as managers, their policies, and their back-up systems. Former Governor Richard Thornburgh of Pennsylvania (now U.S. Attorney General) has reported that Soviet authorities rejected an exchange of information on nuclear reactor safety after the Three Mile Island incident. The Soviets stated they had nothing to learn because Soviet nuclear energy employed vastly different technology. However, familiarity with the lessons learned at Three Mile Island could undoubtedly have improved the Soviets' management of Chernobyl.

Crises *do* happen, of course, even in well-managed and responsible firms. Consequences can harm customers, shareholders, employees, and innocent bystanders. Corporate leaders, therefore, must ensure that the company and its constituencies, including the public, are protected to the greatest degree possible. In this article we discuss approaches that can help prepare a company before a crisis strikes and ways to respond effectively to the event itself.

Preparing for a Crisis

Preparation for a crisis includes establishing prevention and response programs, a crisis management team, and crisis management policies.

Prevention and Response Programs. Many well-managed companies already have policies in place to protect neighbors or the environment and to ensure employee safety and health in the event of an accident. While these policies are the first line of defense, they are not foolproof, and companies should do more. Consider implementing programs to search out potential problems and mitigate risks. Consider new manufacturing techniques or shipping methods to enhance safety. Consider reformulating or repackaging products to prevent contamination. Where exposure cannot be eliminated, focus on accident prevention and contingency planning.

A company's attitude toward risk management is just as important as its formal policies. Crises have occurred when management ignored procedures in order to „get on with the job" or control costs. *Fortune* magazine[1] described a discovery in 1977 by James F. Towey, chairman of Olin Corporation, that employees had falsified records to cover up illegal mercury discharges into the Niagara River. This discovery came after Mr. Towey had aggressively campaigned for improved financial performance. Olin had even threatened to close down plants if regulations became too costly. The author notes, „It never occurred to (Olin top management)... that their attitude of grudging compliance might encourage outright evasion of the law by their subordinates."

Policies and programs for public, customer, employee, and environmental safety require periodic review and auditing, both by internal and external parties. Reviews test adequacy; audits test effectiveness. Reviews include drills, which, though artificial, can expose weaknesses in response strategies. Critiques of a drill are easier to handle than accusations and recriminations after a real crisis.

The board of directors should require regular reviews and audits, as well as comparative evaluations of the programs of other firms. But the board should not micro-manage prevention programs. Instead, it should assure itself that management's policies and programs are effective.

The Crisis Management Team. Every corporation should appoint a crisis management team with a clear line of authority for handling a crisis. Senior managers who are not members of the crisis management team and whose help is not needed should carry on with their normal business.

We have found that few senior line managers are well suited to managing a crisis while simultaneously carrying out their normal operational and business responsibilities. Some good managers lack the special skills required to manage a crisis. Moreover, the crisis management may overextend them, harming normal operations. Furthermore, crises often span multiple areas of authority, causing overlapping and contradictory decisions. Finally, in a crisis, the need to respond quickly to corporate concerns and outside interests may cause top management to „short-circuit" an existing line of authority. The company is much better served if management has taken this step well in advance and specified its reasons for doing so.

Ideally, a strong senior executive should be appointed to lead the crisis management team. The manager should be decisive, but not impulsive – someone who is trusted and who has the authority to act without fear of being second-guessed. The manager also needs a long-term perspective. He or she should be freed from other responsibilities so that leading the crisis management team is this manager's only responsibility until the crisis ends.

A crisis management team should include skilled and trusted legal, public relations, and technical staff. If possible, a company should name back-up members and train them along with the core team. Everyone's roles and responsibilities should be made clear.

The actual training could consist of an initial in-depth examination of what constitutes a crisis, how to gauge the degree to which the corporation has lost operational control over its constituents (i.e., employees, neighbors, regulators, shareholders, industry, customers, and media), and, depending on the exact nature of the crisis event, how to identify quickly the most affected constituents and implement a program to regain control. The initial training should also include case studies of actual crises, together with the lessons learned by the corporations involved. After the initial training, the crisis management team should be subject to a detailed realistic exercise in which a hypothetical crisis is managed through scenario development and role-playing. Further exercises should be conducted once a year to maintain an effective and ready crisis management team.

Crisis Management Policies. An effective crisis management policy should keep in mind three goals: ensuring an effective initial response, maintaining the response throughout a crisis, and minimizing internal and external aftershocks through the sound management of the affected constituents. It is most desirable for corporations that are serious about rational and effective crisis management to develop written policies on the subject. These policies would address issues such as who is empowered to determine when an event is of crisis proportion, and who will declare that a crisis is underway and convene the crisis management team. Policies should be developed to clearly identify the authority vested in the crisis management team leader and each team member. This could include authority to speak publicly for the company, to commit significant resources rapidly, to direct communications to employees, to release information to the media and the financial community, and generally to make broad decisions. The roles and responsibilities of each team member should also be covered by written policy, which should be communicated throughout the corporation.

Planning for a crisis is also an opportunity to evaluate relationships with the media and local government. Has a company built open and candid relationships? If not, it will be too late to do so during a crisis.

When a Crisis Happens

As soon as a crisis occurs – or is suspected of occurring – the appropriate senior corporate officer (usually the chief executive) must convene and deploy the crisis management team promptly. The team must execute tasks quickly and must update its work as additional information becomes available. The team should be based in a „control center“ equipped with superior communications systems. The control center could be at corporate headquarters or at a site near the crisis.

The team should immediately address five key questions:

• What has happened?

• Who are the affected constituents?

• What is the corporation’s legal and financial exposure?

• How should the corporation communicate its position?

• How can the corporation regain lost control?

First, what happened? When a crisis occurs, the first question to address is straightforward: What happened? The answer, however, is rarely straightforward. Some examples will illustrate:

• When Warren Anderson, then chairman of Union Carbide, learned of the Bhopal tragedy, he knew only that there had been a gas leak. It took the company nearly two years to determine exactly what went wrong.

• Governor Thornburgh of Pennsylvania did not receive an accurate report on the Three Mile Island incident until four days after he first heard of it.[2]

• When James Burke, chairman of Johnson & Johnson, learned of the first Tylenol deaths, all he knew was that something had gone wrong with the company’s manufacturing, distribution, or retailing system. It took time to establish that the deadly Tylenol capsules had been deliberately contaminated on retail shelves by an unknown individual.

Why is it so difficult to determine the cause of a crisis? One reason is the unwillingness of those involved to admit what happened, even to themselves. Managers often are indoctrinated not to report bad news – unless they can also report a happy resolution. As one manager put it, „I don’t want to know my subordinates’ problems, only how they solved them.“ This modus operandi – perhaps viable in some contexts – can prevent effective crisis management.

Sometimes the necessary detective work just takes time. Witnesses’ recollections may be selective and their accounts self-serving. Stories first told in confusion tend to harden over time, as repetition reinforces memory. Early reports often prove erroneous.

Limited or fuzzy knowledge can exacerbate pressures on a firm. Rumors spread, sometimes fueled by parties with hidden purposes. Media relations sour. Government officials lose what trust they may have placed in a company. Good relations and trust, once lost, are hard to regain. For example, prior to the *Exxon Valdez* oil spill, *Fortune* magazine had rated Exxon among the ten most admired companies in the United States; today, Exxon is no longer included on that list. Even though it is generally acknowledged that Exxon’s immediate technical response was superb – even heroic – the company lost the effects of years of hard work at image building and public goodwill development.

A basic premise of crisis management, therefore, is that reliable and complete information is often hard, or even impossible, to obtain. Once that reality is accepted, a lack of information can be managed – and even turned to a company’s advantage.

Who are the affected constituents? A second critical question emerges from a crisis: Who are the affected constituents and how have they been affected? The list of parties affected by the crisis can be quite large, depending on the nature of the crisis event. The list could include one or more of the following: the general public, neighbors, customers, regulators, industry groups, competitors, politicians, suppliers, vendors, the financial community, the media, shareholders, employees, and insurers.

In some crises, such as airplane crashes, the list of significantly affected constituents is fairly clear cut:

customers (passengers), regulators, insurers, and employees. In other crises, as in the tanker grounding at Valdez, the effects are ongoing and wide-ranging. Managing the crisis at Valdez required limiting the negative effects of the event itself while confronting still-unclear consequences. The devilish nature of many crises prevents management from initially identifying all the affected constituents. In the Valdez oil spill, the significantly affected constituents undoubtedly included all the interested parties listed above.

In trying to downplay or deny a crisis (to themselves as well as to others), managers may ignore important interests. However, it is critical that managers identify and consider effects of the crisis on both „external“ constituents, such as customers, neighbors, regulators, and the media, and „internal“ constituents, such as employees, shareholders, insurers, and others. If ignored or improperly informed, employees will be confused and can lose morale and loyalty to the firm. Exhibit 1 summarizes the interests of various parties potentially affected by a crisis.

Exhibit 1

Typical Constituencies and Concerns During a Major Crisis

Concerns				
Parties	***Financial***	***Environmental, health, and safety***	***Psychological***	***Other agendas***
Shareholders	Earnings, share value		Pride in company	
Employees	Job security	Exposure to injury, long-term damage	Pride in company	Strengthen union demands
Customers	Alternative suppliers	Product safety	Loss of trust in other company products	Product, service continuity
Competitors	Business opportunity	Similar possibility at their facility; reputation	Desire to seek competitive edge as a result of crisis	Preserve industry reputation
Neighbors	Property loss	Exposure to injury, long-term damage to health, environment	Fear of recurrence	Limit or stop operations
Regulators	Size of penalties imposed	Restoration of environment to original state	Exacerbation of possible existing antagonism	Need for new controls
Politicians			Publicity, image	Public interest
The public		Environmental, health, and safety impact	Curiosity, fear	Public interest
Media	Increased readership and advertising with hard-hitting coverage		Negative attitude toward business	Immediate, sustained public attention
Financial community	Impact on earnings		Drawn to other investments, more reputable companies	Effect on industry

What is the corporation's legal and financial exposure? A crisis poses serious financial risks, including significant declines in earnings, share values, and overall credit rating or borrowing power. It also poses significant questions of liability. A key question is whether it is more important to limit a company's legal exposure or to respond to the public interest. We believe responding to the public interest best serves a company in both the short and the long term.

Not surprisingly, however, there is a strong tendency to favor the former goal – limiting liability. Pursuing that goal seems the responsible way to protect a company. Financial liability can be huge, and executives may be in no position to assess the company's risk. Moreover, legal counselors often articulate legal concerns persuasively, whereas counter-arguments by a public affairs or personnel officer can sound weak or vague.

Yet a legalistic approach to crisis management is often the riskiest. The courtroom is not the only – and not necessarily the most important – forum in which the company will be judged. Efforts to contain legal exposure may harm relations with customers, investors, regulators, and even employees.

One problem is that a company may delay steps to contain damage. Lawyers may warn that aiding victims can be interpreted as an admission of guilt. Or they may try to gain releases or limit liability before dispensing aid. In one case, a discharge from a chemical plant spread a toxic contaminant to a residential neighborhood. Public officials evacuated the area. The firm's public affairs officer proposed sending in clean-up teams and making immediate cash grants to help residents temporarily relocate. Legal counsel, however, argued that assistance and grants should be contingent upon a release from further liability. The result: goodwill was strained while executives debated aid and lawyers drew up proper release forms. Faced with the forms, many neighbors turned to aggressive plaintiffs' lawyers for advice. The irony is that, in the final analysis, the company's counsel admitted that neighborhood assistance would not have significantly changed the firm's total loss exposure.

By contrast, the Shell Oil Company settled most third-party claims from its Norco explosion within days of the event. The company did not seek a formal legal release. The public's reaction and media coverage were most favorable.

Legal concerns can also hinder forthright communication, a key ingredient in crisis management. For example, litigators often see volunteered information as simply helping the „other side" in court. This point of view overlooks the likelihood that potentially damaging facts and speculation will emerge during the discovery process. Moreover, no public relations miracle can save a company that appears to be stonewalling.

While it is essential to be informed of legal consequences, management must balance legal interests with other responsibilities. We recommend drawing on legal advice when it is available, but not delaying action on its account.

How should the corporation communicate its position? Relations with the press in a crisis pose particularly difficult problems. Reporters will bombard the corporation with questions: What happened? What damage has been done? What corrective action will be taken? Why will it work? As we have described, management probably will not fully know what has happened, and the event may not be over. The company will be developing its responses as the evidence develops.

But reporters and their editors want answers. They are likely to quote opinions from any arguably qualified source as definitive. Unfortunately, antagonistic interests – perhaps a special-interest group, a concerned party, or a regulatory agency – will be quick to respond to press inquiries. And once an „answer" is fixed in the public mind, it is hard to dislodge. It becomes the framework for later media coverage and for public policy, including regulatory action.

In the Bhopal tragedy, for example, the press quickly adopted the theory put forward by plaintiffs' lawyers and the Indian Government that the toxic gas release resulted from faulty management supervision of a maintenance operation. Under this theory, of course, Union Carbide could be held liable for damages. Yet, even after the theory was substantially disproved,[3] media commentary continued to promulgate it.[4]

Handling the press effectively is critical from the very start of a crisis. Press coverage will largely determine how customers, employees, the financial community, and the public perceive a company in a crisis. Here are some lessons gleaned from experience:

• Speak with a single voice. If possible, use a single spokesperson.

• Use a streamlined clearance procedure. The public cannot wait while a committee debates what information to release.

• Be informed, accurate, and honest. Admit uncertainties.

• Investigate uncertainties and get back to the questioner, even if all you have to say is, „We still don't know."

• Don't stonewall. „No comment" can do more damage than admitting the truth, however bad.

• Recognize the concerns of different constituencies. Communicate directly with employees, shareholders, politicians, and the media.

As Johnson & Johnson demonstrated in the Tylenol case, fair and candid dealings with the press can yield not merely balanced but respectful coverage. An open-minded and accessible press can be a valuable source of information. After all, reporters make independent inquiries and may uncover facts before the company does. On the other hand, in the case of Three Mile Island, General Public Utilities (the parent company) initially had difficulty in establishing clear communications with both the press and the governor's office, and this greatly exacerbated public concerns. Senior management must commit to clear and open communication. They must inform honestly, listen carefully, and respond fully.

How can the corporation regain lost control?

Once the crisis management team has determined with reasonable certainty what has actually occurred and who has been most severely affected, it must decide what action to take. In a crisis that has caused deaths, the victims, their families, and their neighbors will require immediate attention. In the case of events causing environmental damage, such as an oil spill, regulators, politicians, and the general public would be high on the list of affected constituents. An important element of the crisis management team training should consist of identifying, for a variety of crisis scenarios, the most affected constituents, what should be done to address their needs, and who on the team should do it.

Exhibit 2 shows a schematic of a generalized crisis management situation involving external as well as internal effects, together with responses that have proved valuable in past crises. It should be noted that Exhibit 2 is not intended to be a complete listing of all possible responses. It is simply an illustration of the types of actions that may be considered. A crisis management team must develop lists of specific actions to address the affected constituents for a number of crisis scenarios. The actions must be bold, decisive, and swift if the corporation is to manage the crisis well and regain control over its operations and the external environment.

What Not to Do

Here are some pitfalls to avoid both during and immediately after a crisis:

Derailment of Day-to-Day Business. A crisis, by nature, rivets attention. Everyone from senior management on down becomes preoccupied – even those not directly involved. But operations must be maintained and customers served. In fact, during a crisis, normal business must proceed especially smoothly to reassure customers and employees that the crisis is under control. A crisis encourages competitors to be aggressive, complicating matters farther.

Mass Confusion. In a crisis, everyone is concerned and wants to help. But too much help, and haphazard management, only exacerbate problems. Too many helpers, for example, can confuse lines of authority.

Recrimination. If handled well, a crisis can bring an organization closer together. If handled poorly, however, a crisis can lead to finger-pointing and recrimination. Managers may lose their status, their self-respect, the respect of their colleagues, or even their jobs. Whatever the managers' true responsibility or culpability, there is always nagging doubt. Senior management may become paranoid, distrustful of subordinates and board members alike. The board may find its own confidence strained. The result can be a loss of the candor necessary for effective board/management relations.

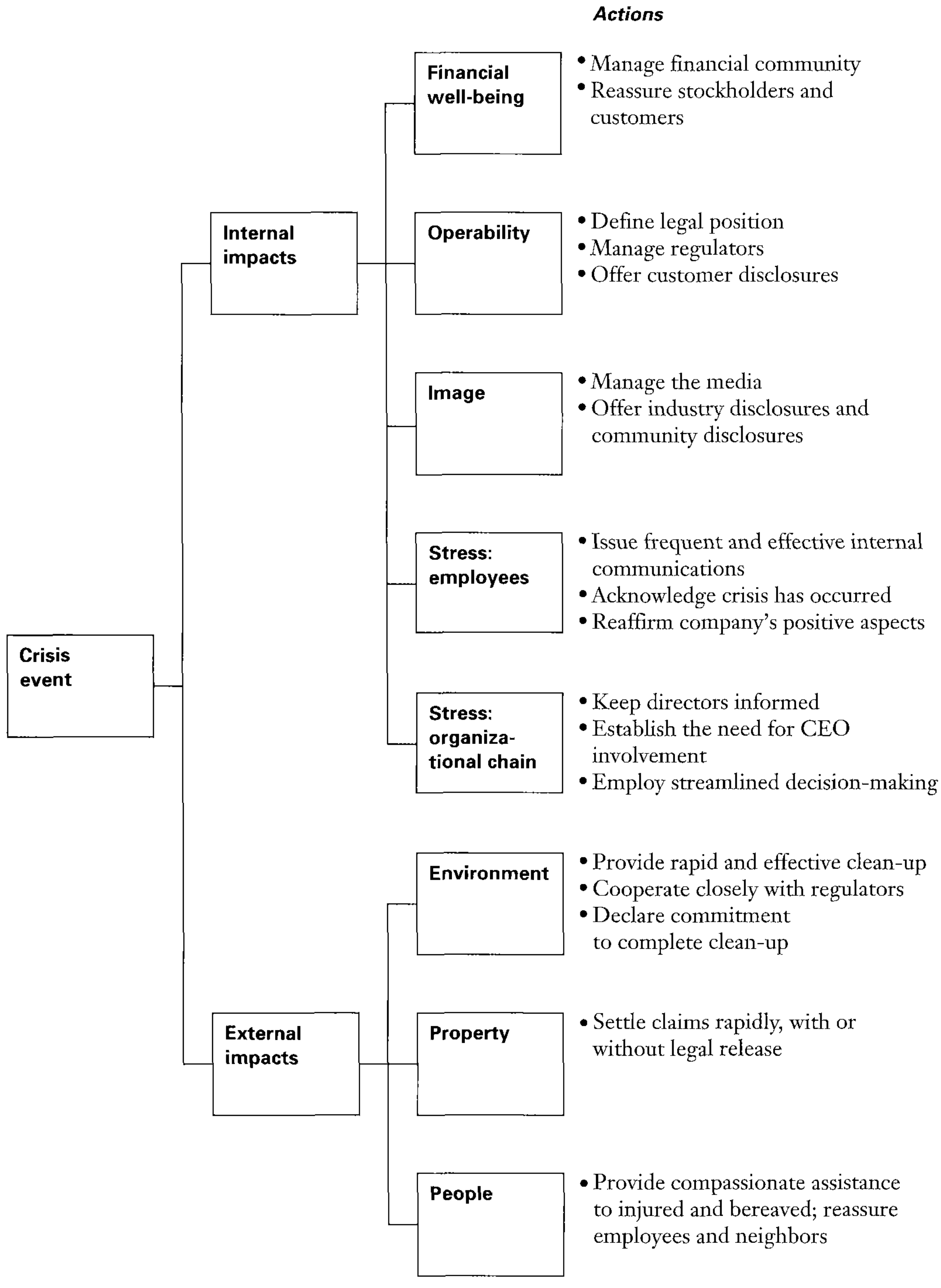
Ignoring Employees. Employees are perhaps the most important constituents of a corporation. During a crisis, their morale is severely affected and their sense of loyalty erodes. If left unattended, their productivity will suffer badly, further affecting the corporation and its competitive position. During a crisis, they should receive regular briefings from the crisis management team on the company's efforts to alleviate the crisis. Positive aspects of the firm should be stressed in these communications. Under no circumstance should the media be the employees' only source of information regarding the crisis.

Micro-Management by the Board. A crisis can raise many doubts in board members' minds: Should management have let it happen? Do managers know what they're doing? Why don't they follow board members' stipulations? What is the company's exposure to financial, or even criminal, liability? Consequently, the board can be tempted to intrude into the day-to-day management of the crisis and even into ongoing business operations.

The board of directors must recognize that its role is one of oversight and avoid stepping on management's toes. Board members' chief responsibility is making sure company management has devised a good plan and has adequate resources to carry it out.

Exhibit 2

Schematic of a Generalized Crisis Management Situation



[1] *Hugh D. Menzies, „The One-Two Punch That Shot Olin,"* Fortune*, p. 120, June 5, 1978.*

[2] *Richard Thornburgh, „The Three Mile Island Experience: Ten Lessons in Emergency Management,"* Industrial Crisis Quarterly*, Vol. 1, No.1, p. 5, Spring 1987.*

[3] *Ashok S. Kalelkar, „Investigation of Large-Magnitude Incidents: Bhopal as a Case Study," International Symposium on Preventing Major Chemical and Related Process Accidents,* IChem E. Symposium Proceedings*, No. 110, p. 5 53, May 1988.*

[4] *Of all the major news media, only* The Wall Street Journal *gave significant coverage to evidence disproving the „management failure" theory.*

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