Reputation: the overall sense of integrity and trust, so what is internal audit's role?

"It takes 20 years to build a reputation and five minutes to ruin it. If you think about that, you'll do things differently."

- Warren Buffett

Reputation is the overall sense of integrity and trust that an organisation exudes. It is a perceived by others. It is intangible. Yet organisations are wholly accountable for it. Effective management of reputation has never been more important than in an era that combines profound corporate uncertainty with intense media capability.

With boards being both culpable and liable for an organisations reputation it is an important topic for CAEs to invite discussion on. This paper explores key aspects of organisational reputation, its fragility, estimating its value and the multifarious role chief audit executives (CAEs) have in providing assurance over its management.

Fragility of reputation

An organisation's reputation is a realisation of all the intentional and unintentional communications and activities that are undertaken. Different stakeholders are likely to have diverse views of an organisation because of their particular priorities and interactions – investors, customers, patients, employees, media, regulators. It is the emotional connection between an organisation and its stakeholders.

It is irrelevant what an organisation thinks of itself, its reputation is what others think of it. Unlike other intangible assets such as brands or intellectual property which can be managed, reputations can only be influenced and are built over time.

Airmic and the Reputation Institute produced a guide to managing reputation risk, designed for risk managers and auditors; it sets out seven dimensions that organisations need to deliver against to drive reputation. Against each one it sets out assessment criteria and outlines potential risk events.

The diversity of stakeholders, volatility of emotion and multiplicity of dimensions demonstrate how easily reputations can be tarnished or damaged. Reputational risk events are not new however the digital dimension is; the speed, scale and nature of communication that gives rise to reputational damage.

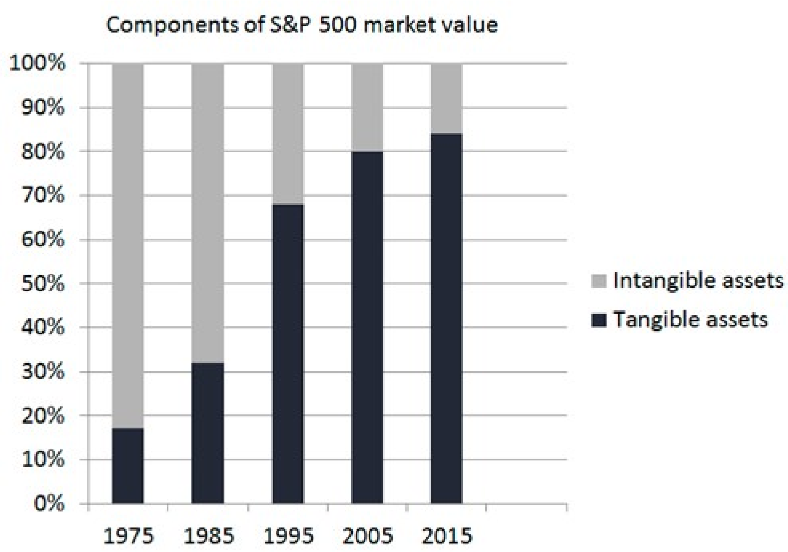
Reputational crises have often been likened to the staggering damage that a hurricane unfurls in its wake. Only the deep rooted trees and buildings with strong foundations withstand the force enough to recover. Damage is costly in the short term but can be recovered and rebuilt, BP (oil spill 2010), Findus (horsemeat 2013), Primark (factory collapse 2013), sometimes in a different form (jeweller Ratner renamed Signet in the 90's). By 2017 BP had recovered much of the reputation value lost though Deepwater Horizon.

Does this remain true in the digital age or is society being desensitised to such issues? What will the future histories tell of the Oxfam scandal in Haiti, Facebook's entanglement with Cambridge Analytica, Boeing's safety record or Twitter warning users of the validity of tweets by US President Donald Trump?

Measuring reputation

A report on resilience estimated that 30% of the market value of the FTSE 100 was attributable to reputation, yet only 8% measured their reputation risk and only 3% had defined their risk appetite for it. As Peter Drucker famously said, "*if you can't measure it, you can't manage it.*"

An evaluation of the American stock market in 2017 demonstrates the importance of reputation as part of the intangible assets of an organisation. It is interesting that despite the recognised value of the intangible (reputation, branding, intellectual property and employee skills), disproportionate effort has often been given by internal audit to assurance over the management and protection of tangible assets.



Source: Intangible asset market value study 2017

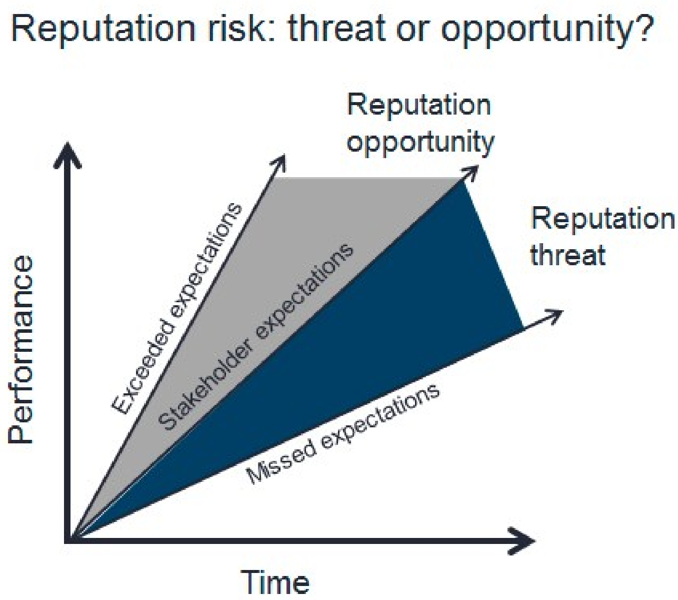
What is the balance within your organisation? Does the risk profile reflect this? Where is your audit resource targeted?

CAEs may wish to review accounting information to understand the extent to which intangible assets are valued. It is a useful discussion topic with the CFO, exploring the work required to get under the bonnet of reputation in order that robust assurance can be provided going forward.

Understanding the seven dimensions of reputation, the related assets and their sensitivity to change is a multi-disciplined task. Mapping the data to a fully inclusive balance sheet (based on intangible asset valuation techniques) may be a useful exercise or too detailed? It is important to be proportionate to the risks, the value of reputational currency and the maturity of thinking.

Is reputation a risk?

A risk is defined as *cause-event-outcome*, in the case of reputation the risk is often stated without the cause such as the cost of losing significant trust among any key stakeholder group.



The Reputation Institute overcome this by using a broad risk statement to define reputation as *a negative event that impacts stakeholders' perception, trust and behaviour*. They also recognise that reputational damage is the negative consequence of risk events such as a product recall, regulatory breach, data loss, disgraced executive, profit warning or strategic drift. Conversely positive outcomes to expectations boost reputation.

But is reputation a risk of itself? A 2017 global risk survey by Aon placed 'damage to reputation/brand' as the top risk that executives are concerned about. How can ownership be attributed to reputation if it is not its own risk? Surely it is the one risk for which CEOs can be held accountable notwithstanding the reputational outcomes associated with other risks.

CAEs may wish to reflect on how reputation is presented in their organisations risk universe/risk register? Is it on the board's risk agenda? Who owns it? Can reputation risk data be isolated for audit planning purposes? If not how useful is the risk data to the executive?

From an internal audit perspective, is it possible to provide assurance over an outcome, the consequence of a risk event? Can assurance over risk management be provided for a nebulous theme or does it have to be something more specific? Whether a single well written risk or a group of risks united by a common outcome, how does a CAE include reputation in the audit plan for it to be meaningful?

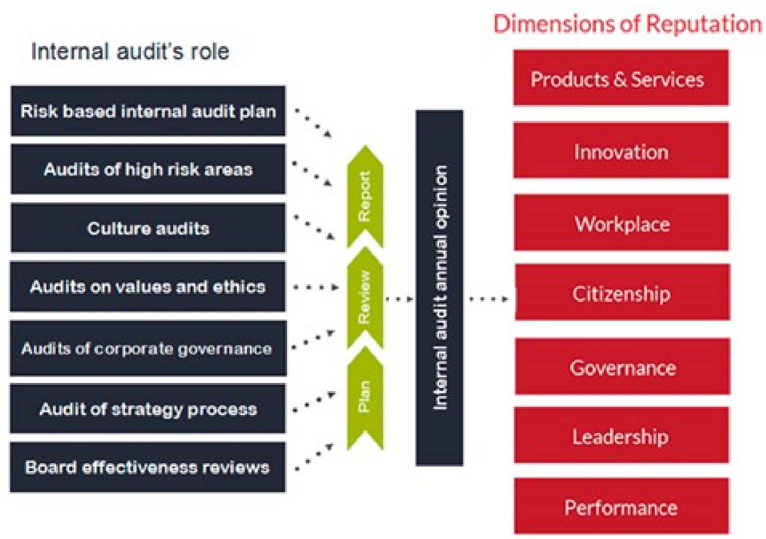
Assurance

Auditing reputation generates similar debate to that of auditing corporate culture; does audit have the skills, is it a one off or a series of audits, should it be part of every audit, can and should it even be audited? The simple answer is yes. The IPPF does not provide a caveat for CAEs wishing to avoid *difficult to audit areas*!

A robust control environment, effective risk management, good governance and a positive culture are the ingredients to maintaining a healthy and strong reputational currency. The assurance that internal audit provides on a regular basis can have a compound effect on the way reputation is strengthened, built and managed.

Process or risk based audits to begin with could be a good introduction to the way in which the organisation manages its reputation. Think about the seven dimensions from earlier, how are they managed? Is there clear accountability for external communications, social media and complaint management? How is reputation accounted for by finance?

Establish the audit foundations and appetite for more detailed reviews of culture, governance, strategy etc.



For CAEs this may be an opportunity to extend internal audits reach across the organisation; when did you last audit the communications department for example?

Including reputation as a standard part of audits is also a good way to introduce and maintain effective assurance. Auditors can identify risks and advice on controls across all seven dimensions of reputation, with CAEs using the information to report on trends and promote open communications on the topic. Could this be an agenda item for a discussion at the audit committee?

In a world of 'fake news', what monitoring tools does the organisation use? Search engine alerts and social media monitoring range from free to use to professional solutions. Typical investigations would include:

- Organisation name – what is the public mood, what are stakeholder saying, particularly reviews and opinion commentary (aka the organisations relevant TripAdvisor)
- Executives – what is being said about key figures and what are they saying themselves
- Trademarks etc. – are they being abused, quoted out of context

Some organisations may have the budget to invest in a reputation assessment by external companies such as the Reputation Institute or Said Business School to inform strategy and performance improvements; interviewing a range of stakeholder's past, present and aspirational, associates and suppliers to ascertain commonalities and differences. What can internal audit learn from this? Does it need to be performed by external experts or can CAEs offer a similar service while gathering evidence for an assurance audit? Surely internal audit has the necessary skills to at least undertake the internal aspect of such a review.

In the world of big data, how is machine learning (artificial intelligence) being utilised to understand reputation. 80% of the data within organisations is unstructured and difficult to analyse. Can this be better utilised to protect and drive reputation?

Ongoing, CAEs listen to the dialogue and debate at a senior level. What does this reveal about reputation issues? Is it given sufficient airtime alongside strategy and operational issues? Is it taken for granted or proactively managed? How can CAEs raise the profile of this important risk management issue?

False assurance

CAEs are always on alert for signs of false assurance. When auditing a potentially subjective topic such as reputation, particular attention is required to avoid basing opinion on perceptions or assumptions rather than fact. Using a framework such as the seven dimensions, clearly communicating the scope of the engagement, establishing the reporting expectations and the role of key stakeholders are good practice approaches to help mitigate the risk ahead of robust quality assurance.

Hypothetically, if an audit team was able to simultaneously audit all seven dimensions of corporate reputation and found all controls to be operating efficiently and effectively, could positive assurance be provided? Imagine the timeline, report is published three weeks after completing fieldwork, later that day the board attend a press event for community event, it's a relaxed affair and out of character a couple of off the record remarks are made about the company, that evening the audit committee chair reads the report and feels a warm glow only to be phoned by journalist for a comment on the remarks, the next day the share price tumbles as the crisis unfolds. How does the CAE feel? What questions are asked? Can positive assurance ever be provided without a caveat?

Closing thoughts

Reputational damage is often caused by the failure of something within the control of the organisation – a process, an employee, change, strategy, corporate culture, personal ethics, a chosen partner/third party. Internal audit are therefore intrinsic to the way in which reputation is understood and discussed by the leaders of the organisation and the oversight bodies. It is incumbent upon CAEs to report the facts in a way that brings practical insight to an unformulated but well understood subject.

According to the Reputation Institute, "protecting a reputation is a defensive reaction, in many respects. Building a reputation, on the other hand, requires on-going commitment, top-down leadership, active engagement, and shared understanding across the workforce to ensure that all employees and suppliers understand the company's ethics and approach to doing business."

> *"You can't build a reputation on what you're going to do"*

- Henry Ford