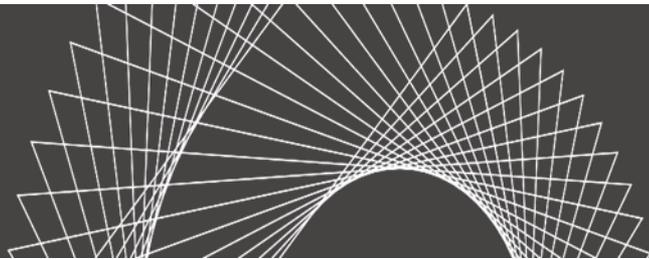


# Crisis Management – Strategies for Avoiding, Mitigating and Responding to a Crisis



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# Agenda

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- Crisis Overview
  - Types of Crises
- Crisis Management
  - Steps in the Crisis Management Process
  - Key Parties and Stakeholders
  - First Reactions
  - Forming an Action Plan
  - Other Considerations
- Case Studies
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  - #3: Catastrophic Events
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# Crisis Overview – A “crisis” is coming ...

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- Like death and taxes every company will eventually face some sort of crisis.
  - Per the Oxford Dictionary, a “crisis” is a time of intense difficulty, trouble or danger.
- Unfortunately, a crisis does not provide advance warning and instead usually comes to the general counsel’s and senior management’s attention only once it has become a material issue.
- The severity of the crisis will vary and depends on a number of factors, including company-specific characteristics (*e.g.*, size, market, product, regulatory environment, capitalization, etc.).

# Crisis Overview – Types of Crises

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- Generally, a crisis falls into one of two categories – the “easily recognizable” crisis and the “lurking” or “building” crisis.
  - “Easily Recognizable” Crises tend to have an obvious catalyst or event, such as:
    - A fire, accident, or similar catastrophic event.
    - Product recalls.
    - A governmental investigation regarding improper or illegal conduct (*e.g.*, EPA notice letter, SEC enforcement action, DOJ subpoena or investigation, etc.).
    - Third party litigation.
  - “Lurking” or “Building” Crises tend to arise from what appear on the surface to be minor events or ordinary course issues not material enough to rise to the C-suite, such as:
    - Departure of an employee, including potentially a senior employee.
    - An “IT” issue.
    - A request for information or documents from a business counterparty.
    - A delay in ordinary course actions, including maintenance, renewals, or repairs.
    - Loss of a material customer or supplier.
    - Allegation of improper employee actions.

# Crisis Management – Steps in the Crisis Management Process

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- Key to any “crisis management” approach are the following steps:
  - **Early Identification**: Identify a crisis or potential crisis events:
    - By proactively identifying specific types of events that your business is likely to face.
    - By identifying events that may serve as warning signs of a looming crisis or may with time or mismanagement evolve into a crisis.
  - **Identify Key Parties**: Identify key parties and stakeholders in a crisis (including parties at risk and which parties at risk may challenge the crisis and/or can be managed to assist/mitigate the crisis).
  - **Develop an Action Plan**: Identify policies, procedures and action plans for addressing the events, parties, stakeholders, and effects (which can include third party advisors, consultants, etc.).
  - **Execute**: Timely and efficiently execute on such policies, procedures and action plans.

# Crisis Management – Examples of Key Parties and Stakeholders In a Crisis

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- Numerous potential parties are affected by, or may have an interest in the effect of, a crisis, including:
  - Boards of Directors (including special committees and appointed board members)
  - Stockholders (including majority stockholders and minority stockholders)
  - Lenders / Debtholders
  - Executive Management
  - Employees
  - Governmental Authorities
  - Other Third Parties
    - Suppliers
    - Customers (including the marketplace generally)
    - Licensors
    - Competitors
- In managing a crisis, it is important to consider key parties and stakeholders, including their respective concerns, perspective, and agenda as well as any potential solutions or conversely issues they may raise.

# Crisis Management – First Reactions

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- When a crisis is identified, the first priority is to approach management of the crisis with the correct mindset:
  - Don't compound your problems.
  - Avoid the temptation to bury your head or minimize the seriousness of the situation.
  - Bad things sometimes happen to good companies; don't dwell on who is to blame for allowing the crisis at the expense of focusing on what to do next.
  - An effective response based on a clear understanding of the facts will help mitigate the crisis, including reducing the time required to resolve the situation and the financial and reputational damage.

# Crisis Management – Forming an Action Plan

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- Key Components of an Action Plan/Response Plan:
  - **People/Safety First.**
  - Triage ongoing/continuing events.
  - Identify your team and roles (including specific tasks, timelines, and use of inside and outside resources).
  - Develop an internal & external communication plan, including:
    - Managing and monitoring public statements and relations (traditional and social media).
      - Issue a “Holding” Statement.
      - Correct any errors in fact that are public.
    - Communicating with Key Parties and Stakeholders.
    - Become the trusted voice (including speaking with one voice).
  - Conduct fact finding/internal investigation – investigate and uncover the facts.
  - Engage with regulatory/governmental entities – voluntary and as required by law.
  - Give the crisis your and management’s full attention.
  - Up-the-ladder reporting.

# Crisis Management – Other Considerations

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- Actions to Avoid:
  - Failing to take proactive protective steps (*e.g.*, removing employees/personnel from situation or danger, pausing production, etc.).
  - Misleading statements or incorrect statements (including denials without facts or support).
  - Assuming someone else is handling or addressing the issue.
  - Allowing an issue to continue or lag.
  - Making light of the situation.
  - Failing to consider both your internal and external audiences.
- Other Considerations:
  - Use those types of potential crises previously identified as an example to game out how you will handle a crisis and to add specific action items tailored to your organization, including your management team.
  - Discuss and consider how a crisis will be handled if key members of management are not available

# Crisis Management – Case Studies

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- Today we are going to walk through three different crisis case studies and discuss key steps and considerations raised by each.
- We note that these case studies are not specific experiences or matters we or our companies or firms have addressed but rather hypotheticals based on our and our peers' experiences.

# Case Study #1: Internal Allegations of Misconduct

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- HiTech, Inc. is a private technology company with \$2 billion in annual revenues, for the past seven years. HiTech, Inc. was historically known for not being innovative, but that changed after the Board and the former CEO undertook a dramatic strategic review, selling off certain underperforming subsidiaries, making strategic business acquisitions, and creating new teams and compensation plans designed to foster innovation. A key player in that transformation was the company's president, who drove the process so successfully that he was named CEO.
- The new CEO has been in the position for three years, though he built his career at the company and now has fifteen years of service. He is very well liked by the Company's stockholders and held in high regard in the industry. Additionally, the company is also preparing to launch a major new product in the next three months, one that promises to continue to build on its new reputation for innovation and improved financial performance.
- However, the General Counsel has approached the Chairman of the Board with word that a male senior executive in finance approached him privately to let him know that a female employee, junior to him, told him while out for drinks with colleagues one night earlier that week, that the CEO had made her feel uncomfortable on several occasions, including requiring her to come to his office alone and then asking her personal questions, talking "very closely" and stopping by her office regularly to offer her a ride home. The female employee does not want to be named. The male senior executive believes the female junior employee is credible but has never witnessed anything himself.
- He noted to the GC that he had heard rumors like this before about the CEO but that everything he heard was from years ago. Separately the head of HR has come to the GC with an anonymous complaint from the Company's hotline that claims the CEO is inappropriately favoring female employees, including in promotion decisions.

# Case Study #1: Identify the Crisis and Identify the Team

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- The General Counsel here correctly identified the crisis and the importance of raising the issue to the Chairman (as opposed to referring it to HR).
- This type of crisis may not be as readily identifiable as the facts may not be known or fully disclosed (in particular as parties may be reluctant to discuss these matters).
- Here the ‘team’ needs to be carefully considered, including:
  - Who in management, if anyone, will be involved?
  - What is the role of the board or a special committee of the board in the internal investigation?
    - Should there be a special committee? Who should be on it?
    - Any changes to reporting structures during the internal investigation?

# Case Study #1: Forming the Action Plan

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- Establish the facts by running an internal investigation.
- How should confidentiality be addressed?
- Should the CEO remain in the office during the internal investigation?
- If the internal investigation results in a finding that is inconclusive what if anything should be done?
  - What if no misconduct is found?
  - How do you communicate the outcome with stakeholders (employees, vendors) and the public?

# Case Study #1: Takeaways

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- Have an action plan:
  - Committee
  - Short list of law firms and PR with relevant experience
- Be prepared in advance for these issues, including to ensure identification:
  - Hotline
  - Policies
  - Tested HR leadership
- Investigation/Communication:
  - Speak to alleged victims, alleged harasser and witnesses
  - Maintain external confidentiality
- Remain flexible on remedial steps
- Review and Document

# Case Study #2: Government Investigations by the CFPB and the SEC

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- University Credit Corp., which started five years ago, provides short-term loans to college students that they can use on expenses, such as books and food.
- Recently, a local news outlet presented a report suggesting that University Credit Corp. charges rates significantly above market. Thereafter, the GC of University Credit Corp. received a request for information from the Consumer Financial Protection Bureau (CFPB) asking about the company's business practices. Some of the information requests relate to the company's proprietary algorithm for determining what rates to charge and how much credit to extend to each student (referred to on subsequent slides as the "CFPB Matter").
- Separately, the GC of University Credit Corp. also received a "wells notice" from the SEC alleging that it had received evidence from an anonymous employee that the company had been retaining accounts receivable long after the company knew that certain students would not pay back the short-term loans and should have been writing off such accounts. Although University Credit Corp. is not publicly traded, it did not disclose the delinquent accounts to private investors in and lenders to the company. The wells notice indicates that a senior officer may have been directing the accounting department to continue to treat delinquent accounts as still receivable, even in some instances after no payments had been received in the prior 18 months. The SEC has requested meetings with the CEO, the CFO and the Chief Accounting Officer within the next 30 days. The GC fears that the SEC will not only bring an enforcement action against the company for civil damages, but the SEC may also make a recommendation to the DOJ to investigate whether the company committed any criminal conduct as well (referred to on subsequent slides as the "SEC Matter").

# Case Study #2: Identify the Crisis and Identify the Team

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- A government investigation is an “Easily Recognizable Crisis” that needs to be effectively managed:
  - Establish “Crisis Team” that can manage both the CFPB and SEC Matters.
  - Assess situation to make sure that Crisis Team understands what happened **prior to** taking external steps.
  - Take control of events to the extent possible and don’t let events control you.
  - Be proactive with stakeholders and government agencies.
  - Potential existential threats to your business so budget can’t be controlling factor but must be carefully and effectively monitored and regulated.
- Building the Team:
  - Crisis team should include internal and external members with necessary expertise.
  - Senior management potentially implicated in SEC Matter/ fact witnesses.
  - Numerous legal, business, and operational disciplines need to be represented.
  - Protect attorney-client privilege.

# Case Study #2: Forming the Action Plan

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- Investigate the facts underlying the claims.
- Communications strategy:
  - Public, internal, stakeholders and regulatory agencies.
  - Need someone internally who can coordinate CFPB Matter and SEC Matter to ensure that all communications are coordinated.
  - Understand and implement effective social media strategy.
- Understand and plan for collateral effects of both CFPB Matter and SEC Matter. For example:
  - Have any debt agreement covenants been breached or could they be breached as a result of the pending regulatory investigations?
  - Are there any current regulatory or contractual disclosure obligations and at what point would such an obligation be triggered?
- Communicate with insurance company.

# CFPB Matter Action Plan – Critical Path Items

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- Understand the public claim and, if possible, the motivation behind it.
  - Was report based on information from sources financed by competitors or independent industry experts?
  - Is there a political motivation behind the story?
  - Does internal view (prior to story and currently) support or refute the basic facts in the story?
  - Is there an internal source for the story (whistleblower for SEC Matter so very likely)?
- Investigate the basis for the CFPB information request and potential collateral impact of the CFPB inquiry.
- Determine if Company loses IP protections if it produces requested information to CFPB.
- Develop communications strategy:
  - Employees need be updated (expect information provided to employees to become public).
  - Determine when CFPB matter needs to be disclosed publicly, if at all.
  - Are there major transactions pending and what should be communicated in connection with those matters?
  - News article is a potential threat to business so a public response is necessary (balance litigation and PR concerns).
  - Two government agencies will also be carefully analyzing any public statements.
- Analyze potential legal and accounting impact of news article, investigation and potential loss of IP rights.

# SEC Matter Action Plan – Critical Path Items

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- Establish internal investigation team (excluding CEO, CFO and Chief Accounting Officer) that reports to special committee of the Board.
  - Develop comprehensive understanding of prior securities offerings.
  - Investigate accounting procedures and interview everyone involved.
  - Determine if there were failures in the audit process.
- Attorney client privilege considerations.
  - Retain independent counsel who wasn't involved in prior transactions or advising company with respect to developing internal procedures.
  - Who does the Company's counsel report to and take instruction from?
  - Each of the senior executives will likely need to retain their own counsel.
  - Does cooperating with SEC or providing a copy (or summary) of internal investigation report waive attorney-client privilege?
- Whistleblower based claim.
  - Coordinate with HR.
  - Will likely receive a claim for compensation from the whistleblower.
- Consider and prepare for parallel criminal and private civil litigation.
- Consider insurance coverage.

# Case Study #3: Catastrophic Events

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- PipeCo Enterprises owns a number of metal pipe factories located in the southeastern United States, including the Gulf Coast.
- Several of PipeCo Enterprises' biggest customers are located in adjacent areas to its facilities in order to permit PipeCo Enterprises to directly supply to their manufacturing facilities.
- Due to the metals and substances used, including certain hazardous items, PipeCo Enterprises has instituted a number of safeguards in its factories to ensure the safety of its employees.
- PipeCo Enterprises also maintains insurance for such factories (property and business interruption).
- A fast-moving category 5 hurricane hit PipeCo Enterprises' second-largest and most productive factory, resulting in a flood severely damaging the factory.
- The hurricane has also damaged certain of PipeCo Enterprises' customers and affected certain of PipeCo Enterprises' suppliers in the region.

# Case Study #3: Identify the Crisis and Identify the Team

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- A factory damaged by a hurricane-caused flood is an “easily recognizable” crisis which requires a quick reaction.
  - The scope of the damage to the factories of other nearby business may take additional time to evaluate due to the lack of direct access.
  - Further, even if the damage to PipeCo Enterprises’ factory was minor, if the surrounding area and the adjacent customers and suppliers suffered damage this can result in a “lurking crisis.”
- The response team should include members of management as well as key operational personnel who can assess the magnitude of the damage and timeline for rebuild/repair.
  - Identify key parties, including insurance providers, key customers, key suppliers, other downstream market participants, and contractual counterparties.
  - The Company should engage its general counsel and its external counsel to identify the legal exposure (including liability issues, environmental issues, or similar items or contractual defaults such as debt covenants, minimum order requirements, minimum supply requirements, etc.) and what liability or third-party remedies may be triggered by this event.

# Case Study #3: Forming the Action Plan

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- Onsite team, investigates the extent of the damage and prepares a repair plan (including engaging third parties, preparing a rebuild budget, and confirming if there are long lead time items to order or commence now).
  - This includes ensuring safety of site and minimizing damage to remaining site (including if portions of site remain operable)
- Engage insurance experts before contacting insurance carriers and providers and form plan for submitting claims (including whether to engage experts and/or counsel directly with insurance providers).
- Financial team to address impact on the business (including effect on financial metrics, available sources of funds to address costs, and potential effect on market place).
- Communications plan
  - Who will prepare the PR response?
  - How will PipeCo Enterprises respond to public requests for information regarding the incident?
  - What message will PipeCo Enterprises convey to employees, suppliers and customers?
- Plan for business impacts (including options to mitigate such impact such as alternative sales/uses).

# Other Key Takeaways

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- The manner in which a Company is prepared for a crisis will affect the potential damage and duration of a crisis.
- Governance practices to help avoid or reduce the negative impact of a crisis:
  - Is there a succession policy for key executive officers? Has the company discussed who would lead if the CEO departed or is unavailable?
  - Communications policy – who is authorized to speak with external parties about a crisis?
  - Delegation of authority policy – are there checks & balances to ensure that the Board and management agree on the best method to respond to a corporate crisis?
  - Does the company regularly review and update internal corporate policies (*e.g.*, regarding harassment and employment decisions)? Does the company offer trainings to employees on these topics?
  - Does the company keep template materials to distribute to suppliers and customers in the event of “common” crises (*e.g.*, a product recall)?
  - Is executive management familiar with its contractual obligations?

# Questions?

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