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Corporate Misconduct and Corporate Reputation: The Role of Penal Sanctions

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Corporate Misconduct and Corporate Reputation: The Role of Penal Sanctions

ABSTRACT

Corporate misconduct, encompassing financial fraud, tax evasion, and environmental pollution, continues to be a pervasive and significant issue in society. Although previous research has provided valuable insights into the impact of corporate misconduct on corporate reputation, the role of legal consequences remains less understood. Criminologists have long explored how penal sanctions influence the social status of offenders. Building upon the Reintegrative Shaming Theory, this study contends that the type of penal sanction imposed also plays a role in shaping the extent of reputational harm resulting from corporate misconduct. The central hypothesis that emerges is that financial sanctions are more reintegrative and less stigmatizing than non-financial sanctions. An experiment involving eight different penalty types demonstrates that financial penalties, in contrast to non-financial ones, are perceived as more integrative and consequently have a less detrimental impact on corporate reputation. Corporate communitarianism, reflecting the extent to which evaluators consider companies as valuable members of society, moderates this mediating effect. These novel findings carry several implications for researchers, managers, and policymakers and underscore the importance of also assessing the impact of penal sanctions on external evaluators' perceptions of the company during legal proceedings and policy development.

KEYWORDS

corporate misconduct, penal sanction, stigmatization, reintegration, communitarianism, corporate reputation

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INTRODUCTION

Corporate misconduct, encompassing financial fraud, tax evasion, and environmental pollution, among other norm violations, remains an enduring and widespread issue in society. Despite the potential consequences of legal prosecution and public disapproval, corporations persist in engaging in criminal activities. A study conducted by Soltes (2019) reveals that, on average, companies internally substantiate more than two instances of misconduct per week.

Notable corporate wrongdoings, such as the 2001 Enron scandal (Nix, Decker & Wolf 2021) and the 2016 Wells Fargo cross-selling scandal (Tayan 2019; Welch 2020), serve as stark examples. Enron's extensive accounting fraud and manipulation of financial statements led to the revocation of its wholesale energy trading license and eventual bankruptcy, destroying its reputation. In contrast, Wells Fargo, while not losing its business license, had to make significant reforms to address unauthorized accounts, improve internal controls, and rebuild public trust. Although Wells Fargo's reputation remains tarnished, it continues to operate in the industry with potential for rehabilitation through further measures.

These anecdotes suggest that corporate misconduct poses a serious threat to corporate reputation. Corporate reputation, in this context, refers to the extent to which a company is highly esteemed, worthy, or meritorious and held in high regard by evaluators (Dollinger, Golden, & Saxton 1998). Given the value of a favorable reputation for company performance (e.g., Pfarrer, Pollock, & Rindova, 2010; Rindova, Williamson, Petkova, & Sever, 2005; Raithel & Schwaiger 2015; Roberts & Dowling, 2002), extensive research explores the impact of corporate misconduct on corporate reputation and emphasizes the importance of defending a company's reputation after misconduct (e.g., Bundy, Iqbal & Pfarrer, 2021; Lamin & Zaheer, 2012; Love & Kraatz, 2009; Pfarrer et al. 2008; Raithel & Hock 2021; Rhee & Haunschild, 2006; Zyglidopoulos, 2001).

Although this research has advanced our understanding of the impact of corporate misconduct on corporate reputation, a closer examination of the Enron and Wells Fargo scandals highlights a factor that has been largely overlooked to date: the varying levels of reputational harm resulting from different penal sanctions (i.e., Enron had its business license revoked, while Wells Fargo did not).

This factor is relevant because a substantial body of research in criminology has examined the role of penal sanctions in response to blue- and white-collar crimes (e.g., Grabosky, Braithwaite & Wilson 1987, Jobard 2023, Laumond 2020, Michel 2021). Penal sanctions serve multiple functions, including general and individual deterrence, retribution, rehabilitation, restitution, and incapacitation (e.g., Bottoms & Von Hirsch, 2010; McFatter, 1982). In criminology, one line of research argues that the type of penal sanction imposed also influences the reputational losses resulting from misconduct (Iacobucci 2014). This argument is backed by Braithwaite (1989) who formulated the Reintegrative Shaming Theory (RST), which distinguishes between reintegrative and stigmatizing sanctions. The central principle of RST is that reintegrative sanctions are socially preferable because they uphold the fundamental goodness of the offender's identity while solely denouncing the deviant act as evil, rather than branding the offender as a person (Braithwaite, 1989). The key argument is that stigmatizing sanctions, which satisfy the victim's or public's desire for vengeance and repayment, label the entire offender as evil. Such denunciation turns the offender into a social outcast, thereby increasing the likelihood of recidivism. Braithwaite further argues that evaluators process signals conveyed through sanctions depending on whether they believe the corporation, just like any individual, is a valuable member of society. This corporate communitarianism (Braithwaite 1989, Bone 2011) could therefore be an important boundary condition for how penal sanctions can affect corporate reputation. Corporate reputation literature, however, lacks theoretical and empirical evidence for the role of penal sanctions and relevant boundary conditions.

This study aims to address this research gap and to explore how penal sanctions with varying reintegrative and stigmatizing potential affect stakeholders' perceptions of a corporation's reputation following corporate misconduct. Drawing on RST, we argue that financial sanctions are more integrative and less stigmatizing than non-financial sanctions. Furthermore, we theorize that the perceived levels of reintegration and stigmatization associated with the penalty mediate the impact of the penalty on reputation loss after corporate misconduct. An experiment comparing eight penalty types with varying financial and non-financial components demonstrates that, on average, financial penalties have a less negative impact on corporate reputation compared to non-financial penalties, and that this effect is mediated by the perceived reintegration potential of the penalty, but this effect is not mediated in parallel by stigmatization potential. Further, this mediation effect of reintegration becomes stronger (weaker) if respondents believe that corporations are (not) a valuable member of society.

These novel findings have several important implications for researchers, managers, and policymakers. We demonstrate that the impact of corporate misconduct on corporate reputation is not solely determined by the type of misconduct and the company's reputation defense strategy, but also by legal ramifications. This finding implies that, for example, during plea bargaining, managers and their legal advisors should also consider the impact of the penal sanction (if conviction is unavoidable) on external evaluators' perceptions of the company. Policymakers should also reflect on the impact of penalty sanctions for corporate misconduct in terms of their ability to condemn the wrongful act while reintegrating the organization as a whole. By thoughtful design of the penal sanction, they can influence the company's reputation damage and therefore affect the company's ability to continue its business.

THEORETICAL BACKGROUND

Corporate Misconduct and Corporate Reputation

Reputation serves as stakeholders' collective evaluation of an organization's ability to outperform competitors in creating value (Fombrun, 2012; Rindova et al., 2005). It is influenced by the organization's financial, social, and environmental impacts over time (Barnett, Jermier & Lafferty, 2006). Essentially, reputation acts as a predictor of future behavior based on stakeholders' expectations and perceptions of past conduct (Bigus, Hua & Raithel, 2023; Fombrun & Shanley, 1990). In simpler terms, corporate reputation reflects how highly esteemed, worthy, or esteemed an organization is perceived to be by evaluators (Dollinger, Golden, & Saxton, 1998).

Violating established norms or engaging in corporate misconduct puts companies at risk of damaging their reputation, resulting in various negative consequences (Coombs & Holladay, 2002). Beyond the direct harm to reputation (e.g., Bundy et al., 2021; Love & Kraatz, 2009; Rhee & Haunschild, 2006), violations can lead to additional repercussions such as the erosion of stakeholder trust and goodwill (Fuoli, van de Weijer, & Paradis, 2017; Zyglidopoulos, 2001), negative media coverage (Zavyalova, Pfarrer, Reger, & Shapiro, 2012), and executive turnover (Arthaud-Day, Certo, Dalton, & Dalton, 2006). Other negative consequences include negative perceptions from employees and customers (Coombs & Holladay, 2014; Davies, Chun &

Kamins, 2010), unfavorable word-of-mouth and stakeholder perceptions (Coombs, 2007), or a decline in stock prices (Raithel & Hock, 2021).

As a result, researchers in management have increasingly focused on understanding how organizations protect and restore their reputation following violations (Bundy et al., 2021; Love & Kraatz, 2009; Mishina, Block, & Mannor, 2012; Rhee & Haunschild, 2006; Rhee & Valdez, 2009; Zavyalova et al., 2012; Zavyalova, Pfarrer, Reger, & Hubbard, 2016). These studies aim to uncover effective strategies and mechanisms that enable companies to successfully navigate these challenges and regain stakeholder trust.

Penal Sanctions and Corporate Reputation

While prior research has typically assumed that reputational sanctions operate independently of legal penalties, Iacobucci (2014) argues that observers evaluate the nature of wrongdoing in light of the actual conduct and the corresponding legal consequences. For instance, when a corporation engages in misconduct despite facing severe legal penalties, observers are more likely to form a negative perception about the corporation's propensity for wrongdoing in the future compared to situations where legal penalties are lenient.

It is worth considering that higher ex post legal penalties may be imposed when the probability of detection is low, following the traditional logic proposed by Becker (1968). Consequently, high ex post legal penalties may overstate expected penalties, while low ex post legal penalties may underestimate them, which adds complexity to the relationship between imposed and expected penalties. Nevertheless, Iacobucci (2014) establishes a connection between expected legal penalties and informal reputational sanctions, without suggesting a direct causal relationship between higher legal penalties and higher reputational sanctions.

It is important to note that the concept of reputational damage, as described here, is not solely based on the negative change in reputation before and after misconduct. Instead, it considers the impact of penal sanctions as an information signal used to rectify the cognitive dissonance caused by misconduct, thereby influencing evaluators' assessments of both the wrongdoing and the penal sanction as well as their conclusions about the "qualities" and future intentions of the company captured by the evaluators' reputation perception.

Braithwaite's (1989) Reintegrative Shaming Theory

In his 1989 book 'Crime, Shame, and Punishment,' John Braithwaite presents Reintegrative Shaming Theory (RST) as an attempt at a general theory of crime. As a theory explaining why people engage in crime, it draws upon various earlier theories such as social control, labeling, subculture, opportunity structure, routine activities, and learning, while also incorporating considerations of gender and social class. The innovative aspect of the theory, however, lies in its answer to the question of how to address crime – through the utilization of shame. This approach had been previously developed regarding corporate crime but was considered problematic for everyday individual delinquency due to the potential for stigmatization (Fisse & Braithwaite, 1983). Therefore, in the pursuit of a general theory of crime, the objective was to avoid stigmatization and instead "maintain bonds of respect" through reintegrative shaming.

Interestingly, and in alignment with Braithwaite's observation that crime is disproportionately committed by young people, he considered the conflict resolution methods of "loving families" (1989: 56) as a model for reintegrative shaming, emphasizing reconciliation and mutual support as essential elements for coexistence. Another crucial model is Japan, which

Braithwaite referred to as “the family model writ large” (1989: 63), describing its society as characterized by high interdependence among individuals and a highly developed sense of communitarianism. This provides an environment conducive to reintegrative and inclusionary shaming, as opposed to stigmatizing and exclusionary shaming.

Consequently, Braithwaite argued that official punishment should not be more severe than necessary to “communicate the degree of community disapproval appropriate to the offense” (Braithwaite 1989: 178). In this vein, formal punishments should be visible and aimed at supporting the social reintegration of the individual, such as community service or forms of restitution, while imprisonment should be avoided. This approach, focusing on repairing the harm caused to individuals or the community by the offender and reintegrating the offender into the community, has established RST as one of the theoretical cornerstones of Restorative Justice (RJ; see Daly & Hayes 2002, Van Ness 2012, Wachtel 2012). Nevertheless, formal sanctions such as community service related to the offense, court-ordered victim sensitivity or empathy training, or financial compensation are only partially restorative (Wachtel 2012). Other, more traditional formal sanctions, such as imprisonment, probation/parole without RJ measures as obligations, or fines, are not considered restorative or reintegrative in the sense of RST because they fail to address the needs of the stakeholders in the social conflict arising from the crime.

While white-collar crime does not align with Braithwaite’s description of the most common features of crime, he included this field in his 1989 book and advocated for reintegrative shaming sanctions for white-collar crime. However, while there are suggestions from RJ theory for reintegrative sanctions in cases of everyday crime, it remains unclear if these same sanctions foster reintegration and repair the reputation of a corporation when applied to cases of corporate crime.

The Reintegrative and Stigmatizing Effects of Penal Sanctions on Corporate Reputation

Traditional penal sanctions, commonly associated with official responses to criminal acts by law enforcement agencies, typically damage an individual's reputation by recording convictions on their criminal record (Herzog-Evans, 2011). While various responses to wrongdoing, including those integrated into penal sanctions systems like community service (under specific circumstances), victim sensitivity or empathy training, and financial compensation, are recognized by experts for their partial restorative and reintegrative qualities, applying such measures becomes complex when dealing with collective entities such as companies committing offenses. Moreover, it's essential to acknowledge that experts' perspectives may not necessarily align with the perceptions of those who form opinions about a company's reputation.

As Braithwaite argued in 1989, reputation is not merely a financial concern for a company; it holds intrinsic value for its management. Corporations seek to avoid the internal repercussions of a tarnished reputation, such as diminished employee morale and the risk of being perceived as lawbreakers. Therefore, any response to corporate wrongdoing must consider the objective of restoring the company's reputation. A negative reputation could lead the offenders to rationalize their misconduct, potentially by deflecting blame onto other stakeholders or mirroring the accusations. These rationalization techniques, akin to those described by Sykes & Matza (1957) for young offenders, were also evident in white-collar criminals as far back as the 1950s and 1960s, as noted by Cressey (1953) and Geis (1967). Braithwaite (1978) observed examples of a damaged reputation contributing to such rationalizations and the perpetuation of a criminal subculture within a particular business sector.

Sanctions can exert not only momentary negative effects on reputation but can also offer an opportunity for redemption and reintegration into society, as demonstrated by Maruna (2011) in the context of street crime offenders. Alternatively, some sanctions may be seen as more exclusionary and therefore more stigmatizing. Hence, it is crucial to consider the potential for redemption and reintegration when determining the most suitable sanction for a particular case.

Most sanctions available in legal systems that address wrongdoing by an entire company tend to be direct financial penalties. These may encompass punitive damages awarded to injured parties, fines that can take the form of donations to charitable organizations, or profit-skimming. Such financial penalties imposed on a company, although a reaction to what amounts to a criminal offense, may not be perceived as a “hard” criminal penalty. Financial sanctions allow offenders to remain within the community rather than being removed from it through non-financial sanctions such as imprisonment or bans. Financial sanctions promote wrongdoers’ continued connection to their support systems and community, which is important for their eventual reintegration into society. Financial sanctions require offenders to take responsibility for their actions and be accountable for the harm they’ve caused. This acknowledgment of wrongdoing can be a step toward reintegrating the offender into the community. Financial sanctions can include restitution to victims or contributions to community programs, serving as a way for the offender to make amends and contribute positively to those affected by the offense. Financial sanctions can be tailored to the specific circumstances of the offense, ensuring that the punishment is proportionate to the harm caused. This aligns with the principles of restorative justice, which emphasize fair and just responses to crime.

Non-financial sanctions that focus on the individual culpability of senior managers encompass the usual array of penalties, including prison sentences, individual fines, community service, and even prohibitions on working within a particular industry. While serving a sentence of imprisonment, offenders often have limited access to rehabilitative programs or the opportunity to address the underlying issues that led to their criminal behavior. Such non-financial sanctions are often viewed as more stigmatizing because they involve physical separation from the community and the social stigma associated with incarceration. It can be challenging for individuals who have been imprisoned to reintegrate into society upon release due to the barriers they may face. Of course, such sanctions affect single actors rather than the corporation as a whole. However, non-financial sanctions such as imprisonment and job ban of managers can highlight ethical concerns, disrupt operations, and lead to pronounced employee and consumer concerns about the integrity and trustworthiness of the corporation, which is embodied by its management. Non-financial sanctions may therefore draw more attention to the ethical and social aspects of corporate wrongdoing. They can highlight concerns about a company's ethical behavior and commitment to social responsibility.

In summary, non-financial sanctions against a company may have a more severe impact on its corporate reputation compared to financial sanctions. This effect is conveyed through varying degrees of reintegration and stigmatization signaled to the external evaluator. These considerations are formulated in H_1 and $H_{2a/b}$.

H_1: *Financial (vs. non-financial) penal sanctions have a less (vs. more) negative effect on corporate reputation.*

$H_{2a/b}$: *The less (more) negative effect of financial (vs. non-financial) penal sanctions on corporate reputation is mediated by the evaluators' (a) perceived reintegration and (b) perceived stigmatization of the penal sanction.*

The Moderating Role of Corporate Communitarianism

The way people perceive and react to sanctions is profoundly influenced by the social structure, according to Braithwaite (1989). This contrast between individualist and communitarian societies is pivotal in comprehending this impact. In individualist societies, where individual interests and independence are highly valued, sanctions are mainly viewed as punitive measures aimed at deterring unwanted behavior (Maignan 2001). These societies prioritize individual responsibility and personal accountability.

Conversely, in communitarian societies, where collective values and interdependence are paramount (Braithwaite 1989; Ploeg et al. 2022), the perception of sanctions considers their effects on the entire community. People in such societies are more attuned to social bonds and mutual obligations within their community, making them receptive to both reintegrative and stigmatizing signals conveyed through sanctions. The deep interconnectedness of individuals in communitarian societies (Braithwaite 1989) leads to a heightened interest in the actions and behavior of fellow community members. They pay specific attention to information regarding the fulfillment of obligations within the community, recognizing that each member bears moral responsibility for the well-being of the community.

Braithwaite (1989) indirectly acknowledges that corporations, like individuals, have legal rights and moral responsibilities within the community. This perspective is further supported by Bone (2011: 293), who characterizes communitarianism as viewing corporations as "individualist entities with the rights and corresponding responsibilities of natural persons." Combining the arguments of both authors, we define corporate communitarianism as the belief that corporations are valuable contributors to the community and play a pivotal role in its well-being.

Individuals who strongly embrace corporate communitarianism hold companies to high expectations and see them as valuable community members. Consequently, when a company engages in misconduct, it is perceived as failing in its role as a valued community member. The signal conveyed through the form of punishment regarding the company's standing within the community carries more weight for those deeply committed to corporate communitarianism, as opposed to those with weaker commitments.

From this perspective, reintegrative signals that reaffirm the corporation's ongoing membership in the community should result in less reputational damage, provided the evaluator believes that corporations are generally valuable members of society. Conversely, penalties that tend to stigmatize the wrongdoer have a more adverse impact on the evaluator's perception of the wrongdoer's reputation. This occurs because a stigmatizing penalty contradicts the evaluator's overarching belief that corporations are essential contributors to society, fostering greater uncertainty about the true character and future intentions of the wrongdoer, resulting in more significant damage to the company's reputation.

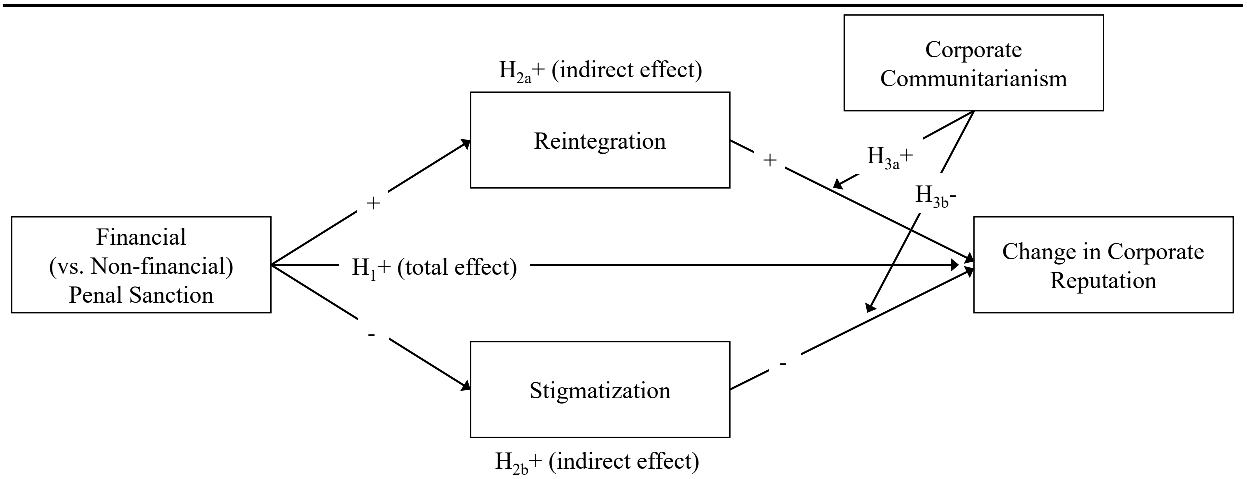
For evaluators who believe that corporations do not contribute positively to society, instances of misconduct align with their negative perception of corporations. Consequently, the penalty sanction is not assessed in terms of whether it does or does not reaffirm the company's standing as a valuable member of society, rendering penalty signals ineffective in shaping the evaluator's perception of the company's reputation.

In sum, corporate communitarianism strengthens the mediating effects hypothesized in $H_{2a/b}$:

$H_{3a/b}$: *Corporate communitarianism moderates the effects of (a) perceived reintegration on corporate reputation positively and of (b) perceived stigmatization on corporate* *reputation negatively, such that the penalty's indirect effects via reintegration and via stigmatization on corporate reputation both become stronger (weaker) if corporate communitarianism is high (low).*

Figure 1 summarizes the conceptual model and hypotheses.

FIGURE 1. Conceptual Framework



EXPERIMENTAL STUDY

Participants, Method, and Design

We recruited 250 U.S.-based, "CloudResearch approved participants" (approval rate >80%, <5,000 studies completed) through the TurkPrime application for nominal payment. Sixty-five participants did not pass the manipulation check (see below) and were excluded (the Appendix shows all study details). Thus, our analyses are based on 185 participants (M_{age} = 41.96, 61% female, 2% non-binary). This study used a one factor (eight different company sanctions) between-subjects design with random assignment.

First, we assessed corporate communitarianism with a self-developed 4-item measure (sample item: "*Corporations are valuable for our society*"). Due to low factor loading of one item, we decided to drop this item and combine the remaining three items into one factor (α = .71; AVE = 64.1%).

Then, we exposed participants to the description of the fictitious company Dairy Delights: "*Dairy Delights is a large ice cream manufacturer headquartered in Michigan, United States. With $20 million net income in 2022, it is one of the most profitable manufacturers in its industry*" and assessed Dairy Delights' pre-manipulation reputation. We used a measure from Raithel and Schwaiger (2015), which consists of six 7-point Likert scales and captures both perceptions of a company's abilities ("competence") and feelings about the company ("likeability"). Sample items include *"[X] is a top competitor in its market*" (competence) and "*I regard [X] as a likable company" (likeability)* (α_{Pre} = .76, AVE_{Pre} = 47.5%).

Next, we told participants that Dairy Delights' top management continued to sell ice cream nationwide despite knowing that it was contaminated with Salmonella and randomly assigned participants to one of the eight conditions presenting the penal sanction:

(1) Dairy Delights is prohibited to produce and sell the involved ice cream products for three months.

(2) Dairy Delights is skimmed its excess profits (disgorgement of 10% of its 2022 profits: $2 million).

(3) Dairy Delights must spend $2 million on corrective advertising in which the CEO acknowledges responsibility and expresses an apology.

(4) Dairy Delights must pay financial redress for hospitalized consumers harmed by the conduct in the amount of $10,000 per case ($2 million in total).

(5) Dairy Delights must donate $2 million to a local community food bank.

(6) The CEO is banned from the company board.

(7) The CEO is sentenced to prison.

(8) The CEO is imposed 120 hours of community service in a local community food bank.

For the analysis, we combined sanctions (1) – (5) as financial sanctions and (6) – (8) as non-financial sanctions. During the manipulation check, participants had to select the correct penalty sanction which applies to their scenario.

Participants then assessed how appropriate the sanction was (1 = Fully inappropriate, 7 = Fully appropriate). In the following, we assessed the mediator *Perceived Reintegration* with a short-form 3-item measure adapted from Harris (2006; sample item: "*Dairy Delights deserves a second chance*"; $\alpha = .84$; AVE = 75.5%). We assessed our mediator *Perceived Stigmatization* with a short-form 3-item measure adapted from Shi et al. (2022; sample item: "*Dairy Delights is dangerous*"; $\alpha = .69$; AVE = 61.7%) (all from 1 = fully disagree, 7 = fully agree). We used principal component analysis with VARIMAX rotation to yield two linear independent measures of our mediators ($AVE_{combined} = 69.3\%$; all factor loadings > .5; all |crossloadings| < .5). Then, participants rated Dairy delights' post manipulation reputation using the same items as for the pre manipulation reputation ($\alpha_{Post} = .92$; $AVE_{Post} = 72.3\%$). We used principal component analysis to calculate the pre- and post-manipulation scores for reputation. The difference between both scores (post minus pre) served as our dependent variable (change in corporate reputation). Finally, we obtained some demographic information, such as age, gender (female, male, non-binary), and political orientation (liberal, republican, prefer not to say).

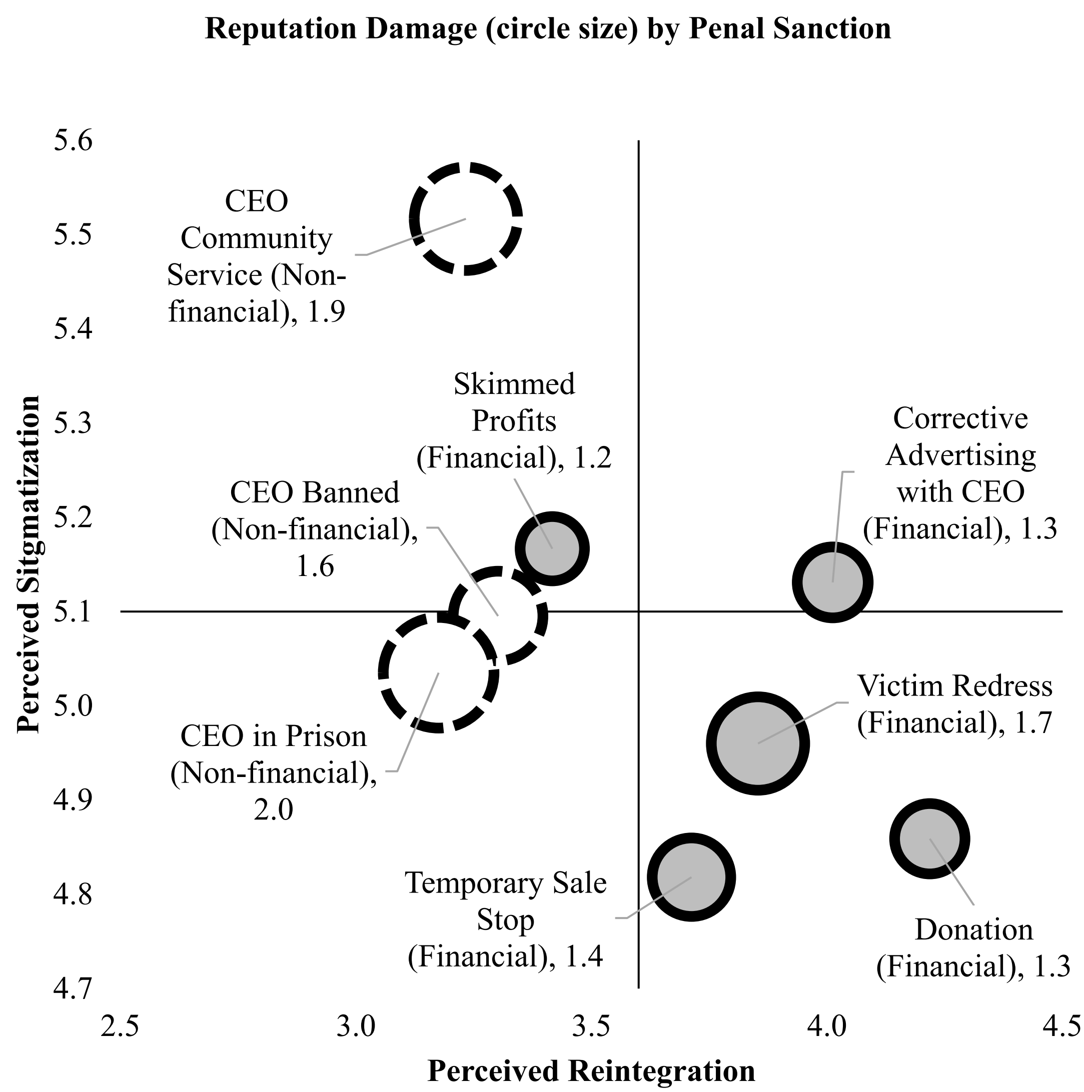
Group equivalence. The two experimental groups financial vs. non-financial penalty are equal with regard to age ($F(1, 183) = .403$, $p = .526$), gender ($\chi^2(2) = 1.501$, $p = .472$), and political orientation ($\chi^2(2) = 1.631$, $p = .442$). Further, the experimental groups are equal with regard to pre-manipulation reputation ($F(1, 183) = 1.887$, $p = .171$).

Results

Visual inspection of data

Figure 2 visualizes the raw data. This chart displays perceived integration (x-axis), perceived stigmatization (y-axis) and reputation *damage* (i.e., negative change in corporate reputation; circle size) for each of the eight penal sanctions. This figure shows that different penal sanctions can send rather heterogenous signals to evaluators as ranges of reintegration (span = 1.04 Likert scale points), stigmatization (span = .70), reputation damage (span = .84) indicate. Further, the correlation of reintegration and stigmatization is relatively high ($r = -.56$) which justifies the decomposition into two orthogonal factors to allow for analytical separation of effects of reintegration and stigmatization. Finally, this figure might also suggest that the penal sanction may have other characteristics beyond the financial dimension (e.g., group vs. personal sanction, salience of the victim) which are also correlates of reintegration, stigmatization, and reputation damage. We explore this question and limitation of this experiment in the discussion section.

FIGURE 2. Reintegration, stigmatization, and reputation damage by penal sanction



Financial vs. non-financial sanctions and reputation (H_1)

There was a significant difference between financial and non-financial sanctions on change in reputation ($M_{financial}$ = .090, *SD* = 1.106 vs. $M_{non\text{-}financial}$ = -.187, *SD* = .941; *F*(1, 183) = 2.783,

p = .097).[1] The reputation damage is smaller for financial sanctions than for non-financial sanctions. This effect is much more pronounced when controlling for pre-manipulation reputation. The regression coefficient of financial (vs. non-financial) sanction is .402 (SE = .140, p = .004). These findings provide support for H_1.

Financial vs. non-financial sanctions and the mediation effect of reintegration (H_{2a})

There was a significant difference between financial and non-financial sanction types on reintegration ($M_{financial}$ = .135, SD = .987 vs. $M_{non\text{-}financial}$ = -.281, SD = .975; $F(1, 183) = 7.275$, p = .008). The perceived integration is larger for financial sanctions than for non-financial sanctions. This effect replicates when controlling for pre-manipulation reputation. The regression coefficient of financial (vs. non-financial) sanction is .318 (SE = .138, p = .022). To test the mediation effect, we employed the SPSS bootstrapping macro developed by Hayes (2017, model 4) with 5,000 bootstrap samples. Sanction type served as independent variable, reintegration as mediator, and change in reputation as dependent variable. Results revealed that perceptions of reintegration mediated the effect (β = .094, SE = .047; 95% CI: [.016, .199]) of sanction type on reputation loss. The effects replicate when controlling for pre-manipulation reputation (β = .201, SE = .090; 95% CI: [.031, .388]). These findings provide support for H_{2a}.

[1] Note that the herein presented results are based on the differences of z-standardized factor scores for pre- and post-manipulation reputation. The positive value for the financial penalty type ($M_{financial}$ = .090) does not imply that a penalty can improve reputation. In fact, the average change of corporate reputation across all sanction types is significantly negative (M = -1.510, SD = 1.264, t = -16.251, p = .000, M_{min} = -2.000, M_{max} = -1.160). This change is measured by the difference of the unstandardized mean item scores for the post- and pre-manipulation reputation measures. This result shows that corporate misconduct involves a reputation damage, and a penal sanction can only limit but not avoid reputation damage for the company. Figure 2 above shows that for each penalty type we observe a reputation *damage*, i.e., negative change in reputation.

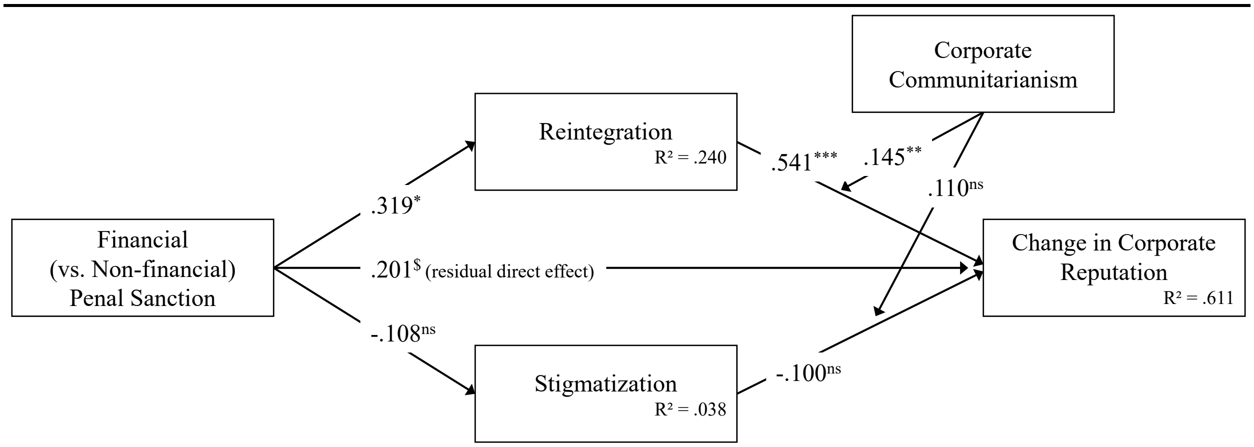
Financial vs. non-financial sanctions and the mediation effect of stigmatization (H_{2b})

There was no significant difference between financial and non-financial sanction types on stigmatization ($M_{financial}$ = -.202, *SD* = 1.082 vs. $M_{non\text{-}financial}$ = .045, *SD* = .809; *F*(1, 183) = .180, *p* = .672). This insignificant effect replicates when controlling for pre-manipulation reputation. The regression coefficient of financial (vs. non-financial) sanction is -.108 (SE = .156, p = .488). As we do not find a significant effect of financial (vs. non-financial) sanctions on stigmatization, we do not find support for the mediation hypothesis H_{2b}.

The moderating effects of corporate communitarianism (H_{3a} and H_{3b})

To test the moderated mediation effect, we employed the SPSS bootstrapping macro developed by Hayes (2017, model 14) with 5,000 bootstrap samples. Sanction type served as independent variable, reintegration and stigmatization as mediators, communitarianism as moderator, pre-manipulation as control, and change in reputation as dependent variable. Figure 3 shows the estimation results.

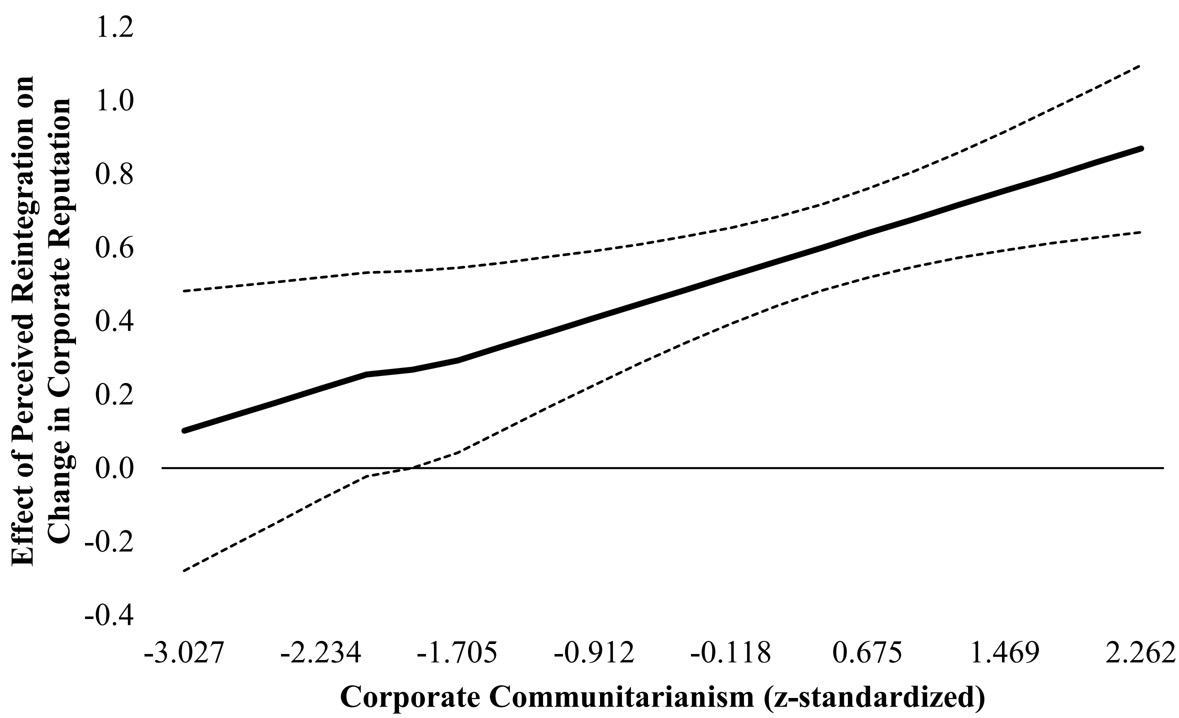
FIGURE 3. **Estimation results for the full model**



Notes: *** p < .001 ** p < .01 * p < .05 $ p < .10
Control: Pre-manipulation Corporate Reputation

The results revealed that communitarianism moderates the mediation effect of reintegration in the relationship between sanction type and change in reputation. The interaction effect reintegration*communitarianism on change in reputation is significantly positive (β = .145, *SE* = .053; p = .007). A flood light analysis (see Figure 4) shows that the Johnson-Neyman (JN) point for communitarianism is -1.879 which implies that already at relatively low levels of communitarianism, the effect of reintegration on change in reputation becomes significantly positive (β_{JN} = .268, *SE* = .136; p = .050). With increasing communitarianism (max = 2.262) this effect builds up (β_{max} = .869, *SE* = .115; p = .000).

FIGURE 4. Floodlight analysis for the effect of perceived reintegration on change in corporate reputation moderated by corporate communitarianism



Note: Dashed lines represent the 95% confidence intervals

When communitarianism increases, the indirect effect of financial (vs. non-financial) sanction via reintegration on change in reputation becomes accordingly stronger. At low levels of communitarianism (16% percentile) the indirect effect is .133 (SE = .064; 95% CI: [.017, .270]), at medium levels of communitarianism (50% percentile) the indirect effect is .170 (SE = .078; 95% CI: [.023, .333]), and at high levels of communitarianism (84% percentile) the indirect effect is .222 (SE = .103, ; 95% CI: [.029, .434]). The index of moderated mediation is significantly positive (β = .046, *SE* = .029; 95% CI: [.003, .113]), which implies that the indirect effect of financial (vs. non-financial) sanctions on reputation via reintegration is moderated positively by corporate communitarianism. These findings provide support for H_{3a}.

The results further revealed that communitarianism does not moderate the mediation effect of stigmatization in the relationship between sanction type and change in reputation (see Figure 3 above). The index of moderated mediation is not significantly different from zero (β = -.012, *SE* = .020; 95% CI: [-.040, .027]). These findings do not provide support for H_{3b}.

DISCUSSION

Implications for Research and Practice

This study represents a comprehensive merger of two distinct areas of research: the analysis of corporate misconduct's repercussions on corporate reputation and the examination of sanctions in the context of criminal offenses. Drawing inspiration from Braithwaite's influential Reintegrative Shaming Theory (1989), the study ventures to shed light on the intricate relationship between various types of sanctions and the reputation of corporations following instances of corporate misconduct.

This research combines two pivotal realms of inquiry. Firstly, it delves into the extensive body of work investigating the profound impact of corporate misconduct on corporate reputation, referencing influential contributions (e.g., Bundy, Iqbal & Pfarrer, 2021; Lamin & Zaheer, 2012; Love & Kraatz, 2009; Pfarrer et al. 2008; Raithel & Hock 2021; Rhee & Haunschild, 2006; Zyglidopoulos, 2001). Secondly, it extends its reach into the jurisprudential landscape that explores the multifaceted role of sanctions as responses to criminal behavior, invoking prominent research (e.g., Grabosky, Braithwaite & Wilson 1987, Jobard 2023, Laumond 2020, Michel 2021). This integration forms the foundation for a comprehensive examination of how sanctions intersect with corporate reputation in the wake of corporate wrongdoing.

One of the salient findings of this study is the discernible influence of the type of sanction employed. It reveals that financial penalties tend to have a less damaging effect on corporate reputation compared to non-financial penalties. This insight holds practical significance for both organizations navigating the treacherous waters of corporate misconduct and the policymakers responsible for crafting punitive measures. It suggests that imposing financial consequences, such as fines, disgorgement, or reparations, may be a more favorable route for preserving a corporation's reputation, compared to non-financial measures like bans or imprisonment. This nuanced understanding aids in guiding the selection of sanctions that best align with the goal of reputation restoration.

The study unearths compelling insights into the mechanisms through which sanctions impact corporate reputation. It highlights the mediating role of perceived reintegration—namely, how stakeholders perceive a corporation's efforts to reintegrate into the community following a sanction. This mediating factor significantly influences the trajectory of corporate reputation. It suggests that penal sanctions aimed at effectively reintegrating a corporation into the societal fabric are pivotal in rebuilding a tarnished reputation. However, the study also underscores that the perception of stigmatization, in contrast, does not play a significant role in shaping corporate reputation post-sanction.

An intriguing facet of the study lies in its examination of how cultural and societal factors, particularly the concept of corporate communitarianism, can moderate the relationship between sanctions and corporate reputation. The study reveals that in communitarian societies or among individuals who hold strong corporate communitarian beliefs, reintegration efforts have a more pronounced impact on corporate reputation. This signifies the need for a nuanced, culturally sensitive approach to corporate reputation management and post-sanction recovery. It highlights that the perception of the corporation as a valuable contributor to the community profoundly shapes the consequences of sanctions and reintegration efforts.

In conclusion, this study offers a nuanced and comprehensive perspective on the interplay between sanctions, corporate reputation, and contextual factors. It provides actionable insights for organizations, policymakers, and scholars, underscoring the significance of understanding the specific nuances of both the nature of sanctions and the cultural context in which they are applied. In practical terms, these findings suggest that organizations (and their legal advisors) facing corporate misconduct should consider the cultural and societal context in which they operate. They should also pay attention to how different types of sanctions, especially financial sanctions, impact the corporation's reputation and its efforts to reintegrate into the community. Additionally, policymakers and regulators should be mindful of the potential consequences of different sanction types on corporate reputation and consider the contextual factors at play when designing penalties for corporate misconduct cases.

Future Research

This study represents a crucial initial step in our quest to better comprehend the role of penal sanctions in shaping reputation perceptions following corporate misconduct. While we have made significant strides in this investigation, a multitude of important questions remain unanswered. The future research landscape in this domain is rich with opportunities to delve deeper into the intricate dynamics surrounding corporate misconduct, penal sanctions, and their far-reaching consequences. Here, we outline several promising avenues for further exploration:

To construct a more comprehensive understanding of the impact of penal sanctions, future research should venture into greater diversity in the types and severity of sanctions. For example, the Australian Competition & Consumer Commission lists a wide range of legal actions to sanction competitive harm or substantial consumer or small business detriment (ACCC 2023). This exploration could encompass a deeper analysis of financial sanctions, encompassing a spectrum of financial penalties in terms of form and magnitude. Additionally, researchers could pivot towards non-financial sanctions, extending beyond the CEO to target specific individuals within the top management team (TMT). These nuances may provide important insights into the differential effects of sanctions.

In real-world scenarios, legal ramifications often do not manifest in isolation. Researchers can delve into the complex interplay of financial and non-financial penal sanctions, examining how these various punitive measures combine and interact. Understanding the potential synergies or conflicts between different penalties could shed light on their collective impact on corporate behavior and post-sanction reputation.

Expanding beyond a singular type of misconduct, future research can embrace a broader spectrum of corporate misbehavior. Different forms of misconduct may trigger distinct responses and carry unique implications for corporate reputation and behavior. Investigating these variations can offer a more nuanced perspective on the consequences of penal sanctions.

The strategies adopted by companies in response to potential misconduct warrant a closer look (e.g., Bundy et al. 2021). Researchers can delve into how these strategies either align with or contradict the imposed penal sanctions, offering insights into the role of pre- and post-sanction corporate behavior in shaping public perceptions and reputation outcomes.

In the aftermath of misconduct, companies often have opportunities to rebuild trust and restore reputation (Bozic 2017). Future research could explore one opportunity which are self-sanctioning measures employed by companies that extend beyond mere compliance with legal sanctions. For instance, the outsourcing of monitoring to external parties or the implementation of internal reforms could be studied as strategies for trust repair (Nakayachi & Watabe 2005).

The time gap between the revelation of potential misconduct and the eventual conviction and announcement of penal sanctions poses a methodological challenge. Researchers can explore how this temporal delay influences external evaluators' responses. Analyzing penal sanction announcements as isolated events can provide valuable insights into the temporal evolution of corporate behavior in response to legal actions.

Drawing from insights in criminology (e.g., Zamble & Quinsey 2001), future research can delve into how various penal sanctions affect the behavior of the offending company and its management. Understanding the relationship between company-level and manager-level sanctions and their impact on recidivism can provide valuable insights into the deterrence effects of legal actions.

In conclusion, this study marks the initiation of a broader research agenda that seeks to unravel the multifaceted relationship between penal sanctions, corporate misconduct, and the strategic responses of companies. By addressing these diverse dimensions, future research endeavors can contribute to a more refined understanding of how legal actions shape corporate behavior and reputation in the intricate landscape of contemporary business. The journey toward a more comprehensive comprehension of this intricate interplay promises to yield valuable insights with far-reaching implications for both academia and the corporate world.

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APPENDIX

Experimental Study Details

[Attention Check]

Study

<u>VERY IMPORTANT</u>: Please read the following instructions very carefully, otherwise you may not be able to complete the study.

In this study you'll be asked to read a few scenarios and then answer some related questions. **Please note that the success of our research depends on the sincerity of your participation. So, please do read and follow the instructions carefully. Thank you!**

Sincerity of your responses is what makes our research successful. If you are reading this then in the text box below please enter 6 and not your MTurk ID as mentioned, to begin the study.

Your MTurk ID

[Participants were not able to complete the survey if they did not enter "6"]
--- page break ---
[Corporate Communitarianism; self-developed]
Please indicate how much you agree or disagree with the following statements:
- Corporations are valuable for our society.
- The government should limit the freedom of corporations.
- It is important to have good relationships with corporations.
- A good life without corporations is not possible.

[All from 1 = Fully disagree to 7 = Fully agree]
--- page break ---
[Reputation – Pre; Raithel and Schwaiger (2015)]
Dairy Delights is a large ice cream manufacturer headquartered in Michigan, United States. With $20 million net income in 2022, it is one of the most profitable manufacturers in its industry.
Please indicate the extent to which you agree or disagree with the following statements:
- I can better identify with **Dairy Delights** than with other companies.
- I would miss **Dairy Delights** more than other companies if it did not exist anymore.

- I regard **Dairy Delights** as a likeable company.
- **Dairy Delights** is a top competitor in its market.
- As far as I know, **Dairy Delights** is respected worldwide.
- I believe that **Dairy Delights** performs at a premium level.

[All from 1 = Fully disagree to 7 = Fully agree]
--- 8 seconds delay & page break ---
During an internal inspection in early 2023, **Dairy Delights** discovered that several batches of vanilla ice cream were contaminated with Salmonella, an organism which can cause serious and sometimes fatal infections in young children, frail or elderly people, and others with weakened immune systems. Healthy people infected with Salmonella often experience fever, diarrhea, nausea, vomiting and abdominal pain.
Nevertheless, **Dairy Delights**' top management continued to sell the contaminated ice cream nationwide. After several cases of salmonellosis are reported in the media and linked to this ice cream, the company issued the following product recall:
--- 10 seconds delay & page break ---
Dairy Delights is recalling 500,000 units of its Vanilla ice cream because they have the potential to be contaminated with Salmonella. To date, more than 200 people have been treated in the hospital after eating the ice cream.
[Penalty 1]
The United States Attorney of the State of Michigan announced that **Dairy Delights** must pay a pecuniary fine of $500,000 and is **prohibited to produce and sell the involved ice cream products for three months**.
[Penalty 2]
The United States Attorney of the State of Michigan announced that **Dairy Delights** must pay a pecuniary fine of $500,000 and is **skimmed its excess profits (disgorgement of 10% of its 2022 profits: $2 million)**.
[Penalty 3]
The United States Attorney of the State of Michigan announced that **Dairy Delights** must pay a pecuniary fine of $500,000 and must **spend $2 million on corrective advertising in which the CEO acknowledges responsibility and expresses an apology**.
[Penalty 4]
The United States Attorney of the State of Michigan announced that **Dairy Delights** must pay a pecuniary fine of $500,000 and must **pay financial redress for hospitalized consumers harmed by the conduct in the amount of $10,000 per case ($2 million in total)**.
[Penalty 5]
The United States Attorney of the State of Michigan announced that **Dairy Delights** must pay a pecuniary fine of $500,000 and must **donate $2 million to a local community food bank**.
[Penalty 6]
The United States Attorney of the State of Michigan announced that **Dairy Delights** must pay a pecuniary fine of $500,000 and the **CEO is banned from the company board**.
[Penalty 7]
The United States Attorney of the State of Michigan announced that **Dairy Delights** must pay a pecuniary fine of $500,000 and the **CEO is sentenced to prison**.

[Penalty 8]
The United States Attorney of the State of Michigan announced that **Dairy Delights** must pay a pecuniary fine of $500,000 and the **CEO is imposed 120 hours of community service in a local community food bank**.
--- 6 seconds delay & page break ---
[Manipulation Check]
According to the information you just read, the United States Attorney of the State of Michigan announced that **Dairy Delights** must pay a pecuniary fine of $500,000 and…

- is prohibited to produce and sell the involved ice cream products for three months
- is skimmed its excess profits (disgorgement of 10% of its 2022 profits: $2 million)
- the CEO is banned from the company board
- the CEO is sentenced to prison
- must spend $2 million on corrective advertising in which the CEO acknowledges responsibility and expresses an apology
- must pay financial redress for hospitalized consumers harmed by the conduct in the amount of $10,000 per case ($2 million in total)
- the CEO is imposed 120 hours of community service in a local community food bank
- must donate $2 million to a local community food bank

--- page break ---
Please indicate how appropriate or inappropriate you think this sanction is:
1 = Fully inappropriate to 7 = Fully appropriate
--- page break ---
Dairy Delights' top management **continued to sell contaminated ice cream nationwide** and **[piped in selected manipulation check]** as a sanction.
Please indicate the extent to which you agree or disagree with the following statements.
Dairy Delights...

- ...deserves a second chance.
- ...can be forgiven.
- ...has learned its lesson.
- ...is dangerous.
- ...is cold blooded.
- ...would sell harmful products again.

--- 6 seconds delay & page break ---
[Reputation – Post; Raithel and Schwaiger (2015)]
Dairy Delights' top management **continued to sell contaminated ice cream nationwide** and **[piped in selected manipulation check]** as a sanction.
Please indicate the extent to which you agree or disagree with the following statements.

- I can better identify with **Dairy Delights** than with other companies.
- I would miss **Dairy Delights** more than other companies if it did not exist anymore.
- I regard **Dairy Delights** as a likeable company.
- **Dairy Delights** is a top competitor in its market.
- As far as I know, **Dairy Delights** is respected worldwide.
- I believe that **Dairy Delights** performs at a premium level.

[All from 1 = Fully disagree to 7 = Fully agree]
--- 8 seconds delay & page break ---
Please indicate your age.
Please indicate your gender.
Please indicate your political orientation.
--- page break ---
What do you think we were examining with this survey?