**Organizational Structure: The Case of Toyota**



**Source: Photograph courtesy of Toyota Motor Sales, USA, Inc.**

On the 28th of August 2009 the emergency services in San Diego received a terrifying phone call from the back seat of a Toyota Lexus. The car was accelerating out of control. As the emergency services tried to get an understanding of the situation, the caller was heard to cry, *“We’re now* *approaching the intersection! Oh, pray. Hold on and pray!”* Then silence.

Everyone in the car was killed. Toyota, lauded for its impeccable reputation for quality and reliability, suddenly faced a huge crisis of trust. But they didn’t react as such. Toyota’s belated recalls, belated communications and disclosure, and belated public apologies did far more damage to its reputation than the original tragic accident, losing them sales, market share, and investor and consumer confidence (its pre-eminent reputation for quality plunged from 30% to 19% of respondents to a *Consumer Reports* survey).

*“Central to Toyota’s problem is its perceived delay in identifying and addressing the situation in the first place... There is a sense that it ignored the problem until* *it was forced to take action”.*

Recalls happen every year, and affect every car manufacturer. They are usually considered a bare minimum ‘distrust regulation’ effort. However, a series of recalls from the same company, for different problems, mounts up to a series of trust violations. Toyota had several (in 2004, 2005, 2007, and 2009-10) for different problems, including with accelerators, engines and braking, totaling more than 8.5 million vehicles. This too, has damaged their trust worthiness.

**Immediate response**

Two days after the San Diego crash, Toyota issued a statement, acknowledging the accident, expressing concern and showing regret for the loss of life. Toyota promised a full investigation, working with the regulator (the National Highway Traffic Safety Administration – NHTSA), but declined to comment on possible causes, to *“avoid speculation and allow any investigation to run its course”.*

On the face of it, this is a good example of an immediate response statement. However, our model also calls for swift and decisive actions against *known* or *likely* causes. Toyota appears to have overlooked this latter intervention, disastrously. In the days after the San Diego crash, the company did not issue a customer warning about its all-weather floor mats, despite these being implicated in fatal accidents two years earlier. Even when the regulator’s preliminary investigation into the San Diego crash cited the floor mats as the likely cause, Toyota did not implement a precautionary rectification until five days later when the NHTSA confirmed their analysis, 19 days after the San Diego fatalities. Fortunately no new fatal accidents happened in that time. Yet even with this tardy intervention Toyota dealers were instructed merely to inspect any returned floor mats, rather than issue a direct customer safety warning. NHTSA issued an alert about the floor mats on the 29th September 2009 and that day Toyota issued explicit warnings and advice to customers, and finally announced a recall of 3.8 million affected vehicles – a month after the San Diego crash (The actual recall began a month later still.)

**Diagnosis**

All car manufacturers must cooperate with authorities’ investigations into fatal crashes, and so the ‘diagnosis’ phase began immediately. When the NHTSA reported on the San Diego crash (10th September 2009), Toyota USA uploaded a statement, asserting that the findings were consistent with the company’s floor mat warning, and that their vehicle was *“among the safest”* on the road. NHTSA countered this apparent denial of culpability, and took the unusual step of condemning the statements as *“inaccurate and misleading”*, embarrassing Toyota further. The American division issued a clarification stating that they had not intended *“to mislead or provide inaccurate information”*, and outlined the company’s *“vehicle-based remedy”* to the sticky floor mat problem. For many stakeholders, the obfuscation undermined Toyota’s original best intentions, and further dented the fragile trust with its many stakeholders. In November 2009, Toyota admitted to a defect with the accelerator pedal in some vehicles, promised this was the root cause, and issued a recall of affected vehicles. However, the installation of a ‘brake override system’, intended to reassert the company’s trustworthiness, seemed to highlight a different design defect. Public skepticism meant that Toyota voluntarily commissioned an independent investigation to defend its electronic control systems. These efforts failed, it seems, because of stakeholders’ pre-existing mistrust.

Although design faults seemed at the time to be likely causes of the crashes, many argued that the problems in the company went deeper. Commentators pointed to Toyota’s aggressive growth strategy, epitomized by a declared ambition to be the world’s top automobile company within a decade, involving rapid global expansion of its manufacturing capacity beyond its native Japan. Even the company President, Mr. Akio Toyoda, admitted as much:

 “*Growth over* *speed”* had impaired the company’s culture of ‘kaizen’ (continuous improvement) and ‘genchi genbutsu’ (inspecting problems at the source).

Its own internal report noted Toyota’s tendency to dismiss customer complaints; poor accountability for safety (as the adage goes, *“when everyone is responsible,* *nobody is accountable”*); poor safety-response procedures, and an *“adversarial”* relationship with regulators. Commentators also cited the company’s previously robust and widely admired corporate culture; efficient, systematic and dedicated, but also conservative, rigidly centralized, and mono-national. At the time, the executive board had 29 Japanese male nationals and no foreigners. Japanese reluctance to concede to shame, and Toyota’s prized reputation for excellence, may account for the firm’s hesitancy in acknowledging the legitimacy of the emerging crisis. The company’s hierarchical and centralized structure matched this culture, limiting the speed and accuracy of information flow, stifling the agility of the corporation’s response. Even its vaunted lean production techniques came in for criticism, with junior employees reportedly fearful of raising concerns.

**Performing interventions**

The diagnosis stage didn’t finish fully until March 2010, but Toyota’s reforming interventions began during September 2009 with the floor mat safety warning and the belated recall of 3.8 million vehicles. Their recall problems persisted throughout 2010, with a further 1.66 million vehicles recalled over other, new problems. Many recalls were voluntary, and timely to prevent future accidents, and Toyota was doubtless trying to demonstrate its ability in tackling latent risks, its integrity in disclosing the possible lapses, and its benevolence in prioritizing customer safety. However, the confusion from so many recalls seemed to alarm existing and prospective customers. The firm’s poor immediate response had done huge damage to its credibility, and set the tone for the story (seized upon by the American media).

The first apology came in early October 2009, when Akio Toyoda expressed his sincere grief regarding the San Diego crash:

*“Four precious lives have been lost. I offer my deepest condolences… Customers bought our cars because they thought they were the safest. But now we have given them cause for grave concern. I regret and apologize for this development. I cannot begin to express my remorse”.*

Interestingly, a Professor of Japanese Studies, Ulrike Schaede, argued that these difficult public apologies *“were meant to send a message to company* *employees and car buyers”* that the company was planning a new direction (our emphasis added to indicate the trust repair targets in the statement).

Akio Toyoda’s op-ed piece in the Wall Street Journal wrote of his commitment to customer safety – his name is on the cars after all – and acknowledged the company’s failings (mainly a preoccupation with technical responses to tragedies), and pointed to its recall response and internal and external audits of their vehicles’ safety features. A torrent of similar apologies followed, expressing *“sincere regrets”* and commitments to make *“fundamental changes* *in the way the company operates in order to ensure that Toyota sets an even* *higher standard for vehicle safety and reliability, responsiveness to customers* *and transparency with regulators”* to *“restore the trust”* of its customers. The apologies were well received in the media, for the most part. That month, Akio Toyoda travelled to Washington to face Congress, and apologized again in person – although he insisted he had not been aware of the problems until late 2009, several months after the high-profile San Diego fatalities. In terms of trying to reform Toyota, we found reference to the following key moves:

• A declared reversion to the “basics” of the ‘Toyota way’.

• A new safety system, combining five accident-avoidance technologies – although other automakers have offered these safety features for years.

• A major restructuring, including a reduction in Directors from 27 to 11, and the re-organization of the departments charged with Corporate Planning and Corporate Social Responsibility to quicken crisis responses.

A new 50-strong global quality taskforce, based regionally, and led by the company President, to improve quality, increase communication, improve regional response and autonomy, and seek support from outside experts.

• Two quality advisory panels consisting of outside experts to evaluate Toyota's safety and quality control processes, in 20 dedicated facilities worldwide (although one was criticized for being a paid consultant for the company), and the appointment of a global Chief Safety Officer.

• In September 2010, the company settled out of court with the family of the San Diego victims (corporate ‘penance’).

• Top management’s pay was docked 10% to help “*atone*” for the recall problems, and several Executives forfeited their bonuses for two years (individual leaders’ ‘penance’).

• Commitment to working with U.S. regulators *“toward a common goal of creating a safe automobile society”*.

**Evaluation**

Toyota Motor Corporation (TYO: 7203) has often been referred to as the gold standard of the automotive industry. In the first quarter of 2007, Toyota (NYSE: TM) overtook General Motors Corporation in sales for the first time as the top automotive manufacturer in the world. Toyota reached success in part because of its exceptional reputation for quality and customer care. Despite the global recession and the tough economic times that American auto companies such as General Motors and Chrysler faced in 2009, Toyota enjoyed profits of $16.7 billion and sales growth of 6% that year. However, late 2009 and early 2010 witnessed Toyota’s recall of 8 million vehicles due to unintended acceleration. How this could happen to a company known for quality and structured to solve problems as soon as they arise? To examine this further, one has to understand about the Toyota Production System (TPS).

TPS is built on the principles of “just-in-time” production. In other words, raw materials and supplies are delivered to the assembly line exactly at the time they are to be used. This system has little room for slack resources, emphasizes the importance of efficiency on the part of employees, and minimizes wasted resources. TPS gives power to the employees on the front lines. Assembly line workers are empowered to pull a cord and stop the manufacturing line when they see a problem.

However, during the 1990s, Toyota began to experience rapid growth and expansion. With this success, the organization became more defensive and protective of information. Expansion strained resources across the organization and slowed response time. Toyota’s CEO, Akio Toyoda, the grandson of its founder, has conceded, “Quite frankly, I fear the pace at which we have grown may have been too quick.”

Vehicle recalls are not new to Toyota; after defects were found in the company’s Lexus model in 1989, Toyota created teams to solve the issues quickly, and in some cases the company went to customers’ homes to collect the cars. The question on many people’s minds is, how could a company whose success was built on its reputation for quality have had such failures? What is all the more puzzling is that brake problems in vehicles became apparent in 2009, but only after being confronted by United States transportation secretary Ray LaHood did Toyota begin issuing recalls in the United States. And during the early months of the crisis, Toyota’s top leaders were all but missing from public sight.

The organizational structure of Toyota may give us some insight into the handling of this crisis and ideas for the most effective way for Toyota to move forward. A conflict such as this has the ability to paralyze productivity but if dealt with constructively and effectively, can present opportunities for learning and improvement. Companies such as Toyota that have a rigid corporate culture and a hierarchy of seniority are at risk of reacting to external threats slowly. It is not uncommon that individuals feel reluctant to pass bad news up the chain within a family company such as Toyota. Toyota’s board of directors is composed of 29 Japanese men, all of whom are Toyota insiders. As a result of its centralized power structure, authority is not generally delegated within the company; all U.S. executives are assigned a Japanese boss to mentor them, and no Toyota executive in the United States is authorized to issue a recall. Most information flow is one-way, back to Japan where decisions are made.

On the 20th May 2010, the President of Toyota USA reviewed progress with the company’s reforms to a Congressional committee. In July 2010, Toyota published a report covering its evaluation of measures for improving quality assurance and preventing the recurrence of quality lapses, as well as improving internal and external communications with regard to product quality. The external review panel is scheduled to continue monitoring progress until 2012. Toyota has taken serious actions to put things right. However, their sluggish and contradictory reaction handling of the crisis incurred retribution in April 2010, when the NHTSA fined Toyota a record $16.4m for *“failing to react”* in a timely manner, despite apparently knowing of the potential risk to consumers. Though they denied the allegation, Toyota accepted this ‘penance’, to avoid a lengthy dispute. IHS Global Insight, an automotive consultancy, said the company was *“paying the price for not taking the claims seriously at first”*, and attracting unusually negative publicity as a result. Multi-million dollar law suits are still in train.

A bitter irony is that regulatory investigations in August 2010 found “driver error” to be the most likely cause of all but one of 58 examined incidents. That Toyota was unable to recover much reputational credit from this revelation emphasizes how much trust and goodwill had been damaged, and how the company surrendered control of the narrative with its tardy initial response. Even recently, skeptics (and lawyers) remain unconvinced of the firm’s ethical stance. They point to evidence that the company has known about several design faults for years, and have even boasted of $100m in savings from a limited recall in 2007.One commentator put it:

*“Nothing erodes confidence in a company’s reputation so much as internal documents subordinating safety concerns to the bottom line”.*

It remains to be seen how well Toyota recovers.