

## CASE STUDY

# Whose Business Is It, Anyway?

The Spirit and the Law  
of Sharing Information

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ONE CORNER OF BRADFORD INC.'S STATEMENT OF PRINCIPLES peeked out from the stack of manila folders on Hadley Gaines' desk. A tableau for the times, the investor relations director observed to himself. In day-to-day practice the family-restaurant franchisee's code of ethics was about as instructive as the piece of paper in the folders—handy but hardly compelling.

Hadley's prickly mood in part reflected the hammering Bradford's stock had taken in the week since its earnings conference call. Earnings met expectations, albeit barely. Most of the revenue gain came from restaurants in one city that had hosted a weeklong, statewide high school sports tournament. During the question-and-answer period, the chief executive officer happened to mention the recent resignations of two directors.

Until now that information had seemed of little consequence. One director headed Bradford's restaurant-construction and building-management

subsidiary, but inside the company it was understood that he was a figure-head—he had assumed the title and the board seat as part of Bradford’s acquisition of his company two years earlier. The other director, a member of the audit committee, had been in poor health. Bradford’s legal counsel was of the opinion that all that was necessary by way of announcement was to include the resignations in routine filings with the Securities and Exchange Commission.

Hadley had raised the possibility of news releases as the events occurred but was persuaded by the chief communications officer, with the CEO’s concurrence, that the more significant news would be the appointment of new board members. Besides, to tell the truth, Hadley was happy to avoid questions about the progress of the director search or speculation about whether the positions would be filled by members of the company’s founding family, subjects that were sure to come up if the replacements weren’t immediately identified.

Moreover, Hadley was concerned with bigger matters than board vacancies. For one thing, like many companies, Bradford had characterized its unexciting financial performance as a reflection of the stalled economy. That was beginning to wear thin with two big shareholders who urged more aggressive expense control in light of consumer spending trends.

A private investor’s comment during the conference call fanned yet another internal concern. The shareholder complained about the quality of service in restaurants he frequented and questioned whether the company was diverting funds from training programs in order to mask declining profit margins. The comment hit a particularly raw nerve with senior managers. Just a few days before, the CEO had reacted to the most recent customer satisfaction survey by scheduling a summit meeting of key store managers and store operations executives. The last time such events converged, sweeping menu and management changes followed.

Hadley was also aware of newly strained relations between Bradford and its franchiser because of the franchiser's demand that its own audit team review Bradford's accounting. The internal rumor mill said the action was prompted by the size and timing of bonuses for Bradford's top executives and dissatisfaction with how it allocated shared expenses after it acquired its construction and building-management partner.

The fact that the franchiser would question the bonuses at all annoyed Hadley and others who had helped build Bradford from being a single restaurant to being the operator of almost 40 stores in a three-state region. They worked hard and generally were amply rewarded under an incentive compensation program that promoted entrepreneurial behavior and Bradford's version of the philosophy that what's good for the company is good for America.

Hadley was frustrated. Under normal conditions, he reasoned, the investors' issues would represent little more than background noise. Still, he had a sense that in the spirit of teamwork and transparency that was encouraged in the company's statement of principles, he wasn't delivering on implied promises to his key constituency—Bradford's investors. Hadley tried to convince himself that this is what it's like to practice investor relations in a post-bubble stock market and a sluggish economy. Is it? Or have Hadley and Bradford stepped onto a slippery slope of evaporating investor confidence?

*For answers to those questions and suggestions on how Hadley should be managing Bradford's IR program in light of these situations, IRQ turned to experts in investor relations and communication. Here are their responses.*

### **IR REQUIRES PROACTIVE CONSISTENCY**

Hadley Gaines has to be more self-assured and proactive in his position as director of investor relations. Some areas where he can improve his

performance and learn from the circumstances are the earnings call, board membership change, conflict among executives and financial audit.

**Earnings Call.** Hadley must control the conference call. Conference calls have time constraints. In that time the company needs to disseminate information regarding earnings, the state of the business and future direction — all within the confines of Regulation FD. The call also is an opportunity for analysts and shareholders to ask questions relevant to the company’s overall operations.

With this in mind, Hadley must make sure that anyone speaking during the earnings call has a script and that incoming questions are monitored. The questions asked should be broad enough to be relevant to the majority of listeners. Having a script would have allowed Bradford Inc. to prepare for questions regarding the board resignations and possible replacements.

The private investor’s implications that management misappropriated funds and ignored customer-service issues could have been prevented if Hadley had been in charge of the earnings call. The individual investor should have been encouraged to address the quality issues through Bradford’s customer-service department. By allowing this person to speculate on related issues, the company — and Hadley in his role as IR director — allowed a single investor to take up valuable time and possibly prejudice first-time listeners by planting doubt with regard to management competence and ethics. The call also put managers on the defensive in that it set an expectation for them to explain and presumably deny allegations.

However, once the subject was raised, the implication of fund misappropriation should have been addressed immediately during the conference call. The executive management should have said in no uncertain terms that the statements were false and that Bradford does not tolerate and has never tolerated misappropriations of funds. In addition, specifics should have been given on how senior management takes a proactive approach

to customer service by sending out surveys to gauge customer satisfaction and then following up with changes. The most important thing is addressing these issues directly and immediately.

The second issue that Hadley must deal with is large investors' apparent lack of confidence in Bradford's executive management, as demonstrated when they pressed the company to reassess expenses. If Bradford's management is convinced that the company's performance is a direct result of the economy, it must stand by that assessment in earnings reporting as well as other discussions. On the other hand, if there are opportunities to decrease expenses, these should be examined—internally.

The fundamental point is that executive management has to instill confidence in its shareholders that it is doing what is best for the company. Although shareholders should voice their concerns, they also have to step back and allow the management team to manage without interference.

**Board Membership Change.** Because Bradford chose to disclose board membership changes through SEC filings instead of in a press release, it appeared as though the company was trying to hide something.

Given that the board is the foundation of the company and guides executive management, a press release should have been sent out regarding the changes. Regardless of whether the two individuals were figureheads, their departures demonstrated a change in the dynamics and makeup of the board that may be reflected in company practices, which in turn may affect its financial performance.

Hadley should have been especially cognizant of the ramifications of the resignations given the current environment regarding corporate governance. Immediately announcing the resignation of the board members would have kept speculation to a minimum. By not revealing the resignations before the earnings call, Bradford put itself in the defensive position of explaining them during the earnings call instead of concentrating on the

company's financials and direction. Had management had scripts, they would have been better able to anticipate questions.

In the future Hadley must make sure that executive management is clear on the possible consequences of not fully evaluating their decisions. This leads to dealing with internal conflict.

**Executive Conflict.** The CFO's apparent lack of involvement in Bradford's discussion about communicating the board resignations is a concern. The outcome of the discussion is likely to lead to financial consequences, and the CFO should have been part of it. By not including the CFO, Bradford weakened its management's ability to evaluate the financial ramifications and how and when the information should be disclosed. In the future, Hadley should make sure that the entire executive management team, not a subset, is part of any discussion that may affect the company.

Another concern is Hadley's attitude about avoiding hard questions regarding the board changes. As the director of investor relations, it is his job to discuss these things. Hadley must be proactive in disseminating information so that Bradford builds a reputation as a company that delivers pertinent information regardless of its nature. By being consistent and forthcoming, Bradford builds a reputation for reliability and honesty in the information it disseminates.

**The Financial Audit.** The last issue that Hadley and the Bradford executive management team have to address is the internal financial audit that the franchiser is requesting.

First, the entire management team should review the Sarbanes-Oxley Act. Because of changing legislation, public companies' financial documents will be scrutinized externally and—as we can see in this case—internally.

It seems that the biggest issue for this management team is not that it has anything to hide but that executives' egos are hurt because they feel that they should be above scrutiny. In an ever-changing economy where

more emphasis is being placed on corporate governance and the financial stability of a company, they should welcome scrutiny that will set them apart from others who have something to hide. As a matter of fact, Bradford has the convenience of having a franchiser peruse its books before that is done externally.

**Conclusion.** Hadley must be proactive and assertive. In the office, Hadley must strive to be a credible, competent and contributing part of the executive management team so that his opinions are taken into consideration even when the CFO is not present. In addition, he and the CFO should take part in all discussions that have possible financial implications.

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With external audiences, Hadley has to be assertive and comfortable in his position as the director of investor relations. He must be willing and ready to deliver all news with consistency and integrity. This is the easiest way for Bradford and Hadley to build credibility.

Controlling the conference calls with scripts and making sure that the conference call is a discussion of the earnings and related developments are other areas where Hadley can improve. Last, Hadley must screen the questions to make sure that they are relevant to the majority of listeners. The conference call should not turn into a debate between executives and callers or become a vehicle to address issues that belong in other parts of the company.

Keeping these things in mind, Hadley should see a change in the company's public perception and a greater respect and need for his position inside Bradford Inc.

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