

Disaster Planning — with a Personal Twist

Maintain my integrity and credibility by practicing investor relations in accordance with the highest legal and ethical standards.

— NIRI Code of Ethics

By Jay Gould

A fire guts corporate headquarters. A hurricane floods the data center. A key product is the subject of a national recall. IROs are adept at developing contingency plans that deal with the unexpected.

It's our second nature — a basic job requirement.

Today we live in a world of heightened regulatory oversight, 20/20 hindsight analysis and courtroom Monday morning quarterbacking. But are there a subtler situations for which IROs need to plan?

Consider Violet, the IRO for Magnum Manufacturing.

Magnum had been struggling to put together a consistent track record of earnings, and, happily, its last three quarters demonstrated measured progress, and the market had taken notice. The fourth-quarter package from accounting was showing the year being capped off with a slightly stronger than expected quarter and full-year performance. But as Violet delved into the details, she noted that a gain from the sale of a significant asset had been recorded in one of Magnum's subsidiaries. Without it, the fourth quarter would have fallen a penny short, and bonuses — the first in two years — would be reduced.

As she prepared the earnings press release and conference call materials, Violet disclosed the gain in early drafts. But in the give-and-take of drafting and editing

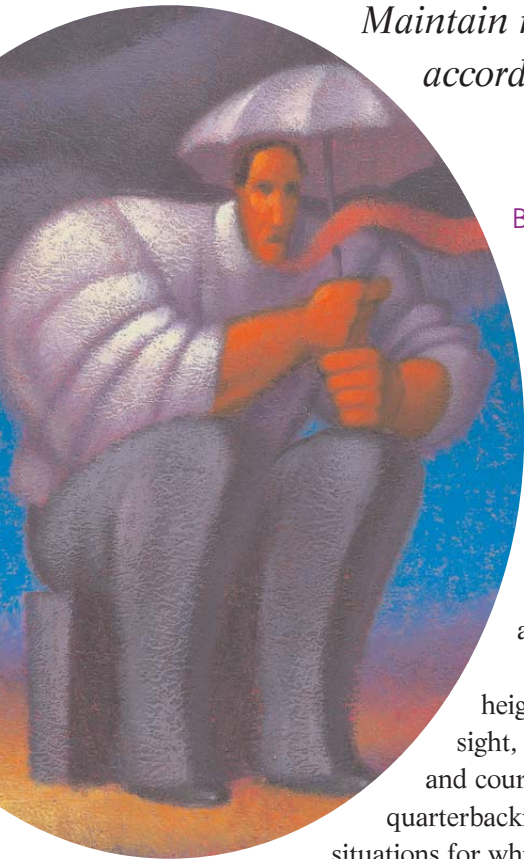
these materials, the CEO expressed a desire to not mention it. He argued that selling assets from time to time was part of managing a portfolio of companies. There was no need, he argued, to draw attention to it. "Let's post a good year," the CEO said. "It will be boost the morale of our employees. Besides, we've stopped giving earnings guidance, so we don't have to worry about setting analyst expectations for next year."

Violet took exception to her CEO's outlook and argued that non-disclosure was misleading and, given the bonus payment, potentially qualitatively material. In a compromise solution, the CEO, CFO and IRO agreed to remove the disclosure of the gain from the earnings release but retain it for the conference call script.

During the conference call, however, the CEO skipped that part of the script. After the call, Violet expressed her concern to the CFO that this had not been disclosed as planned. He said he would make certain the disclosure would be in a footnote in the upcoming 10-Q and thus would pass review at the quarterly disclosure committee. The 10-Q was filed with the footnote, and not a single analyst picked up on the disclosure. Estimates were raised.

Maybe nothing will come from all of this, thought Violet. Sooner or later market expectations will be corrected — if not by anything else, then maybe by first-quarter results. Life will go on.

But if there is any lesson to be learned by testimonies of IROs in recent corporate scandals, it's that they cannot afford to just stand by. Failure to speak up and insist that disclosures be made can result in their being held personally responsible and possibly prosecuted for violation of SEC disclosure rules.



In hindsight, did Violet do all she could to plan for this event?

Not by a long shot. She should have made certain management was fully on board with both the letter and spirit of the company's disclosure policy. She should have consulted the general counsel and sought his or her help to persuade the CEO and CFO. In addition, NIRI's Code of Ethics, which Violet had signed and stands behind, clearly states that an IRO must "recognize that the integrity of the capital markets is based on transparency of credible financial and non-financial corporate information, and will to the best of my ability and knowledge work to ensure that my company or client fully and fairly discloses this important information." This is fundamental.

Violet also could have made certain her relationship with Magnum's inside general counsel was more collaborative and less adversarial than was the case. Today more than ever, IROs and general counsels need to be in concert with regard to disclosure issues. She should have established a better working relationship beforehand with the counsel. In this instance, when she needed an ally, she felt uncomfortable approaching him.

She also could have advocated that the disclosure committee meet not only before filing the 10-Q but also before issuing the earnings press release. We all don't need another meeting. Yet a disclosure review meeting before the earnings press release would have provided Violet the proper forum to express her concerns and have them documented, along with the rationale for the decision made.

Finally, she could have made it well known to the company's management, by deed more than word, that her credibility and personal integrity could not be compromised.

Violet had clearly seen her management's tendency to walk a thin ethical line, and she feared they could easily slip to the wrong side. She pondered what happened in this instance and worried that a situation like this — or worse — could likely repeat itself. She felt so uncomfortable with the situation that she decided to resign. To her, it was the ethical thing to do.

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After leaving Magnum, and while events were still fresh in her mind, Violet wrote a memo to the file. She wanted to document for herself the basis of her concerns, with whom she discussed them and how decisions were made and events unfolded.

She hopes this memo is never needed. But having this document reassures her that her memory of events many months later will remain clear. We leave her as she debates whether to use the company's whistleblower hotline to notify the board of directors.

Resigning, writing letters to the file and being a whistle-blower are the toughest calls an IRO will ever have to make. There are often a host of reasons — many economic — to let a sit-

uation slide and hope nothing comes from it. But IROs are stewards of investor trust, more so now than ever. We all know how the market reacts to news of the resignation of a CFO for "personal reasons." Is it too much of a stretch to think the same importance may now be attached to the resignation of an IRO? Think about it. **IRU**

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