

Reluctant Chairman

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The chairman of the board of Rhomboid Cooperative (NASDAQ: RMBD) was meeting with the general counsel, controller and director of communications.

“How do we win our reputation back with members and the public?” he asked.

Rhomboid had just fired the CEO and CFO for deceptive accounting. As a result of the dismissals, a multi-billion merger on which the company was depending for growth had fallen through. Rhomboid was now relying on the willingness of avocado growers who had founded it to continue with the company. It was not clear they would. At issue was payment to growers of \$22.5 million in one year and \$71.2 million the following year that were not accounted for in the proper fiscal years. The effect of shifting payments was to make Rhomboid's earnings look larger than they were. Rhomboid needed the larger earnings to complete a merger with Healthpath Snack Foods, a division of a major consumer packaged goods manufacturer that was being spun off. To complete the fiasco, the manufacturer sold Healthpath Snack Foods shortly after the broken Rhomboid deal to another food company. There was now no chance of launching Rhomboid into the next tier, and it would have to return to its modest profits as a marketer of avocados and of four small consumer brands of snacks, none of which used the fruit.

Rhomboid in a press release had praised the consumer packaged goods company for its integrity and honesty during merger talks, but it didn't remove the sting of failure. Rhomboid employees were visibly deflated. The CEO and CFO had steered the business for 10 years. They had moved it beyond its roots of selling perishable fruit to a more stable year-around business, but the CEO had taken on more than he could handle with Healthpath. It was understandable. Healthpath snacks were low in cholesterol, calories and salt and they would have been an ideal complement to Rhomboid's existing business.

The general counsel picked up from the chairman and reviewed the status of the search committee for a new CEO and CFO. The committee had held an organizational meeting, retained an executive search firm and started reviewing internal candidates.

The controller reported that the new auditor, KPMG Peat Marwick, had not found further expense shifting in reviewing the books for the last five years. “Barring what they will find through year 10, this incident is over,” he said, “but for SEC and shareholder suits.” The GC nodded. There had been two dozen shareholder suits filed against Rhomboid already, and a joint investigation by the Department of Justice and Securities and Exchange Commission was continuing.

The chairman was not mollified. "Where there is fudging once, there is usually fudging many more times," he said. "Let's not close the case before the year-10 review is complete. The question is how we work around the blemish on the company and its brands." He looked at the director of communications.

The director, a 25-year veteran of the company and much-liked spokesperson to avocado growers, waved his hand dismissively. "I've talked to 50 growers over the last two days. They're unhappy to see the CEO and CFO gone, but they're not moving to Persea." Persea Foods was a rival growers' coop that had not diversified like Rhomboid and as a consequence, was only half of Rhomboid's size. Persea was known for guarding the interests of its members and for its marketing prowess. It was the author of *Avocado Recipes*, a bible for cooks that had been published, expanded and refreshed for 24 years. Persea had eroded Rhomboid's share over the last 15 years but not enough to cause concern. A large part of Rhomboid's presence with growers was due to the director of communications who met with them constantly.

"They see the timing issue as a bookkeeping mistake and not an attempt to screw them," the director said. The chairman nodded. "However, they're not happy with our attention to the snack foods division. They see it as distracting from their needs and profits." This was an old issue and a sore one. Growers had never reconciled themselves to being the cash cow for Rhomboid as it moved into packaged foods. The director of communications had brought the issue repeatedly to the attention of the CEO and chairman, both of whom had ignored him as being in the pocket of the growers.

"If growers are happy and the brands are OK, then we don't have a problem, just an embarrassment," said the chairman. He looked relieved.

"It's going to cost before it's over," said the GC. "Twenty, 30 million in legal, audit and settlements." The GC did not bring up the crash of the stock price, which was a quarter of what it had been the year before. Rhomboid's share price was at 19.00, down from 80, on 5.36 million shares outstanding. "And the clawback is unsettled."

The chairman shook his head slightly. The CEO's employment agreement had a provision for return of compensation in the event of moral turpitude. The CEO had taken home \$8.36 million the year before in salary and exercise of options. At least half of that was in jeopardy, if the board elected to sue. The chairman was pushing for it against both the CEO and CFO. He was angry with the position the two of them had put the board in. The chairman's friends had expressed support for him, but he knew they were relieved that it was not they who had to handle the matter. The seven other directors on the board were in the same embarrassment.

However, three of the directors were pushing to let the CEO keep his money and to move beyond the incident as quickly as possible. That didn't seem realistic to the chairman, but it was not an issue for this meeting.

"We need to show members and employees that we're not drifting," said the director of communications. He looked at the chairman. "You need to be out there while search committee is working."

"We're not making major decisions before a new CEO is on board," the chairman said.

"You don't have to. Show your face and let everyone know you are in charge."

"And increase the risk of another suit...?" said the GC. "It's best not to be too public. Too many unanswered questions."

"So what do I say to members when they call? And, they are calling."

"A search is underway," said the GC. "Say nothing else."

"I'd rather keep it low-key," said the chairman. "I'll meet privately with senior executives and large growers. I don't want to go beyond that."

"There are rumors," said the director of communications.

"There are bound to be, but I'm not going to get ahead of DoJ and the SEC."

The controller interrupted. "The shorts are having a field day. Our IR counsel has been picking up wild rumors all over the Street."

The chairman didn't respond.

"Can't I at least release a statement to employees and members?"

"Don't go beyond the GC's advice," said the chairman.

The director of communications knew a statement announcing the search wasn't going to answer member or employee questions if the board sued the former CEO and CFO. Nor would it stop newspaper and online stories that had been tracking Rhomboid since the CEO's and CFO's departure. Moreover, those shorting the stock had already profited and would continue to do so if they could drive it down further. Rhomboid was becoming a tempting acquisition target. He wondered if Persea was watching.

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Questions for discussion:

1. Was the chairman's decision correct?

2. What should Rhomboid be saying to employees and members?
3. What should Rhomboid be saying to investors?
4. How would you handle this situation?