COMPLIANCE WEEK

Making The Most Of The IRO And IR Dept.

By Louis M. Thompson, Jr., *Compliance Week Columnist* — June 19, 2007

Given the increasing role of investor relations in bringing important intelligence to the board of directors, dealing with activist mutual and hedge funds that want to engage the board on strategy, and communicating with the investment community at a strategic level, it's time for many companies to evaluate the best reporting relationship of IR within senior management.

Since the market became institutionalized in the late 1980s, investor relations has become more of a finance than communications function. Most investor relations officers (IROs) now report to the chief financial officer, particularly in larger companies.

The National Investor Relations Institute describes investor relations as "a strategic management responsibility that integrates finance, communication, marketing, and securities law compliance, to enable the most effective two-way communication between a company, the financial community, and other constituencies, which ultimately contributes to a company's securities achieving fair valuation."

Unfortunately, for a number of IROs, this definition is more of an ideal than a reality.

That's partly because they are drawn to the IR function from corporate finance with little or no communications or marketing experience. While knowledge of finance is essential, the demand for communications skills is increasing. Understanding that effective communication requires knowledge of strategies and tactics is a first step. Knowing what to do and how to employ effective communication strategies and tactics is the next one.

For those with a finance background, communication skills can be learned through various educational forums under the tutelage of a knowledgeable communications expert in the company or from an outside communications counselor.

There are two perspectives for where the IR function should be positioned. From an investor or analyst point of view, the issue is not so much *where* it is positioned as much as whether the IRO is perceived to have sufficient access to senior management to speak for the company. Too many analysts and portfolio managers view the IRO as a "gatekeeper" who is trying to protect the time the CEO and CFO devote to the Street's informational needs. Those who are perceived to have sufficient access

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Prior to joining NIRI, Thompson was assistant White House press secretary to President Gerald Ford.

A veteran of the U.S. Command in Vietnam and the Office of the Secretary of Defense, Thompson has held executive communications positions for a number of organizations, including the American Enterprise Institute for Public Policy Research, and the National Council for Economic Education.

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generally enjoy the confidence of the analysts and institutional investors and are effective in their role.

Then there is management's perspective. I moderated a CFO forum last year where the majority of participants believed their primary IR role was to work with the buy-side analysts and investment banks, while their IROs managed the needs of the sell-side. The CFOs also believed it was their job to communicate the company's strategic message and, in effect, a majority relegated their IROs to more tactical responsibilities—a very counterproductive approach. There is no reason that the CFO and IRO cannot share the role of communicating the company's strategy. And if the CFO does not have confidence that the IRO can do it, then he or she needs to find someone who can and empower that person with the necessary access to be a partner in strategic communication.

Recently, Jerre Stead, chairman and CEO of IHS, a multibillion-dollar Denver-based company, addressed the National Investor Relations Institute's Rocky Mountain chapter on the CEO's perspective of investor relations. Stead has served as chairman or CEO of seven large corporations and has served on 27 boards during his career. He believes the IR and corporate communications functions should be combined and report directly to the CEO. He said that he and his senior vice president for investor relations and corporate communications, Jane Okun, communicate with investors, analysts, employees, and the public more than any two people in the company, and he said that it is critical that their communications and messaging be completely in sync.

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Okun came to her present role with an MBA, a background in corporate finance, investor relations, integrated communications, and corporate planning at several Fortune 500 companies, as well as experience as a CPA with a major accounting firm. The CFO is also part of the team who communicates with the investment community. Stead went on to say that before he accepts a new board position, he checks to see where IR is positioned in the company. If it doesn't report directly to the CEO, he will not accept the board seat.

There is no question that an IRO must have a command of finance as it pertains to IR. This takes many forms: what the company's current stock price implies about valuation; how changes in an analyst's model affect his or her valuation of the company and, ultimately, the recommendation and target price; and, how a corporate transaction or initiative translates into a change in valuation. Finally, analysts have very strong skills in financial analysis and largely base their recommendations on detailed quantitative analysis. Therefore, the IRO must be able to speak in quantitative terms and have meaningful discussions with analysts and the portfolio manager. This requires a understanding of accounting, financial statement analysis, and corporate finance.

What raises the need for strategic communication skills is the role in developing the company's integrated strategic messaging to a variety of audiences and communicating those messages to the investment community. Having IR as a part of the corporate communications team and reporting directly to the CEO is the optimum relationship. This would include a strong "dotted line" between the IRO and the CFO.

Another important role for the IRO in today's environment of shareholder activism is to serve as an information and intelligence source for the board of directors. Typically, IROs prepare written reports for the board, primarily focusing on factors that affect stock price performance, naming the major investors, identifying who's buying the stock or selling and why, and providing the characteristics of the shareholder mix and a summary of analyst reports. Beyond that, there is a growing trend for IROs to be invited into the boardroom for a strategic-level discussion beyond what they provide directors in their board meeting books.

To do this—to gain enough trust and acceptance among the investor community, so that the IRO, in turn, can learn the sentiments of that community that the board of directors would want to hear—the IRO obviously must have internal access to senior management and the strategic decision-making process. They need to provide directors feedback on whether the Street understands and accepts the company's strategy and such issues as the agenda of activist investors that may knock on the board's door requesting a meeting to challenge the company's direction.

The IRO also needs to participate in creating the messaging to investors to win their support on contested proxy issues. In the 2007 proxy season, say-on-pay proposals were at the forefront of shareholder proposals. Pay for performance was a key reaction to the new proxy disclosures on executive compensation. This requires a communication plan to deal with investors' reaction to these issues.

If companies want to improve their relationships with the investment community, they must view IR as part of a strategic integrated communications program and must ensure that the IRO has a seat at senior management's table so that the investment community perceives that person as a strategist—and not merely a tactician providing maintenance information for analysts and investors.

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