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Madonna and Ritchie, with son Rocco.

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Money

SECTION B

Monday, January 15, 2001

Photos by Patty Wood for USA TODAY

Dinnertime: Katy Harrelson, at right with a plate, dishes up meals for customers at a Luby's in Houston. The first Luby's opened in 1948 in San Antonio.

Cover story

Luby's proxy fight illustrates investors' readiness to act

By Gary Strauss
USA TODAY

Luby's on the table: Customers head for a meal at a Houston branch of the restaurant.

SAN ANTONIO — If Luby's annual shareholder's meeting was an anger-barometer of shareholder angst, Corporate America may be in for a long proxy season.

Luby's, a troubled, San Antonio-based chain with 220 restaurants in 10 states, survived a contentious proxy fight Friday with the Committee of Concerned Luby's Shareholders.

The dissident group, which wanted more proactive directors to engineer a quicker corporate turnaround, didn't garner enough votes for its slate of directors. Still, the board faced lots of criticism from hostile shareholders. "I'm glad this is over and we can get down to the business of running the company," said a still rattled David Daviss, Luby's chairman and acting CEO, following the rancorous, 2¼-hour meeting.

As this food fight demonstrates, the first proxy season of the new millennium promises to be a season of shareholder discontent. Historically, dissidents have rarely won proxy battles. But with scores of stocks down sharply in 2000, investors no longer appear willing to accept management spin control without question or rubber-stamp a company's director slate.

"Logic tells you the complaining among shareholders will be a lot more intense because of the state of the markets," says Carol Bowie of the Investment Responsibility Research Center, a nonprofit research firm. Key complaints among investors: stock option awards with few ties to corporate performance, and excessive golden parachutes.

Luby's is typical of an old-line business facing the modern pressures of a rapidly changing industry. After the opening of its first site here in 1948, Luby's bloomed into a Southern icon, its cafeteria-style restaurants relished by families and senior citizens for abundant portions, moderate prices and made-from-scratch fare — even the mayonnaise.

Please see COVER STORY next page ▸

Dissidents used Internet to get support

Continued from 1B

But the past few years have been unkind to Luby's and other cafeteria operators. Sandwiched between cheaper fast-food chains and pricier casual-dining eateries, cafeteria industry revenues have steadily dropped the past few years.

Luby's 4,280 shareholders have suffered more than most. Daviss acknowledged as much Friday. "I feel your pain," he told them.

Cover story

Luby's shares have slumped 75% from their 1993 peak, about 50% the past year alone. The cash-strapped firm slashed its 80-cent stock dividend, then omitted it completely late last year. The board is seeking Luby's fifth CEO since 1996. And Luby's turnaround strategy has yet to take hold.

Management got an earful from shareholders who took issue with directors' compensation, their small holdings of company stock, lackluster oversight and even Daviss' authority to control shareholder comments at the annual meeting.

In the end, the dissidents lost the election. But shareholders did approve their plan that all directors be elected annually rather than in staggered, multiyear terms. "The stock has been disappointing, the quality of the restaurants has gone down, and management isn't getting enough done," said David Poundstone, 81, a retired electrical engineer who voted for the dissidents. "I wanted to send a message."

Greenberg: Led proxy fight.

Internet empowerment

Most Internet stocks might be on life support, but the Net continues to empower shareholder dissidents and activists such as eraider.com, which has been taking stakes in laggard firms since 1998.

Core members of the Committee for Concerned Luby's Shareholders, led by attorney Les Greenberg and Texas investor Thomas Palmer, got acquainted bemoaning the company on a Yahoo message board. They're believed to be the first grassroots effort to successfully use the Internet to bring a proxy fight to a vote. "Luby's board needs fresh blood and oversight," says Greenberg, who holds 5,600 shares.

Greenberg's guerilla movement also sought input into Luby's discussions with two Houston restaurateurs who recently acquired a 6% stake in the company and have yet to fully make their intentions clear.

Daviss, who took to calling the dissidents "insurgents" during the proxy fight, said their Net-propelled campaign drove customers away, distracted management and has hampered CEO recruiting efforts to replace Barry Parker, recently ousted by the board.

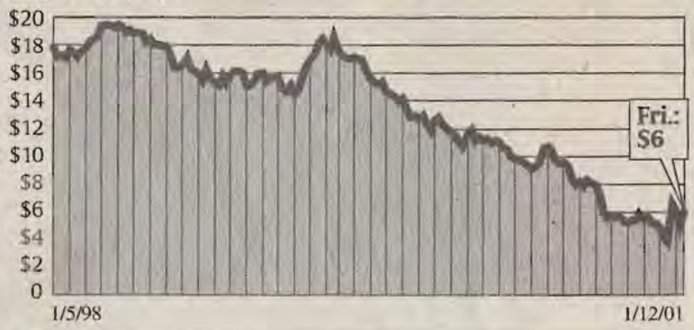
Daviss conceded their complaints may be valid, but said that given their lack of restaurant industry experience and management expertise at publicly held companies, they weren't qualified to be directors.

If the dissidents accomplished anything, they thoroughly shook up Luby's staid corporate culture. In fact, only two seminal events might have caused bigger jolts — the infamous shooting rampage by a gunman at a Killeen, Texas, restaurant that killed 23 patrons and wounded 20 more in 1991, and the 1997 suicide of then-CEO John Curtis Jr.

"This (proxy fight) is small potatoes by comparison," says Daviss. "But we've taken it seriously."

Restaurant's stock value sees steady downturn

Luby's weekly highs:



Source: CSI

Company profile

Luby's

Industry: Restaurants
Headquarters: San Antonio
CEO: David Daviss (acting)
Restaurants: 220 in 10 states
Employees: 13,000
Exchange: NYSE: LUB

By Elizabeth Wing, USA TODAY

The fight's legal and administrative expenses cost Luby's $250,000. Recent regulatory filings underscored the board's increasing annoyance. Daviss charged in a Securities and Exchange Commission filing that he'd been offended by some of Greenberg's online "unfounded accusations and rhetoric."

The proxy fight also put Luby's on the defensive. "Although our intentions were good, in retrospect, the hiring of (ex-CEO) Parker and the strategy put in place during his tenure did not reverse the trend of declining same-store sales. This, together with the more competitive restaurant environment, has hurt the value of the investment of our shareholders," the board said in an earlier mea culpa filed with the SEC.

Stiff competition

To be sure, Luby's, like rivals Piccadilly, with 235 cafeterias in 16 states, and Furr's Restaurant Group, with 100 outlets in 12 states, are likely to remain under competitive siege, says Jeff Dabbs, a stock analyst for Kercheville & Co.

Consumer sentiment was already shifting when Curtis became CEO in early 1997. Three months into the job, he committed suicide. Despite a close-knit corporate structure that had always promoted insiders, Luby's directors sought an outsider as CEO.

"Competing in a rapidly changing marketplace, we felt we couldn't be successful without making changes," Daviss says. "And we didn't see anybody at Luby's with the scope and breadth to do it."

Overlooking his lack of restaurant experience, the board hired Parker. He had previously headed Dallas-based apparel retailer County Seat, which filed for Chapter 11 bankruptcy following his 1996 departure.

Parker's three-year run, ending with his forced resignation in late September, was rocky at best. Parker initially had ambitious plans, including a 100-restaurant expansion. Luby's also attempted to burnish its image with its first extensive advertising campaign, store remodels and new menu items.

Some efforts, such as outsourcing food, didn't go over well with customers and failed to provide expected savings. Parker's best move was accelerating take-out and drive-through service, says Southwest Securities analyst Stephen Spence, which now accounts for 12% of sales.

His management style and many initiatives never sat well with store managers. Luby's occasionally summoned field managers for leadership seminars, but senior executives took little interest in their ideas. Retired senior executives said their offers to help advise the company were also rebuffed.

"After Parker arrived, it became a top-down organization that didn't want our opinions," says Roger Voss, a field manager from 1990-1999.

Parker says he had clear strategic differences with the board concerning how long it was going to take to turn around the company. "There are long-term problems that require long-term solutions," says Parker, noting that the cafeteria concept has limited potential.

Stock analysts and other observers blame some of Luby's slide on Parker's decision to jettison the company's lucrative compensation plan for store managers. Luby's traditionally took 60% of store profits. With lead managers getting the rest, some took home $150,000 or more annually. After a new pay plan was implemented in 1998 to boost corporate profits, managers' salaries were quickly halved, or worse.

The pay plan was the company's biggest mistake during Parker's tenure, Daviss says. Scores of managers left, and their departures hurt the relationships many restaurants had with regulars, who were on a first-name basis and who were treated like family.

In the end, many of Parker's initiatives failed. And the residual debt from expansion and remodeling will likely keep the dividend from being reinstated.

White knight?

Luby's shares, which had been trading as low as $3.50 in December, surged to $6 late last month on word that Houston-based brothers Harris and Christopher Pappas had accumulated a 6% stake to become the firm's largest individual shareholders. The Pappases have been discussing possible roles with the company since late October, according to SEC filings.

Daviss refused to elaborate Friday. The Pappases, whose restaurant group operates 60 casual dining restaurants in five states, aren't talking.

Greenberg fears that the Pappases may try to acquire Luby's for its valuable real estate holdings at a cut-rate price. "Our concern is if the company is put up for sale, don't go with the first one that asks you to dance," he says.

If the Pappases are merely friendly investors, it's unclear how long they'll be patient. Almost half their 1.34 million shares trade at or below their purchase price, according to SEC filings. Now that the proxy fight is over, Daviss says the board can discuss options. Meanwhile, he'll intensify efforts to hire a new CEO.

A turnaround specialist won't come easily or cheaply, Spence says. Despite new marketing efforts, Luby's posted a $2 million loss during its first fiscal quarter ended Nov. 30 — in part due to a $354,000 charge toward Parker's golden parachute. Revenue fell 7% to $114 million from $123 million.

Darrell Wood, who oversees Luby's store operations, says new marketing efforts, meals and a return to made-from-scratch philosophy will boost sales. "It's going to take time to turn things around. But will we do better in a competitive environment? Absolutely."

But shareholders at Luby's and other moribund companies will be keeping the pressure on. "If there aren't results, next year's meeting will be contested even more," investment manager Guy Adams said after the Luby's meeting. "The clock is started, and people are going to have to see some visible results."