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Denny's Restaurants:
Creating a Diverse Corporate Culture (A)

On the morning of February 5, 1995, Jim Adamson walked into the corporate headquarters of Flagstar Companies (renamed Advantica Restaurant Group in 1998) in Spartanburg, South Carolina. As Flagstar's newly hired CEO, he was responsible for the future of the firm – a future he knew would be difficult. After a series of recent events, Adamson knew that Flagstar was in need of serious change. His predecessor, Jerry Richardson, struggled to keep the company alive with $2.3 billion in debt from a series of restructuring attempts in the 1980s. Despite his attempts, the company lost money for five consecutive years from 1989 to 1994.

Adamson also had to consider the issue of discrimination. Flagstar was the parent company of Denny's restaurants, a chain that had become a symbol for racism in the United States. He also had some serious questions about the firm he had just taken charge of. Would he be able to improve the financial performance of the firm? Could he begin to change the pervasive culture throughout the firm that had allowed these events to take place? As he sat at his new desk, Adamson began reviewing the challenges he faced.

April Fool's Day

On April 1, 1993, a group of 21 uniformed United States Secret Service agents stopped at a Denny's Restaurant not far from the Andrews Air Force Base in Annapolis, Maryland. Theyhad a free hour before their detail would assemble and had decided to stop for breakfast. Of the 21 men, seven were African-American. Six of them – Alfonso Dyson, Melvin Fowlkes, Merrill Hodge, Joseph James, Leroy Snyder, and Robin Thompson – sat at a table together. The other 15 agents sat elsewhere.

This case was prepared by Research Assistants M. Jennifer Abes, W. Brent Chism, and Thomas F. Sheeran under the direction of James S. O'Rourke, Concurrent Professor of Management, as the basis for class discussion rather than to illustrate either effective or ineffective handling of an administrative situation. Information was gathered from corporate as well as public sources.

3-5 pages double-spaced

Many of the agents ordered the All-You-Can-Eat breakfast, a menu feature allowing a customer to choose five items from the menu and eat all he wanted for one price. After 30 minutes , however, the table of black officers had still not been served any food, while the other officers were already eating. Robin Thompson asked their server twice about their meals, but was told to wait. William Winans, a white officer who was sitting nearby, noticed that the server had made a face and rolled her eyes as she left the table. After 45 minutes had passed, the black officers noticed that customers who entered half an hour after they had arrived were already served their meals. Further, their fellow officers were being served second helpings. At this point, Thompson asked to see the restaurant manager.

Given that the group was on a tight schedule, James Sobers, the agents' supervisor, advised that they should file a complaint against the restaurant. When the restaurant manager approached them, the agents asked for his name and the address of the Denny's regional management office. The manager, who did not seem to understand English, only provided them with the address of the restaurant itself.

Alfonso Dyson stated later, "I didn't want to believe it was discrimination. But I couldn't think of what else it would be." [1] The six Secret Service agents, soon after the incident, filed a class action race-discrimination lawsuit against Denny's.

Events That Followed

Some three weeks later, on April 24, 1993, the company released a statement from corporate headquarters regarding the event, stating that after an on-site investigation of the incident, the manager involved was terminated. They also stated their commitment to further investigation of the incident and the elimination of any possible racial discrimination.

The incident involving the Secret Service agents was far from a one-time occurrence. Rather, discrimination against minorities was pervasive throughout the Denny's culture. Discrimination had been previously reported, even before any lawsuits were filed. This incident, however, triggered a growing number of customer complaints and subsequent lawsuits. Denny's had become, in the words of Jim Adamson, "a poster child for racism."[2] One law firm, Saperstein Mayeda, even ran advertisements targeted at minorities, inviting those who thought they had been discriminated against at any Denny's restaurant to contact the firm for information. This led to a strong, negative public image for Denny's and more plaintiffs. Also contributing to negative publicity was the fact that another, similar class-action lawsuit had been filed by a group of young African Americans who were asked to prepay at a Denny's restaurant in California. Ironically, the lawsuit had been settled the same day that this incident had occurred.

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[1] Adamson, Jim, *The Denny's Story*, New York, 2000, pp. 8-9.

[2] Adamson, Jim, *The Denny's Story*, New York, 2000, p. 9.

Jerry Richardson, CEO of Flagstar companies at the time, quickly settled both lawsuits. By December 1995, Denny's had paid $54 million to 294,000 customers and their lawyers, the largest public accommodations settlement ever.[3] Denny's was forced to sign a consent decree with the U.S. Justice Department, which mandated that Denny's restaurants publicize its nondiscriminatory policies and train employees about diversity issues. Further, a civil rights monitor was assigned to keep tabs on all 1,721 existing restaurants, as well as any future restaurants, for the next seven years.

Flagstar Companies: Corporate History

In 1961, Jerry Richardson, former wide receiver for the Baltimore Colts, and Charles Bradshaw, his college football teammate, bought the first Hardee's franchise in Spartanburg, South Carolina. By 1969, they grew their franchise into Spartan Food Systems and went public. In 1979, a conglomerate, TransWorld Corporation, acquired the company. Bradshaw chose to leave the company while Richardson decided to stay on and run his division. In 1986, TransWorld spun off many of its non-food related investments and renamed itself TW Services. The following year, TW Services purchased Denny's restaurants, along with El Pollo Loco, a chain of grilled-chicken restaurants, and Richardson became president of the food service company. (In an effort to centralize overall company operations, Denny's corporate headquarters was moved from Irvine, California to Spartanburg in 1991). In 1989, the company took on a huge debt as a result of a hostile takeover by the private equity firm of Gollust, Tierney, & Oliver. In 1992, Kohlberg, Kravis, Roberts & Co. (KKR), rescued the company by investing $300 million of equity to restructure its debt. This investment gave them control of the company, and a new name in 1993: Flagstar Companies.

Flagstar Companies: Key Leaders

Jerry Richardson, CEO of Flagstar, had mishandled several financial and racial issues during his tenure. In 1990, before any racial issues were publicized, Richardson had hired a consulting firm, Synetics, to help Flagstar a strategy to mold the company into a top-rank food service organization. Following a series of employee focus groups, Synetics' initial observations focused on a lack of diversity within the company. Despite being warned that the firm was in a dangerous position, Richardson saw no urgency to make any changes. His response to Synetics was, "I'm sure you're right about our being behind on diversity, but I never thought about it."[4] When racial problems first arose, Richardson and his management team wrote them off as isolated incidents.

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[3] Rice, Faye, "Denny's Changes Its Spots," *Fortune*, 1996.

[4] *Ibid*, p. 4.

Despite such neglect, Richardson grew Flagstar under his leadership into a $3 billion company, and made Denny's restaurants the nation's largest, best-known family restaurant chain. His goal was to make Flagstar the best food service company in the world by the year 2000. After a 33-year career in the restaurant business, however, Richardson resigned as Chairman of the Board and Director of Flagstar Companies. After relinquishing his Chief Executive title, Richardson turned his attention to the Carolina Panthers, a National Football League team that he owned. The majority owner of the Flagstar Companies, KKR, recruited Jim Adamson from Burger King to replace Richardson as CEO of Denny's parent company. Within months after the secret service agent incident, Adamson hired Ron Petty, former head of Burger King USA, as CEO of Denny's to manage the chain's transformation.[5]

Jim Adamson's personal history was a good fit for the job as Flagstar's new CEO. After growing up in the racially mixed environment of Army bases around the world and in the neighborhoods of Washington, D.C., and Oahu, Hawaii, Adamson was sensitive to acts of racial discrimination. Because of that background, Adamson would be certain not to tolerate them at Flagstar. He had developed a reputation as a calm and approachable leader. A former boss once noted that because of his sincerity, Adamson's team was devoted to him.

Racism within Flagstar

By the early 1990s, racial issues were still common to Flagstar. Many communities in California had already begun to complain about the treatment they had received at Denny's restaurants. Further, the U.S. Department of Justice had begun looking into charges that Denny's demonstrated a pattern of discrimination against customers who were African-American. In fact, Richardson, who was chairman of Flagstar at the time, had begun talking with local NAACP members as early as January of 1992 to find ways to respond to the challenge of diversifying the company.[6]

Although there had never been a deliberate corporate policy advocating discrimination, top executives of Flagstar did not pay much attention to what was happening in their restaurants. Their ignorance allowed many restaurant managers to set their own racist policies. Some managers asked African American diners to show identification before being served, requested that they pay before food arrived, and forced them to wait interminably for their meals.[7] Some were even known for ordering "blackouts," a situation in which employees were directed to lock patrons out of the restaurant.

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[5] Adamson, Jim, *The Denny's Story*, New York, 2000, p. 20.

[6] Adamson, Jim, *The Denny's Story*, New York, 2000, p. 14.

[7] Segal, David, "Denny's Serves Up A Sensitive Image," *Washington Post*, 04/07/99, p. E1.

Flagstar was insensitive to minority business people, as well. Samuel Maw, Flagstar's executive vice president and chief procurement officer, claimed that it was extremely difficult to find minority vendors. Minority vendors who called on Denny's, however, claimed they were ignored by the company's buyers.

Key External Factors

Because of the nature of race relations in the United States, any organization that participates or is accused of discriminatory practices will face a number of external challenges, including unwanted press attention, lawsuits, and scrutiny from organizations such as the National Association for the Advancement of Colored People (NAACP) and People United to Save Humanity (PUSH). Denny's faced such a situation on April 1, 1993. The same day that the firm settled a federal discrimination lawsuit, a Denny's restaurant in Maryland refused to serve six African-American Secret Service agents while their white counterparts were served. Because of this incident and the company's checkered past, Adamson knew that Denny's was at a crossroads. He had to fix this or risk losing the company.

During this latest crisis, Denny's endured relentless press coverage of not only the current racial incident involving the six Secret Service agents but also its history of nationwide discrimination. The media coverage included a press conference with the six agents, interviews with disgruntled employees, and other angry former customers. Closely following the media coverage was a class action lawsuit and additional scrutiny from organizations such as the NAACP, PUSH, and the Southern Christian Leadership Conference (SCLC). The class action lawsuit helped prolong damage from the racial problems at Denny's and its parent company. Additionally, these activist groups began using Denny's to help promote their own agendas and organize boycotts of the restaurants. Adamson knew those groups, well intentioned though they may have been, would have the potential to damage to the long-term growth of a firm more than any lawsuit.

Can Denny's Hit a Grand Slam?

Adamson stood up and walked to the window. It would take an enormous amount of hard work, innovation, and commitment to turn this company around. Many stakeholders were involved. Could he satisfy each of their needs? Denny's current strategy was somewhat low-key and focused principally on internal change. Would this strategy work to resurrect Denny's name?

Questions

1. As Jim Adamson, what would your managerial approach be in this sensitive situation?

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