

Developments in Business Simulation & Experiential Exercises, Volume 11, 1984

EXECUTIVE BAILOUT AT SHAKE & SPEAR, INC.

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ABSTRACT

This exercise examines interactions between top management and the outside board of directors in developing executive compensation policy. The exercise focuses on two behavioral properties of memo writing: to compare the differential effects of responding to memoranda with and without carbon copies to important people; and, to examine when and under what circumstances it may or may not be strategically appropriate to put policy development on sensitive matters into writing and the possible consequences of both a written and unwritten history of policy evolution. This exercise addresses ethical, legal and economic implications of "golden parachute" compensation for a top management team.

DIRECTIONS

1. You are a member of the compensation committee of the board of outside directors of Shake and Spear, Inc. Select a person to chair your committee. This person will serve as a spokesperson for your team. Then do the following: (1) read the background information on Shake & Spear, Inc.; (2) read the memo from the Chairman of the Board to the chair of the compensation committee; and (3) read the report on "golden parachute" compensation from the Research and Development Department.
2. Your task is to: a. write a memo to the Chairman as to how he should respond to Bill Spear and b. write a memo on golden parachute compensation policy recommendation to be present at the monthly Board of Directors meeting. You have 50 minutes to complete this task.

BACKGROUND INFORMATION ON SHAKE & SPEAR, INC. - Shake & Spear, Inc. was established in 1892 in Venice, New York when Anthony Shake, a dry goods merchant from New York City and William Spear, a sporting and camping manufacturer in Venice, merged. Thus began a long history of expansion through small acquisitions. Its prize possession is its health care division originally acquired during World War I. As a result, today Shake & Spear is a large and highly diversified international company. It has a history of superior management, quality products, good customer relations and proud company employees.

Shake & Spear went public in 1939, but the majority of its stock is still held by family members and Bill Spear, Jr. still sits on the Board of Directors. In addition, the company is still largely run by third and fourth generations of Shakes and Spears. The Board of Directors is composed of twelve members, nine Outside directors, and three inside directors. The current President and Chief Executive Officer is William Spear, III, grandson of one of the founders. Next in line is Marcia Shake, Executive Vice President and grand niece of Anthony Shake. In fact, five of the top management positions are filled by direct descendants of Mr. Shake and Mr. Spear. Though public, it is really a "family" run business--and Bill Spear would like to keep it that way, since his oldest son has just come to work for the company after finishing his MBA at Harvard.

Over the past decade, Shake & Spear has been a prime target for take over. It is a highly successful company with a reputation of being "ahead" of its time and always a jump ahead of the competition. Its health care products division has been the prime target for takeover. Bill Spear has been president and CEO for the past eleven years and is credited with repelling takeovers. He is very innovative, entrepreneurial and the company expanded internationally under Bill's tenure. He is dedicated to keeping the business in the "family." Bill recently asked Portia Shake, the Vice-President for Research and Development, to do some intensive research on change of control compensation packages currently in effect in large business and industry. Bill is convinced that such compensation packages are a strategic tool in increasing the price of a takeover so that potential raiders have to rethink their plans.

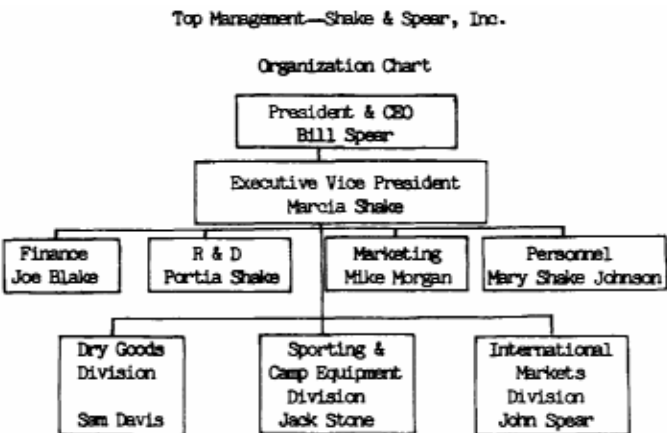


Exhibit 1

SHAKE & SPEAR, INC.

To: Leslie Leads, Chair, Compensation Committee
From: Gill Martin, Chairman of the Board
Subject: "Golden Parachute" Compensation Policy for Top Management at Shake & Spear, Inc.

"The quality of stockholder mercy is not strained. It allows executives with 'golden parachutes' to dropped as the gentle rain after a takeover attempt. These people are twice blessed. They are blessed if they win, for they keep their companies, their positions, and their compensation. They are blessed if they lose, for they still keep their compensation even if not their jobs."

The above came to me from a colleague who has just gone through some "sticky" golden parachute litigation. --A little levity to accent a very serious matter! Last Tuesday I had lunch with Bill Spear (our regular monthly luncheon meeting where we "informally" discuss important issues).

As you are well aware, Shake & Spear has been a target for takeover in the past and we have repelled such efforts. In our conversation, Bill indicated that he got "wind" of a rumor that Touchstone Industries is planning to acquire about 20% of our stock.

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Bill believes that Touchstone will be successful in their efforts. Bill indicated that his top management team is worried about a change in control and would like us to initiate a change in control compensation package for Bill and his top management team.

I asked Bill to send me a memo outlining his thoughts and recommendations as to who would be included, but reminded me that our conversation was "strictly off the record." Bill promised, however, to send along a report on "golden parachute" compensation recently completed by our research department (copy attached). Since such a package would include a minimum of nine people, this could be a hefty sum for our shareholders to bear.

I am asking that you and your committee meet and advise me on the following: (1) How should I respond to Bill Spear? and (2) Develop a golden parachute compensation policy recommendation to be presented at our regular monthly Board of Directors meeting on the last Thursday of this month. This will be the only item on our agenda.

Thanks. If you have any questions, please don't hesitate to call.

SUMMARY REPORT ON CHANGE IN CONTROL COMPENSATION FOR THE EXECUTIVE MANAGEMENT TEAMS IN AMERICAN BUSINESS AND INDUSTRY

The following is an edited version of this report. The full version is available from the authors.

Young and Fazan International, an executive recruiting firm, recently examined the proxy statements of 255 industrial companies from the Fortune 500 and Second 500 lists. The study found that 15% offered parachute provisions to top management teams. The following tables are based on a recent survey of Fortune 500 companies with golden parachute agreements (Fortune, December, 1982).

See Tables Below

Table 1
Largest Industrials With Parachutes

COMANY	FORTUNE 500 RANK	SALES in billions
Phillips Petroleum	15	\$16.0
Sun	17	\$15.0
United Technologies	20	\$13.7
Ashland Oil	35	\$ 9.3
Allied	55	\$ 6.4
International Paper	77	\$ 5.0
American Can	81	\$ 4.8
Bendix	86	\$ 4.4

Table 2
Most Generous Agreements

COMPANY	CHIEF EXECUTIVE	NWNT In millions*
American Family	John Adams	\$ 7.8
GK Technologies	Robert Jensen	\$ 7.3
Conoco	Ralph Bailey	\$ 4.1
Bendix	William Agee	\$ k.0
Thiokol	Robert Davis	\$ 4.0
Allied	Edward Hennessy	\$ 3.9
Pennzoil	J. High Liedtke	\$ 3.7
American Medical Int'l	Royce Diener	\$ 3.1
Time Inc.	J. Richard Munro	\$ 3.0

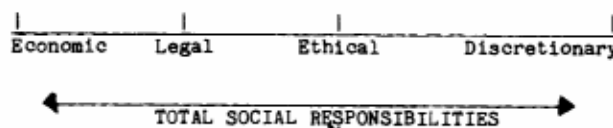
Processing Questions

- Summary of responses. Differential effects between memo with a carbon copy and memo without a carbon copy.

Memo	Summary of Responses	
	Memo 1	Memo 2
With Carbon Copy		
Without Carbon Copy		

- How did your committee deal with the issue of Bill Spear's request as being "strictly off the record."
- Did your team recommend that the Chairman of the Board not respond in writing to the company president? Why or why not?
- Did your committee send a carbon copy of their memoranda to any other parties? If so, to whom?
- What are the economic, legal, ethical, and discretionary responsibilities of golden parachute compensation?

Social Responsibility Categories



Note: Exhibit 2 (Same as Exhibit 1 - only
cc: Bill Spear)

Table 3
Most People Covered

COMANY	PROTECTED EXECUTIVES
Beneficial	234
Kimberly-Clark	80
United Technologies	64
Colt Industries	30
Martin Marietta	28
Mapco	23
PèF	21
art	20

Table 4
Fastest-Opening Parachutes
(20% change of ownership triggers benefits)

COMANY	BIGGEST STOCKHOLDERS	PERCENTAGE HELD
Mohasco	Gulf & Western	23.5%
Olin	Hartford National	15.9%
McNeil	Richard A. Michelson	15.2%
C. R. Bard	International Paper	14.3%
Control Data	Morgan (J. P.) & Co.	9.3%
Rubbermaid	Balke & Co.	9.0%
Tampax	Endowment Mgt. & Research	7.6%
Midland-Ross	T. Rowe Prioce Associates	9.6%