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"Golden Parachutes": A Closer Look

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The much maligned 1982 merger merry-go-round which eventually involved four of the nation's major firms (Bendix, Martin Marietta, Allied, and United Technologies) was initiated by one man, William Agee, then the CEO of Bendix. After it became clear that Bendix would not succeed at acquiring Martin Marietta and that it would, in fact, be acquired by Allied acting as a "white knight," Mr. Agee convinced Bendix's board of directors to approve "golden parachute" (GP) contracts for himself and fifteen other Senior Bendix executives.[1]

Mr. Agee's contract entitled him to over $4 million in compensation (over $800,000 per year for five years) upon 1) a change of control at Bendix, and 2) Agee's termination, either voluntary or involuntary. Eight days after Allied acquired Bendix, Agee voluntarily chose to resign and receive his $4 million. The storm surrounding this particular merger controversy highlighted what many believe to be an abuse of managerial power, namely, golden parachute contracts.

Although Agee is but one of a handful of executives to exploit this new managerial perquisite, the number of executives who have GPs in their employment contracts is significant. One study estimates that the number of executive employment contracts containing GPs more than doubled between 1979 and 1982.[2] Estimates of the percentage of firms that have awarded their managers such contracts range from 25 to 50.[3] In the Bendix merger, 16 Bendix executives, 28 Martin Marietta executives, 2 Allied executives and 64 United Technologies executives were covered by GPs.[4] The increasing number of GPs has led one writer to suggest that GPs are "the hottest new executive suite perk."[5]

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Even though GPs seem to be reasonably well accepted in corporate circles, the public response to GPs has been less than favorable. The *Washington Post* described GPs as "executive incompetence insurance."[6] *Business Week* referred to GPs as "the gilded ripoff" and argued that the ethical differences between GPs and theft are "hard to discern."[7] Editorials and articles which criticize GPs have also appeared in *Forbes* and *Fortune.*[8] GPs at Bendix, Brunswick, Gulf Resources and Chemical, and Conoco have been the targets of shareholder suits, and both Congress and a government-commissioned panel studying takeover regulation are investigating various methods for controlling the use of golden parachutes.[9]

To date, the study of GPs has not kept pace with the growing controversy surrounding them. Research relating to GPs remains largely anecdotal and continues to be based on rather amorphous definitions and samples. A closer look is necessary.

What Is a Golden Parachute?

A golden parachute provides "employment-contract provisions that guarantee them (usually top executives) cash settlements equal to several years' salaries if their company changes hands."[10] For descriptive purposes such a definition suffices, but for analytical purposes this definition must be examined in more detail. Aside from one criterion—change of control—this definition does little to differentiate GPs from other types of severance pay. Does the amount of compensation or the organizational position of the recipient distinguish GPs from other severance pay agreements? Or is the difference between a GP and severance pay explained by the fact that GPs are a component of individual employment contracts while severance pay is determined by company policy? Distinguishing GPs on the basis of organizational position, size of compensation, or the vehicle of implementation seems fruitless.

A factor which does distinguish GPs from traditional severance pay does exist, however, and that factor is voluntary, as well as involuntary, termination. If, after a change in control, an employee chooses to resign from the acquired company and thereby receives severance compensation, then the employee is, indeed, benefiting from a GP. Although involuntary termination is still a possibility under a GP agreement, it is the possibility of voluntary termination which distinguishes GPs from traditional severance pay. In short, the ability "to pull the ripcord" is the second distinguishing factor in our definition of a GP.

Another point which must be considered in relation to the definition of a GP pertains to guaranteed employment. A guaranteed employment provision in an executive's contract says that after a change in control the executive is guaranteed a specified position for a given number of years. In some cases the guarantee goes on to say that if the executive's position is changed, the executive may choose to resign and collect the compensa-

tion which he/she would earn through the remainder of the guarantee period. The determination of whether a position has changed is most often left with the affected executive. In many other cases, however, it is not specified as to what would happen if the executive chooses to leave the company or if the executive chooses to minimize his/her activity within the company and maximize activity in other endeavors. Because of the clear control which the executive has in the first case and the ambiguity which exists in the second case, guaranteed employment provisions are also a component of our definition of a golden parachute.

In sum, GPs may be defined as provisions which allow for corporate executives to receive severance compensation if they are voluntarily or involuntarily terminated after a change of control. Guaranteed employment provisions are a particular type of GP.

Who Has Golden Parachutes?

As noted earlier, the estimates of the percentage of major firms granting GPs vary from 25 percent to 50 percent. Part of the wide variation in these estimates may stem from differences in the definition of GPs. Further, it is possible that many GPs may have been drafted but not yet formally enacted—implementation could therefore await the actual tendering of a hostile takeover bid, thereby saving firms the embarrassment of disclosing GPs. Another explanation for the differences could be different sample populations.

In an effort to provide a base from which future research might be conducted, the authors undertook an intensive examination of the proxy statements of all of the 1981 Fortune 500 companies. Content analysis of the proxy statements was conducted throughout the summer and fall of 1982. To gather the most current information available, the 1982 proxy statements were examined. With the 1980 amendments of Item 4 of Regulation S–K, the SEC requires "after the fact" disclosure of special executive compensation programs in proxy statements or 10–K reports. For consistency, the proxy statements were chosen as the data source. The definition of a GP developed in the preceding section was used to determine which firms in the 1981 Fortune 500 had golden parachutes for their executives.

We determined that 55 (eleven percent) of the 1981 Fortune 500 firms had GPs in place. Of the 55 firms, 39 had GPs that were clearly defined, i.e., after a change of control the executive could voluntarily leave the company and receive previously agreed upon compensation. Five firms had guaranteed employment provisions that allowed the executive to receive compensation if the executive believed that his/her position had been altered. Eleven firms had guaranteed employment provisions with no future specifications. Table 1 presents the list of the 1981 Fortune 500 firms that had GPs at the time of their 1982 proxy statements.

Table 1: Firms with Golden Parachutes (n = 55)

Air Products and Chemicals	Dexter	Phelps-Dodge
Allied	Diamond Shamrock**	Phillips Petroleum
Allis-Chalmers*	Emhart	Robertson, H. H.
American Bakeries	Ferro	Schering-Plough
AMF	FMC	Sheller-Globe*
Amstar	Genesco**	Stanley Works
Arcata	Gulf Resources and Chemicals	Sterling Drugs
Bendix	Harnischfeger	Stokely-VanCamp
Brunswick*	International Paper	Sun Co.
Bucyrus-Erie**	Kimberly-Clark	Sunbeam
Ceco**	Louisiana Pacific	Superior Oil
Celanese	Manville	Thiokol**
Clorox	Midland-Ross**	Time, Inc.
Colt Industries**	Mohasco	Todd Shipyards
Conoco*	Morton-Norwich**	Uniroyal**
Control Data	National Gypsum**	United Technologies
Dana**	National Steel	U.S. Industries
Data General	Peabody International	Warnaco*
		Williams Co.

* Guaranteed employment where a lump sum payment would be made if the executive chose to leave after a change in control.

** Guaranteed employment after a change in control. No specifications were made beyond the guarantee.

Table 2: Industries* Represented in Sample (number of firms from each industry)

Aerospace (1)	Natural Resources—Fuel (4)
Appliances (1)	Office Equipment, Computers (2)
Automotive (3)	Paper and Forest Products (3)
Building Materials (2)	Personal Care Products (1)
Chemicals (8)	Publishing, Radio and TV Broadcasting (1)
Conglomerates (2)	Service (2)
Drugs (2)	Special Machinery (4)
Food Processing (3)	Steel (1)
General Machinery (2)	Textiles, Apparel (2)
Leisure Time (2)	Tires and Rubber (1)
Metals and Mining (2)	
Miscellaneous Manufacturing (6)	

* Using industries as broken down in *Business Week's* "Annual Corporate Scoreboard" (March 15, 1982).

The industries represented by these 55 firms are noted in Table 2. Firms in the chemical industry and in miscellaneous manufacturing accounted for 8 of the 55 and 6 of the 55 firms, respectively. Overall, 22 industries are represented in our list of 55 firms with GPs. With the

Table 3: 1981 Fortune 500 Ranks of Firms with Golden Parachutes

Ranks	#	% of Sample	Cumulative Percent	% in each hundred
1–50	4	7.3	7.3	
				14.6
51–100	4	7.3	14.6	
101–150	6	10.9	25.5	
				25.4
151–200	8	14.5	40.0	
201–250	7	12.7	52.7	
				16.3
251–300	2	3.6	56.3	
301–350	6	10.9	67.2	
				20.0
351–400	5	9.1	76.3	
401–450	6	10.9	87.2	
				23.6
451–500	7	12.7	99.9	

possible exceptions of chemicals and miscellaneous manufacturing, GPs seem to be no more prevalent in one industry than another.

In addition to determining which firms and industries had GPs, we also examined the factor of company size. First, the 55 firms were ranked against the Fortune 500 firms. As indicated in Table 3, the firms issuing golden parachutes were rather evenly distributed throughout the Fortune 500 — the top 100 accounted for 14.6 percent of the 55 firms, the second 100 accounted for 25.4 percent, the third 100 for 16.3 percent, the fourth 100 for 20.0 percent, and the fifth 100 for 23.6 percent. Gross size alone does not seem to be a major variable for determining which firms have GPs. This is particularly surprising since one would expect that management in larger firms would be less concerned about hostile takeovers and therefore would be less likely to have GPs implemented.

To examine further the question of size, an additional list was compiled. This compilation focused on the firm's ranking in its industry as well as its standing in relation to other Fortune 500 firms from the same industry (see Table 4). The results of this compilation show again a rather even distribution. A little over 20 percent of the firms with GPs are in each of the top two quartiles of their industries. Nevertheless, based on these data, it does not seem that size of firms is a significant determinant of GPs.

Beyond size, another general characteristic we examined in the 55 firms with GPs was financial performance. The percentage changes in sales and profits for each firm were compared to the percentage changes in sales and profits for the firm's industry composite in *Business Week*'s "Annual Corporate Scoreboard." The comparison was conducted for the years 1980 to 1981 and 1981 to 1982. The results are shown in Table 5.

Table 4: Industry Quartiles of Firms in Sample*

	#	Percent of Sample	Cumulative Percent
Top Quartile*	12	21.8	21.8
2nd Quartile	12	21.8	43.6
3rd Quartile	16	29.1	72.7
4th Quartile	15	27.3	100.0

* Firm rankings are by sales using data from *Business Week's* "Annual Corporate Scoreboard" (March 15, 1982). Only Fortune 500 firms were included in the industry quartile computation.

As shown in the first part of Table 5, 68 percent of the firms with GPs performed worse than their industry in relation to change in sales from 1980 to 1981; 55.3 percent performed worse than their industry's sales performance from 1981 to 1982. In relation to profitability, 62.0 percent did better than their industry from 1980 to 1981, but in a curious reversal, 59.6 percent did worse than their industry from 1981 to 1982.

The second and third parts of Table 5 examine this relationship a bit more closely. The second part shows that profitability is a less important factor than sales in the 1980 to 1981 performance of firms with GPs. Of the 34 firms that had lower sales increases than their industry, half had a better profit performance and half had a worse profit performance. Firms with better sales performances than their industries tended to have better profit performances as well. In terms of the changes from 1981 to 1982, the performances of the firms are fairly even. Over 38 percent did worse than their industry on both sales and profits, but slightly over 23 percent did better than than their industry on both dimensions.

The surest conclusion to draw from the examination of performance data would be that no relationship exists. However, in both of the examined time periods, firms with GPs had poorer sales performance than did their industries. Based on this observation, it seems sales performance is the important dimension.

In sum, firms with GPs are spread throughout the Fortune 500 and throughout their respective industries. The firms are more likely to have performed worse than the industry in relation to sales; profitability performance does not seem to be an important factor.

What Is Included in a Golden Parachute?

The precise contents of a GP are impossible to determine without having access to the employment contracts of the executives who have GPs. From the examination of the proxy statements, however, a general picture of what is included in a GP can be drawn.

Table 5. Performance of Firms with Golden Parachutes

The comparisons in this table are based on *Business Week's* "Annual Corporate Scoreboard." The percentage changes in sales and profits for each firm were compared to the percentage changes in sales and profits for the firm's industry composite.

	1980 to 1981 Sales Performance	1980 to 1981 Profit Performance	1981 to 1982 Sales Performance	1981 to 1982 Profit Performance
Firms Performing *Better* than the Industry	12 (24.0%)*	31 (62.0%)	18 (38.3%)	19 (40.4%)
Firms Performing *Worse* than the Industry	34 (68.0%)	19 (38.0%)	26 (55.3%)	28 (59.6%)
Firms Performing *Same* as the Industry	4 (8.0%)	0 (0.0%)	3 (6.4%)	0 (0.0%)
Total Compared	50	50	47	47
Data Not Available	5	5	8	8

* Percentage of Total Compared for the Category (e.g. 12 is 24.0% of 50).

1980 to 1981

	Firms Performing Better than the Industry on Profit	Firms Performing Worse than the Industry on Profit	Total
Firms Performing Better than the Industry on Sales	10 (20.0%)	2 (4.0%)	12
Firms Performing Worse than the Industry on Sales	17 (34.0%)	17 (34.0%)	34
Firms Performing the Same as the Industry on Sales	4 (8.0%)	0 (0.0%)	4
Total	31	19	50

1981 to 1982

	Firms Performing Better than the Industry on Profit	Firms Performing Worse than the Industry on Profit	Total
Firms Performing Better than the Industry on Sales	11 (23.4%)	7 (14.9%)	18
Firms Performing Worse than the Industry on Sales	8 (17.0%)	18 (38.3%)	26
Firms Performing the Same as the Industry on Sales	0 (0.0%)	3 (6.4%)	3
Total	19	28	47

For example, the number of executives covered by GPs ranges from one to 80. Thirty-four of the 55 companies (61.8 percent of the sample) provided GPs to ten or less of their executives; 24 of those companies (43.6 percent of the sample) provided GPs for five or less of their executives. In only one case was the coverage ambiguous; at Superior Oil, all present and future officers were covered by GPs.

Since change of control is a key variable in distinguishing GPs from severance pay, it too is important in relation to the contents of GPs; however, in the proxy statements, only 31 percent of the sample defined what the firm meant by change of control. In approximately half of the proxy statements where change of control was not defined, it was noted that the definition of the term could be found in the executives' employment contracts. Of those companies which did define change of control in their proxy statements, the definition centered on change in the majority of the board, accumulated ownership by one entity or a combination of both factors.

A change of over half the directors in a short time period appears to be a near-universal GP trigger. However, some firms are also basing the trigger on changes in accumulated ownership. Often these clauses allow executives to collect their GPs if any single entity accumulates more than a given threshold percentage of the firm's outstanding stock. These thresholds range from 20 to 50 percent. Given this rather liberal definition of change of control, GPs could be triggered inadvertently. In fact, "when Gulf & Western's stake in Mohasco, an interior furnishings company, went over the magic 20% mark, four executives bailed out with some $800,000 among them."[11]

In relation to the total dollar commitment under GPs, only two firms estimated their potential costs. Bendix estimated its costs at $15.7 million for 16 covered executives, and Gulf Resources and Chemical Group estimated its costs at $9.4 million for 13 executives.

With regard to specific compensation of executives, the costs are as difficult to measure as total dollar commitment. For example, at H.H. Robertson the GP compensation is based on a sliding scale over four years, but at Manville the GP compensation is based on one month of salary for each year at Manville. In general, GPs provide the equivalent of 1 to 6 years of salary, with 2 to 3 years of salary being the most common compensation. Guaranteed employment contracts generally extend from 3 to 5 years after a change of control or until some specified date, generally in the second half of the 1980s. Besides compensation based on salaries, many GPs also include provisions for accelerating stock options and long-term incentive compensation. Bonuses are also estimated and paid, and fringe benefits (most often insurance and pension) are included as well. The total compensation received by an individual is therefore a function of several variables and, at best, is difficult to determine prior to the execution of the GP.

A final area of interest concerning the contents of GPs relates to limitations. In 30 of the 55 companies with GPs there was a specified time limit in which the executive could take advantage of a GP. With the guaranteed employment provisions, that time limit centered on a date — generally in the 1980s, as mentioned above. For the lump-sum type of GPs, this limitation involved a time period from six months to five years after a change of control. The most frequent time limitation was two years.

In only six of the 55 companies with GPs were there any "offset" provisions, i.e., provisions which reduce or eliminate GP compensation or benefits if the executive takes a position with another company. In three of these six companies the offset related to insurance benefits — in one company benefits would be reduced by 50 percent, and in the other two companies benefits may be reduced under certain unspecified circumstances.

Even though it is impossible to predict the exact contents of a GP, it is still possible to describe the contents of a "typical" GP. A typical agreement would contain the following:

- coverage for one to 10 executives
- change of control, being defined as a change in the majority of the board or the acquisition of over 20 percent of the outstanding stock by some distinguishable party
- compensation consisting of two to three years' salary plus accelerated stock options, bonuses, and long-term incentive compensation
- insurance benefits for two to three years after a change of control and pension or retirement provisions
- a two-year time frame after a change of control in which to activate the GP

The Arguments for and Against Golden Parachutes

Arguments for Golden Parachutes — The following excerpt from the proxy statement of Superior Oil summarizes three of the key arguments for GPs:

> The Board of Directors is determined that the senior executives of the Company be able to devote their full attention and energies to the pursuit of the Company's business under any circumstances and that they not be unsettled by any real or rumored possibilities of change of control of the Company. The purpose of the Board of Directors is to assure retention of senior executives to carry on the Company's business as usual and to assure that, should the Company receive proposals from third parties with respect to its future, the officers of the Company and its subsidiaries can, without being influenced by the uncertainties of their own respective situations, (a) assess such proposals, (b) formulate an objective opinion as to whether or not such proposals would be in the interest of the Company and its shareholders, and (c) take such other action regarding such proposals as the Board of Directors might determine to be appropriate.[12]

Implicit within this statement are three arguments: the objectivity argument, the loyalty argument, and the retention argument.

The *objectivity* argument suggests that without assurances about their futures, executives might be more concerned about their own interests than about those of the shareholders. Presumably, executives would therefore be more concerned about being viewed favorably by their future boards than by their current boards. GPs eliminate this potential problem because the executive knows, at least at a minimum, what the future holds.

The *loyalty* argument implies that GPs are justified on the basis of reward for past service. Many companies believe that they have a responsibility to their employees that is nearly as important as their responsibilities to their stockholders and customers. GPs are one way of assuring that new, uncaring management does not run roughshod over the firm's old, loyal employees.

The *retention* argument is probably the one most commonly used to defend GPs. The suggestion is that GPs encourage executives to stay with their firms, both during a takeover attempt and after the completed takeover. This argument presupposes that without GPs the uncertainties surrounding a takeover might be sufficient to cause a number of key executives to "jump ship" at a time of severe organizational trial. GPs therefore "buy" the continued leadership of senior management. As such, GPs are merely another form of executive compensation similar to bonuses, stock options, etc. In fact, they could be viewed as just another facet of a total executive compensation package.

Beyond these three arguments lies what might be called the *cost* argument. This argument proposes that GPs add to the acquisition cost of a takeover, thus becoming a legitimate means of forcing the acquirer to re-evaluate his intentions. Since GPs go into effect only in the event of a successful takeover, they can be used as a device for raising the price to the "raider" but not to a compatible "white knight." A second aspect of this argument is that the cost of GPs is actually borne by the stockholders of the acquiring firm and not the stockholders of the executives' firm. Issues of fiduciary responsibility are therefore irrelevant to the GP contract.

Arguments Against Golden Parachute — In general, the criticism of GPs centers on four arguments — the managerial performance argument, the "arm's length" argument, the fiduciary responsibility argument, and the public relations argument. Most of the criticism stems from the suspicion that GPs are implemented in order to benefit existing management and not necessarily shareholders.

The *managerial performance* argument has several dimensions. The first dimension relates back to the objectivity argument for GPs and suggests that GPs are compensating managers to perform as they already should. This argument is based on the "trustee" notion of management, i.e.,

management serves as a trustee of shareholder property and is therefore already charged with maximizing shareholder wealth. To provide additional compensation in order to get managers to objectively evaluate takeover offers is tantamount to management extortion of the shareholders.

Another dimension of the managerial performance argument relates to the relationship between managerial performance and takeovers. Takeovers generally occur only when some external group believes that they can manage the firm's assets more efficiently than current management. This argument suggests that GPs are nothing more than multi-million – dollar rewards to executives who have so mismanaged a company that the company's stock price is depressed to the extent that an outside group is willing to pay a considerable sum in order to gain control of the target's assets. Recent evidence suggests that takeovers result in gains to the stockholders ranging from 14 percent to 50 percent.[13] Thus firms which become takeover targets are vulnerable because their current management is very inefficient.

The *"arm's length"* argument focuses on the relationship between executives and their boards of directors. The central premise of this argument is that executives, through control of their boards of directors, give themselves the golden parachutes. GPs are thus seen as yet another manifestation of the effects on a firm when control shifts from stockholders to managers—a phenomenon first discussed by Berle and Means in 1932 and thoroughly documented in the past two decades[14] There is generally little argument about compensation levels that are determined in a free market. However, substantial evidence indicates that management does control the boards of many major firms, and thus GPs become more a function of management's political control and less a function of the supply and demand of senior managers.

The *fiduciary responsibility* argument is based on the relationship between management and stockholders. This argument equates GPs with theft. For example, given that a "raiding" firm is willing to pay only so much to acquire a target firm, and given that the target successfully pumps up the costs that the raider must pay, then the target is worth correspondingly less. For every additional million dollars that a raider must pay in GPs, a million dollars is taken from the target's shareholders.

Finally, the *public relations* argument suggests that GPs are irresponsible. In a time of economic hardship and union givebacks, news of GPs can prove, at best, to be a serious embarrassment. Even if GPs can be justified economically or ethically, one must ask whether or not the existence of GPs compensates for the various costs associated with the negative publicity they arouse — costs which may eventually include additional government regulation.

Discussion

The Legal Perspective — There have been at least four shareholder suits brought in relation to GPs. Further, both Congress and a government-commissioned panel studying takeover regulation are considering various methods for controlling GPs. Still, at this time, GPs do not appear to be illegal. In fact, the legality of GPs has rested on "the business judgment rule." The business judgment rule can be interpreted to suggest that "management has the right, and even the duty, to oppose a tender offer it determines contrary to the firm's best interest."[15] To the extent that management can successfully claim that GPs aid opposition to hostile tender offers, the courts are likely to uphold these agreements. The business judgment rule has served as an effective shield against virtually all suits that question management decisions — decisions which include the implementation of GPs.

The unanswered legal question, however, centers on management's relationship to the members of the board. More specifically, the concern is with the separation of senior-level management decision making and decision making by the board. For example, in the Gulf Resources case the role of Robert H. Allen is at issue. The new board controlling Gulf Resources has refused to pay Allen's GP because Allen was both Chairman of the Board and CEO of Gulf Resources prior to its acquisition. The new board claims that "as chairman he [Allen] ratified the decision to cover him and his fellow officers with the severance plan, which reportedly amounted to some $13 million."[16] Thus, the old board "did not have the degree of independence and disinterestedness necessary to authorize the (parachute) agreement."[17]

The question of management and board decision making is further complicated when, as in the case of the Brunswick Corporation, directors as well as managers receive GPs. At Brunswick, any outside director over 55 years of age with more than five years' service may quit after a hostile takeover and continue receiving an annual retainer of $22,000 for life.[18] Given such circumstances as those in Gulf Resources and those in Brunswick, there is a definite possibility that the courts may actually set a new precedent in the area of GPs.

Still, the legal community is strongly divided over GPs.[19] Some attorneys see GPs as nothing more than common-law fraud. Others view GPs as no different from other executive perquisites. The more moderate view of GPs and perhaps the most likely view for the future is that GPs will be considered on a case-by-case basis and no precedent will be established. In rendering their decisions, the courts will examine the time at which a GP was enacted and whether or not the board provided due consideration.

The Ethical Perspective — Even if GPs are legal, they are not necessarily ethical. In fact, it is difficult to find any ethical justification for them.

This isn't to suggest that high compensation in itself is unethical since fortunes of a major company often turn on the judgment of senior management. Income differentials are a necessary element of a market economy and one that helps drive it toward efficiency. Rather, the ethical validity of GPs hinges upon considerations of management's responsibilities to its shareholders during takeover attempts.

Consider, for example, the previously discussed arguments for GPs — the objectivity, loyalty, retention, and cost arguments. None of these arguments unambiguously meets the objective of improving shareholder wealth. The objectivity argument hinges on the assumption that senior management will act first in its own self-interest and second in the shareholders' interests. Given that this assumption is true, what does a GP contribute? As the critics of GPs point out, a GP may serve as a "bribe" to get management to do what it should be doing anyway. Furthermore, a GP might also remove the incentive for management to see the best deal for the firm. Once a GP is implemented, the connection between management's self-interest and shareholder interests is completely severed. If it is assumed that managers act in their own self-interest without a GP, why is it assumed that they will disregard that self-interest once a GP is provided? Frank H. Easterbrook and Daniel R. Fischel have presented a powerful case for total managerial passivity in the face of a takeover; they contend that *any* managerial resistance ultimately decreases shareholder wealth.[20] Ironically, however, that position is not taken by the advocates of GPs. Instead, GPs are somehow supposed to motivate senior management to aggressively seek the best deal for the shareholders. Given the assumption of managerial self-interest, the logic of the argument is strained at best.

Similarly, the loyalty argument seems flawed. A firm is a takeover target (generally at a premium over recent market price) because some other company believes that it can manage the firm's resources considerably more efficiently than can existing management. In other words, the market has given the management of the target a failing grade. Why would shareholders want to reward that management group with golden parachutes?

The retention argument for GPs is equally questionable. Most takeover specialists scoff at the notion that management is likely to depart during a takeover attempt. They note that there is virtually no evidence of managers bailing out in a time of crisis. Rather, the group dynamics of senior management are such that to do so would be seen as "disloyal" and the person bailing out would lose face.[21]

Finally, the cost argument from the shareholders' view seems flawed. Given that the market determines the value of a target in a takeover attempt, driving the cost up for a raider but not for a white knight serves only one interest — management's. Do shareholders really care whether their stock is acquired by a raider or a white knight? More than likely they

don't — but management does. What then, besides a possible transfer of funds from shareholders to managers, does a GP accomplish?

Our conclusion is that from the shareholders' perspective, GPs are of little value. GPs serve management's interests by reducing the uncertainty and costs resulting from management performance, but GPs do little for shareholders. The authors see GPs as a direct and unjustified transfer of wealth from shareholders to managers. This makes them unethical.

Conclusion

When William Agee pulled the ripcord on his golden parachute, he provoked a major controversy in both the popular and the business press over abuses of managerial perquisites. Though there have been a few notable instances of golden parachutes being refused by senior management,[22] the trend appears to be toward even greater use of this perquisite.

The widespread public perception that the mere existence of golden parachutes is fundamentally perverse is fueled by the fact that they reward the captains of the losing side. These negative public perceptions led in March 1983 to the establishment of an SEC advisory panel on takeovers and associated practices. Whether new regulations would take the form of prohibiting GPs or the form proposed by Easterbrook and Fischel of eliminating management's right to oppose a takeover,[23] is not the question here. Instead, the concern is that GPs are giving American business another "black eye." The existence of GPs today is similar to the existence of insider trading prior to 1933; insider trading amounted to theft, even before it was made illegal. As S. Prakash Sethi has noted, "corporate interests must emanate from the public interest and cannot be inconsistent with it."[24] Not only is it in the public interest and shareholder interest to eliminate GPs, but it is also in the interest of the American business community.

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14. See R. Joseph Monsen and Anthony Downs, "A Theory of Large Managerial Firms," *Journal of Political Economy* (June 1965), pp. 221-236; and Robert Larner, *Management Control and the Large Corporation* (New York, NY: Dunellen, 1971).
15. Easterbrook and Fischel, op. cit., p. 1163.
16. Klein, op. cit., p. 56.
17. Ibid., p. 56.
18. N.R. Kleinfield, "'Golden Parachutes' for Ousted," *New York Times,* April 6, 1982, p. D17.
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22. Tim Mertz, "Texas Gas 'Golden Parachutes' Rejected by Aides, Two Days After Board Voted Pacts," *Wall Street Journal,* June 13, 1983, p. 7.
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