

When the Fairy Tale Goes South: Executive Compensation Agreements

Spoiler Alert: This story does not have a happy ending. But it really happened and could happen again. Imagine starting a business, inviting men and women you trust to serve on the Board and help lead the company. After years of success and growth, the Board wants to merge the company and profit; but to do so will end the company and careers of many loyal employees and friends. Imagine the Board engineers a coup. Further imagine the Board tries to buy your vote and cooperation with a lucrative severance package. You balk because you are the Trustee of the ESOP and besides the jobs and well-being of your employees is on the line. Now finally imagine you're fired as CEO and voted off the Board. Your compensation is frozen and if you fight back you risk tens of thousands of dollars litigating your rights. Success is far from certain, and even if you win, the company has been so badly shaken in your absence that the ranks of senior leadership and key customers are decimated. Happily ever after?

Can this bad dream be transformed into a fairy tale? The good news is: Yes it can.

Whether you are a new, long-time, or prospective Senior Management Official (SMO), an employment contract is vital. It spells out employment duties and rights, but equally important, it should draw the center line and install the guardrails for navigating the tricky switchbacks encountered during leadership transition, both voluntary and Board-initiated.

For SMOs at nonprofits, this may be even more important because funding-pressure on Boards can unrealistically inflate the lotto-dream that a new CEO will be the ticket. SMOs of educational institutions may be particularly at risk without a complete employment package since the academic calendar controls hiring for these senior positions.

What should an employment contract include? A well drafted contract sets out in clear and measurable terms the job description, any performance goals and measures that the SMO must meet to qualify for bonuses, stock options, or merit pay and, most relevant to this Alert the terms under which he or she may be released. These terms include not only notice provisions, but severance pay and benefits-especially health care and retirement contributions, vesting of stock rights, out-placement services, the continued access to Company property such as office space and equipment, administrative support and transportation. Employment agreements enable SMOs to protect themselves from summary termination and damage to their financial health, personal and private reputation, and future job prospects.

Employment contracts are a matter of arm's length negotiations and have very few legal limitations, as long as they don't create excessive compensation, protect law-breaking or interfere with a fiduciary duty. The best time for structuring an agreement is at the outset of the relationship, when the parties are still courting. It is at this time that Company officials will be most amenable to reasonable requests from the SMO. ***So look at your own agreement or situation and ask yourself, do you have:***

- J A guaranteed severance agreement in writing for the continuation of salary and benefits for a sufficient transition period?
- J Immediate vesting of a minimum number of shares and clearly written rights to options upon meeting certain performance goals?
- J An automobile allowance?
- J The right to an office-either at the Company or an off-site location--that is convenient and will allow you to conduct a full range of business?
- J Indemnification and insurance that is guaranteed and not up to the vote of a Board? (An alternative is to have the Company provide you with the amount necessary to buy your own policies that you control.)
- J The right to have all attorney's fees and costs paid and advanced without the need to post a Bond in the event that you are sued-including by your own Company (with the normal exclusions for fraud or illegal conduct)?
- J A golden parachute that provides a significant payout if you are terminated or demoted without cause?

If you would like a review of your or your entity's current SMO employment contracts, please call or email Gammon & Grange, P.C. attorneys **Christine Johnson** and **Bob Flores**.



Bob Flores, *Senior Counsel* at Gammon & Grange, P.C., has more than two decades working with small businesses and nonprofit executives ensuring that their companies and organizations implement policies and procedures to effectively manage human capital, comply with regulations and law, and mitigate risk. Bob works with start-ups, is an entrepreneur himself, and has helped companies and nonprofits navigate the government contracting process. He served in the Manhattan District Attorney's Office and the United States Department of Justice and has significant experience in business law and litigation. Contact Bob at jrf@gg-law.com



Christine Lambrou Johnson, *Of Counsel* at Gammon & Grange, P.C., is an experienced litigator representing nonprofits and business entities in their obligations under discrimination and employment laws. She successfully defended numerous discrimination suits while serving as Assistant Attorney General for the State of Illinois.

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