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Memorandum to General Partners: Pearsall position statement

Duane Pearsall

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MEMORANDUM

TO: General Partners
FROM: Duane Pearsall
DATE: December 11, 1991
SUBJECT: Position statement for Duane D. Pearsall

Position relative to my role as a General Partner of both CVF I and CVF II.

Commensurate with this major change in the structure and operating character of Columbine, I believe it is an appropriate time for the remaining partners to recommit themselves to the support of each other partner and to the highest ethical principles in our relationships throughout this industry.

The first step in this recommitment is to agree that under no circumstances will we make any degrading or disparaging remarks concerning Mark Kimmel. We will also live by the spirit and the intent of the Agreement of Separation. I, personally, will not tolerate anything but the highest level of ethics in the administration and implementation of all elements of the Withdrawal Agreement with Mark Kimmel.

I will plan to retire at the end of Fund I or approximately October 31, 1993. I look forward to these remaining 22 months for two fundamental reasons. First, our level of communications between partners will be enhanced dramatically. Second, there is a level of good chemistry and mutual respect that most certainly will result in a higher level of productivity and success.

Although, as I have declared, I will not be part of Fund III. However, I will do everything possible to help in the formation of that fund should that be the consensus of your judgment.

Commitment and Compensation

I agree to increase my commitment of time to Fund I and Fund II to no less than 50% for a compensation from CVM II of $72,500 per year. In addition, I will accept an annual allocation of $16,000 to cover expenses under the same expense/bonus plan as used by the other partners. This anticipates travel commitments of approximately one-fourth that of the other partners.

Participation in the Distribution of Excess Funds From CVM I

The attached chart is a summary of bonuses paid from CVM, Inc. and CVM I from 1988 through September 30, 1991. The following is a listing of some of the "rationale" for judging how the CVM I surplus would be distributed:
1. In proportion to the original CVM, Inc. ownership, which is probably legally correct.
2. By the partners' contribution to the Fund I performance.
3. Simply equal distribution to each of the Fund I partners.
4. Adjusted by individual fund raising performance for Fund I.
5. Percent of time committed to Fund I in the past.
6. Percent of time committed to Fund I going forward.
7. Number of deals supervised in Fund I.
8. One's handicap at Castle Pines.
9. Ratio of winners versus losers under his control.
   a. By number of deals.
   b. By dollars.

It is clear that none of the above items by themselves are a basis for making a distribution judgment. However, assuming that salaries in Fund II are proportionate to the time commitment for each partner, basing the distribution of Fund I excess upon a time commitment essentially for Fund II, is not only inequitable, but flagrantly so. A coverup to this distribution became obvious when I never had the opportunity to co-sign one of those checks.

As I said earlier, I am looking forward to the new partnership because I believe we have eliminated the source of the element of "mistrust". I am not interested in diluting Sherman or Terry from their four-thirteenth's interest in the Fund I excess. I accept the offer of a lump sum compensation for the past inequity in the form of CVM II's reimbursement to Fund I as a participation in the severance payments to Mark. I expect that would compensate for the inequity up through 12/31/91.

Although it is hard to judge the value of one point of a General Partner's carried interest, I will assume that the Fund will breakeven and one percent represents $400,000. Therefore, I propose that I be allocated one-half percent of the one and one-half percent residual available following Mark's departure. That increase in carried interest, together with the continuing one-thirteenth distribution of Fund I excess provides a means of not diluting the current distribution to Sherman and Terry, or interfere with the Withdrawal Agreement with Mark.
In the spirit of openness and equality among the partners, I believe there currently exists an inequity relative to Carl's participation in Fund I benefits. I estimate Carl spends as much as 20% of his current effort on Fund I business with no ultimate reward. I, therefore, recommend that the remaining one percent of the residual of one and one-half percent of Mark's carried interest be allocated to Carl, bringing his carried interest from 3 points to 4 points.

Twice in the history of these Funds I have given away carried interest voluntarily. First, you will remember the residual carried interest from the buyout of David Miller. My portion of that distribution was given to Terry and Mark equally in recognition of their fund raising efforts for Fund I. My recollection of the allocation initially for Fund II prior to raising funds was 5 points each to three partners, 3 points to me and 2 points unallocated. When it became obvious that we would need more unallocated points to entice a new GP, I voluntarily gave up 1 point. Later, when negotiations with Carl got serious, and we felt we needed one unallocated point for future contingencies and it would take 3 points to entice Carl, I gave up another point. As I remember, my rationale in this judgment was simply that Fund II would be a ten year program and at my age the carried interest would not be important. In addition, I elected not to be an active participant in the fund raising effort, whereas Carl was doing an outstanding job and without him there would be no Fund II. Not to recognize that performance and his continuing contribution to Fund I, in my opinion, reestablishes a serious inequity.

I apologize for the length of this memo, but with the above adjustments, I believe we have a great opportunity to have both a productive and an enjoyable experience.