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Bad Chemistry

W.R. Grace Is Roiled By Flap Over Spending And What to Disclose

Departed CEO Made an Issue Of the Chairman's Perks, Son's Use of Grace Funds

Mentor and His Protege Part

The Grace Commission won plaudits a decade ago for an assault on waste, perks and dubious spending in the federal government. Some say J. Peter Grace's company could use the same advice.

Documents obtained by The Wall Street Journal indicate that Mr. Grace, the 81-year-old chairman of W.R. Grace & Co., and his son, J. Peter Grace III, have been the personal beneficiaries of hundreds of thousands of dollars in company expenditures and perquisites that the company didn't disclose.

By Wall Street Journal staff reporters James P. Miller, Thomas M. Burton and Randall Smith.

Reports prepared for directors say a company formed by Peter Grace III used about $1.3 million of a W.R. Grace subsidiary's funds for working capital without proper authorization. Meanwhile, his father, who retired as chief executive officer at the end of 1992 after 47 years and now is ill with lung cancer, has continued to receive such company-paid perks as $165,000 annually for full-time and part-time nursing care, $200,000 annually for security guards, $74,500 annually to maintain a New York apartment largely for his family's personal use, plus a full-time cook.

"The very things the Grace Commission said about the government were true within Grace," says Jack Shelton, an ex-employee and head of American Breeders Service, a cattle-breeding business Grace sold last year. "The corporate culture had gotten mired down, lazy and fat."

Those perks and the younger Mr. Grace's business dealings recently helped spark a heated internal debate pitting the elder Mr. Grace against the company's president and CEO, J.P. Bolduc. It culminated suddenly a week ago in Mr. Bolduc's resignation, attributed by the company to "differences of style and philosophy."

Mr. Bolduc, 55, had been a protege of the senior Mr. Grace, helping him run the Grace Commission, the company and a range of Catholic charities to which Mr. Grace has been a generous contributor. But the two men slowly turned into adversaries over the past few months.

Mr. Bolduc's abrupt departure spurred much concern among big shareholders about the direction of the 139-year-old, $5 billion-a-year industrial company. They credit Mr. Bolduc for improving earnings by refocusing Grace on its core specialty-chemicals and health-services businesses. In doing so, he jettisoned pet subsidiaries of Mr. Grace, who had led the company into fields as diverse as ethnic restaurants, energy, cattle breeding and sport stores.

On Wednesday, institutional investors expressed their concerns in a meeting with Thomas A. Holmes, a 71-year-old Grace director who has been named acting president and CEO. Jeffrey Cianci, an analyst at Bear Stearns, sees "a good chance" institutional holders could propose their own partial slate of directors for a coming election. But the deadline for doing that is today.


J. Peter Grace

Mr. Bolduc's bold restructuring reportedly wasn't the cause of the rift between him and his mentor. It sprang at least in part from an effort by Mr. Bolduc to rein in the senior Mr. Grace's longtime perks and spending patterns, according to people familiar with the company.

And one director, Charles H. Erhart Jr., said in an interview yesterday that the board had learned of allegations of sexual harassment against Mr. Bolduc by female employees. (When Mr. Erhart was called again later at the same home phone number, he denied having ever spoken to a Wall Street Journal reporter.)

Part of Mr. Bolduc's cost-reduction program was cutting off capital to the hotel-services unit run by Peter Grace III, according to associates of Mr. Bolduc. Late last year, Mr. Bolduc decided that a number of transactions, including those with Peter Grace III, needed to be disclosed to the Securities and Exchange Commission. By raising that issue, he touched off what became the odd spectacle of dueling outside-counsel reports, commissioned by himself and by the senior Mr. Grace.

Mr. Grace's report, prepared by the New York law firm of Milbank, Tweed, Hadley & McCloy, was finished in January. Simultaneously, a legal opinion written for Mr. Bolduc by another New York firm, Proskauer Rose Goetz & Mendelsohn, concluded that various payments "exceeded the threshold requiring disclosure of personal benefits to a CEO."

Grace's 22-member board, which included Mr. Bolduc, decided it needed to get a reality check in the form of its own legal report. It hired a third New York law firm, Patterson, Belknap, Webb & Tyler, which submitted its report to the board at the beginning of February. That document, written in part by former federal Judge Harold R. Tyler Jr., said Grace "would be

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Bad Chemistry: Grace's President Clashed With Company Chairman

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taking a very aggressive position" not to disclose some of the senior Mr. Grace's perks, such as nursing care.

Mr. Erhart, who besides being a director is a former Grace president, said in his initial interview yesterday that Mr. Bolduc and the senior Mr. Grace "certainly didn't scream and yell at board meetings" over their differences about disclosure. But he added in the approximately 15-minute interview that the disagreements, while "not a major part" of Mr. Bolduc's leaving the company, "may have been a part."

Many of Grace's board members are retired executives who are longtime associates of the chairman. In 1993, Grace, which is based in Boca Raton, Fla., raised the pay of outside directors from $3,000 per board meeting and $900 per committee meeting to a flat $24,000 apiece annually plus $2,000 for each board meeting and $1,000 per committee meeting.

Last year's proxy statement showed that Grace paid five directors hefty consulting fees ranging from $85,000 to $585,000. A spokeswoman says one of those has since ended. When the senior Mr. Grace ceded his posts as CEO and president at the end of 1992, the company gave him a one-time payment of $5 million, and his severance package includes a yearly pension of $1 million. The company also pays him a consulting fee of $50,000 a month.


J.P. Bolduc

The Grace directors accepted Judge Tyler's recommendation – and Mr. Bolduc's contention – that the company needed to disclose some of the matters at issue to the SEC. The company spokeswoman says Grace "is in the process of preparing disclosure documents to comply with SEC regulations." Grace's proxy statement for 1994 is expected to be filed with the SEC within a few weeks.

Some of the matters considered for SEC disclosure involve Grace's plan to sell its Grace Hotel Services Corp. unit to HSC Holding Co. – formed by the younger Mr. Grace, who is in his 50s. Judge Tyler concluded that, on balance, "the use by HSC of up to $1.3 million" of Grace Hotel Services funds "was not properly authorized" by either the subsidiary or W.R. Grace. But Judge Tyler acknowledged there is a dispute over this and said the matter didn't require disclosure.

The Proskauer law firm's discussion of these transactions was more pointed. "We understand that without authorization, the son used approximately $1.3 million" of Grace Hotel Services funds "to pay bills of HSC and for other purposes. When this was discovered by company officials in November 1994, the son resigned as chairman" of Grace Hotel Services "and HSC agreed in writing to repay the funds diverted to it." Proskauer's report says that as of Jan. 17, $1 million had been paid back and $381,000 was being held in escrow pending final accounting of the matter.

Proskauer concluded that this use of funds should have been disclosed. Peter Grace III couldn't be reached for comment.

Company-paid benefits of the senior Mr. Grace include a private nurse hired after he had hip-replacement surgery in January 1990 due to the effects of cancer. The Proskauer document reported, for example, that in July and September 1991, Mr. Grace – then still CEO – went on trips to Asia and that the company paid $10,788 for the nurse who traveled with him. Also, that year he made several trips to Singer Island, Fla., and the company paid about $6,800 for the nurse's travel expenses, the report said.

It added that Mr. Grace's health-insurance carrier found the nursing payments not medically necessary and wouldn't pay the bills.

W.R. Grace's Directors

J. Peter Grace, 81, chairman of W.R. Grace and former CEO

Thomas A. Holmes, 71, acting W.R. Grace CEO and retired chairman and CEO of Ingersoll-Rand Co.

George C. Dacey, 74, retired president of Sandia National Laboratories.

Edward W. Duffy, 68, retired CEO of Marine Midland Banks Inc.

Harold A. Eckmann, 73, retired chairman and CEO of Atlantic Mutual Insurance Co

Charles H. Erhart Jr., 69, retired W.R. Grace president.

James W. Frick, 70, president of James W. Frick Associates, a consulting firm to colleges.

Constantine L. Hampers, 62, executive vice president of W.R. Grace.

Gordon J. Humphrey, 54, former U.S. senator from New Hampshire, founder of Humphrey Group Inc.

George P. Jenkins, 80, former CEO of Metropolitan Life Insurance Co.

Virginia A. Kamsky, 41, president and CEO of Kamsky Associates, an investment-banking firm.

Peter S. Lynch, 51, vice chairman of Fidelity Management & Research Co.

Robert C. Macauley, 71, chairman of Virginia Fibre Corp

Roger Milliken, 79, CEO of Milliken & Co.

John E. Phipps, 62, a private investor.

William Wood Prince, 81, former Armour & Co. CEO.

John A. Puelicher, 74, retired chairman of Marshall & Ilsley Corp.

Eben W. Pyne, 77, retired senior vice president of Citibank.

D. Walter Robbins Jr., 75, a W.R. Grace consultant.

Eugene J. Sullivan, 74, retired Borden Inc. CEO.

David L. Yunich, 77, a W.R. Grace consultant and former R.H. Macy & Co. vice chairman.

According to the Proskauer report, Mr. Bolduc about three years ago told the senior Mr. Grace the company shouldn't pay for the nurses any longer, and Mr. Grace agreed. Nevertheless, Mr. Grace continued to submit the nursing bills and they were paid. For each of the past five years, the company has paid about $165,000 for full-time and part-time nurses used by Mr. Grace, the report said.

The nurses' payments weren't reported in questionnaires prepared by Mr. Grace as a company director and submitted to company financial officers.

Judge Tyler's report concluded that payments for a $2.1 million New York apartment, which requires about $74,500 annually to maintain, and a $30,000-a-year cook also should be disclosed. The apartment, his report notes, hasn't generally been available to other executives. The Proskauer document indicates that in October 1986, Mr. Grace's wife listed herself, her husband and their then-24-year-old son as the people using the apartment. The apartment, in the River House, bars corporate ownership of apartments and requires that its units be used solely for residential purposes, the report noted.

The Proskauer document said the full-time cook prepares meals for the senior Mr. Grace and his secretaries at the apartment and at his office and she cleans the apartment.

Judge Tyler's report urged the company to file a "corrective amendment" to its 1992 annual 10-K disclosure about the previously undisclosed perks, his use of the corporate aircraft and any other possible benefits or arrangements. The law firm noted that "it is, of course, quite possible" such a filing would trigger an SEC inquiry "focusing on the company's position that it properly omitted disclosure of arrangements" with Mr. Grace. The law firm added that "there can, of course, be no guarantee that the staff of the SEC would agree with the company's analysis" and suggested that company officials meet informally with the SEC staff before the documents are filed.

While Mr. Bolduc won the battle over disclosure of these Grace-family relationships to the company, he lost the war. Allegations against him surfaced soon after Mr. Bolduc successfully convinced the board that such disclosure was necessary. Mr. Erhart, the director and former president, said yesterday that some women employees had complained about alleged sexual harassment by Mr. Bolduc. He didn't offer specifics.

Mr. Bolduc won't comment on any of these allegations, his lawyer, Gerald Walpin, said yesterday. "Since he is no longer with the company, he feels it is not appropriate to comment" on company matters, Mr. Walpin said. A person close to Mr. Bolduc contends that the departed CEO never had a chance even to know who the accusers were or what specifically they had alleged; this person describes the allegations as "an attempt to sling mud on him."

Mr. Erhart, who said the accusers didn't want their identities to become public, added in his initial interview yesterday that the board overwhelmingly decided the allegations were significant enough to warrant asking for Mr. Bolduc's resignation. Only Mr. Bolduc and one other director disagreed, Mr. Erhart says.

Mr. Bolduc isn't leaving empty-handed, however. The company said yesterday that he will receive about $20 million in his exit package, including the repurchase for about $12 million of about 270,000 shares of W.R. Grace stock he owned outright. In addition, he will receive $3 million in incentive compensation for 1994 and other long-term compensation, and about $5 million to buy out his multiyear contract.

—Richard Gibson contributed to this article.