COMPANY: MARSH & MCLENNAN (MARSH, INC.,

PUTNAM FUNDS, AND MERCER CONSULTING)

INDUSTRY: INSURANCE (MARSH, INC.), MUTUAL FUNDS

(PUTNAM FUNDS), AND CONSULTING (MERCER)

SITUATION

Starting in late 2003, Marsh & McLennan (MMC), with a reputation as one

of the most staid and well-managed companies in the United States, became

embroiled in a series of ethical scandals. The first involved Putnam Funds, a

mutual fund company in Boston and traditionally the cash cow of MMC.

Putnam first lost huge bets on technology and growth stocks when the stock

market imploded in 2000. Then it was the first mutual fund company named

in the market-timing scandal that involved mutual fund companies across

the industry. (Market timing is shifting money in and out of mutual funds

based on the performance of one or more market indicators. In the recent

scandal, large investors were allowed to “time the market” by trading late—

after the markets had closed—which provided a clear advantage for the big

guys and a clear disadvantage for the little guys.) There is no doubt that of

all the mutual fund companies, Putnam took the biggest hit for the scandal,

and it continues to struggle to make its way back. Its assets under

management—the major measure of stability and heft in the industry—

fell from $370 billion in late 2000 to $194 billion during the first quarter of

2005.25 But Putnam was only the beginning of trouble at MMC.

In October 2004, New York State Attorney General Eliot Spitzer filed a

civil complaint against MMC, the parent company of Marsh, Inc., the world’s

largest insurance broker. In the suit, Spitzer charged that Marsh betrayed

clients by steering business to underwriters with whom it had cozy relationships

in exchange for millions in backdoor payoffs. As one Marsh executive

said, “We need to place our business in 2004 with those that have superior

financials, broad coverage, and pay us the most.” Spitzer’s complaint uncovered

a broad mosaic of industry-wide bid rigging for which Marsh served as

the chief architect. Other companies such as AIG, Hartford, and ACE were

involved, but Marsh was the big player in the arrangement.26 (At the time of

Spitzer’s suit, Jeffrey Greenberg was CEO of MMC; his brother, Evan

Greenberg, was CEO of ACE; and the legendary Maurice “Hank” Greenberg,

father of Jeffrey and Evan, was CEO of AIG and would later face enormous

troubles of his own.)

HOW THE COMPANY HANDLED IT

To stanch the bleeding at Putnam, MMC forced out Putnam’s CEO, the

imperious Lawrence Lasser, who took a $78 million severance payout and

left the company that he had captained for years.27 MMC quickly hired

squeaky-clean Charles “Ed” Haldeman as the new CEO to lead Putnam out

of the swamp. In April 2004, Putnam settled with the SEC and agreed to

accept new employee trading restrictions and to conduct and provide regular

compliance reviews. The company also paid $110 million in various fines.

(There were additional charges, settlements, and fines from a variety of

sources, including the Commonwealth of Massachusetts.)28 Haldeman

brought in a new management team and made other changes, but the

company continues to struggle to regain its former position as a leader

in the industry.

Its parent, MMC, had a more difficult time with its woes. In a highly

unusual move, Spitzer refused to negotiate with the company as long as its

executive team was in place. Soon after, CEO Jeffrey Greenberg and the top

company lawyer resigned and Michael Cherkasky took the helm. Cherkasky

was Spitzer’s former boss in Manhattan’s district attorney’s office and the

CEO of Kroll, Inc., a leading risk consulting company acquired by MMC

shortly before its legal woes began. Cherkasky’s relationship with Spitzer

proved very helpful forMMC—the company quickly agreed to a settlement of

$850 million and also agreed to lead the insurance industry in reforming

industry practices

A note: Mercer HR Consulting, the other third of the MMC business, also

had its own troubles. It disgorged more than $440,000 in fees from the New

York Stock Exchange (NYSE) after admitting that it misled the NYSE board

of directors regarding the $140 million pay package of Richard Grasso, then

CEO of the NYSE

RESULTS

In 2004, MMC’s stock price fell from a 52-week high of $47.35 to a low of

$22.75—an incredible fall fromgrace for a company that had performed so well

and so predictably for decades.31 In a mere four days of trading, the company

lost $11.5 billion in market value.32 That plunge hurt MMC employees more

than most investors because, until shortly before these problems,MMCemployees

could invest theirMMCretirement savings only inMMCstock. The thinking

among MMC senior executives was that people would be more motivated to

produce excellent results if their entire retirement savings were tied up inMMC

stock. In a real ethical lapse, senior executives had other investment options—it

was only rank-and-file employees who were restricted to MMC stock. MMC’s

strategy was particularly unfathomable when you consider thatMMC’s Mercer

HR Consulting employed numerous retirement experts who routinely advised

their clients about the importance of providing employees with diversified

options for retirement investments. After years of listening to employees plead

to be allowed to diversify and afterwatching Enron’s employees lose their shirts

when their company’s stock plunged, MMC executives finally allowed for

limited diversification. Beginning in 2003, MMC employees could diversify

part of their retirement investments into a few Putnam funds—nowhere near the

number or range of options provided by other large corporations to their

employees. Many MMC employees who did not move quickly enough to

diversify lost much of their retirement investments after MMC stock plummeted.

Note to students—diversify your investments, and never put all your

investments in company stock! (Also, in the interest of full disclosure, please

note that one of this book’s authors, Katherine Nelson, was employed as a

principal at Mercer HR Consulting from 1998 to 2001 and was an “employee

investor” of MMC.)

In addition to the substantial settlements, the financial losses, the pessimism

of financial analysts, and the enormous hit taken by MMC investors and

employees, 5,000 jobs were lost and the company’s reputation remained

damaged for a number of years.

COMMENTS

One of the wisest comments about the crisis at MMC comes from the former

CEO of Putnam Funds, Charles Haldeman, who said, “What our parents told

The results of these very public conflicts of interest will be felt for years. Various

regulators and attorneys general from a number of states are still investigating the

banks and their business practices. As a result of the various debacles in the banking

industry, Citigroup has been fined more than $5.5 billion since 2003, and JPMorgan

Chase has been fined more than $4 billion.38 Other financial institutions have also been

fined sums totaling in the billions, and numerous corporate brands have been muddied.

However, all of that “justice” has not yet restored the faith of the public in the markets,

nor will it help the hundreds of thousands of individual investors who have lost their

shirts because of these shenanigans. In a 2002 Business Week poll of its readers,

93 percent said they had “only some” or “hardly any” trust in the executives who run

big companies, and 95 percent felt that way about big auditing companies.39 More

recently, a 2010 survey indicated that 70 percent of the public believes that businesses

and financial companies will go back to “business as usual” after the 2008–09

recession.40 In the same survey, only 29 percent of respondents in the United States

thought that they could trust banks “to do the right thing.” That’s down from 68 percent

in 2007.41 In a 2012 survey, Wall Street and Congress were in a dead heat as the least

trusted institutions in the U.S., and public confidence in them could be measured in

single digits.42 It is a sad commentary.

us about protecting our reputation is true. If you lose it, it’s hard to win it back

again.” Haldeman also talked about the isolation that existed in Putnam before

his arrival. Apparently, Putnam had a history of not cultivating relationships

with the press or the government, and when the scandal broke, it had no friends

to turn to. Haldeman also vowed to change that. “At the time of our problems,”

he said, “We didn’t have those relationships and it was difficult for us. At a

time of need we didn’t have too many friends or supporters. We don’t want to

be in that position again.”34 Haldeman served as CEO of Putnamfrom the time

the crisis broke in 2004 until 2008, when MMC sold Putnam to Power

Corporation and replaced Haldeman.35

The scandal that rocked MMC was an example of how former New York

State Attorney General Eliot Spitzer liked to turn an industry upside down.

Writer Peter Elkind wrote of Spitzer’s strategy in Fortune magazine: “The

strategy has been remarkably consistent. Step one: Wade broadly into a gray

area of odorous but long-accepted industry practices. Step two: Seize on

evidence of black-and-white outrageous conduct—typically in email form—

and use it to marshal public outrage. Step three: In the resulting tsunami of

scandal, swiftly exact reform of the whole industry, including gray-area

behavior.” Within two weeks of filing charges, Marsh and its largest competitors

had agreed to stop bid rigging. Similarly, industry-wide mutual fund

abuses stopped within weeks of Spitzer filing charges against Putnam.36

Please note that Eliot Spitzer has had his own ethical lapses. A little over a year

after being elected governor of New York State, he was caught up in a federal

wiretap of a prostitution ring (he was found to be a client) and resigned in

disgrace in early 2008.