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Take the Money and Run

ON SEPTEMBER 29, 2003, John Hancock and Manulife held a conference call to discuss Manulife's $10-billion stock acquisition of Hancock. David D'Alessandro, Hancock's devious, overpaid Chairman and CEO, touted the benefits of the deal and said that he wasn't planning to leave after the merger was completed, even though he would become the number two man. "We're very excited about the future of this company," he said of the proposed corporate unification, "and the kind of money we can make—frankly—running such a large organization." If D'Alessandro was excited about the kind of money he *could* make in the future, he must have been ecstatic about the amount of money he *had* made in the previous four years.

The following day D'Alessandro told Hancock's employees what a great job he'd done running the company: $6.5 billion of value had been created for shareholders since the IPO in January 2000.

This was sheer fantasy. In fact, Hancock's demutualization and concurrent IPO had *deprived* policyholders of about $2.5 billion and paved the way for D'Alessandro—who is cozy with Hancock's directors—to finagle about $100 million in compensation from the company. (To read about this in detail, see the following issues of *Schiff's*: December 1999; May 20, 2003; July 18, 2003; October 23, 2003; October 27, 2003; November 7, 2003.)

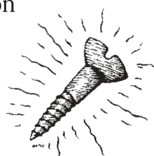
Hancock and Manulife completed their merger on April 28, 2004. On May 24, Hancock put out a grim press release summarizing a national survey it had commissioned. "Americans are increasingly pessimistic about their retirement prospects, with dreams of early retirement all but gone," the press release began. According to the survey, the average age at which people expected to retire had risen to 64.4 years, and eighteen percent of respondents said they didn't expect to be able to retire until they were seventy. Even worse, "nearly seventy percent of respondents are either somewhat or very concerned that they will not have enough money to live comfortably in retirement," the press release stated.

Of course, not all Americans are in such hard shape. On June 10, Manulife announced that David D'Alessandro, 53, "decided to retire" as CEO of Manulife effective November 30.

According to Hancock's 2003 proxy statement, when D'Alessandro turns sixty-five he will receive a $1,257,081 annual pension.

Sell Too Low, Buy Higher

ON JUNE 23, MERCER Insurance Group, whose stock was trading at about $12, announced that its board had authorized the repurchase of 250,000 shares, which would be held as treasury shares available for issuance in connection with Mercer's "stock incentive plan." Since the company's tangible book value is almost $14 per share, a repurchase doesn't seem like a bad idea.



The bad idea was going public in the first place. In December, Mercer *Mutual* completed a subscription-rights demutualization (an abusive transaction permitted in Pennsylvania), issuing stock at $10 per share. The net proceeds to Mercer were $8.46 per share.

The IPO was a great deal—for Mercer's directors, officers, and employees, who were given the right to buy five percent of the offering at the super-cheap offering price. In addition, a company ESOP got ten percent of the shares, *paying for them with money borrowed from Mercer*.

Mercer has a history of trying to get the better of its policyholders. When it attempted to demutualize in 1999, it didn't tell policyholders about an offer for the company made by Franklin Mutual in which all of Mercer's policyholders would have received money. (Policyholders get nothing in a subscription rights demutualization.) Franklin's president, George H. Guptill, Jr., waged an expensive proxy fight to defeat Mercer's demutualization, and succeeded—an historic result.

Although Mercer couldn't sucker enough policyholders to vote in favor of its plan the first time around, it was able to do so four years later.

'Workman's Comp Madness'

CHARLIE MUNGER, the persnickety vice-chairman of Berkshire Hathaway, has developed a cult following among value investors. Unlike his partner, Warren Buffett, he hasn't cultivated a folksy, genial persona; he doesn't speak with a gentle wit or punctuate his stories with quotes from Yogi Berra or Mae West. Instead, he's famously straight-talking and cranky.

In the foreword to *Damn Right!* (a biography of Munger by Janet Lowe), Buffett refers to his friend and partner's renowned bluntness: "Miss Manners clearly would

need to do a lot of work on Charlie before she could grant him a diploma."

Last October, Munger delivered an eighty-five minute speech to the economics department at the University of California, Santa Barbara. Notwithstanding its off-putting title, "Academic Economics: Strengths and Faults After Considering Interdisciplinary Needs," the speech was easy to understand. It has been transcribed by writer-investor Whitney Tilson, and posted on his website. (Go to www.t2partnersllc.com. Click on "Public Site." Under "Most Recent Articles" go to "6/4/04 – *Munger Goes Mental*." The article contains a link to the speech.)

In his speech, Munger shares his knowledge, pontificates on a wide range of subjects—the bulk of which come under the heading "What's Wrong with Economics?"—and, as he is wont to do, skewers those he deems to be fools; for example:

> When I talk about this false precision—this great hope for reliable, precise formulas—I am reminded of [the economist] Arthur Laffer, who's in my political party [Republican], and who is one of the all-time horses' asses when it comes to doing economics. His trouble is his craving for false precision, which is not an adult way of dealing with his subject matter.
>
> The situation of people like Laffer reminds me of a rustic legislator—and this really happened in America. I don't invent these stories. Reality is always more ridiculous than what I'm going to tell you. At any rate, this rustic legislator proposed a new law in his state. He wanted to pass a law rounding Pi to an even 3.2 so it would be easier for the school children to make the computations. Well, you can say that this is too ridiculous, and it can't be fair to liken economics professors like Laffer to a rustic legislator like this. I say I'm under-criticizing the professors. At least when this rustic legislature rounded Pi to an even number, the error was relatively small.

Munger's story about Pi isn't completely accurate. In 1897, the Indiana House of Representatives passed Bill No. 246, which had been drafted by a wacky mathematician and submitted by his Representative, Taylor I. Record, as a courtesy. The stated purpose of the bill was to present "a new mathematical truth" that was offered to the state of Indiana "free of...any royalties." The bill's text is 443 words of mathematical mumbo jumbo about squaring the circle, and the words "Pi" and "3.2" are never mentioned. The calculations in the text, however, effectively set Pi at 3.2. The bill was postponed indefinitely when it got to the State Senate.

Later in the speech Munger gets onto the topic of "workman's comp madness," and discusses how people take advantage of the system. "All human systems are gamed, for reasons rooted deeply in psychology, and great skill is displayed in the gaming because game theory has so much potential," he says. "That's what's wrong with the workman's comp system in California. Gaming has been raised to an art form. In the course of gaming the system, people learn to be crooked."

Oddly, rather than express contempt for the crooks, Munger faults "the people who *design* easily-gameable systems," saying that they "belong in the lowest circle of hell."

Munger tells a story to illustrate his point. "I've got a friend whose family controls about eight percent of the truck-trailer market," he says. "He just closed his last factory in California and he had one in Texas that was even worse. The workman's comp cost in his Texas plant got to be about thirty percent of payroll. Well, there's [not much] profit in making truck trailers. He closed his plant and moved it to Ogden, Utah, where a bunch of believing Mormons are raising big families and don't game the workman's comp system. The workman's comp expense is two percent of payroll."

To anyone in the insurance business, this reduction in comp costs must seem remarkable—almost incredible. Munger discusses why the company's workers' comp varies so much from Texas to Utah. "Are the Latinos who were peopling his plant in Texas intrinsically dishonest or bad compared to the Mormons?" he asks rhetorically. "No. It's just the incentive structure that so rewards all this fraud is put in place by these ignorant legislatures, many members of which have been to law school, and they just don't think about what terrible things they're doing to the civilization because they don't take into account the second order effects and the third order effects in lying and cheating."

We were skeptical that any company could reduce its workers' comp costs from thirty percent of payroll to two percent by moving from one state to another, and mentioned this to our "foreign correspondent" Isaac Schwartz (who recently completed his junior year at Wharton), who had also read Munger's speech.

The scholarly Schwartz, intrigued, called Munger, who, it turns out, answered his own phone and chatted with Schwartz for several minutes. Unfortunately, when Schwartz asked him for the name of the truck-trailer company that had reduced its comp costs, Munger said he couldn't recall it. He did say, however, that it was run by one of his friends. When Schwartz asked for the friend's name, Munger said he couldn't remember that, either—the friend is just an occasional golf buddy.

Armed with this information, Schwartz, who's as dogged as Phillip Marlowe, went looking for some answers. There aren't many large manufacturers of truck trailers, and with a little digging, Schwartz soon deduced that the company Munger was referring to is Utility Trailer Manufacturing. Its headquarters are in City of Industry, California (greater Los Angeles), and it has a large manufacturing facility near Ogden, Utah.

Schwartz called Utility Trailer and queried spokesman John Stanton about how the company had reduced its workers comp costs from thirty percent to two percent. "That information is totally incorrect," Stanton replied. "First of all, we've always had a plant in Utah. When the Texas plant closed, we'd had a plant in Utah for twenty years..."

Oh well. So what if Munger's story doesn't quite check out. He's worth billions and we're not. Besides, at the end of his speech, Munger avows, "My inspiration again is Keynes: Better roughly right than precisely wrong."

Damn right!

Progress?

IN 1957 CONNECTICUT GENERAL moved from downtown Hartford to Bloomfield, six miles away. Its new headquarters, set on a 650-acre "campus" with sculpture gardens and reflecting pools, was designed in the International Style by Gordon Bunshaft (who also designed Lever House). The building was immediately recognized as a masterpiece of Modernist architecture, and the American Institute of Architects called it one of "ten build-

ings in America's future." In 1962 Bunshaft designed the widely admired Emhart building on an adjoining site. (The building was subsequently bought by Connecticut General.)

In the ensuing decades many companies moved from downtown office towers to pastoral suburban settings. In 1982 Connecticut General merged with INA, changed its name to CIGNA, and moved its headquarters to Philadelphia.

By the late 1990s, CIGNA considered the Bunshaft buildings to be obsolete, and plans were made to replace them with a golf course, residences, stores, offices, and a hotel and conference center. The National Trust for Historic Preservation called the CIGNA Campus one of the "11 Most Endangered Places" in 2001.

The Emhart Building was razed last summer, and the original "Wilde" building, named after Frazar B. Wilde, Connecticut General's president in 1957, may await a similar fate.

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Letters to the Editor

WE OFTEN GET CALLS, letters, and emails from readers who ask that we not quote them by name. Generally, these people don't want to be identified because the price of going public with the truth is not worth the consequences—losing their jobs.

Here at *Schiff's*, we're always delighted to receive (and publish) documents that deserve to see the light of day, and to provide a forum for spirited opinion.

Our June 16 issue, "Insurance Regulator Sucks up to Big Insurers," prompted a number of responses from readers. The article discussed how, in 2000, Joseph Belth, editor of *The Insurance Forum*, went to court to compel the New York State Insurance Department to obey the law and provide him with salary information from the Schedule G supplement to annual statements that insurance companies file with the department. Although the Schedule G had been public for ninety-four years, the insurance department quickly decided to keep it secret after it had been requested to do so by Equitable and Prudential.

Our article also discussed our Freedom of Information Law (FOIL) request for the complete Schedule G's for several life-insurance companies, and how the department refused to provide us with the information, censoring all salary data below $600,000.

The following was sent in by one reader:

> I am appalled that the New York State Insurance Department is willfully failing to comply with both the letter and the spirit of the statute on disclosure. If we had not had the wave of corporate governance failings recently, I would be sympathetic with the Insurance Commissioner's position. However, the many examples of corporate malfeasance and board misfeasance lead me to be convinced that oversight is needed. *In this situation you are not asking for more regulation, but simply adherence to a statute already on the books.*
>
> By the way, you may be barking up the wrong tree in your search to find out whether there was/is any nepotism between directors and their companies. I am willing to bet that if you ever get this information, you will find relatives of regulators on insurance company payrolls. Many years ago we bought an insurance company in [name of state withheld]. We were pressured to hire relatives of politicians. Some were actually good employees, but the pressure was wrong either way.

Joseph Belth, who has fought numerous battles to obtain "public" documents, also wrote to us:

> I read with keen interest your excellent June 16 article. You quoted extensively from Judge Figueroa's 2001 decision in my lawsuit against the New York State Insurance Department relating to disclosure (or nondisclosure) of executive compensation data.
>
> In the material you quoted, the judge said that "Belth was also publishing this information on the Internet." That is incorrect. I have never published—and I do not intend to publish—that data on the Internet. What prompted Equitable and Prudential to ask the Department to refrain from disclosing names in the compensation exhibits was publication of the data for a few large companies on a website operated by an association of current and former Equitable agents.

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