ANNUAL REPORT **2006**

MMC

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**MMC** is a global professional services firm with annual revenues of approximately $12 billion. It is the parent company of Marsh, the world's leading risk and insurance services firm; Guy Carpenter, the world's leading risk and reinsurance specialist; Kroll, the world's leading risk consulting company; Mercer, a major global provider of human resource and specialty consulting services; and Putnam Investments, one of the largest investment management companies in the United States. More than 55,000 employees provide analysis, advice, and transactional capabilities to clients in over 100 countries.

This annual report contains "forward-looking statements," as defined in the Private Securities Litigation Reform Act of 1995. Please see "Information Concerning Forward-Looking Statements" on page 101 of this annual report.

As a result of strong operating cash flows, successful restructuring actions, and strategic dispositions, total net debt at the end of 2006 was $2.9 billion, a reduction of $640 million from the end of 2005. We also raised MMC's quarterly cash dividend 12 percent to $.19 per share payable in the first quarter. One of MMC's historic strengths has been its financial flexibility, which has given the company the ability to grow. We dramatically improved our financial position in 2006. MMC has enormous opportunities for investment in its businesses, and we are poised for meaningful growth in 2007.

## ONGOING TRANSFORMATION

To foster growth, reinforce our focus on excellence, and improve our governance structure, we must be willing to embrace change. Our actions in 2006 indicate that we are successfully doing so.

Putnam has been an important contributor to MMC's success over the last three decades, but we have decided to focus on growing our risk and human capital businesses to achieve superior long-term shareholder return. In January, Great-West Lifeco, a subsidiary of Montreal-based Power Financial Corporation, agreed to purchase Putnam for $3.9 billion in cash. We expect this transaction to close in the middle of 2007, subject to certain customary conditions.

In September, we named Matt Bartley chief financial officer of MMC. Matt had been our treasurer for the prior five years. He has an intimate knowledge of the financial dynamics of MMC's operating companies and will be an integral part of MMC's growth.

In May, we were pleased to welcome Steve Hardis as non-executive chairman of MMC's Board of Directors. Steve has been a member of the Board since 1998. He is an effective leader and valuable partner. Under Steve's leadership, the Board has continued its ongoing review of MMC's corporate governance practices and implemented a number of significant changes. Among other things, the Board implemented stock ownership requirements for directors and executive officers, and adopted a bylaw providing for majority voting in uncontested director elections. These changes are the latest in a series of governance enhancements we have made in the last two years.

## GROWTH: PRIORITY ONE

MMC is in the right markets at the right time. Risk and human capital issues are dominating today's headlines and corporate agendas. There are hazard risks including fire, flood, and earthquake; financial risks such as currency volatility, interest rate swings, and loan defaults; operational risks such as technology failures and supply chain interruption; strategic risks associated with technological advances, formidable competition, and major shifts in the perception of established brands; and human capital risks such as competition for talent, increasing pension liabilities, and rapidly rising healthcare costs. These risks are front page in our newspapers and front-of-mind for our clients. As a result, the demand for comprehensive risk solutions is growing rapidly.

Our companies help clients identify, plan for and respond to today's critical issues and risks. Marsh, Guy Carpenter, Kroll, Mercer Human Resource Consulting, and Mercer Specialty

Consulting are market leaders with exceptional people and distinguished global clients. In short, we have the global platform and depth of talent and expertise to help clients turn critical issues and risks into competitive advantages.

Each of our operating companies has specific strategic plans and targets in place, yet across many of our businesses there are common themes: continued operational improvements; training and professional development for our colleagues; aggressive recruiting; accelerated investment in high-potential markets such as Asia; expanded presence in European and other more established markets; advancement of our leadership position in the U.S. middle market; product innovation; and diversification of product and service offerings. Our operating company leaders offer more insights about their plans in the pages that follow.

To achieve our goals, our companies will focus on core competencies in risk and human capital. They will continue to refine their business models and pursue collaborative opportunities across the MMC spectrum to deliver integrated advice and solutions. The needs of our clients are our responsibility and also represent an opportunity to grow MMC.

## LOOKING AHEAD

We have so many ways to win as a company. Our colleagues are innovators and entrepreneurs who have the ideas, ingenuity, drive, and experience to fuel our growth. They act with integrity, resolve, and a sense of urgency in serving our clients. We have a clear operational and strategic imperative—use our superior brands and distribution to drive the growth of our businesses, and to do so efficiently.

MMC made significant progress in 2006, but we can—and will—do better. We view 2007 as a year of opportunity, a year of innovation and imagination. It is a year for decisive action. We will continue to move forward aggressively to improve our results in 2007 and beyond. We expect to achieve higher revenues, operating income, and margins. Over the next three years, our companies will work together to leverage our market-leading positions to deliver exceptional value to our clients, shareholders, and colleagues alike.

For 135 years, MMC has built a reputation for excellence and is now the world's leading global advice and solutions firm. This is just the beginning of our turnaround. Our management team is energized, optimistic, and focused. We are committed to bringing MMC back to its former glory—and more.

Sincerely,

Michael G. Cherkasky
*President and Chief Executive Officer*

February 28, 2007

# *Risk and Insurance Services*

## MARSH

***Brian M. Storms**, chairman and chief executive officer*

*Brian Storms assumed his position at Marsh in September 2005, after a period at the helm of Mercer Human Resource Consulting. Prior to joining MMC, Brian spent more than 25 years in a range of international management roles in the financial services industry.*

*What is your vision for Marsh?*

We will complement our capabilities as the world's leading broker by leading the industry as the preeminent broker and risk advisor, helping our clients turn risk into a competitive advantage. The market opportunity goes well beyond insurance. Our clients have asked us to play a bigger role across the full spectrum of the risk lifecycle, helping them navigate the increasingly fluid, complex global risk landscape. While insurance brokerage is and always will be at the core of what we do, we are expanding our horizons to capture the enormous growth potential in the accelerating market for broader risk advisory services. We intend to be a leader in both.

*How is Marsh being transformed?*

We are repositioning every aspect of our business, executing against two primary strategic imperatives: 1) build a world-class, globally integrated operating platform; and 2) drive profitable growth by creating a differentiated approach to risk management and by investing in priority growth areas.

Operationally, we are retooling for maximum efficiency and growth across three dimensions: distribution, product, and infrastructure.

Distribution—how Marsh acquires, services, and retains clients—is a critical focus, and we are rewiring our go-to-market approach to deliver a seamless, responsive, and consistently high quality client experience. Our clients are clear about their expectations. They want our best knowledge and capabilities regardless of where they access us; they want us to leverage our size and global reach to assert our placement strength on their behalf, with complete transparency; they want us to deliver sophisticated advisory capabilities; and they want us to provide innovative solutions to their evolving risk needs. With greatly enhanced tools, training, and discipline, we believe that our global distribution platform will enable us to meet and exceed our clients' high expectations.

In the product area, we are exploiting our unrivaled intellectual capital and re-energizing our legacy of innovation. This includes global integration of our risk practices and specialties, significant investment and expansion in our industry expertise, and an expanding pipeline of unique new product innovations.

reinsurer start-ups, and non-traditional forms of capacity such as catastrophe bond issuance. The active hurricane season predicted for 2006 did not occur, so 2006 should be a very profitable year for reinsurers.

Total global reinsurance premium is about $150 billion, of which Guy Carpenter places approximately 10 percent. The reinsurance markets accept business on a direct basis and through intermediaries. Brokers are capturing an increasing share of the market as both buyers and reinsurers recognize the value brokers bring to the reinsurance transaction. Guy Carpenter is ideally suited to deliver significant value to clients in a fast changing market that requires a highly technical, global approach. Our 2006 revenues grew 5 percent on an underlying basis to $880 million, driven by double-digit growth in new business. We were pleased that strong new business production levels continued through the January 2007 renewal season.

*How does Guy Carpenter differentiate itself?*

We have a full service model. We deliver sophisticated analytics, specialty-line expertise, and customized reinsurance solutions to achieve optimum terms and conditions for clients. We have a unique and strong global platform, with 2,600 colleagues conducting business in over 80 countries around the world. That platform enables us to leverage our global network for clients through effective sharing of knowledge and expertise.

Our portfolio is diversified, with about 40 percent in property catastrophe lines,

# Risk Consulting and Technology

## KROLL

***Simon Freakley,*** *president and chief executive officer*

*Simon Freakley assumed his current position at Kroll in 2004. Prior to the company's acquisition by MMC in 2004, he led Kroll's Restructuring and Consulting Groups. Simon is one of the industry's leading experts in business turnaround and recovery strategies.*

*What is Kroll's business?*

Kroll is the world's leading risk mitigation company. We provide advice and solutions to help clients solve problems and capitalize on opportunities. Historically, Kroll has been well known for its work in due diligence consulting. Today, we are much more than that. Through strategic acquisitions beginning in the late 1990s, Kroll has transformed its business from a concentration in consulting to a platform that is now evenly divided between consulting and technology-enabled solutions.

Some of our most high profile consulting work is in independent monitorships and corporate restructurings. This area also includes our more traditional services such as business intelligence and investigations, financial advisory, corporate preparedness, and security. On the technology side, we have leading businesses in electronic discovery, data recovery, and background screening—all growing markets. Mortgage credit screening and substance abuse testing complete our portfolio of scalable, technology-based businesses, all of which have recurring revenues and contribute to our balance of cyclical and counter-cyclical businesses.

*How did Kroll perform in 2006?*

We had revenues of $979 million, an increase of 12 percent from 2005, or 9 percent on an underlying basis. Consulting revenues increased 13 percent, while revenues from technology-enabled solutions rose 12 percent. The operating margin was 15 percent, including amortization expense.

Toward the end of the year, we sold our international high-risk asset and personnel protection division as part of a strategy to focus on higher-margin security segments such as consulting, training, and homeland security solutions.

*What will drive your growth?*

We are very optimistic about our prospects because powerful market drivers play directly to our core competencies. For example, increasing globalization and foreign direct investment drive growth in our due diligence and restructuring businesses, the latter helping corporations to restructure these investments when they encounter problems. As the leading transatlantic restructuring business, Kroll is well positioned to capitalize on the inevitable swing of the pendulum, when default rates return from recent historic lows.

The exponential growth of electronic information plays to our competencies in electronic discovery and data recovery. Globally, more than 93 percent of data is now created electronically and less than 30 percent ever makes it to paper. Any major fraud, litigation, or compliance review becomes enormously difficult for corporations and regulators without access to the kinds of electronic tools and computer forensic expertise Kroll provides. The intensified regulatory environment creates demand for many of our compliance and monitoring services, including court-mandated independent monitorships, anti-money laundering training, and Foreign Corrupt Practices Act programs.

Identity theft is an emerging risk that Kroll is well placed to address. According to a 2005 FBI report, identity theft is one of the dominant white-collar crimes of the 21st century, with about 5 percent of Americans having their identities compromised annually. We have leveraged our expertise in background screening and credit-checking technology to develop an identity theft business from scratch—a great example of how we innovate organically to drive growth in new markets.

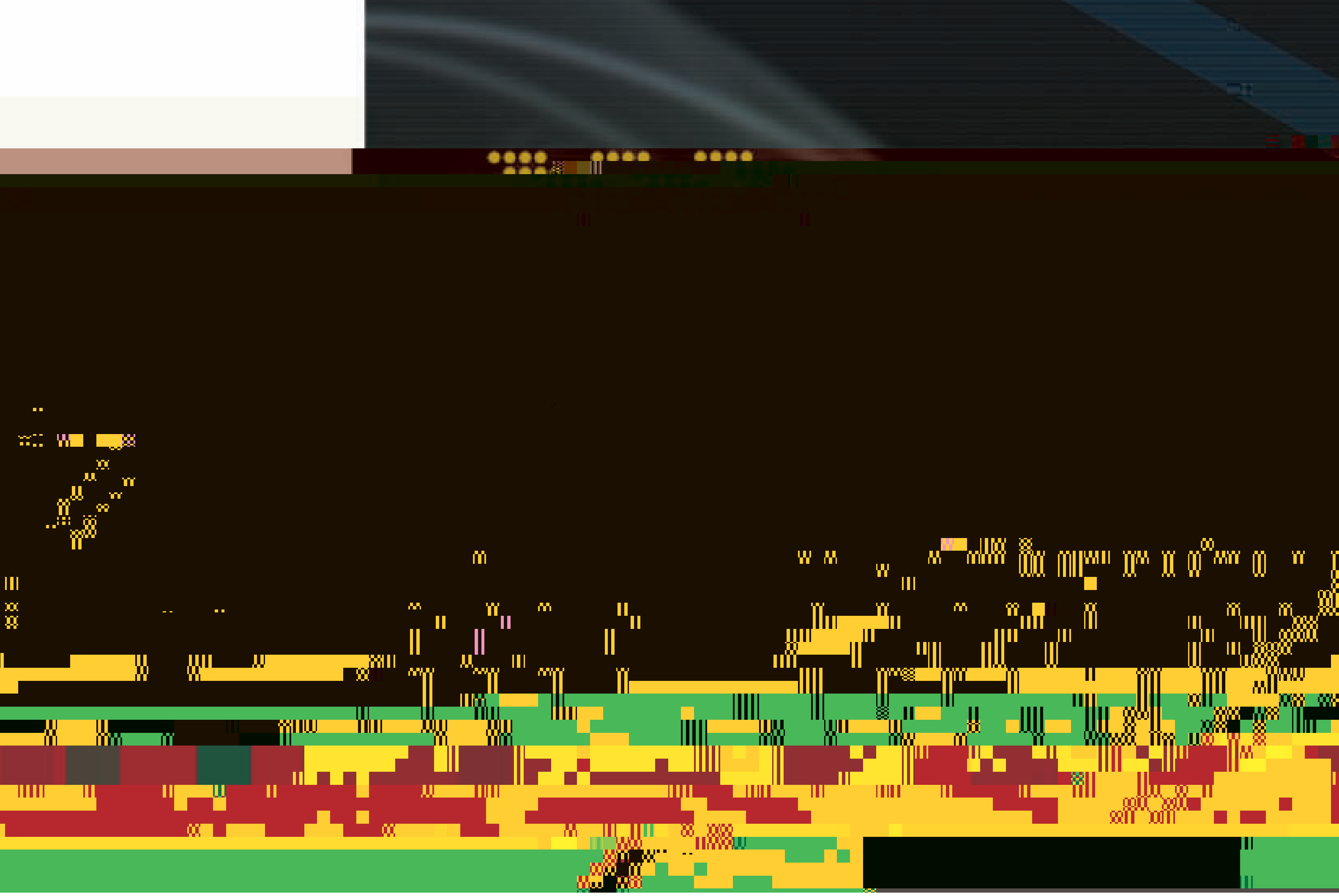
We also see increasing demand among clients for integrated, enterprise-wide solutions to problems. Kroll is uniquely positioned to provide these services, especially in collaboration with its sister companies in MMC. In addition, strategic acquisitions have always played a key role in Kroll's growth, and we expect this to continue in the future. We have been able to successfully leverage the capabilities of the businesses we acquire, thereby driving long-term growth in new and important ways.

We see sustainable competitive advantage in capitalizing on our brand and global reach. Our widely recognized brand gives us access and credibility because people are accustomed to Kroll dealing with difficult situations and complex problems. It also lets us attract and retain the best talent because we are seen as market leaders in much of what we do. Our broad service offerings give us a diverse revenue stream and the ability to capitalize on global opportunities at multiple points in the cycle. For all of these reasons, we are extremely optimistic about Kroll's future. ■

## MERCER HUMAN RESOURCE CONSULTING

***M. Michele Burns,** chairwoman and chief executive officer*

*Michele Burns was named to her position at Mercer Human Resource Consulting in*



*Tell us more about your business model.*

Our role is to provide advice and solutions, depending on our client needs. We are the market leader in retirement and investments. The major trends affecting this market—aging populations, pension reform, and the shift from defined benefit to defined contribution plans—are top-of-mind for companies and the public sector globally. Our capabilities allow us to provide clients with a unique mix of advice and services. For example, we help clients define their worldwide pension strategy as well as evaluate pension costs, risks, and funding requirements. In certain cases, we develop and implement investment strategies for the assets. In some countries we administer these plans on an outsourced basis.

The health and benefits market is being transformed by underlying trends affecting employers worldwide, such as rising healthcare costs, aging of the workforce, privatization of healthcare, and the shift of more responsibility to the individual beneficiary. Our clients look to us for both consulting and services aimed at designing and implementing employee and retiree health and welfare plans that address these issues. Our sales model is powered by Mercer’s intellectual capital and consulting services, delivered in partnership with the Marsh distribution channel.

Talent is an excellent illustration of Mercer’s ability to deliver both advice and solutions across an integrated continuum. We provide consulting services and related content and products that seek to optimize our clients’ performance through their workforce. We have the broadest consulting expertise and product offering in the marketplace. For instance, in addition to value-added consulting in areas such as executive remuneration, workforce strategies, and HR effectiveness, we provide

in-depth analysis as well as web-based software solutions. These services are complementary across our businesses, giving us the opportunity to grow and extend our relationships.

In outsourcing, we follow a total benefits outsourcing model, meaning that we can provide solutions to clients for defined benefit, defined contribution, and health and benefit plans individually or on a bundled basis.

*What were Mercer HR's financial results?*

Our businesses performed well in 2006. Increased demand for services resulted in revenues growing 8 percent, or 7 percent on an underlying basis, to over $3 billion. The retirement and investments businesses represent 39 percent of revenues; health and benefits, 24 percent; outsourcing, 22 percent; and talent, 15 percent. Retirement and investments and talent performed particularly well. We are optimistic about growth and profitability in 2007.

*How will Mercer HR continue to grow?*

We offer a complete array of the capabilities that a client might need and that CEOs, CFOs, and HR executives care about as they try to ensure the competitiveness of their companies. We believe we are the premier provider in the areas we serve, and we expect to retain our standing as the preeminent firm for HR consulting and services. We operate in large and growing markets that provide us with the platform to achieve organic revenue growth, with improving profitability. In the near term, we are working to deploy services and capabilities more effectively.

In retirement and investments, we are standardizing processes in actuarial services, using technology-based solutions in retirement service centers located in lower-cost markets domestically and abroad. In addition, we are packaging solutions to help clients in the transition from defined benefit to defined contribution plans. Multiple

MMC entered the specialty consulting space in 1983 through the acquisition of NERA. Subsequent growth has been through a combination of organic development and targeted acquisitions. Currently, Mercer Specialty Consulting represents about 30 percent of MMC's overall consulting segment revenues. Our business is well diversified by both industry and geography, with about 60 percent of our activities in North America and 40 percent in Europe and Asia.

*Please describe your financial performance.*

We have more than doubled our revenues in the last four years and generated revenues of $1.2 billion in 2006. This represents an increase of 19 percent over the prior year, or 16 percent on an underlying basis. Each of our five units had double-digit growth in 2006, and our business expanded in all major geographies.

*What is your group's place in the market?*

The global consulting market is estimated at $200 billion, and the segments our companies address are about one-quarter of that amount. We rank in the top tier of consulting firms serving these markets and have been the fastest growing firm among our major competitors. We are the only publicly held firm in the elite tier and benefit from having MMC's capital resources behind us.

We are deeply committed to specialization in our practices, believing it is critical to our future success. Clients increasingly demand tangible results from consultants, and we can have a more significant impact than our competition because we have deeper insights into the industries and functions we serve. Our advantage is that we have formed our consulting group by pooling enterprises that already had strong specializations, rather than trying to convert a firm with a generalist tradition into a specialist firm.

*How do you attract top talent?*

Growing competition for talent is one of our biggest challenges, and we must continuously revise and improve our value proposition for professionals. Our advantage is that we offer a faster career growth track for high achieving professionals than our competition. Our people are entrepreneurial, with the energy and knowledge to enter new markets successfully. We must also maintain our content edge by investing in the development of our intellectual capital. Our clients have increasingly sophisticated strategic planning, marketing, risk management, and financial capabilities, and we must bring them something that goes beyond what they can already do internally. The quality of our people and our commitment to their development make that possible.

*What are the opportunities?*

All of our businesses have the opportunity to expand organically into new geographic markets. Additionally, greater collaboration across our units, and with other MMC companies, will enable us to blend our expertise and develop new propositions for clients. We also plan to grow through targeted consulting acquisitions that expand our business into new market segments and capabilities. Finally, there is an opportunity to evolve our business model through acquisitions from a pure advice model to an advice-plus-solutions business.

*What is the outlook?*

We expect to grow revenues to $2 billion by 2010 and increase margins by implementing a more unified operating platform across our businesses. We have demonstrated that we can grow consistently and profitably and can successfully enter new markets, organically and through acquisitions. In short, the future for Mercer Specialty Consulting looks very bright. ■

# *MMC's Management Team*

*From left:* David Spiller, president and chief executive officer, Guy Carpenter; John P. Drzik, president and chief executive officer, Mercer Specialty Consulting; M. Michele Burns, chairwoman and chief executive officer, Mercer Human Resource Consulting; Simon Freakley, president and chief executive officer, Kroll; Brian M. Storms, chairman and chief executive officer, Marsh.
*Not pictured:* Charles E. Haldeman, Jr., president and chief executive officer, Putnam Investments.

*Standing, from left:* Peter J. Beshar

## General

Marsh & McLennan Companies, Inc. and Subsidiaries (“MMC”) is a global professional services firm. MMC’s subsidiaries include Marsh Inc. (“Marsh”), which provides risk and insurance services; Guy Carpenter & Company, LLC (“Guy Carpenter”), which provides reinsurance services; Kroll Inc. (“Kroll”), which provides risk consulting and technology services; Mercer Inc. (“Mercer”), which provides human resource and specialty consulting services; and Putnam Investments (“Putnam”), which provides investment management services. MMC’s approximately 55,000 employees worldwide provide analysis, advice and transactional capabilities to clients in over 100 countries.

MMC operates in four principal business segments based on the services provided. Risk and Insurance Services includes risk management and insurance and reinsurance broking and services, provided primarily by Marsh and Guy Carpenter. Risk Consulting & Technology, conducted through Kroll, includes risk consulting and related investigative, intelligence, financial, security and technology services. Consulting, which comprises the activities of Mercer Human Resource Consulting and Mercer’s Specialty Consulting Businesses, includes human resource consulting and related services, and specialized management and economic consulting services. We conduct Investment Management through Putnam. Please see Note 18 to the consolidated financial statements, which discusses MMC’s agreement to sell Putnam to Great-West Lifeco Inc.

We describe the primary sources of revenue and categories of expense for each segment below, in our discussion of segment financial results. Management evaluates performance based on segment operating income, which reflects expenses directly related to segment operations, but not MMC corporate-level expenses. A reconciliation of segment operating income to total operating income is included in Note 17 to the consolidated financial statements included elsewhere in this report. The accounting policies used for each segment are the same as those used for the consolidated financial statements.

This MD&A contains forward-looking statements as that term is defined in the Private Securities Litigation Reform Act of 1995. See “Information Concerning Forward-Looking Statements” on page 101 of this report.

## Significant Developments in 2006

MMC’s historical financial information should be viewed in light of the significant developments discussed below.

As described more fully below, results of operations in 2006 reflect, among other items:

- stock option expense under SFAS 123(R) (“Share-Based Payment”), which MMC adopted effective July 1, 2005. MMC’s 2006 results include stock option expense in each segment for the full year. The 2005 results reflect a charge for six months (from the date of adoption on July 1, 2005) recorded in corporate expenses;
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### Consolidated Revenues and Expenses

Consolidated revenue for the year ended December 31, 2006 was $11.9 billion, a 3% increase over the prior year. Higher revenue in the consulting and risk consulting & technology segments was partly offset by lower revenue in the risk and insurance services and investment management segments. Consolidated revenue increased 3% on an underlying basis, which includes the impact of a $71 million reduction in market services revenue.

MMC does business in over 100 countries, as a result of which the impact of foreign exchange rate movements may impact period-to-period comparisons of revenue. Similarly, the revenue impact of acquisitions and dispositions may affect period-over-period comparisons of revenue. Underlying revenue measures the change in revenue from one period to another by identifying these impacts. The impact of foreign currency translations, acquisitions and dispositions on MMC's operating revenues by segment is as follows:

| *(In millions, except percentage figures)* | **Twelve Months Ended December 31, 2006** | 2005 | **% Change GAAP Revenue** | **Components of Revenue Change: Currency Impact** | **Acquisitions/ Dispositions Impact** | **Underlying Revenue** |
|---|---|---|---|---|---|---|
| **Risk and Insurance Services** | | | | | | |
| Insurance Services | **$ 4,390** | $ 4,567 | (4)% | — | (2)% | (2)% |
| Reinsurance Services | **880** | 836 | 5% | — | — | 5% |
| Risk Capital Holdings (a) | **193** | 189 | 2% | — | (5)% | 7% |
| Total Risk and Insurance Services | **5,463** | 5,592 | (2)% | — | (2)% | — |
| **Risk Consulting & Technology (b)** | **979** | 872 | 12% | — | 3% | 9% |
| **Consulting** | | | | | | |
| Human Resource Consulting | **3,021** | 2,794 | 8% | 1% | — | 7% |
| Specialty Consulting | **1,204** | 1,008 | 19% | 1% | 2% | 16% |
| Total Consulting | **4,225** | 3,802 | 11% | 1% | 1% | 9% |
| **Investment Management** | **1,385** | 1,506 | (8)% | — | — | (8)% |
| **Total Operating Segments** | **$12,052** | $11,772 | 2% | — | — | 2% |
| **Corporate/Eliminations** | **(131)** | (194) | | | | |
| **Total Revenue** | **$11,921** | $11,578 | 3% | — | — | 3% |

initiatives are expected to be implemented in several phases – Phase 1 began in September 2006, with several additional phases to follow. The discussion below identifies the areas impacted and savings expected from various phases of the 2006 Plan.

Phase 1 of the 2006 Plan is expected to result in cost savings of $160 million. The expected savings from this phase comprise $70 million from operating company process improvements and $90 million from corporate infrastructure and process improvements in IT, real estate and corporate functions. Staff reductions of more than 750 are expected. During 2006, MMC recorded a net charge of $10 million in connection with actions taken under Phase 1 that includes a $74 million gain on the sale of five floors in MMC's headquarters building, more than offset by costs primarily related to severance and exit costs for facilities. Through December 2006, the actions under Phase 1 are expected to result in annualized savings of approximately $110 million beginning in the first quarter of 2007. These actions under Phase 1 are expected to be completed by the second quarter of 2007, except for certain actions related to MMC's headquarters building, discussed below.

As part of its ongoing review of operations, Marsh has identified additional actions that are expected to result in the reduction of 170 positions ("Phase 2"). These actions are expected to increase the expected annualized savings from the 2006 Plan by approximately $40 million and result in additional charges of approximately $40 million related to severance and exit costs for facilities. In the fourth quarter of 2006, MMC incurred costs of $14 million related to this second phase of the 2006 Plan.

MMC currently expects additional annualized savings of $190 million under one or more future phases of the 2006 Plan, resulting from infrastructure improvements in information technology, procurement, human resources, finance and real estate, as well as organizational structure and business process improvements. Detailed plans relating to these future phases are not yet complete, and may impact the amount of expected savings, expected costs or both that will result from these planned actions. Savings from these additional phases are expected to be realized as the actions are implemented through the end of 2008.

As noted above, MMC has been reducing its occupancy at its headquarters building in New York. Phase 1 of the 2006 Plan includes net costs of $8 million and expected annualized savings of approximately $25 million related to these actions. The expected net costs of $8 million comprise both gains on the sale of owned floors and losses on sub-leases of leased floors, which will be recognized at the earlier of when the floors are vacated or when sub-lease agreements are executed. During the fourth quarter of 2006, MMC sold its condominium interest in five floors of its headquarters building, realizing a gain of $74 million. The disposal of these floors is an integral part of MMC's overall restructuring plan and the gain from this disposal has been included as a reduction of other operating sell, are included in discontinued operations in the consolidated statement of income. The prior year's amounts have not been restated because t

Effective October 1, 2004, Marsh eliminated contingent compensation, or market services agreements with insurers, under which it had received revenues based upon such factors as the overall volume, In December 2006, MMC, through its subsidiary Risk Capital Holdings, contributed its limited partnership interest in Trident III, valued at $182 million, to the U.K. Pension Fund. The transaction was recorded at the estimated fair value of MMC's investment on the date of the contribution. Risk Capital Holdings' revenue in 2006 included $38 million of mark-to-market gains for Trident III recognized through the date of the contribution.

At December 31, 2006, the balance of accounts receivable related to accrued market services revenue earned prior to October 1, 2004 was approximately $43 million, compared with $132 million at December 31, 2005. MMC intends to collect the remaining MSA revenue earned prior to October 1, 2004, and is seeking to enforce its rights under the contracts to collect amounts due. However, there is no assurance that MMC will be successful in collecting all amounts due. To the extent such accrued amounts are not collected, a charge to earnings would result. In 2007, MMC collected an additional $23 million of accrued market service revenue.

Revenue in the risk and insurance services segment decreased 10% in 2005 compared with 2004, reflecting decreases in both insurance services and reinsurance services revenue. In insurance services, underlying revenue decreased 13%. Excluding the impact of decreased market services revenue, underlying revenue decreased 6%, reflecting lower new business volume and lower commercial premium rates. The decrease in underlying revenue was most significant in the United States; however, the percentage decline improved in the fourth quarter compared with earlier quarters in 2005 despite continued premium rate declines in the commercial insurance marketplace. Market services revenue declined from $521 million in 2004 to $114 million in 2005.

**Expense**

In 2006, expenses in the risk and insurance services segment decreased 9% compared to the prior year. The decrease reflects cost savings from restructuring; a decrease in restructuring charges from $257 million in 2005 to $100 million in 2006; a decrease of $45 million in settlement, legal and regulatory costs related to market services agreements and associated shareholder and policyholder litigation; and a decrease of $78 million related to employee retention awards. In addition, 2006 expenses reflect lower incentive compensation costs and lower costs related to professional liability claims. Partly offsetting these decreases were costs of $47 million in 2006 related to employee stock options. The operating margin for 2006 improved to 12.4% from 5.5% in 2005.

Expenses in the risk and insurance services segment decreased 14% in 2005, compared wilhe prior

The results of operations for the risk consulting & technology segment are presented below:

| *(In millions of dollars)* | **2006** | 2005 | 2004 |
|---|---|---|---|
| **Revenue** | **$979** | $872 | $371 |
| **Expense** | **830** | 751 | 326 |
| **Operating Income** | **$149** | $121 | $ 45 |
| **Operating Margin** | **15.2%** | 13.9% | 12.1% |

**Revenue**

Risk consulting & technology revenues increased 12% in 2006 compared with 2005, 9% on an underlying basis. The technology services group, Kroll's largest business unit, increased revenues by 12%. This unit's Kroll OnTrack electronic discovery business responded successfully to market conditions and continued its improvement from the first quarter of 2006. The consulting services group reported double-digit growth, primarily due to strong operations performance by corporate advisory and restructuring partially due to success fees on several large engagements. Background screening was driven by strong growth in the identity theft business.

In the fourth quarter of 2006, Kroll completed the sale of KSI, its international security operation that provides high-risk asset and personal protection services. The financial results of KSI are included in discontinued operations. Effective January 1, 2007, Kroll will transfer to Marsh certain businesses which had revenue of $25 million in 2006.

The year-to-year comparisons of the segment's revenue between 2005 and 2004 are significantly impacted by the fact that we acquired Kroll in July 2004. As a result, 2004 results include only six months of Kroll's operations. Underlying revenue growth in 2005 was 22% due to growth in the technology services, corporate advisory and restructuring and background screening practices.

primarily life, health and accident coverages. Revenue for Mercer global investment's discretionary investment management business and certain of Mercer HR's outsourcing business defined contribution administration services consists principally of fees based on assets under administration.

Revenue in the consulting business is affected by, among other things, global economic conditions, including changes in clients' particular industries and markets. Revenue is also subject to competition due to the introduction of new products and services, broad trends in employee demographics, the effect of government policies and regulations, and fluctuations in interest and foreign exchange rates. Revenues from the provision of discretionary investment management services and retirement trust

## Investment Management

MMC conducts business in its Investment Management segment through Putnam. Putnam provides investment management and related services through a broad range of investment products, including the Putnam Funds, its own family of mutual funds which are offered to individual and institutional investors. In support of the primary investment management business, Putnam subsidiaries provide other related services including transfer agency, underwriting, distribution, shareholder services, custodial, trustee and other fiduciary services. Putnam Fiduciary Trust Company ("PFTC") serves as transfer agent, dividend disbursing agent, registrar and custodian for the Putnam Funds and provides custody services to several external clients.

On January 31, 2007, MMC entered into a stock purchase agreement with Great-West Lifeco Inc. ("GWL"), a majority-owned subsidiary of Power Financial Corporation, pursuant to which GWL will purchase Putnam Investments Trust. MMC expects the sale of Putnam to close in mid-2007. Putnam to firms that distribute shares of the Putnam Funds. These 12b-1 plans, and Rule 12b-1 fees paid by the Putnam Funds thereunder, are subject to annual renewal by the fund trustees and to termination by vote of the fund shareholders or by vote of a majority of the trustees who are not affiliated with Putnam.

PFTC receives compensation from the Putnam Funds for its administrative (transfer agency and shareholder services) and custodial services pursuant to, respectively, investor servicing agreements which may be terminated by either party on 90 days' notice, and pursuant to written custody agreements which may be terminated by either party on 30 days' notice. These contracts generally provide for compensation on the basis of several factors which vary with the type of service being provided. The transfer agent servicing fee received by PFTC is a fixed rate per account for retail shareholders and a fixed rate service fee based on assets under management for mutual fund defined

## Corporate Items

### Corporate Expenses

Corporate expenses of $137 million in 2006 were $150 million lower than in 2005. The decrease is primarily due to the impact of stock option expense, which was recorded as a corporate charge in 2005 and was charged to the business segments in 2006, and lower net restructuring charges, largely resulting from a gain on the disposal of five floors in MMC's headquarters building, partly offset by higher professional services fees.

In 2006, MMC corporate recorded a net credit of $31 million for restructuring and related charges. A $74 million gain on the sale of five floors in MMC's headquarters building was partly offset by

### Income Taxes

MMC’s consolidated effective tax rate was 31.8% in 2006 compared to 33.7% in 2005. The change primarily reflects the release of valuation allowances on certain deferred tax assets and the resolution of tax audit issues, partly offset by an adjustment of the 2005 tax provision estimates to the tax return amount.

MMC’s consolidated effective tax rate was 33.7% in 2005, a decrease from 59.4% in 2004. The

**Operating Cash Flows**

Putnam has investment commitments of $140 million for three active Thomas H. Lee ("THL") funds, of which Putnam believes approximately $42 million will not be called. Putnam is authorized to commit to invest up to $187 million in future THL investment funds, but is not required to do so. At December 31, 2006 none of that additional $187 million is committed. These commitments will remain with Putnam when the anticipated sale of Putnam closes.

Approximately $37 million was invested in 2006 related to all of the commitments discussed above (including investments in Trident III prior to its contribution to MMC's U.K. pension plan).

### Commitments and Obligations

MMC's contractual obligations were comprised of the following as of December 31, 2006 (dollars in millions):

| | Payment due by Period | | | | |
|---|---|---|---|---|---|
| Contractual Obligations | Total | Within 1 Year | 1-3 Years | 4-5 Years | After 5 Years |
| Bank borrowings-international | $ 8 | $ 8 | $ — | $ — | $ — |
| Current portion of long-term debt | 1,103 | 1,103 | — | — | — |
| Long-term debt | 3,865 | — | 669 | 566 | 2,630 |
| NYAG/NYSID settlement | 340 | 170 | 170 | — | — |
| Net operating leases | 3,472 | 462 | 762 | 566 | 1,682 |
| Service agreements | 451 | 129 | 182 | 99 | 41 |
| Other long-term obligations | 86 | 73 | 10 | 2 | 1 |
| Total | $9,325 | $1,945 | $1,793 | $1,233 | $4,354 |

### Market Risk

Certain of MMC's revenues, expenses, assets and liabilities are exposed to the impact of interest rate changes and fluctuations in foreign currency exchange rates and equity markets.

*Interest Rate Risk*

MMC manages its net exposure to interest rate changes by utilizing a mixture of variable and fixed rate borrowings to finance MMC's asset base. MMC uses interest rate swaps on a limited basis to manage exposure to interest rate movements on its cash and investments as well as interest expense on borrowings. Rate swaps are only executed with highly creditworthy counterparties.

MMC had the following investments and debt instruments subject to variable interest rates:

| *(In millions of dollars)* | **December 31, 2006** |
|---|---|
| Cash and cash equivalents invested in certificates of deposit and time deposits (Note 1) | **$2,089** |
| Fiduciary cash and investments (Note 1) | **$3,704** |
| Variable rate debt outstanding (Note 11) | **$ 601** |

These investments and debt instruments are discussed more fully in the above-indicated notes to the consolidated financial statements.

Based on the above balances, if short-term interest rates increase by 10% or 48 basis points over the course of the year, annual interest income, including interest earned on fiduciary funds, would increase by approximately $15 million. However, this would be partially offset by a $2 million increase in interest expense resulting in a net increase to income before income taxes and minority interest of $13 million.

*Foreign Currency Risk*
The translated values of revenue and expense from MMC's international risk and insurance services and consulting operations are subject to fluctuations due to changes in currency exchange rates. We periodically use forward contracts and options to limit foreign currency exchange rate exposure on net income and cash flows for specific, clearly defined transactions arising in the ordinary course of business.

*Equity Price Risk*
MMC holds investments in public and private companies, as well as in certain private equity funds managed by Stone Point. Publicly traded investments of $124 million are classified as available for sale under SFAS No. 115. Non-publicly traded investments of $75 million are accounted for using the cost method and $366 million are accounted for using the equity method under APB Opinion No. 18, "The Equity Method of Accounting for Investments in Common Stock". Changes in value of trading securities are recognized in income when they occur. The investments that are classified as available for sale or that are not publicly traded are subject to risk of changes in market value, which if determined to be other than temporary, could result in realized impairment losses. MMC periodically reviews the carrying value of such investments to determine if any valuation adjustments are appropriate under the applicable accounting pronouncements.

*Other*
A significant number of lawsuits and regulatory proceedings are pending. See Note 16 to the consolidated financial statements.

**Management's Discussion of Critical Accounting Policies**

The preparation of financial statements in conformity with accounting principles generally accepted in the United States ("GAAP") requires management to make estimates and judgments that affect reported amounts of assets, liabilities, revenue and expenses, and disclosure of contingent assets and liabilities. Management considers the policies discussed below to be critical to understanding MMC's financial statements because their application places the most significant demands on management's recognize the funded status of its overfunded defined benefit pension and retiree medical plans (the "Plans") as a net benefit plan asset and its unfunded and underfunded plans as a net benefit plan liability. The gains or losses and prior service costs or credits that have not been recognized as components of net periodic costs are recorded as a component of Accumulated Other Comprehensive Income ("AOCI"), net of tax, in MMC's balance sheet. MMC adopted the provisions of SFAS 158, prospectively, on December 31, 2006.

Tax law requires items be included in MMC’s tax returns at different times than the items are reflected in the financial statements. As a result, the annual tax expense reflected in the consolidated statements of income is different than that reported in the tax returns. Some of these differences are permanent, such as expenses that are not deductible in the returns, and some differences are temporary and reverse over time, such as depreciation expense. Temporary differences create deferred tax assets and liabilities. Deferred tax assets generally represent items that can be used as a

**New Accounting Pronouncements**

New accounting pronouncements are discussed in Note 1 to MMC's consolidated financial statements.

In September 2006, the FASB issued SFAS 158 which requires that MMC recognize the funded status of its overfunded defined benefit pension and retiree medical plans (the "Plans") as a net benefit plan asset and its unfunded and underfunded plans as a net benefit plan liability. The gains or losses and prior service costs or credits that have not been recognized as components of net periodic costs are recorded as a component of AOCI, net of tax, in MMC's balance sheet. MMC adopted the provisions of SFAS 158, prospectively, on December 31, 2006. The impact of adopting SFAS 158 caused a reduction in assets of $660 million and an increase in liabilities of $245 million, including a related adjustment to tax benefits of $423 million. The net impact of adopting SFAS 158 was a reduction of MMC's stockholders' equity of $905 million, $804 million including an adjustment for the impact of recording a minimum pension credit prior to the adoption of SFAS 158. This adoption has no impact on MMC's consolidated statements of income or cash flows. The adoption of SFAS 158 does not impact any financial covenants in MMC's bank agreements, nor does MMC expect adoption to adversely impact its credit ratings. SFAS 158 also requires companies to measure the funded status of their plans as of their year-end balance sheet date no later than 2008. MMC's existing policy is to measure the funded status of its Plans as of its year-end balance sheet date and therefore is not impacted by this requirement.

In September 2006, the FASB issued SFAS No. 157, "Fair Value Measurements" ("SFAS 157"), which defines fair value, establishes a framework for measuring fair value, and expands required disclosures about fair value measurements. The provisions of SFAS 157 are effective as of the beginning of MMC's 2008 fiscal year. MMC is currently evaluating the impact of adopting SFAS 157 on its consolidated financial statements.

In June 2006, the FASB issued FASB Interpretation No. 48, "Accounting for Uncertainty in Income Taxes – an interpretation of FASB Statement No. 109" ("FIN 48"), which clarifies the accounting for uncertainty in income tax positions. This interpretation requires that MMC recognize in its consolidated financial statements the impact of a tax position when it is more likely than not that the tax position would be sustained upon examination by the tax authorities based on the technical merits of the position. This interpretation also provides guidance on derecognition, classification, interest and penalties, accounting in interim periods, disclosure, and transition. The provisions of FIN 48 will be effective for MMC beginning in the first quarter of 2007, with the cumulative effect of any change in accounting principle recorded as an adjustment to opening retained earnings. On February 27, 2007 the FASB issued draft implementation guidance in the form of a proposed FASB Staff Position subject to a thirty day comment period. Pending finalization of this guidance, MMC is evaluating the impact of adopting FIN 48 on its consolidated financial statements.

Marsh & McLennan Companies, Inc. and Subsidiaries

**Consolidated Statements of Income**

| For the Years Ended December 31,<br>*(In millions, except per share figures)* | **2006** | 2005 | 2004 |
|---|---|---|---|
| Revenue: | | | |
| Service revenue | **$11,699** | $11,395 | $11,527 |
| Investment income (loss) | **222** | 183 | 200 |
| Operating revenue | **11,921** | 11,578 | 11,727 |
| Expense: | | | |

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Marsh & McLennan Companies, Inc. and Subsidiaries

**Consolidated Statements of Cash Flows**

| For the Years Ended December 31, *(In millions of dollars)* | **2006** | 2005 | 2004 |
|---|---|---|---|
| Operating cash flows: | | | |
| Net income | **$ 990** | $ 404 | $ 176 |
| Adjustments to reconcile net income to cash generated from operations: | | | |
| Depreciation of fixed assets and capitalized software | **391** | 391 | 392 |
| Amortization of intangible assets | **97** | 99 | 64 |
| Provision (benefit) for deferred income taxes | **60** | 36 | (71) |
| Net (gains) losses on investments | **(222)** | (183) | (200) |
| Disposition of assets | **(218)** | (19) | — |
| Accrual of stock-based compensation, resulting from adoption of SFAS 123(R) | | | |

Marsh & McLennan Companies, Inc. and Subsidiaries

**Consolidated Statements of Stockholders' Equity and Comprehensive Income**

| For the Years Ended December 31,<br>*(In millions, except per share figures)* | **2006** | 2005 | 2004 |
|---|---|---|---|
| COMMON STOCK | | | |
| Balance, beginning of year | **$ 561** | $ 561 | $ 561 |
| Issuance of shares under stock compensation plans and employee stock purchase plans | **—** | — | — |
| Balance, end of year | **$ 561** | $ 561 | $ 561 |
| ADDITIONAL PAID-IN CAPITAL | | | |
| Balance, beginning of year | **$ 1,143** | $ 1,316 | $ 1,301 |
| Acquisitions | **—** | (15) | 1 |
| SFAS 123(R) periodic compensation costigu,1-6(e)-2(n)-3(s)-m (0 10 113.4 6[)-12(o)-5(m)(4TT0 19i-6)-4(i)e-4(i4)2.511 | | | |

Net uncollected premiums and claims and the related payables were $8.7 billion and $10.4 billion at December 31, 2006 and 2005, respectively. MMC is not a principal to the contracts under which the right to receive premiums or the right to receive reimbursement of insured losses arises. Net uncollected premiums and claims and the related payables are, therefore, not assets and liabilities of MMC and are not included in the accompanying consolidated balance sheets.

In certain instances, MMC advances premiums, refunds or claims to insurance underwriters or insureds prior to collection. These advances are made from corporate funds and are reflected in the accompanying consolidated balance sheets as receivables.

**Revenue:** Risk and Insurance Services revenue includes insurance commissions, fees for services rendered, interesvi9]TJ 10 0 0 10DC EMC 46A(S5 142z2mn)1(u)-3(e i)-2(n)-8(c)-10(l)1(30 0 9(i)-2(n))-2(5(a)1l)-4(e)-8(

Investment Management revenue is derived primarily from investment management fees and 12b-1 fees. Investment management fees are recognized as services are provided. Such fees are based on the net assets of the funds and are collected directly from the applicable funds. Mutual fund distribution fees are recognized over the period in which the fees can be charged to the related funds, or when a contingent deferred sales charge is triggered by a redemption. Sales of mutual fund shares are recorded on a settlement date basis and commissions thereon are recorded on a trade date basis. Fees resulting from achievement of specified performance thresholds are recorded when such levels are attained and such fees are not subject to forfeiture.

MMC has deferred the recognition of performance fee revenue in connection with the management of certain private equity funds of $172 million at December 31, 2006. This revenue is based on the investment performance over the life of each private equity fund, and future underperformance may result in the forfeiture of such revenue. As noted above, MMC only recognizes performance fee revenue when such fees are no longer subject to forfeiture, which for the $172 million noted above, may take a number of years to resolve.

**Cash and Cash Equivalents:** Cash and cash equivalents primarily consist of certificates of deposit and time deposits, generally with original maturities of three months or less.

**Fixed Assets:** Fixed assets are stated at cost less accumulated depreciation and amortization. Expenditures for improvements are capitalized. Upon sale or retirement, the cost and related accumulated depreciation and amortization are removed from the accounts and any gain or loss is reflected in income. Expenditures for maintenance and repairs are charged to operations as incurred.

Depreciation of buildings, building improvements, furniture, and equipment is provided on a straight-line basis over the estimated useful lives of these assets. Leasehold improvements are amortized on a straight-line basis over the periods covered by the applicable leases or the estimated useful life of the

Certain investments, primarily investments in private equity funds, are accounted for using the equity

Tax law requires items to be included in MMC's tax returns at different times than the items are reflected in the consolidated statements of income. As a result, the annual tax expense reflected in the consolidated statements of income is different than that reported in the tax returns. Some of these differences are permanent, such as expenses that are not deductible in the returns, and some differences are temporary and reverse over time, such as depreciation expense. Temporary differences create deferred tax assets and liabilities. Deferred tax assets generally represent items that can be used as a tax deduction or credit in tax returns in future years for which benefit has already been recorded in the financial statements. Valuation allowances are established for deferred tax assets when it is estimated that it is more likely than not that some portion or all of the deferred tax assets will not be realized. Deferred tax liabilities generally represent tax expense recognized in the financial statements for which payment has been deferred, or expense for which a deduction has been taken already in the tax return but the expense has not yet been recognized in the financial statements.

U.S. Federal income taxes are provided on unremitted foreign earnings except those that are

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accounting principle recorded as an adjustment to opening retained earnings. On February 27, 2007 the FASB issued draft implementation guidance in the form of a proposed FASB Staff Position subject to a thirty day comment period. Pending finalization of this guidance, MMC is evaluating the impact of

### 3. Other Comprehensive Income (Loss)

The components of other comprehensive income (loss) are as follows:

own direct investments in insurance and financial services companies, including Ace Ltd., XL Capital Ltd. and Axis Capital Holdings Ltd., as well as its investments in Trident II and other funds managed by Stone Point.

### 5. Discontinued Operations

In the fourth quarter of 2006, Kroll completed the sale of Kroll Security International (“KSI”), its international high-risk asset and personal protection division. The gain on the disposal of KSI and the financial results associated with 2006 and prior periods are included in discontinued operations.

In the first quarter of 2006, MMC determined that Price Forbes, its U.K.-based insurance wholesale operation, met the criteria for classification as a discontinued operation. The 2006 results of Price Forbes, which include a charge to reduce the carrying amount of its assets to fair value less cost to sell, are included in discontinued operations in the consolidated statement of income. The results of Price Forbes were insignificant to MMC’s 2005 results and therefore, prior year amounts have not been restated. MMC completed the sale of Price Forbes in September 2006.

MMC sold Crump Group, Inc., its U.S.-based wholesale insurance broker, during the fourth quarter of 2005, and its majority interest in SCMS, a provider of claims management and associated productivity services, on January 31, 2006. The account balances and activities of these entities are presented as discontinued operations in the accompanying consolidated financial statements.

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## 6. Goodwill and Other Intangibles

MMC is required to assess goodwill and any indefinite-lived intangible assets for impairment annually or more frequently if circumstances indicate impairment may have occurred. MMC performs the annual impairment test for each of its reporting units during the third quarter of each year. MMC completed its annual impairment tests in the third quarter of 2006 and determined that such assets were not impaired.

Changes in the carrying amount of goodwill are as follows:

| *(In millions of dollars)* | **2006** | 2005 |
|---|---|---|
| Balance as of January 1, 2006 | **$7,246** | $7,459 |
| Goodwill acquired | **132** | 45 |
| Disposals | **(29)** | (95) |
| Purchase accounting adjustments in accordance with SFAS No. 141 | **(111)** | (38) |
| Other adjustments [(a)] | **90** | (125) |
| Balance as of December 31, 2006 | **$7,328** | $7,246 |

(a) Primarily includes foreign exchange

Goodwill allocable to each of MMC's reportable segments is as follows: Risk and Insurance Services $3.7 billion; Risk Consulting & Technology $1.6 billion; Consulting $1.9 billion; and Investment Management $0.1 billion.

The goodwill balance at December 31, 2006 and 2005 includes approximately $115 million and $121 million, respectively, of equity method goodwill.

Amortized intangible assets consist of the cost of client lists, client relationships and trade names acquired, and the rights to future revenue streams from certain existing private equity funds. The gross cost and accumulated amortization by major intangible asset class is as follows:

| December 31, *(In millions of dollars)* | **2006** Gross Cost | **2006** Accumulated Amortization | **2006** Net Carrying Amount | 2005 Gross Cost | 2005 Accumulated Amortization | 2005 Net Carrying Amount |
|---|---|---|---|---|---|---|
| Customer and marketing related | **$655** | **$266** | **$389** | $638 | $191 | $447 |
| Future revenue streams related to existing private equity funds | **200** | **142** | **58** | 200 | 125 | 75 |
| Total amortized intangibles | **$855** | **$408** | **$447** | $838 | $316 | $522 |

Aggregate amortization expense for the years ended December 31, 2006 and 2005, was $97 million

## 7. Income Taxes

Income before income taxes and minority interest shown below is based on the geographic location to which such income is attributable. Although income taxes related to such income may be assessed

| December 31,<br>*(In millions of dollars)* |
| --- |

MMC is routinely examined by the Internal Revenue Service and tax authorities in the United Kingdom, as well as states in which it has significant business operations, such as California, Massachusetts and New York. The tax years under examination vary by jurisdiction. MMC regularly considers the likelihood of assessments in each of the taxing jurisdictions resulting from examinations. MMC has established tax allowances which it believes are adequate in relation to the potential assessments. MMC believes the resolution of tax matters will not have a material effect on the consolidated financial condition of MMC, although a resolution could have a material impact on MMC's net income or cash flows and on its effective tax rate in a particular future period.

## 8. Retirement Benefits

MMC maintains qualified and non-qualified defined benefit pension plans for its eligible U.S. employees and a variety of defined benefit and defined contribution plans for eligible non-U.S. employees. MMC's policy for funding its tax qualified defined benefit pension plans is to contribute amounts at least sufficient to meet the funding requirements set forth in U.S. and applicable foreign law.

*Implementation of SFAS 158*

In September 2006, the FASB issued SFAS 158 which requires that MMC recognize on a prospective basis the funded status of its overfunded defined benefit pension and retiree medical plans (the "Plans") as a net benefit plan asset and its unfunded and underfunded plans as a net benefit plan liability. The offsetting adjustment to the amount of assets and liabilities required to be recognized is recorded in AOCI,

| December 31, *(In millions of dollars)* | U.S. Pension Benefits | | U.S. Postretirement Benefits | |
|---|---|---|---|---|
| | **2006** | 2005 | **2006** | 2005 |
| Amounts recognized in the Consolidated Balance Sheets under SFAS 158: 74N/A$—N/AN/AN/AN/AN/A$118N/A$N/A | | | | |

The following schedules provide information concerning MMC's non-U.S. defined benefit pension plans and non-U.S. postretirement benefit plans.

| December 31, | Non-U.S. Pension Benefits | | Non-U.S. Postretirement Benefits | |
|---|---|---|---|---|
| *(In millions of dollars)* | **2006** | 2005 | **2006** | 2005 |
| Change in benefit obligation: | | | | |
| Benefit obligation at beginning of year | **$6,288** | $5,936 | **$ 70** | $ 62 |
| Newly disclosed plans | **142** | — | **—** | — |
| Service cost | **152** | 157 | **2** | 1 |
| Interest cost | **312** | 296 | **3** | 3 |
| Employee contributions | **33** | 37 | **—** | — |
| Actuarial loss (gain) | **(238)** | 648 | **—** | 9 |
| Effect of settlement | **(5)** | (14) | **—** | — |
| Effect of curtailment | **(35)** | | | |

The non-U.S. defined benefit plans do not have any direct or indirect ownership of MMC stock.

If compensation cost for all MMC's share-based payment arrangements had been recognized based on the fair value method prescribed by SFAS 123 for the periods prior to the adoption of SFAS 123 (R) on July 1, 2005, MMC's net income and net income per share in 2005 and 2004 would have been reduced to the pro forma amounts indicated in the table below.

| *(In millions of dollars, except per share figures)* | 2005 | 2004 |
|---|---|---|
| **Net Income:** | | |
| As reported | $ 404 | $ 176 |
| Adjustment for fair value method, net of tax | (69) | (146) |
| Pro forma net income | $ 335 | $ 30 |
| **Net Income Per Share:** | | |
| *Basic:* | | |
| As reported | $0.75 | $0.33 |
| Pro forma | $0.62 | $0.06 |
| *Diluted:* | | |
| As reported | $0.74 | $0.33 |
| Pro forma | $0.61 | $0.06 |

The pro forma information reflected above includes stock options issued under MMC's incentive and stock award plans and the Putnam Investments Equity Partnership Plan and stock issued under MMC's stock purchase plan. In addition, the pro forma information reflected above is based on recognizing the costs of employee stock option awards granted prior to July 1, 2005 to retiree-eligible individuals over the full vesting term of the award. Effective July 1, 2005, MMC began recognizing new employee stock option awards granted to retiree-eligible individuals over a shorter period, consistent with the retirement vesting acceleration provisions of these grants. If the costs of employee stock option awards granted prior to July 1, 2005 to retiree-eligible individuals had been recognized for these individuals under this accelerated method, pro forma net income for the years ended 2005 and 2004 would have amounted to $340 million and $44 million.

**MMC Incentive and Stock Award Plans**

In 2000, the Marsh & McLennan Companies, Inc. 2000 Employee Incentive and Stock Award Plan (the "2000 Employee Plan") and the Marsh & McLennan Companies, Inc. 2000 Senior Executive Incentive and Stock Award Plan (the "2000 Executive Plan") were adopted. The types of awards permitted under these plans include stock options, restricted stock, stock bonus units, restricted and deferred stock units payable in MMC common stock or cash, and other stock-based and performance-based awards. The Compensation Committee of the Board of Directors (the "Compensation Committee") determines, at its discretion, which affiliates may participate in the plans, which eligible employees will receive awards, the types of awards to be received, and the terms and conditions thereof. The right of an employee to receive an award may be subject to performance conditions as specified by

The assumptions used in the binomial option pricing valuation model for options granted during 2006 and 2005 are as follows:

| | 2006 | 2005 | |
|---|---|---|---|
| | | Post 6/30/05 | Pre 7/1/05 |
| Risk-free interest rate | **4.7%-5.3%** | 4.0%-4.1% | 4.1%-4.5% |
| Expected life (in years) | **5.0-7.1** | 5.2-6.5 | 6.7-6.8 |
| Expected volatility | **29.0%** | 29.0% | 17.9% |
| Expected dividend yield | **2.3%** | 2.3% | 2.2% |

A summary of the status of MMC's stock option awards as of December 31, 2006 and changes during the year then ended is presented below:

| | Shares | Weighted Average Exercise Price | Weighted Average Remaining Contractual Term | Aggregate Intrinsic Value ($000) |
|---|---|---|---|---|
| Balance at January 1, 2006 | **66,295,396** | **$34.33** | | |
| Granted | **6,500,438** | **$30.19** | | |
| Exercised | **(2,677,038)** | **$19.46** | | |
| Canceled or exchanged | **—** | **—** | | |
| Forfeited | **(5,749,912)** | **$36.72** | | |
| Expired | **—** | **—** | | |
| Balance at December 31, 2006 | **64,368,884** | **$34.30** | **5.4 years** | **$77,219** |
| Options vested or expected to vest at December 31, 2006 | **63,022,417** | **$34.39** | **5.3 years** | **$75,778** |
| Options exercisable at December 31, 2006 | **28,153,184** | **$40.35** | **3.2 years** | **$20,071** |

The weighted-average grant-date fair value of MMC's option awards granted during the years ended December 31, 2006, 2005 and 2004 was $8.55, $6.51 and $7.51, respectively. The total intrinsic value of options exercised during the same periods was $31 million, $36 million and $46 million, respectively.

As of December 31, 2006, there was $84 million of unrecognized compensation cost related to MMC's option awards. The weighted-average period over which that cost is expected to be recognized is 1.4 years. Cash received from the exercise of stock options for the years ended December 31, 2006, 2005 and 2004 was $52 million, $45 million, and $111 million, respectively.

MMC's policy is to issue treasury shares upon option exercises or share unit conversion. MMC intends to issue treasury shares as long as an adequate number of those shares is available.

*Restricted Stock:* Restricted shares of MMC's common stock may be awarded under MMC's incentive and stock award plans and are subject to restrictions on transferability and other restrictions, if any, as the Compensation Committee may impose. The Compensation Committee may also determine when and under what circumstances the restrictions may lapse and whether the participant receives the rights of a stockholder, including, without limitation, the right to vote and receive dividends. Unless the Compensation Committee determines otherwise, restricted stock that is still subject to restrictions is forfeited upon termination of employment. Shares granted generally become unrestricted at the earlier of: (1) January 1 of the year following the vesting grant date anniversary or (2) the later of the recipient's normal or actual retirement date. For shares granted prior to 2004, the grant date anniversary is ten years. For shares granted during 2004 and 2005, the grant date anniversary is 7 years and 5 years, respectively. However, certain restricted shares granted in 2005 vest on the third anniversary of the grant date. There were no restricted shares granted in 2006.

A summary of the status of MMC's restricted stock awards as of December 31, 2006 and changes during the period then ended is presented below:

## 11. Debt

MMC's outstanding debt is as follows:

| December 31,<br>*(In millions of dollars)* | **2006** | 2005 |
|---|---|---|
| **Short-term:** | | |
| Bank borrowings — International | **$ 8** | |

A portion of insurance fiduciary funds which MMC holds to satisfy fiduciary obligations is invested in high quality debt securities which are generally held to maturity. The difference between cost and fair value of these investments is not material.

**Short-term and Long-term Debt**: The fair value of MMC's short-term debt which consists of bank loans approximates its carrying value. The estimated fair value of MMC's long-term debt is based on discounted future cash flows using current interest rates available for debt with similar terms and remaining maturities.

## 13. Integration and Restructuring Costs

2006 Plan

In September 2006, MMC announced that it would undertake restructuring activities designed to enhance operational efficiencies and improve profitability (the "2006 Plan"). The restructuring activities are expected to be implemented in several phases – the first phase which began in September and is expected to be completed over the next two quarters, and one or more additional phases. In connection with Phase 1 of the 2006 Plan, MMC incurred net restructuring charges of $10 million during the third and fourth quarter of 2006, as follows: risk and insurance services - $49 million, risk consulting & technology - $1 million, consulting - $28 million and corporate - $(68) million. The corporate amount includes a $74 million gain on the sale of five (5) floors in MMC's headquarters building. Utilization of the 2006 Plan charges for Phase 1 is summarized as follows:

| *(In millions of dollars)* | **Accrued in 2006** | **Utilized in 2006** | **Remaining Liability at 12/31/06** |
|---|---|---|---|
| Severance and benefits | **$ 59** | **$(21)** | **$38** |

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2005 Plan

In March 2005, MMC announced that it would undertake restructuring activities involving staff

*Related Litigation*

Numerous lawsuits have been commenced against MMC, one or more of its subsidiaries, and their

for selecting, removing and monitoring other fiduciaries did not comply with ERISA, and that MMC knowingly participated in other defendants' breaches of fiduciary duties. The consolidated complaint seeks, among other things, unspecified compensatory damages, injunctive relief and attorneys' fees and costs. The amount of Plan assets invested in MMC stock at October 13, 2004 (immediately prior to the announcement of the NYAG Lawsuit) was approximately $1.2 billion. The consolidated complaint alleges that during the purported class period, which extends from July 1, 2000 until January 31, 2005, MMC's stock price fell from $52.22 to $32.50. In December 2006, the court grorpun Du0 In D4(n D)ÿ ru0 In D4(n D)ÿ ru0 In D.2n Djthe NYAG Lawsuit. MMC and its subsidiaries have cooperated with these requests from regulators. MMC has been contacted by certain of the above state entities indicating that they may file civil actions or otherwise seek additional monetary or other remedies from MMC.

- In September 2005, the National Association of Insurance Commissioners (the "NAIC") issued a press release indicating that over 30 state insurance regulators (including several referred to in the preceding paragraph) working collaboratively through the NAIC had reached a multi-state regulatory settlement with MMC and Marsh. The NAIC settlement agreement reaffirms MMC's commitment, under the Settlement Agreement with NYAG and the NYSID, to establish a no-fault compensation fund for policyholder clients across the United States, and provides for state-by-state enforcement of the business reforms agreed to be implemented pursuant to the Settlement Agreement. The NAIC settlement agreement has been executed by MMC and Marsh, and the NAIC has advised that the agreement has been adopted by insurance commissioners in 33 states, the District of Columbia and Guam.

Putnam-Related Matters

On January 31, 2007, MMC entered into a stock purchase agreement (the "Putnam Sale Agreement") with Great-West Lifeco Inc. ("GWL"), a majority-owned subsidiary of Power Financial Corporation, pursuant to which GWL has agreed to purchase Putnam Investments Trust. The Putnam Sale Agreement provides that MMC will indemnify GWL with respect to certain Putnam-related litigation and regulatory matters following the closing of this transaction, as indicated below. MMC expects the sale of Putnam to close in mid-2007.

*Regulatory Matters*

- In 2003 and 2004, Putnam entered into settlements (the "Putnam Trading Settlements") with the Securities and Exchange Commission (the "SEC") and the Commonwealth of Massachusetts (the "Massachusetts Securities Division") with respect to excessive short-term trading by certain former Putnam employees in shares of the Putnam mutual funds (the "Putnam Funds"). Under the Putnam Trading Settlements, Putnam agreed to pay a total of $193.5 million ($108.5 million in restitution and $85 million in civil fines and penalties). In addition to the $108.5 million in restitution, Putnam Funds shareholders will receive a distribution of $45 million from the civil penalty Putnam previously paid to the SEC. An

*“Market-Timing”-Related Litigation*

MMC and Putnam have received a substantial number of civil complaints, filed in various state and federal courts, based on allegations of “market-timing” and, in some cases, “late trading” activities. All of the actions filed in federal court have been transferred, along with actions against other mutual fund complexes, to the United States District Court for the District of Maryland for coordinated or consolidated pretrial proceedings. The lead plaintiffs in those cases filed consolidated amended complaints in September 2004. MMC and Putnam moved to dismiss the various complaints pending in federal court in Maryland, which are described below:

- MMC and Putnam, along with certain of their former officers and directors, were named in a

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the five funds at issue, and seeks relief for a period after the filing of the original complaint. In February 2007, the Court denied defendants’ motion to stay the new complaint and granted plaintiffs’ motion to consolidate the two cases. The parties are engaged in fact discovery.

As described more fully in Section [illegible]

- MMC and its subsidiaries are subject to a significant number of other claims, lawsuits and proceedings in the ordinary course of business. Such claims and lawsuits consist principally of alleged errors and omissions (known as E&O's) in connection with the performance of professional services. Some of these claims seek damages, including punitive damages, in amounts that could, if awarded, be significant. MMC provides for these exposures by a

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## MANAGEMENT'S ANNUAL REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING

The management of Marsh & McLennan Companies, Inc. is responsible for establishing and maintaining adequate internal control over financial reporting. MMC's internal control over financial reporting is designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles.

MMC's internal control over financial reporting includes those policies and procedures relating to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of MMC; the recording of all necessary transactions to permit the preparation of MMC's consolidated financial statements in accordance with generally accepted accounting principles; the proper authorization of receipts and expenditures in accordance with authorizations of MMC's management and directors; and the prevention or timely detection of the unauthorized acquisition, use or disposition of assets that could have a material effect on MMC's consolidated financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

Management evaluated the effectiveness of MMC's internal control over financial reporting as of December 31, 2006. In making this evaluation, management used the criteria set forth by the Committee of Sponsoring Organizations of the Treadway Commission (COSO) in Internal Control — Integrated Framework. Based on its evaluation, management determined that MMC maintained effective internal control over financial reporting as of December 31, 2006.

Deloitte & Touche LLP, the Independent Registered Public Accounting Firm that audited and reported on MMC's consolidated financial statements included in this annual report, also issued an attestation report on management's evaluation of the effectiveness of MMC's internal control over financial reporting as of December 31, 2006.

Michael G. Cherkasky
President and
Chief Executive Officer
February 28, 2007

Matthew B. Bartley
Chief Financial Officer
February 28, 2007

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated financial statements as of and for the year ended December 31, 2006 of the Company and our report dated February 28, 2007 expressed an unqualified opinion on those financial statements and included an explanatory paragraph regarding the Company's changes in accounting for pension and postretirement benefits and share-based payments.

Deloitte & Touche LLP

New York, New York
February 28, 2007

Marsh & McLennan Companies, Inc. and Subsidiaries

## SELECTED QUARTERLY FINANCIAL DATA AND SUPPLEMENTAL INFORMATION (UNAUDITED)

| | First Quarter | Second Quarter | Third Quarter | Fourth Quarter |
|---|---|---|---|---|
| | *(In millions of dollars, except per share figures)* | | | |
| **2006:** | | | | |
| Revenue | **$3,016** | **$2,970** | **$2,872** | **$3,063** |
| Operating income | **$ 401** | **$ 339** | **$ 321** | **$ 397** |

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## INFORMATION CONCERNING FORWARD-LOOKING STATEMENTS

This Annual Report c

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BOARD OF DIRECTORS

# SHAREHOLDER INFORMATION

Designed and Produced by Taylor & Ives, NYC

Marsh
11m /Avenue
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