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# Risk-Taker's Reign at Merrill Ends With Swift Fall

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The six-year reign of [E. Stanley O'Neal](#) at [Merrill Lynch](#) has been one of contradictions. He was a loner in an industry that places a premium on relationships. And he pushed Merrill into risky investments despite his experience as chief financial officer, where assessing risk was one of his responsibilities.

Now after an \$8.4 billion write-down and an unauthorized merger approach to a rival bank, [Wachovia](#), Mr. O'Neal has lost the confidence of his board and is expected to resign as chairman and chief executive as early as today.

Directors, having decided Mr. O'Neal should leave, met through the weekend to determine who should succeed him.

One possible successor who has drawn support from within the firm is Laurence D. Fink, the head of the asset management firm [BlackRock](#), which is 49 percent owned by Merrill. One option the board is considering would keep Gregory J. Fleming as a Merrill co-president and name Robert J. McCann, the president of Merrill's wealth management unit, a co-president.

Mr. O'Neal's fall has been stunning in its speed and ferocity. This spring, Merrill's stock was trading around \$95 a share, and Mr. O'Neal was being celebrated for transforming Merrill into a more aggressive, risk-friendly institution. Last week, the stock sunk to as low as \$59 a share.

The events underscore that on Wall Street, even the highest paid chief executives with handpicked boards are not immune to the furies of investors and employees.

His fall is also a reminder of how dangerous it is to tinker with a firm's culture. Having declared the idea of a nurturing Mother Merrill passé, Mr. O'Neal has discovered how vengeful a spurned culture can be.

Mr. O'Neal's ascent — through hard work and the cultivation of crucial relationships — was unusual for its swiftness. He also has the ability to be at the center of major financial disruptions without taking on significant blame. He was a senior banker in the junk bond division when the firm had a \$470 million write-down; he was a co-head of Merrill's institutional business in 1997, a few months before the Asian financial crisis hurt the markets. He was chief financial officer in 1998 when the firm had a quarterly loss because of bond trading and exposure to the troubled hedge fund Long Term Capital Management.

People who have worked with Mr. O'Neal, 56, describe an aloof, calculating man who during his 20 years at the firm has made few friends. While he has been quick to forge temporary alliances with superiors like [Herbert M. Allison Jr.](#), a former president who was his first mentor, and Arshad R. Zakaria and Thomas H. Patrick Sr., who championed his candidacy for the top job, he has been equally quick to cut ties to them.

Some of his closest relationships date back to his days in the [General Motors](#) treasury department where he was first noticed as a smart, ambitious executive. It was at G.M. that he met his wife, Nancy Garvey, who was an economist and remains one of his closest confidantes, and John D. Finnegan, the chief executive of Chubb whom he recruited to the Merrill board in 2004.

But colleagues say there was a part of Mr. O'Neal that seemed to resist this ascent. Twice, he came close to leaving the firm and was notorious for his propensity to fall into a funk when things were not going his way. A golf fanatic — his handicap is nine and he belongs to four country clubs — he often plays alone, in addition to the usual rounds with clients and a circle of friends outside Merrill.

But, colleagues also say that at times of crisis, he can display energy, acumen and leadership, as he did in the days after the terrorist attacks on Sept. 11. Then Merrill's president, Mr. O'Neal worked countless hours as the firm tried to regain its footing.

For many, especially those far from the intrigues and complexities of Wall Street, Merrill Lynch stands for solidity and good faith, principles that were rocked by the events of the last few months. But old Merrill hands feel that the firm will survive, despite the notion that it may become vulnerable to a takeover.

"This is a resilient franchise," said Stephen Hammerman, a former vice chairman of Merrill who supported Mr. O'Neal's bid for chief. Mr. Hammerman said he felt concern for Merrill Lynch employees who have seen the stock decline.

For a time, Merrill's business flourished as Mr. O'Neal took on more risk and made deep cuts. In 2006, Merrill made \$7 billion from using its capital to trade for itself and clients, compared with \$2.2 billion in 2002. Some riskier businesses that the firm was involved with, like private equity and lending, fared well this summer.

Merrill's exposure to the volatile and ultimately toxic market for complex debt instruments called collateralized debt obligations exploded to more than \$40 billion from around \$1 billion

about 18 months ago. Initially, the increased risk was a boon — part of a shift from the firm's classic position as a money manager with an excellent stock underwriting business to a bank that had become increasingly hooked on the high-octane, high-risk returns that came from investing its own money.

In the second quarter, just before the collapse in the credit markets, fixed-income revenues skyrocketed 201 percent over the same quarter a year earlier. Underpinning this growth was the firm's market-leading position in packaging different and risky kinds of debt.

Directors were briefed about the firm's subprime exposure in April and collateralized debt obligations in July, according to a person briefed on the presentations. While Merrill was scrambling to reduce its exposures, worsening conditions in late July shut down the market for even the highest-rated collateralized debt obligations, making it clear that Merrill's position was starting to look problematic, this person said.

From late July through September, Mr. O'Neal was actively involved in tackling the problem, said a person briefed on the events. He led daily meetings, and called in during his vacation.

He also had another window into the market's fall. As a director at BlackRock, Mr. O'Neal had been briefed on the dangers of high-risk subprime exposure.

On its second-quarter conference call, Merrill and Mr. O'Neal projected a sunny outlook, promoting the firm's risk management practices.

But in July, when the credit markets froze, it was clear that Merrill stood to lose a lot of money. As the market deteriorated, and Merrill faced bigger losses, tensions were beginning to boil over. In contrast to past Merrill chiefs who cultivated a clubbier style of management, Mr.

O'Neal was not averse to letting rivalries fester.

According to people briefed on the situation, Mr. O'Neal wanted to fire his chief financial officer, Jeffrey N. Edwards, and replace him with a longtime friend, H. McIntyre Gardner.

At the end of July, Ahmass L. Fakahany, who despite his lack of any trading experience had assumed broad responsibility over the firm's risk exposure, kept the board briefed on the situation. He sent an e-mail message to [Charles O. Rossotti](#), the director in charge of Merrill's risk committee, according to one person briefed on the communication. In the message, which he copied to Mr. O'Neal, Mr. Fakahany told the board of the exposure.

With the markets worsening, Mr. Fakahany and Mr. Fleming sent a three-page letter to directors on Aug. 9, titled "Board Market Update End July Results: Note from Fakahany and Fleming," discussing the mounting losses and troubles, and explaining that significant deterioration had taken place in July, according to a person briefed on the situation. The letter was also sent to Mr. O'Neal and Merrill's general counsel, Rosemary T. Berkery. The deterioration continued, ultimately reaching \$7.9 billion in late October, almost \$2.5 billion more than Merrill had announced only weeks earlier.

For the board, the fast accumulation of bad news came as a shock. A year earlier, directors had paid Mr. O'Neal \$46 million after the firm's impressive results. Now the biggest losses in the firm's 93 years were looming.

When directors were briefed late last week about Mr. O'Neal's approach to [G. Kennedy Thompson](#), the chief executive at Wachovia, they were furious. Mr. Fleming, who is close to Mr. Thompson, had followed up Mr. O'Neal's initial overture, making it look as if it was more than just putting out feelers.

Even after that board meeting, it was by no means unanimous that Mr. O'Neal would have to leave. As late as Tuesday, the day before earnings were to be reported, one director told a friend that it was a mistake to lump Mr. O'Neal with other troubled chief executives like [Charles O. Prince III](#) of [Citigroup](#), who is under scrutiny because of write-offs. Internally, employees viewed the merger talks as the last straw.

“We made some stupid mistakes and most of us said, ‘Let’s figure out how to make this better,’” said a financial adviser with over 25 years of experience at Merrill. “But then you throw in the merger talks and the typical guy says ‘We are desperate.’ The sentiment is, these guys have to go.”

But sentiment was building against Mr. O'Neal among former Merrill executives, some of whom made direct appeals to the board. If he leaves, Mr. O'Neal could be paid at least \$159 million, according to an analysis by James F. Reda & Associates, a compensation consulting firm. Had he succeeded in putting together a merger, he might have left with as much as \$274 million.

Mr. O'Neal does not have a severance contract, but the board's compensation committee could grant him severance.

By late in the week, it had become clear that a change was needed. At that point, three directors, all of whom had been recently selected by Mr. O'Neal, had taken the lead in considering life without him at Merrill — Mr. Finnegan, Mr. Rossotti and Armando M. Codina, a prominent real estate developer who knew Mr. O'Neal from the G.M. board.

