Pensions and Investments

May 1, 2000, Monday

SECTION: Pg. 6

LENGTH: 1291 words

HEADLINE: A CHANGE IN PLANS? SBC suit may alter running of 401(k)s

BYLINE: Arleen Jacobius

BODY:

LOS ANGELES - The outcome of a $1.15 billion lawsuit filed by participants of SBC Communications Inc.'s 401(k) plan ultimately could force other sponsors to change how they run their plans.

"If the court ultimately agrees with some of the legal positions in the complaint, and I think there is a chance it could happen, then I think it could be groundbreaking," said C. Frederick Reish, an ERISA attorney in the Los Angeles law firm of Reish & Luftman.

On April 18, 18 participants in plans sponsored by SBC and its subsidiaries ~ including Pacific Telesis Group, which SBC purchased three years ago ~ filed a class-action suit against the companies in U.S. District Court for the Central District of California, Los Angeles, claiming self-dealing and mismanagement of San Antonio-based SBC's 401(k) plan.

The suit contends the companies improperly liquidated about $600 million in participants' investments in what turned out to be the higher-performing stock of AirTouch Communications Inc., a former Pacific Telesis subsidiary, and transferred ~ or "mapped" ~ the proceeds into SBC common stock that did not perform as well.

In addition, participants say SBC gave them misleading and incomplete information about their right to withdraw their AirTouch stock from the 401(k) plans before it was liquidated.

The issue of how participants should be informed of changes in investments or changes in how sponsors manage 401(k)s could have a significant impact on how plan sponsors run their 401(k) plans, Mr. Reish said.

When plan sponsors make a change, Mr. Reish asked, is it "such a significant event" that the company has a legal duty to give participants notice. That is, when does a plan sponsor have to voluntarily give participants information and how much information does the sponsor have to give?

"When you make these decisions, you have to communicate with employees and tell them why you are doing it, and you have to have a rationale for doing it because you are going to be questioned on it," said Richard L. Menson, a partner and head of the Chicago office of the ERISA law firm McGuire Woods Battle & Boothe LLP, Richmond, Va.

This is true particularly when plan changes are made as a result of a merger or acquisition, Mr. Menson said.

In the SBC case, plan participants argue the price of AirTouch stock has essentially tripled in value since SBC liquidated the AirTouch stock funds in the 401(k) plans in spring 1998.

In 1994, Pacific Telesis Group spun off its wireless subsidiary, eventually renamed AirTouch.

Pacific Telesis shareholders received AirTouch shares in amounts proportionate to their holdings of Pacific Telesis stock. This included almost all of the participants in Pacific Telesis' two 401(k) plans.

In spring 1997, SBC took control of the Pacific Telesis plans. The participants now suing SBC contend AirTouch stock doubled in price by the time SBC began selling off the plans' stock, and later tripled.

At the same time, the value of the SBC stock in their $19.3 billion 401(k) plans has gone down, they allege.

The participants also allege SBC engaged in self-dealing by "stripping" about 40,000 employees of their AirTouch stock and redirecting the money into SBC company stock. They also say SBC violated the Employee Retirement Income Security Act by putting its own interests ahead of those of its participants.

The complaint alleges that employees lost about $1.15 billion in profits as a result of SBC's action.

SBC responds

Money from the sale of AirTouch stock did not all go into SBC stock, said Selim Bingol, SBC company spokesman. In that respect, the complaint "is flat wrong," Mr. Bingol said. Plan participants had five investment choices for converting their AirTouch funds.

Although SBC executives declined to comment further, a statement released on the day the complain was filed stated that SBC's policy to restrict stock ownership to SBC stock in the plan. (Plan service provider Metropolitan Life Insurance Co., which is not being sued, also declined to comment.)

"Our position on this issue is very clear," the statement states. "No SBC savings plan includes direct stock ownership in any other company that is not related to SBC.

"After acquiring Pacific Telesis in 1997, SBC moved to bring the two companies' savings plans in line with one another. After lengthy internal review, including negotiations and agreement with our labor union, and after months of prior notice, SBC gave management and non-management employees alike five different investment choices for converting their AirTouch funds.

"All the money from the liquidated AirTouch stock was reinvested, dollar for dollar, in these other vehicles, and SBC did not profit from the conversion whatsoever."

'Tough issue'

"Company stock is a real tough issue" in a plan merger, said William J. Arnone, partner with consulting firm Ernst & Young LLP, New York. "If you have a policy not to permit other stock in your 401(k) plan, you need to educate participants so they don't claim surprise later on."

Scott Hanson, a financial planner with about 600 Pacific Telesis employees as clients, said he was surprised SBC did not try to merge the 401(k) plans sooner.

"The company provided participants with that information that they had the right to move out of AirTouch stock and into other investment options in the plan," said Mr. Hanson, chief financial officer of Hanson McClain, Sacramento, Calif. "I knew employees had the right to receive in-service distribution. Hindsight is 20-20 and it was not the general consensus that AirTouch would do great. A lot of people wanted to sell the stock. It was just emerging from the dead."

Another issue raised by the complaint is whether plan sponsors should be required to inform participants not only about their investments, but also about their divestment options, said Dennis Leybold, attorney with Stoel Rives LLP, Portland, Ore.

Too much company stock?

Mr. Leybold said the lawsuit also could cause plan sponsors to rethink their use of company stock in 40 l(k) plans.

"Too many plans use too much company stock," Mr. Leybold said.

Much of what gave rise to the case was the bad luck of having a competitor's stock in the SBC plan and the fact that the AirTouch stock went up, he said.

"I hope this is not going to be a situation where a bad fact makes bad law," he said.

But the plaintiffs' lawyer disagreed. "What happens in all 401(k) plans is that companies are tempted to manipulate large asset pools in ways that may benefit the company and not in the best interest of employees," said Eli Gottesdiener, partner in Sprenger & Lang PLLC, the Washington-based law firm that is representing the SBC participants. "If the company is going to start making changes in the plans, there has to be a firewall between their fiduciary and their corporate side, and if they are not going to do that, it is a breach of their fiduciary duty. These suits are going to continue as long as there are not good controls."

Mr. Gottesdiener has filed two other class action lawsuits on behalf of participants in 401(k) plans. One was filed against First Union by its own plan participants for providing only First Union funds in their 401(k) plan to boost the money in those funds, they allege. That case has not yet made it to trial.

The First Union lawsuit, filed in September, was related to another suit against First Union arising from its liquidation of assets in the Signet Banking Corp. 401(k) plan and transferring about $250 million into the First Union 401(k) plan.

Taken together with the current lawsuit, these actions have the potential of defining new 401(k) plan rules, Mr. Reish said.

GRAPHIC: William J. Arnone of Ernst & Young said "Company stock is a real tough issue" in a plan merger.