

The Wall Street Journal
November 4, 2004

Bank of America Pensions Draw Ire
Employees File Lawsuit, Call Cash-Balance Plan Part of 'Arbitrage Scheme'

By Ellen Schultz

The debate over whether and how companies can use their employees' pension plans as profit centers seems unlikely to end soon. Employees of Bank of America Corp. are suing the company over its cash-balance pension plan, which they say the company used as part of an "arbitrage scheme" to enrich itself at the expense of participants. According to the suit, employees were required to invest their pension assets in hypothetical portfolios tracking the returns of in-house mutual funds managed by the bank.

Moreover, the bank encouraged the employees to transfer more than \$2.7 billion of 401(k) assets into the bank's pension plan in 1998 and 2000. This unusual arrangement, the suit alleges, enabled the bank to invest the money for higher returns than what it would pay the employees in "virtual" returns, and to harness their 401(k) assets to boost the company's income. While the pension arrangement may be unique, the case may draw wide interest, as it comes in the wake of heightened scrutiny by the Securities and Exchange Commission over ways companies can use pension plans to affect earnings.

Heloise Hale, spokeswoman for Bank of America, says in a statement that cash-balance plans "offer many advantages to our associates and we believe they meet the needs of today's diverse and mobile work force better than traditional pension-plan designs. We believe that our plans have been designed and operated in accordance with applicable law. We intend to defend ourselves vigorously against the claims in this lawsuit."

The suit, *Pothier v. Bank of America Corp.*, was filed in federal court in the Southern District of Illinois on June 30. Last week, nearing the traditional 120-day deadline for notifying defendants, summons were served upon several dozen current and former directors of the bank who are named in the suit, as well as the bank, its trustees, and PricewaterhouseCoopers, the consulting firm that designed the unusual pension. In 1985, BankAmerica Corp., as it was then called, converted its traditional pension to create one of the first cash-balance plans. Unlike a traditional pension, which calculates a benefit by multiplying years on the job by salary, a cash-balance plan instead freezes the old pension, and converts its value to a dollar amount. This "account" grows with annual credits based on pay, plus interest, usually pegged to one-year Treasury rates.

In 1998, BankAmerica merged with NationsBank Corp., and became Bank of America, based in Charlotte, N.C. Prior to the merger, NationsBank had converted its traditional pension to "an unusual and particularly aggressive sort of cash-balance

pension plan," the suit says. Instead of crediting the employee "accounts" with a pre-set interest formula, the NationsBank pension credited the accounts with the returns on a limited number of hypothetical investment options that the employees select, whose returns mirrored those of the mutual funds managed by the bank or its affiliates. After adopting this unusual cash-balance-plan structure, NationsBank encouraged its employees to transfer \$1.4 billion in 401(k) accounts to the cash-balance plan, the suit says. Then, following its merger with BankAmerica, former BankAmerica employees were encouraged to transfer \$1.3 billion in 401(k) accounts from the old BankAmerica 401(k) to the cash-balance plan at the new Bank of America.

The suit charges that it was improper for the bank to charge its employees fees on the virtual funds. This reduced their effective "returns," and created a conflict of interest, the suit says, because the bank had control over the levels of fees and thus, to some extent, over the returns in the "funds."

In addition, the arrangement gave the bank an incentive to encourage employees to choose the lowest-return options, the suit charges, because the company could invest the money to potentially earn a higher return.

The design thus created a "massive, leveraged arbitrage opportunity that cynically depended on the company...profiting from its employees' investment mistakes and presumed naivety," the complaint says. It added that the participants are "not well-equipped...to invest pension plan assets like professionals," noted Eli Gottesdiener, the attorney representing the bank employees, in the complaint.

The bank benefited from this arrangement in another way, the suit says. The infusion of almost \$3 billion in assets into the pension plan boosted the company's income.

Under accounting rules, companies earn "expected" rates of return on pension assets. As a result, the \$1.4 billion in 401(k) assets that was transferred into the Bank of America pension in 1998, and the \$1.3 billion infusion in 2000 both earned "expected returns" of 10%, which provided a lift to income.

"The pension strategy was driven by a single-minded goal of gathering assets in the cash-balance plan so that the company could pad its bottom line via the pension arbitrage scheme," the complaint says. The complaint alleges self-dealing, breach of fiduciary duty, and violations involving party-in-interest transactions. It also alleges that the cash-balance pension plan violated age-discrimination laws, and that the bank shortchanged people by incorrectly calculating lump sums when they departed. Also named in the complaint was the consulting firm that designed the pension, Price Waterhouse (now PricewaterhouseCoopers), which declined to comment.