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The pension game**ADVERTISEMENTS**

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By David Warsh, 4/24/2001

One of the biggest changes wrought by the great bull market of the 1980s was that corporations learned to think of pension funds as assets to be managed at least partly for the benefit of shareholders rather than as trusts operated strictly for the benefit of employees. For a time, corporate raiders actually used their targets' surplus pension funds to help pay for their raids after they took control. Congress put a stop to the practice in 1990 with a 50 percent tax on such "reversions."

About the same time, a handful of companies began developing a new approach to retirement benefits called "cash-balance" pension plans. Ostensibly designed to attract younger workers by vesting benefits immediately in highly portable plans, cash-balance plans also gave employers a powerful tool to use against older workers.

With conventional defined-benefit plans, the eventual payout is related to time of service; much of the benefit is earned the last five years. By "front-loading" benefits, cash-balance plans reduce the incentives to employees to stay around. No longer does the employee who stays longest does the best.

With the boom of the 1990s, companies once again have been learning to use the huge surpluses that have built up in their pension funds, this time mainly for their own accounts. The new cash-balance plans have proved to be a cornucopia of benefits - for corporations. A raft of controversial and little-understood new practices have been detailed over the past few years in an extraordinary series of reports by Ellen E. Schultz, a reporter for the Wall Street Journal.

Some corporations have terminated pension plans and substituted "replacement" plans, containing as little as one-quarter of previous assets, thereby avoiding the 50 percent excise tax and flowing the difference directly to reported earnings tax free. Other companies have discovered ways to use cash-balance conversions to smooth their reported earnings.

Summing up, Schulz has written, "The upshot of the pension changes, which are often poorly explained to employees, is that millions of people will retire with pensions that are sharply lower than they once would have been" despite the boom.

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Now one of the lesser abuses (known as "whipsaw" to pension professionals) has been stopped by a decision of the US Court of Appeals for the Second Circuit in New York. A pension plan conversion by the Bank of Boston in the long ago winter of 1990 may come back to haunt the "cash-balance" industry. Certainly it will cost cash-balance companies a good deal of money.

Lynn Esden was a 36-year-old assistant branch manager for the Bank of Vermont when its corporate parent in Boston laid her off. Her traditional defined-benefit plan had been converted to cash-balance the year before. From the traditional plan, she received a lump-sum benefit of \$3,772; her cash-balance account came to \$1,548 - not much, she thought, for a year as a manager.

When she saw a story on the the front page of the Burlington Free Press about the National Center For Retirement Benefits, a company organization that for half of any potential gains reviews documents for puzzled pensioners. She thought, "What have I got to lose? Fifty percent is better than nothing."

The "pension detectives" found what they thought was a significant error under the IRS rules that govern cash-balance accounting - the heads-we-win, tails-you-lose choice known as "whipsaw" - but the bank didn't agree. The detectives sent Esden to an Illinois lawyer, Douglas Sprong. He lost in the US District Court but won on appeal, and the Supreme Court declined to review. Case closed. Law changed.

The overall cost to the bank may be \$7 million or so spread over some 5,500 claimants. (FleetBoston Financial, formed through the merger of Bank Boston and Fleet Financial, will pay.) Esden won enough for a good vacation. A new, more generous basis for valuing lump-sum payouts was established - "the Roe v. Wade of cash balance law!" one lawyer exclaimed. And another glimpse was afforded of the fertile field for mischief that pension fund management has become.

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